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**Pakistan's Trade Policy, 1999–2008:
An Assessment**

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C O N T E N T S

	Page
Abstract	vii
I. Introduction	1
II. Annual Trade Policy	1
1. The Process	1
2. Scope and Coverage	2
3. Implementation	4
4. Effectiveness	5
III. Trade Policy beyond Annual Trade Policy	7
1. Domestic Actors	7
2. Outside Influences	8
3. Market Access	9
4. Trade Remedies	10
IV. Extent of Reforms	10
V. Trade Policy Consistency	14
VI. Policy Redux	18
VII. Conclusion	20
References	21

List of Tables

Table 1. Category-wise Number of Proposals and Their Implementation, 1999-2008	3
Table 2. Pakistan's Tariff Structure, 2001-02 and 2004-08	13

List of Figures

Figure 1. Trade Liberalisation Indicators	12
Figure 2. Average Import Tariff Rates	12
Figure 3. Distribution of MFN Tariffs, 2001-02 and 2007-08	13
Figure 4. Export Growth Rate	14
Figure 5. Average Per Annum Growth in Exports/GDP, 1990–2004	16

ABSTRACT

Employing the Annual Trade Policy issued each year by the Ministry of Commerce as a simplified case study, this paper examines the reasons for the ineffectiveness of this policy instrument and the inherent inconsistencies and conflicting signals to the market that it contains. Capacity constraints and the lack of a sufficient belief in the virtues of trade liberalisation have led to a situation where the more significant trade reforms have almost invariably been ushered in by the IMF/IFIs. It is argued that reforms under external influence are not always properly sequenced, and are seldom of a lasting nature; that 'ownership' of trade reforms can only be ensured when the policy-makers and the decision-makers come to understand trade policy's role in nurturing quality institutional environment. This would require, *inter alia*, institutional capacity strengthening of the Ministry of Commerce (and its subordinate bodies) and giving it effective authority to formulate trade policy.

JEL classification: F13, O24, O19

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I. INTRODUCTION

A sound public policy edifice is a necessary pre-requisite for good governance. The quality of policy, in all its aspects, from formulation to decision-making, is a vital determinant of a Government's ability to deliver. While the policy decision process in Pakistan is well understood, and adequately backed with the required statutory provisions, the policy-making process is less so. Equally hazy is the post-decision process: implementation, evaluation, and review of policy.

This Paper attempts a more detailed look at the public policy apparatus through an assessment of Pakistan's trade policy as it has evolved over the last ten years. The examination of how trade policy is formulated—and by whom—also brings out the capacity issues, both of making policy and implementing it.

For a number of reasons Trade Policy is an interesting vehicle of investigation: it is being constantly reshaped, not the least due to the globalisation imperative; there is a plurality of actors involved; and it has a significant bearing on public welfare.

Pakistan's trade reform process, initiated in earnest in the late 1980s, intensified during the last ten years, especially the first half of the decade, that coincided with the 'actualisation' of WTO obligations and the IMF programme (2000–2004). The space provided by debt rescheduling and enhanced capital inflows in the wake of 9/11 and certain policy adjustments facilitated this intensification as the traditional revenue and balance of payments arguments against trade liberalisation lost some of their urgency.

While this paper's primary area of investigation is the process of trade policy formulation in Pakistan, using the Trade Policy announced each year by the Ministry of Commerce as a case study, it also touches upon certain concomitant issues like the depth of reforms and the likelihood of their sustainability. It looks at the capacity asymmetry of domestic and external actors, and tries to plumb the reasons for a general reluctance to liberalise despite sufficient empirical evidence to do so, especially in the context of export growth and investments that trade liberalisation is said to promise. Finally, it seeks to identify the major issues of trade policy formulation and possible responses.

II. ANNUAL TRADE POLICY

1. The Process

The Annual Trade Policy (ATP) is the successor to the annual Import Policy that was a major policy instrument at a time when imports were strictly controlled. Once imports started to get liberalised (with the switch from the

‘positive list’ what could be imported and under what conditions—to the ‘negative list’ everything importable except prohibited or regulated) the annual Import Policy lost its rationale and the Ministry of Commerce (MoC) chose to substitute it with the ATP¹ to reflect the shift in focus from import substitution to export enhancement. (In the early years the ATP used to consist of two parts—the import policy and the export policy).

Formal commencement of the ATP exercise is heralded by the meeting of the Advisory Council around end April.² However, ATP formulation is a continuous process and throughout the year MoC consults individuals, trade bodies, and government agencies. MoC also rakes old ATPs (to resuscitate good ideas inadequately executed), IFI/Donor reports, regional experiences, work of international organisations like UNCTAD, ITC etc. in search of ideas. Inputs are also sought from trade offices abroad, the WTO Mission in Geneva, and the Trade Development Authority (TDAP, formerly Export Promotion Bureau i.e. EPB).

The ATP is approved by the Cabinet,³ usually at a specially convened session that is also attended by the Deputy Chairman Planning Commission, the Governor State Bank and Secretaries of the relevant Ministries. By and large, most Cabinet members tend to focus more on proposals pertaining to imports, generally resisting import liberalisation measures that are seen by them to be politically less palatable.

There is little evidence of an extensive use of the usual policy-making tools (diagnosis, evidence-based research, development of policy options etc.). There appears to be a greater reliance on experience, close interaction with the trade, and a perceptive understanding of the issues in ATP formulation.

Political interaction is limited to the consideration of the ATP proposals by the Cabinet. Parliamentary over-sight is virtually non-existent, especially since the Finance Bill does not include any ATP related demands. The occasional meetings of the Standing Committees rarely go into the details of ATPs.

2. Scope and Coverage

While its thrust and style varies from Secretary to Secretary, the ATP generally consists of three parts:

¹There is not a good explanation for the ATP to be an annual feature, or for that matter to be announced after the budget. The business community, however, continues to look forward to it, partly in the expectation that the ATP will provide what the Finance Bill did not. The ATP rarely does so.

²The Advisory Council is too large (200 plus members) and too diverse in its composition to be an effective ‘advisory’ body. It rarely meets more than once in the year, but its meeting is presented as ‘stakeholder participation.’

³Following the practice of the erstwhile Import Policy the ATP Summary for the Cabinet is marked Secret and rarely made available before the meeting, denying the Cabinet members the opportunity to properly study the Summary.

- (a) Review of the preceding year's import/export performance.
- (b) Changes in trade regime warranted by bilateral/multilateral/plurilateral obligations, or for purposes of trade facilitation, or for removal of anomalies.
- (c) Export enhancement measures.

