PAKISTAN'S FOREIGN ECONOMIC RELATIONS[1]

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The 2021 National Security Policy has made Geo-economics as its main pivot. It is therefore, essential to look in a coherent and comprehensive manner as to how Pakistan's economic relations with other nations should evolve to meet this objective. In designing foreign economic policy we should always keep in mind that such a policy would be a by-product of the country's larger foreign and domestic economic policies. For example, if foreign policy with one particular country or group of countries is silent, ambivalent or agnostic then a foreign economic policy cannot be built upon strong economic cooperation with that country or group. Similarly, if the domestic economic policy is constrained by fiscal problems than giving aid to promote Pakistani goods in international markets would be an exercise in futility.

In the domain of foreign policy, ambiguity, diplomatic language, courtesies and sensitivities mask a lot and reveal very little. But foreign economic policy must be more direct, focused, target oriented if it has to meet its goals. Globalisation, technology, demographics and demand patterns are important drivers of any country's foreign economic policy. At the same time we are also at a severe risk because of the onslaught of climate change that has already hit us badly. We are also confronted with the change in geopolitical power balance. A fuller understanding or comprehension of these driving forces and risks is extremely critical for formulating, adjusting and fine tuning of our own policies.

What should be the goals for setting the future relationships?

The primary objective should be to maximize the opportunities offered by globalization and financial integration for the benefit of the majority of Pakistanis and to manage threats to the Pakistani economy. The country could double its per

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capita income and reduce poverty levels within the next 10-12 years if this goal is met. Disparate countries in East Asia such as Philippines, Indonesia, Malaysia, Thailand and Vietnam were able to demonstrate that international trade and foreign direct investment (FDI) can bring about a miraculous change in the living standards of hundreds of millions of impoverished people. Poverty levels in East Asia are now among the lowest in the world. The success of East Asia was combination of a smart government and a dynamic private sector working together.

China did even better than the newly industrialised countries (NICs) and East Asia, raising the real per capita incomes of 1.2 billion people four times during the last 25 years and brought down poverty from 50 percent to 10 percent.

Another country in which the number of inhabitants crosses the 1 billion mark, India, with often chaotic and messy democracy, has delivered an annual growth rate of 6 percent over last 15 years and reduced the poverty level down to 23 per cent despite the country's multifarious problems. This period was marked by opening up of India, liberalisation of trade and foreign investment.

This requires that we very carefully choose those instruments that benefit our economy and avoid those which create volatility and adversity. What instruments are available to achieve this objective? In my view, there are at least ten possible instruments which can be used in varying degrees and with varying intensities. These instruments are:

Trade:

a) Increase the world market share in exports of merchandise goods and promote regional trade
b) Initiate participation in the exports of services particularly ICT and Professional services
c) Act as the transit route for cross-border flows of goods, infrastructure and services
d) Take part in the global supply chain by providing components, parts etc

Investment:

e) Attract foreign direct investment particularly for exports and infrastructure
f) Encourage Pakistani companies to place equities abroad and acquire contracts and companies overseas
g) Set up joint venture companies with multinational companies

Technology:

h) Promote transfer of technology to Pakistani companies and facilitate Pakistani companies in acquiring international presence

Labour and manpower:

i) Train and Supply the type of workers required by deficient countries and maximize workers' remittances
j) Maximize the emigration of skilled manpower possessing higher technical & financial skills.

Using the above framework we would now suggest the nature of bilateral relationships with (a) the United States (b) China (c) Gulf States (d) South Asia (e) Afghanistan . Relations with the Central Asian Republics are very much contingent upon the happenings in Afghanistan and with Iran on the fate of the agreement with the Western powers.

United States

US has been a major provider of economic , military and humanitarian assistance. Since 2014 this aid has been substantially cut which is a welcome move both for the US as well as Pakistan as it had become highly contentious issue due to the widely differing perceptions held in the two countries.

US assistance has proved to be more effective and responsive to the natural disasters such as earthquake and floods and has won kudos from the affectees. The recent timely support for the 2022 floods is an example of this effectiveness.