It is really the Export Enhancement Measures (EEMs) that constitute the 'centrepiece' of the ATP. To have a summary view of the general thrust of the proposals contained in the last ten ATPs they have been classified into six broad categories. The number of initiatives taken in each category are tabulated in Table 1, that also shows the number of proposals that were actually implemented. (All the proposals are not necessarily 'new'— there is a degree of repetition, or modification, of proposals contained in the earlier ATPs).

Table 1

Category-wise Number of Proposals and Their Implementation, 1999–2008

Category	Number of Proposals	
	Made	Implemented
1. Production/Export Assistance (Incentives)	54	41
2. Customs Related (Zero Rating, Duty Free Imports, Bonding, Export Controls, Procedural Implements, etc.)	70	64
3. Trade Facilitation	39	34
4. Promotion and Development	76	36
5. Infrastructural, Physical and Social	25	6
6. Import Liberalisation	38	36

The dominance of customs related EEMs that marked the earlier ATPs receded with the gradual removal of quantitative restrictions (QRs) and lowering of tariffs.⁴ In the more recent ATPs the emphasis seems to be on incentives (freight subsidy, cheaper export re-finance, subsidised interest rates for capital investment, warehousing and offices abroad, rebates etc.)⁵ and developmental initiatives. The 'import liberalisation' proposals mostly pertain to the enlargement of the 'positive list' of imports from India, relaxation of restrictions on import of second hand machinery, and removing of licensing/NOC requirements.

⁴The 1999-2000 ATP observed, "...there is need to remove those barriers that inhibit exports. This is certainly not easy on account of the traditional focus on import substitution".

⁵There is sufficient empirical evidence [see, for instance, Azhar (2001) and Haque and Kamal (2007)] to suggest that barring exceptional circumstances subsidies do more harm than good, and indeed MoC sought to roll them back during 2000-02. But the Pakistani exporters do not see them as subsidies but 'compensation' for the cost penalties that are not of their making (e.g. over valued exchange rate, inefficient infrastructure, erratic power supply, preferences and subsidies available to their competitors etc.).

It has to be noted here that MoC's trade policy initiatives are not just restricted to the ATPs and not all that it does gets reflected in the annual trade policy announcement. MoC does seek to influence, whenever it can and not always without success, various trade policy instruments, in particular the tariff policy, export refinance policy, and trade facilitation. It is also quite proactive in its interaction with the other Ministries on trade related deregulation matters. On occasion it develops strategic 'visions' as well that are based on sound analysis and are well articulated. (Textiles, Leather Goods, Engineering Goods, Rice, Horticultural Products). But on the whole, MoC does lack sufficient policy space and more often than not seeks incentives more than resolution of the structural problems.

3. Implementation

There is a fairly prompt implementation of ATP proposals that require the issuance of an SRO, either by the FBR or the MoC. Proposals that require action by another Ministry can be more time consuming, notwithstanding the fact that being Cabinet decisions they are of a binding nature. Where MoC fails in its 'bilateral' attempts it takes recourse to the ECC or the powerful Federal Export Promotion Board that is presided over by the Prime Minister and whose Secretariat is the MoC.

A full and proper implementation of ATP proposals, especially the more significant ones, shows at best a mixed record. For illustrative purposes Box 1 summarises the implementation status, eleven months after the announcement, of the more pertinent measures announced in the ATP 2007-08.

The real reasons for non or partial implementation appear to be

- (a) Design flaws, emanating from inadequate research.
- (b) Long gestation nature of some of the proposals.
- (c) Ownership and funding issues.⁶
- (d) Capacity weaknesses of the principal implementing agency, the Trade Development Authority (TDAP), and inadequate monitoring mechanism.

[Implementation, of course, does not always mean achievement of the objective. Implementation of the proposal to set up the Skill Development Council, for instance, does not mean that sufficient availability of skilled manpower has been ensured. For the purposes of this examination implementation is to be construed in the sense of output and not outcome].

⁶For several proposals requiring a financial outlay there is no 'budgetary support'. MoC has to rely on the Export Development Fund (EDF, sourced from the 0.25 percent surcharge on exports) and the Export Marketing Development Fund (EMDF, financed from the Federal Budget. Before the textile quota regime expired an important source used to be the auction proceeds of 'tree quota' i.e. available to Government). Both these funds are of limited size and have large throw-forwards.

Box 1. Implementation Status ATP 2007-08	
Proposal	Current Status
Long Term Fixed Rate, Export Oriented Projects Financing Schemes to Additional Sectors	Scheme being reviewed.
EPZ Incentives to Export Oriented Units (EOUs)	CBR has issued SRO. Weak exporter response so far.
Establishment of Equity Fund for Brand Acquisition And SPS Compliance	TDAP consultant proposed to be engaged for pre-feasibility study.
First Year Allowance (FYA) for PME Investments	FYA already available under the current income tax regime. (Possible that MoC and FBR not on the same page).
Export Credit Risk Management	PCI for GoP equity in Export Finance Guarantee Agency being processed
Setting Up of Social, Environment and Security Compliance Board	EDF funding approved. To Rs for Board being developed.
Setting Up of Skill Development Council in TDAP	Being processed.
Setting Up of Agri-marketing Integrated Centres	Being processed (Consultant and project co-ordinator to be hired. Private sector company has to be selected to manage AMICs for which PCI has to be prepared).
Assistance in Reaching International Standards	Public Notice notifying the scheme and inviting applications is being processed.
Financial Support for Compliance Certifications	Public Notice is being processed.
Assistance for Opening Exporters' Offices Abroad	EOIs invited from interested exporters
Support for Marketing of Branded Products	Public notice being issued
Retail Sales Outlets	EOIs being invited
Overseas Business Support Units	Being processed.
E-Marketing	Being processed.
Financial Support for British Retail Consortium Certification	Being processed.
International Consultants to Identify Industrial, Agricultural And Service Sectors of Current And Future Potential And Prepare Short, Medium And Long Term Plans.	Being processed.
Inland Freight Subsidy For Engineering Goods' Exports	Being processed.
Financial Assistance to Set Up Slaughter Houses	Being processed.
Establishment of Women Entrepreneur Cities in Karachi and Lahore	PC-1 being developed.
Export of Pharmaceutical Products	Modalities for implementation have been worked out, in consultation with PPMA, and Public Notice being released.
Appointment of Consultant to Support Production and Export of Japonica Rice	Being processed.

4. Effectiveness

There are no defined objectives of the ATP, rendering it difficult to assess its effectiveness. The goals are rarely explicit. There is a weak targeting effort (and therefore it tends to benefit the bigger exporters more) and vague cost and time lines. There does not seem to be a broad framework or strategy driving the proposals contained in the successive ATPs. Thus, more than a 'policy', in a strategic or directional sense, ATP comes across as a conglomeration of ideas aimed at facilitating greater exports. Trade liberalisation per se does not emerge as a major objective.

An examination of ATP effectiveness, thus, has to be restricted to the contribution of ATPs to export growth. This is quite challenging, not just because of the plethora of exogenous variables affecting outcome, but also the absence of studies or workings leading to the development of the ATP proposals

to show the linkage between the proposed intervention and the likely export gain.

An analysis (Box 2) of the Rapid Export Growth Strategy (REGS),⁷ that was introduced in ATP 2005-06 and is said to be the basis for the subsequent

Box 2. Rapid Export Growth Strategy (REGS)

Improved market access, promotional efforts in new markets, strengthened trade offices, skill and infrastructure development are stated to be the 'pillars' of REGS. These strategic objectives are to be achieved ('tactical thrust') through diversification, trade facilitation, competitiveness ('reducing the cost of doing business'), capacity building (WTO and trade negotiations), compliance and quality infrastructure, export of services, and buyers driven FDI.

For purposes of an assessment the specific measures proposed in the three ATPs (2005-06-2007-08) to support the objectives (categorised into seven major ones) are looked at to see consistency and outcome. (It is, of course, recognised that ATP is not the only vehicle to meet these objectives; they can be, and often are, pursued outside the ATPs).

1. MARKET ACCESS. A staggering number of PTAs has been finalised, more are being pursued (see Box 4 for details). However, no progress has been possible in the principal markets (EU27 and US), except the Reconstruction Opportunity Zones (ROZs) initiative for the US market (no official assessment of the likely export gains of ROZs is available).

In terms of outcome the PTAs are too recent to permit an assessment. The choice of partners (with the possible exception of China), however, does not promise a major export *creation* impact, at least over the short term.

2. DIVERSIFICATION. For market diversification 13 'priority countries' were identified in Africa, Latin America and the Central Asian Republics. The ATPs do not propose any specific measures to penetrate these markets, save the general approaches (local marketing executives, honorary Consul Generals, exhibitions and delegations, warehousing) that are yet to be properly implemented.

For product diversification several incentives were proposed for gems and jewellery, footwear, pharmaceuticals, horticultural and agricultural products, and engineering goods. The measures, by and large, are in the nature of incentives and are not robust enough to have a significant effect, nor do they address the real export inhibiting factors.

No specific support measures were suggested for towel, denim, chemicals and services that were identified as 'focus products' in ATP 2006-07 to increase their exports to \$1 billion each by 2009.

[Diversification is a goal that has so far eluded Pakistan. Appropriate *policy options* to deal with this important issue have not been developed. There are, for instance, those who hold diversification is more than a function of incentives and market access (especially where it does not factor in revealed comparative advantage). It is argued without fresh export oriented investments that ensure scale, technology and innovation, and superior managerial skills- and produce what the markets want rather than market what is produced- diversification will not be possible).

3. COMPETITIVENESS. 'Reducing the cost of doing business', and 'level playing field' are the oft repeated demands that have been met through 'incentives' to the extent possible. All three ATPs emphasise 'Domestic Commerce' as a means to improved export competitiveness. Other than the establishment of a Domestic Commerce Wing in MoC, it is still 'work in progress'. No progress is known to have been made on development of 'competitiveness indicators'. It would appear a far greater effort, including at microeconomic level, is needed to meet this major challenge.
4. CAPACITY BUILDING. There have been weak impulses (TDAP restructuring, National Tariff Commission strengthening, WTO and Trade Agreements, Trade Offices), mostly not fully implemented. Capacity remains a critical constraint.
5. SKILL DEVELOPMENT. A Garments Skill Development Board has been set up. Certain selected units have been declared as skill development centres. In terms of outcome, the problem persists.
6. SERVICES EXPORTS. Again, few and weak initiatives. Only one consultancy (architecture) has been completed, which is being processed. There is a recognition of the strong potential of export of services but the required roadmap and strategy do not seem to be in evidence.
7. BUYER DRIVEN FDI. None of the ATPs suggest any specific measures. It appears this objective is being pursued within the overall FDI regime. Considerable investment has been made in the Textiles sector, and some in Cement and Chemicals (Ethanol), but this has been domestic rather than FDI.

⁷An earlier ATP (2002-03) had spoken of a somewhat different 'National Export Strategy' whose elements were: sound macroeconomic framework, capacity development of exporters (microeconomics), enhanced market access, reduced anti-export bias, improved social and physical infrastructure, deregulation, and lowered barriers to fresh entry (new generation of exporters). Frequent changes to strategy underscore the inherent policy inconsistency.

ATPs as well, fails to bring out a strong co-relationship between the ATP measures and export growth objectives. The proposed initiatives are either too basic to have a salutary effect—of the ‘trouble shooting’ kind—or insufficiently prepared to tackle the issues constraining greater exports. REGS, for instance, rightly dwells on ‘competitiveness’ but offers little by way of sustainable solutions that get to the heart of the problem. Even in the area of Market Access, where impressive progress has been made, at least in terms of the number of agreements made, the choice of preferential trading partners makes it unlikely that it will materially affect either export diversification or growth until appropriate investments are made to meet the demands of these markets.

ATPs (including pre-REGS), appear to have been more successful in Trade Facilitation and a more open import regime. While the influence of external actors in this regard cannot be totally excluded several of the initiatives have been ‘home grown’ and motivated by export growth considerations.

III. TRADE POLICY BEYOND ANNUAL TRADE POLICY

If the ATP has only a marginal relevance to its classical definition where are the contours of real trade policy shaped and how is it executed? Not unexpectedly, there are several players. Also, other policies act upon and interact with trade policy. The more salient of these influences are discussed below.

1. Domestic Actors

Ministry of Commerce may have the *presumed* responsibility for Trade Policy, and is required to ‘defend’ it at WTO’s six yearly Trade Policy Review at Geneva in the presence of all member states, but in actual practice several critical tools of Trade Policy (tariffs, concessional SROs, simplification of Customs procedures and related trade facilitation, exchange rate, payment terms, conditions of repatriation of export proceeds, export finance rates and caps, etc.) are beyond its domain. Even in the more narrow interpretation of trade policy, i.e. exports enhancement, Ministry of Commerce is not unhindered. It is only in matters falling under the Import and Export (Control) Act, that is administered by MoC and relates more to conditions and procedures of import/export, that it has exclusive jurisdiction, though it has to depend upon the Customs for implementation.⁸

The fact is that several important actors inhabit the Trade Policy formulation arena, the principal being the Central Board of Revenue (now FBR) and the State Bank. For sectoral measures Ministries of Agriculture, Industries,

⁸Under the Rules of Business the Commerce Division’s remit includes ‘import and export’ regime (including related treaties and agreements), ‘tariff (protection) policy and its implementation’, and ‘export promotion’.

and Privatisation and Investments are the key players. Provincial Governments, too, weigh in (for instance when the Sindh Government chose to levy a ‘cess’ on imports that amounted to para-tariffs). Most recently, the Planning Commission has pitched in with its ‘Export Plan-Pakistan Inc.’ that proposes a roadmap to take exports to \$40 billion plus by 2013, prompting WTO’s December 2007 Trade Policy Review to observe that the Planning Commission ‘is actively involved in setting trade policies, including export promotion and trade development.’

While a division of powers is very much in the scheme of things what the examination of the prevalent system unmistakably brings out is the absence of a strong and well equipped focal point for Trade Policy formulation. This has contributed to the striking absence of an overall strategic framework, shared and owned by all the players, to drive trade policy. Interestingly, GoP’s Rules of Business do not assign Trade Policy to any Ministry. In fact trade policy as such is not mentioned at all. Apparently, the Government does not perceive trade to require a distinct and specific policy field; rather an outcome of other policies.⁹

2. Outside Influences

Being a ‘founding member’ of the WTO, the pains of the complex ‘accession process’ that usually requires a large liberalisation effort, were not visited upon Pakistan. Several WTO provisions, most notably the Special and Differential treatment (even though it is largely of the ‘best endeavour’ kind), that allowed the Developing Countries either exemptions or more time, gave sufficient room for manoeuvre. Except where self-motivated, or propelled by IMP / IFIs, Pakistan by and large sequenced the WTO commitments at a pace of its own choosing. For instance, it secured more time for compliance of Trade Related Investment Measures (TRIMs), Agreement on Customs Valuation, Agreement on Subsidies and Countervailing Measures; and where it was tardy (e.g. requirement of ‘Notifications’) it only got gentle reminders. Pakistan also took its time in getting its tariffs ‘bound’ (i.e. the tariffs cannot be increased beyond the rate notified to the WTO, except where an exemption is obtained for balance of payments reasons), and barring the Textiles related tariffs that were bound at the level of applied rates (as part of Pakistan’s protracted negotiations with the EU to secure duty free market access), the bound rates are much higher (about four times) than the applied rates. In essence, WTO on its own has hardly sent Pakistan scurrying to the trade reform drawing board.

The real thrust for trade policy reforms has come from the IFIs and the IMP. It was especially quick and intense in the first half of this decade. To

⁹Shahid Javed Burki notes: “Public policy in Pakistan has never explicitly looked at international trade as a contributor to economic growth, poverty alleviation, and improvement in income distribution... When policy makers have turned to trade, they have done so to improve the balance of payments situation.” [Burki (2008)].

nudge Pakistan on the path of liberalisation, IMP came in with performance criteria and structural benchmarks, prior actions and conditionalities¹⁰ in its Stand By Arrangement and Poverty Reduction and Growth Facility. The World Bank and Asian Development Bank paved the way by piggy-backing these reforms on their substantial loans.

3. Market Access

Arguably, the only area of trade policy that was genuinely ‘home grown’, and not influenced by IMP/IFIs, was the almost relentless pursuit of preferential trading arrangements (PTAs). This is a significant departure from Pakistan’s traditional approach of liberalising trade either unilaterally or multilaterally. Greater market access and diversification are the stated objectives but the proliferation of preferential arrangements elsewhere, that have put Pakistan’s exports at a disadvantage, has no doubt been an important consideration. Box 4 summarises the various PTAs that Pakistan has and is seeking.

Box 4. Pakistan’s PTAs

Pakistan now is a member of four regional / plurilateral PTAs: SAFTA (2006, with SAARC), PRETAS (2005, with OIC countries, target effectiveness date 1 Jan. 2009), ECOTA (2003, with ECO countries, yet to be ratified by the requisite number of countries), and D-8 PTA (Pakistan, Bangladesh, Egypt, Indonesia, Iran, Malaysia, Nigeria and Turkey. Yet to be ratified).

Pakistan also has bilateral Free Trade Agreements (FTA) with Sri Lanka (2005), Iran (2006), China (2007), Malaysia (2008), and Mauritius (under implementation). It is also negotiating FTAs with Singapore and the Gulf Cooperative Council (GCC) and pursuing various forms of preferential trading arrangements with Turkey, MERCOSUR, EFTA and some 20 other countries. With the U.S., despite the long negotiated Trade and Investment Framework Agreement, an FTA remains a forlorn hope, though the authorities are quite excited with the Reconstruction Opportunity Zones bill currently under consideration of the U.S. Congress. With the EU the duty-free market access secured after long negotiations on a quid pro quo basis—clearly a spectacular highlight of Pakistan’s trade diplomacy—was lost in 2005. It also did not qualify for EU’s GSP+ arrangement for sustainable development and good governance, leading the authorities to claim that Pakistan has been unfairly discriminated against. FTA with EU remains a high priority despite the European Commission’s current reluctance.

¹⁰Ishrat Hussain highlights the sheer volume of the required actions: “The performance criteria had five pages of footnotes on adjusters, qualifiers, and precise numbers to be achieved.” [Hussain (2003)].

FTA/PTA based Market Access has clearly emerged as Pakistan's principal trade policy instrument. While the concluded FTAs/PTAs are of too recent a vintage to permit a fair evaluation, the overall approach does raise some concerns. Besides the glaring capacity constraints to negotiate, and implement, such a large number of FTAs/ PTAs, with a noticeable degree of overlap, the trade regime is likely to become more complex and more uncertain. Further, as each FTA/PTA requires preferential tariff treatment there will be a temptation to keep the MFN duty rates high to permit future concessions. There is also the fear that the multiplicity of these agreements could be efficiency-reducing, divert more trade than they create,¹¹ and induce sub-optimal trade patterns.¹²

The advantages of PTAs also get diminished in one other important aspect if not proactively pursued: using market access as a tool to attract foreign direct investment. If an FTA/PTA is a genuine means of freer access to a market it should automatically create interest among foreign companies to invest in Pakistan to take advantage of lower tariffs on made in Pakistan goods. It is not known how Pakistan proposes to 'market' its PTAs to induce export oriented FDI.

4. Trade Remedies

While actively pursuing the trade openness agenda in the early part of this decade Pakistan does not seem to have paid equivalent attention to defence remedies and legitimate safeguard actions. Having been obliged, with good reason, to do away with Regulatory Duties, which was a quick and convenient way to defend an industry against a surge of imports, Pakistan was slow to put in place an effective defence mechanism. The time it took to prepare WTO compliant laws,¹³ reform the NTC (National Tariff Commission, the institution responsible for contingency protection), and the complexity of filing the cases before the NTC, put the affected domestic producers under severe pressure, and proved fatal for some SMEs.

Pakistan has not taken any countervailing or safeguard actions.¹⁴ In anti-dumping it carried out 24 investigations and imposed 19 measures (India, in contrast, has taken several times more measures over an equivalent period).

IV. EXTENT OF REFORMS

The IMF led trade reforms of this period were quite deep and wide-ranging. They went beyond tariff reduction and removal of quantitative restrictions to embrace virtually every facet affecting trade: from exchange rate mechanism to production/export assistance, to state trading. Some of the major reforms are summarised in Box 3.

¹¹Word Bank (2006).

¹²Tumbarello (2007).

¹³The Anti-Dumping Duties Rules were finalised in 2001, the countervailing Duties Rules in 2002, and Safeguard Measures Rules in 2003.

¹⁴The sole safeguards investigation, on footwear imports, was terminated in August 2005.

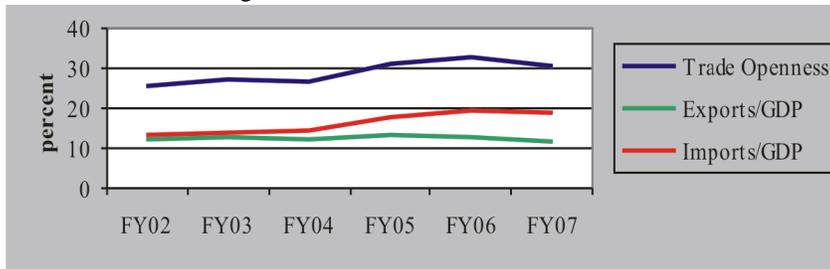
Box 3. Summary of Trade Reforms

1. Import Related
 - Almost all QRs removed. Restrictions on imports from India and on second hand machinery being continuously relaxed
 - Requirement of importer registration (with EPB) done away with
 - Licensing requirement minimised
 - LC margin requirements withdrawn
 - Import Policy and Procedures rewritten for greater simplicity and transparency
 - Afghanistan Transit Trade rules liberalised
 - Local content conditions withdrawn
2. Export Related
 - Export bans! restrictions on almost all products removed
 - Minimum Export Prices withdrawn
 - Export duties withdrawn
 - Most export subsidies withdrawn
 - Registration (of exporters) requirement withdrawn
 - Pre-shipment registration of export contracts now restricted to cotton and urea only (to check domestic shortages)
3. Tariffs
 - Maximum tariff rate reduced to 25 percent (except automobiles/luxury items)
 - Simple average MFN rate down to 14.5 percent (import weighted even lower)
 - Almost all tariff rates have been bound with WTO
 - Most rates are on ad valorem basis
 - Duty slabs reduced to four
 - Regulatory duties (as contingent protection measure) done away with
 - Number of concessionary SROs substantially reduced
 - Para tariffs largely merged
 - Customs valuation shifted from 'Import Trade Price' basis to transaction value
4. Custom Procedures and Trade Facilitation
 - Single Administrative Document (SAD) introduced, (in place often different documents that used to be required)
 - Electronic documentation and clearance introduced. Physical cargo inspection rates reduced to 4 percent
 - Steps needed to clear vessels reduced from 26 to one; clearance time shortened to about eight hours; part dwell times reduced from 11 to 4 days
 - Revised Kyoto Convention acceded to in addition to Nairobi and Istanbul Conventions
5. State Trading
 - Rice and Cotton Export Corporations wound up
 - State trading restricted to exceptional circumstances, (through TCP, which does not have any exclusive rights or duty preferences)
6. Others
 - Compliance with all WTO commitments
 - Standards harmonised with international requirements
 - Imported and domestic goods undergo the same conformity testing procedures
 - Exchange rate mechanism reformed
 - Export refinance rates made market compatible
 - Paris, New York, ICSID conventions acceded to
 - Telecom sector deregulated
 - Bilateral Investment Treaties signed with 48 countries.
 - FDI regime made more attractive
 - Extensive Financial Sector Reforms
 - Competition Commission set up (replacing Monopoly Control Authority) Intellectual Property Rights Organisation set up.

N.B. some of these measures may have been rescinded or modified in recent years.

These reforms had a significant effect on Pakistan's trade openness (trade measured as a ratio of GDP). Imports and exports as a percentage of GDP improved from 25.7 percent in 2001-02 to 32.7 percent in 2005-06, before declining to 30.4 percent in 2006-07. (Figure 1).

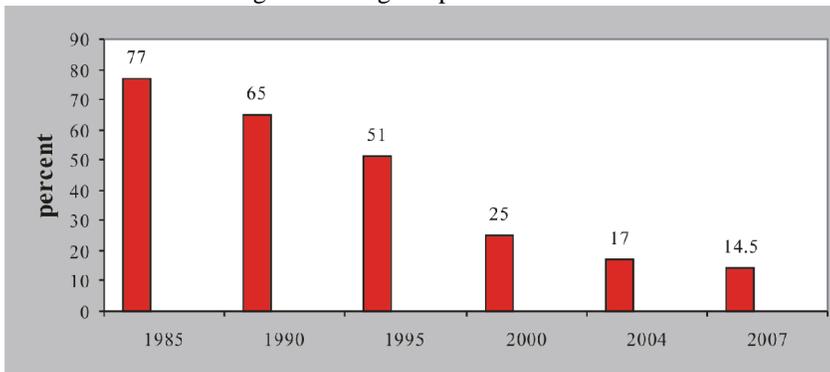
Fig. 1. Trade Liberalisation Indicators



Source: SBP.

The most glaring impact was on tariff structure (Table 2), with the simple average (unweighted) MFN tariff rate coming down to 14.5 percent in 2007-08 compared to about 45 percent a decade earlier. (Figure 2). Import weighted average tariff came down to 8 percent and average effective rate to 7.6 percent.

Fig. 2. Average Import Tariff Rates



Source: UNCTAD (Trains).

About 40 percent of the tariff lines now attract a duty rate of 5 percent or less (Figure 3). Tariff dispersion and escalations were also positively affected. It has to be noted that lower tariffs did not adversely affect import related revenues. In fact tariff revenue as a percentage of total tax receipts they went up from 15.3 percent in 2001-02 to 20 percent in 2006-07 because of greater imports and the levy of General Sales Tax on several products at the import stage.

Table 2

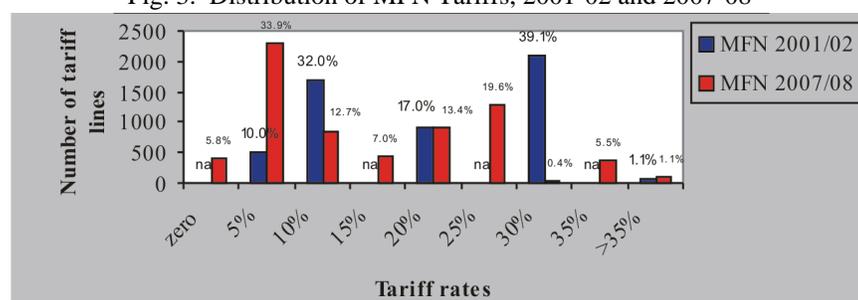
Pakistan's Tariff Structure, 2001-02 and 2004-08

	2001-02	2004-05	2005-06	2006-07	2007-08
Bound Tariff Lines (% of All Tariff Lines)	36.6	–	98.4	98.0	98.0
Simple Average Applied Rate	20.4	16.8	14.4	15.0	14.5
Agricultural Products	21.8	19.0	15.6	15.4	14.9
Industrial Products	20.2	16.5	14.2	14.9	14.5
WTO Agricultural Products	22.1	19.3	15.7	15.3	14.8
WTO Non-agricultural Products	20.1	16.5	14.2	15.0	14.5
Textiles And Clothing	26.4	21.7	18.9	19.4	19.3
Domestic Tariff "Peaks" (% of All Tariff Lines) ^a	0.9	1.2	1.1	1.0	1.1
Overall Standard Deviation of Tariff Rates	16.0	11.9	11.0	11.3	11.7
Coefficient of Variation of Tariff Rates	0.8	0.7	0.8	0.8	0.8
Duty Free Tariff Lines (% of All Tariff Lines)	0.0	0.0	0.0	0.0	5.8
Non-ad Valorem Tariffs (% of All Tariff Lines)	0.9	0.6	0.7	0.7	0.6

Source: WTO.

^aDefined as those exceeding three times the overall simple average applied rate.

Fig. 3. Distribution of MFN Tariffs, 2001-02 and 2007-08



Source: WTO.

Note: Calculations exclude specific rates and include the ad valorem part of compound rates. Data points above the bars denote the share of total lines. 2001-02 tariff consists of 5477 tariff lines and 2007-08 consists of 6909.

Have these tariff reforms been deep enough? Pakistan's 'foreign partners' do not seem to think so. The WTO finds Pakistan's reforms to have been 'uneven' since its last review of Pakistan's Trade Policy [WTO (2007)]. World Bank thinks that although lower, 'the anti-export bias from tariffs and other trade restrictions remains high favouring import substitution and reducing Pakistan's resource-use efficiency, export competitiveness, and diversification' [World Bank (2006)].¹⁵ World Bank's concerns 'informally shared' with GoP authorities are said to be more stringent. Both IMF and ADB, in their discussions with the authorities, are also said to stress the need to persist with

¹⁵Using the Overall Trade Restrictiveness Index (OTRI), that computes the tariff equivalent of a country's import restrictions, World Bank researchers find a 21 percent equivalent import tariff rate for Pakistan—lower than India, Malaysia, the Philippines, and Bangladesh; higher than Sri Lanka, Thailand, Indonesia and Turkey. [Kee, *et al.* (2006)].

trade reforms. This is also the underlying message of some of the studies commissioned under the Competitiveness Support Fund.

V. TRADE POLICY CONSISTENCY

Technically speaking, Pakistan is correct when it claims that its trade liberalisation has been 'autonomous'. Behind the scenes, though, it remains mindful of the 'Washington Consensus' even after the 'successful completion' of the IMF's Poverty Reduction and Growth Facility. Despite this, recent evidence tends to suggest a growing incidence of 'backsliding', raising the question of the sustainability of the trade reforms process.

While the recently introduced import tightening measures (increased duties and GST, some para-tariffs, LC margins) can perhaps be defended on account of the extraordinary growth in trade deficit,¹⁶ early indications of at least some roll-back were already there, especially since the ending in 2002-03 of the unilateral 'tops down' tariff programmes. The process of roll-back of Production and Export assistance (subsidies) has been stalled and even reversal in certain cases. Several measures that tend to exacerbate tariff disparities and dispersion were taken. The Regulatory Duty (RD) provisions were amended to take away NTC role and the condition of limiting RD applicability to a maximum duration of one year. Commitment to phase out concessionary SROs seems to have been put on hold, and the number of duty slabs almost doubled since 2002-03. [This sampling of apparent 'reversals' is not intended to question the quality of decisions but merely to illustrate the directional change].

Besides the inconsistencies there also seem to be certain inherent contradictions. If the avowed, if not the principal, aim of Trade Policy is export growth, do not the more recent policy moves militate against exports? Higher effective rate of protection will accentuate the anti-export bias by making the domestic market more profitable. Also, tariffs are an implicit tax on exports, and as Tokarick argues they discourage exports by raising the cost of imported inputs. [Tokarick (2006)]. Already low import content is one of the obstacles to greater exports which will be exacerbated by costlier imports. This will also mean greater reliance on duty neutralising schemes that have high transaction costs and divert exporter attention from marketing to refunds.

Again, direct export subsidies are counter-productive. They distort investment decisions and encourage rent-seeking. In the ultimate analysis it becomes a zero sum game and often you require more subsidies as the competitors up theirs, in response to yours, to maintain your current levels of export. Subsidies also tend to depress unit prices as at least in part they have to be passed on to the buyer.

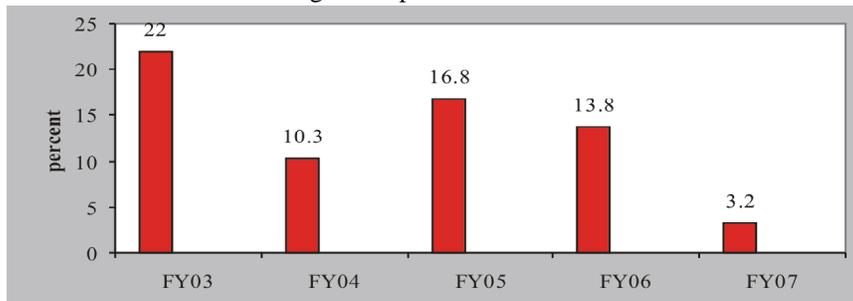
¹⁶Some will no doubt question the need for such measure given the recent close to 15 percent depreciation of Pak Rupee, besides the 'inelasticity' of most imports.

What could be the explanation for these policy inconsistencies, that also cast a shadow over the sustainability of the trade reform process? Would the policy attitude have been different if the nexus between trade liberalisation and growth and welfare gains was more explicit and better understood?

There is a considerable body of literature based on cross-country investigations to suggest a positive relationship between trade openness and economic performance.¹⁷ Indeed, the well-known work of Frankel and Romer (1999) concludes that a one percentage point increase in trade-to-GDP ratio leads to a 2 percent increase in per capita income. Even the sceptics such as Rodrik and Stiglitz do not oppose trade liberalisation per se but qualify it: the former to the need for institutions and policies to manage downside risks [Rodrik (2002)] and the latter, additionally, to the need to balance the asymmetry of trade relations, where the developing countries open up their markets to goods from the advanced industrial countries without full reciprocation. [Stiglitz (2006)].

It will be difficult to irrefutably establish the virtues of trade liberalisation if seen, as is often the case in Pakistan, through the narrow prism of sale of goods and services to earn foreign exchange. In Pakistan's case exports did start to grow, almost as soon as the deeper trade reforms had been implemented, maintaining a compound annual growth rate of 16 percent between 2002 to 2006, before tapering off to about 3 percent last year (a likely 10 percent this year). (Figure 4).

Fig. 4. Export Growth Rate



However, this more than doubling of export value over the decade loses much of its lustre when viewed in the context of the following factors:

- (a) The extraordinary advantage of duty-free market access to EU, Jan 2002 to Dec. 2005 (This also had a positive sympathetic effect on the other markets, especially the U.S.)
- (b) Emergence of Afghanistan as Pakistan's third largest market, post 9/11.

¹⁷See for instance, Sachs and Warner (1995), Bhagwati (2004), Winters, McCulloch, and Mackay (2004), Edwards (1998).

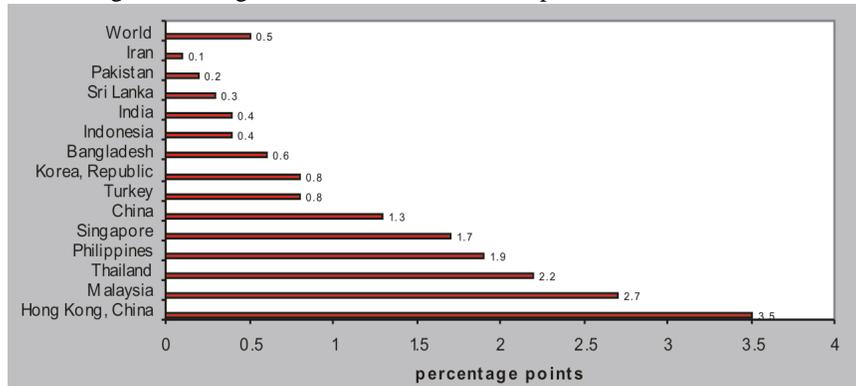
- (c) Higher growth rates of competitors (China, Vietnam, Bangladesh, India, Sri Lanka).
- (d) There was little product or market diversification, as SBP's entropy index establishes [SBP (2007)].

Contrariwise, there are certain exogenous factors that contributed to the recent slowing down of the growth rate, besides of course the continual anti-export bias referred to above:

- (a) Higher inflation rate relative to trading partners (Relative Price Index) causing a continuous appreciation of real effective exchange rate since 2003-04.
- (b) Withdrawal of duty-free access to the ED market.
- (c) Accession of Vietnam to WTO and expiry of safeguards on Chinese textile exports.
- (d) Market access challenges. According to a World Bank study [Kee, *et al.* (2006)] Pakistan had the fourth lowest market access among 91 economies for which the Market Access Overall Trade Restrictiveness Index (MAOTRI)¹⁸ was computed.
- (e) Reluctance of buyers to visit Pakistan.

Notwithstanding these external shocks the decision-maker is less than convinced that trade openness has had a significant impact on export growth. The fact that compared to competition Pakistan has had a low Export/DP growth rate (Figure 5), and that the share of exports in GDP declined from 12.6 percent in 2001-02 to 11.8 percent in 2006-07, is often cited. Some also suspect that the

Fig. 5. Average Per Annum Growth in Exports/GDP, 1990–2004



Source: WTO, World Trade Data.

¹⁸MAOTRI measures the tariff equivalent of trade restrictions on a trading partner's exports. Among selected Asian economies (including China and India) Pakistan faced the highest tariff equivalent of 8 percent. Sri Lanka was second with 22 percent.

‘real’ export growth figure could be even lower because of the reported incidence of over...invoicing.¹⁹

Behavioural response to trade liberalisation of other key variables—GDP Growth, Inflation, Employment, Poverty, Income Distribution, Investments—using Pakistan-specific empirical evidence, has not been sufficiently researched to establish a clear co-relationship. There are few forward-looking or counterfactual simulations available to guide the policy maker. Where an attempt has been made, for instance the trade liberalisation—poverty reduction nexus, a positive relationship has been concluded,^{20,21} but even here it has been difficult to isolate the effect of trade liberalisation alone. The policy makers in Pakistan continue to perceive poverty reduction as a derivative of growth; and they are sceptical if trade liberalisation has been the major impulse in this regard.

There is, thus, a weak inherent commitment to trade reforms in the Government’s policy setting. In situations of trade-offs, whether revenue or current account deficit, it is not found unwilling to forego trade reforms, as the recent developments have demonstrated, even if there is little evidence to suggest that the surge in imports is a consequence of trade liberalisation, rather than supply-side constraints aggravated by demand growth.

The wavering attitude of the Pakistani policy-makers towards trade liberalisation perhaps ensues from a less than full appreciation of

- (a) Relevance of trade reforms to overall development objectives—growth, poverty alleviation, reduction of income and regional disparities, consumer interests etc. and not just to export growth.
- (b) The synergetic relationship between trade reform and the overall policy and institutional environment.
- (c) Trade policy no longer being limited to the traditional instruments of commercial policy—import regime, tariffs, customs administration. It now has to embrace ‘new issues’ as well (e.g. Services, Intellectual Property Rights, Behind-the-border regulatory agenda, Competition, Government procurement).

It also bears reiteration that the reforms induced by the outside actors are tolerated (as part of the balance of payments rescue effort) rather than owned (as critical to improved economic performance). There is thus a weak commitment to these reforms that are stalled or rolled back once the outside-led programme is completed or aborted.

¹⁹‘Mis-invoicing’ represents the difference between the figures reported by the exporting country and those reported by the importing country. It is understood that now there is growing incidence of both over-invoicing (to take advantage of subsidies) and under-invoicing (to save an importing country duties and sales tax) on the *same* transaction.

²⁰Siddiqui and Kamal (2006).

²¹Ahmad (2008).

VI. POLICY REDUX

There is sufficient evidence to suggest that the trade policy formulation in Pakistan has been inconsistent, not sufficiently focussed on complementarity with the other related policies, and unduly influenced by external actors.

Perhaps the single most important factor contributing to the trade policy formulation weaknesses is trade policy's place on the Government's overall policy agenda. Trade Policy does not seem to have a place of its own. It is often treated as a subset of the fiscal policy. It is viewed more as an export enhancement instrument than a tool for institutional reform and attainment of development objectives. There seems to be a greater awareness of the risks of trade liberalisation than its benefits. A freer trade regime is widely perceived as a threat rather than a way to reduce corruption and rent-seeking; there is a reluctance to bind tariffs even though they could generate greater predictability in incentives and solidify property rights. Lack of genuine stake-holder participation and a weak political interaction allows the fears, often misplaced, to persist.

For a trade policy to move up the Government agenda the emphasis will have to be placed on trade policy's role in creating the 'quality institutional environment' that Rodrik speaks of. The trade policy objectives should go beyond revenues and trade balance to address the fundamental question: will the contemplated trade reforms improve the quality of institutions? The academia and the researchers will need to do more Pakistan-specific work to guide the policy-makers in this regard.

The institutional arrangement for trade policy formulation is the second missing link, partly explaining the policy inconsistencies and questionable sequencing of trade reforms. While it is not intended to in any way to question the existing inter-ministerial division of responsibilities there is clearly the need for a sufficiently empowered focal point for trade policy. Theoretically, the Ministry of Commerce is expected to perform this function but its efficacy is reduced, not just for reasons of insufficient institutional capacity, but also because of its 'dependency syndrome' on agencies such as FBR and SBP—it is so often on the receiving end, in its pursuit of export incentives. Its ability to 'influence' the thinking of the agencies that have a bearing on trade policy matters is more personality driven than institutional. (As pointed out earlier, the Rules of Business do not show Trade Policy as one of MoC's responsibilities). The Federal Export Promotion Board (FEPB) is a powerful forum but it is seldom used for policy direction purposes. It also does not meet on a regular basis.

While there is not much that can or should be done about the plurality of trade policy actors, Ministry of Commerce needs to be categorically assigned the principal responsibility for trade policy formulation. Further, the FEPB, to meet each quarter, should be used exclusively for policy decisions and not facilitation

or incentivisation. The over-riding objective should be for the trade policy reform to be embedded in the institutional setting and complemented by other reforms.

The way the Ministry of Commerce is currently structured it is unlikely to perform this enhanced role. It lacks 'Capacity, most singularly in research and analysis that is needed for sound policy formulation, effectively interacting with other agencies, and avoiding what is demanded (by interest groups) at the cost of what is needed. This also diminishes its ability to 'influence' other agencies. Hiring consultants is not without its utility but cannot be a substitute for an in-house capacity.

MoC's attached departments concerned with trade matters can also do with a massive capacity upgrade. The National Tariff Commission has seen its role transformed to contingency protection ~P trade defence mechanisms. Besides being given greater resources to 40 this better it could also be entrusted to undertake a competent assessment of downside risks of trade reforms. The new appellation of the much restructured Export Promotion Bureau, the Trade Development Authority, does signal a shift from promotion to development—and from exports to trade, but it is yet to discard its earlier traditional functions besides finding it difficult to extricate itself from the seemingly perpetual whirlpool of transition. Properly equipped, TDAP, being the MoC's implementation arm, can be a most useful source of inputs for policy making. The Foreign Trade Institute of Pakistan (FTIP) has a lot to learn from its Indian counterpart and ought to become for MoC what PIDE was intended to be for the Ministry of Finance and the Planning Commission. It could also play a role in influencing the mindset of civil society and the business community and minimising backlash against reforms.

External influence need not necessarily be resisted. It is often benign and invariably well researched. By the same token it does not always have to be accepted. Generally speaking, external policy prescription has two weaknesses: it relies more on statistical analysis than an 'intuitive feel' of the ground realities; and, being unsure of the period of its welcome, it seeks a faster pace of reform than may be necessary. This challenges administrative capabilities as well as social peace, especially in the absence of viable social insurance institutions or safety net for the 'losers' in the reform process. Also, the imperative to improve export competitiveness, as one liberalises, gets less attention.

A proper sequencing of reforms is of critical import but with the limited time usually available to them the external actors cannot always ensure this. It is only a strong domestic institutional capacity that can check the less desirable aspects of outside intervention. An asymmetry of capacities tends to promote adversarial relationships at the cost of partnerships that such institutions are intended to foster.

VII. CONCLUSION

This study finds more than a coincidental link between the role of multilateral agencies and the evolution of Pakistan's trade policy. It is these agencies that have essentially guided the trade liberalisation process in Pakistan. Further, it is more than the dictates of globalisation that provided for such a pronounced role of external actors. It was in no small measure facilitated by the inherent weaknesses of Pakistan's own policy making apparatus. The vacuum was too compelling for these agencies to ignore.

Trade Policy, both institutionally and in terms of priorities, has not dominated Pakistan's policy agenda. Those who do believe in trade reforms come across a severe lack of commitment on the part of the decision makers.

It is questionable if the Ministry of Commerce, supposedly the lead agency, has the wherewithal, or, indeed, the responsibility for trade policy formulation. The 'annual trade policy' ritual may serve some facilitation and export promotional purposes but it will be difficult for it to lay claim to the kind of institutional and wider policy reform that a genuine trade policy ought to seek. MoC seems to have problems enough to get its ATP proposals, barely touching the cusp of policy, fully and properly implemented. It faces the challenges of inter-ministerial 'power game' as well as capacity.

Capacity is not solely a Ministry of Commerce issue. It is quite endemic all through the policy spectrum. The study highlights the asymmetry of capacity between the domestic and the external actors that tends to breed suspicion and an aura of forced interventions. This raises questions of ownership of reforms and their sustainability.

A definitive, evidence-based, linkage between trade liberalisation and public welfare-growth, poverty reduction, income equality—is not easy to incontrovertibly establish in the case of Pakistan that is exposed to several simultaneous variables. This weakens the resolve.

The prevalent 'street perception' is that trade liberalisation is inimical to national aspirations. It is viewed as a surrogate for globalisation, which in turn is perceived as the new variant of imperialism. In any political setting the slogan of self-sufficiency—and therefore import substitution and therefore protectionism—is almost certain to attract more votaries. No serious effort has been made to educate public opinion. It is often forgotten that trade policy is much more than trade liberalisation. If anything, a good trade policy can serve to check the costs of globalisation while capitalising on the opportunities.

All these factors contribute to trade policy being relegated to a low position in the Government's policy making pantheon.

The trade policy making and execution weaknesses are unlikely to be corrected without a realisation of their virtuous effect on the other policies and strategies, and how, together, they can impact public welfare. The cause of trade policy will be better served by restoring it to the general policy matrix rather

than letting it languish within the narrow confines of WTO compliance and export growth. Its importance is more likely to be accepted when it is seen as an agent of change, contributing to transparency, consistency and predictability of policies; as a powerful instrument of good governance.

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