The Biden Administration has rightly moved its focus away from Security, AfPak India-Pakistan to Trade, Investment and Technology Transfer. This is a highly desirable shift provided this strategy is executed with full force because past attempts have not been successful. The US Chamber of Commerce has been rightly calling for easing access for the country's textiles to American markets. American tariffs on Pakistan's leading exports average approximately 10 percent, about four times the average US tariff rates on imports from other countries. A reduction in tariff rates would not confer any favour on Pakistani exporters but provide them with a level playing field. For a country that so strongly believes in marketplace competition, this is a correction not a concession.

Pakistan needs foreign direct investment in energy transmission and distribution, gas pipelines, oil and LNG terminals, refining capacity, petrochemical complex among others. US investors should be encouraged through Export-Import Bank loans and Overseas Private Investment Corporation guarantees to participate in Pakistan's energy development plans

There is one of these area which no other country is better in performing. The 21st century is going to be marked by a dramatic shift from an industrial economy to one that is knowledge-based.. How far this can practically be achieved in the next decade will depend upon the foundations on which this economy is erected, ie the quantity and quality of scientific and technological manpower. We lag behind other peer countries and have a lot of catching up to do. The United States leads the world in higher education and scientific and technological research. We should approach them to resume their assistance in training our teachers and scientists in the leading US institutions, forging links and exchanges of scholars between Pakistani and American universities and strengthening the capacity of our research organisations in agriculture, water resources, renewable energy and low-cost building materials.

Among the world's top 40 universities, two-thirds are in the US. Technology companies founded less than two decades ago feature among the top 10

companies of the world. Of Nobel Prize winners, 356 out of 870 have been Americans (the highest of any nation) — but 70pc of all Nobel Prize winners work in the US. Forty per cent of the world's total spending on science and research is accounted for by the US. All cutting edge research and application development in the areas of artificial intelligence, robotics, lasers, sensors, avionics, biotechnology and genetics is being carried out in this country. MIT and Stanford alumni companies generate annual revenues of $4.9 trillion and have created 8.4m jobs since 1930. The National Science Foundation reported that in 2010, 45pc of US engineering students in MSc and PhD programmes were from overseas.
Asian countries are taking full advantage of training their scientific manpower, but it is highly disturbing to observe the declining proportion of Pakistani students enrolled in US universities.

In 1989-90, Pakistani students in the US numbered 7,070 compared to those from India at 26,240 — one Pakistani for every four Indians. By 1999-2000, the disparity
increased to a ratio of 1:7 — but an even greater precipitous fall has taken place since then. In 2014-15, Indian students had reached 132,888 while Pakistani students were only 5,354 — yielding a ratio of 1:25. A cursory glance at the Fulbright Scholar Programme for Pakistan —the largest US programme in the world — shows that the majority do not go for STEM subjects or attend top universities, and very few go for PhD degrees.

<u>CHINA</u>

There are several areas where the ongoing cooperation between Pakistan and China should be continued but at least three areas need emphasis. These are:

(a) Completion of ongoing projects under CPEC i.e. addition of capacity to the national power grid by bringing the hydropower, renewable energy and coal projects to culmination. ML1 Railway track has been pending for approval for several years and each year of delay adds to the logistical costs to the economy and fiscal deficit by absorbing the losses of Pakistan Railways operating an outdated system. Gwadar Port has to made operational and connected with China by filling in the missing links in KKH, Western Corridor etc.

(b) Despite the revised Free trade agreement with China, the volume of Pakistani exports has not made any significant penetration in the Chinese markets. An actionable plan developed in conjunction with the private sector to be monitored by the Cabinet regularly should aim to achieve at least 1 percent of the Chinese imports by 2030. This would require , investment in expanding production of goods and services in which Pakistan has comparative advantage, performance linked incentives, Liberal tax and regulatory regime . Pakistani professionals and managers should be attached with the Chinese companies for some time to better understand their market conditions , standards and requirements.

(c) Intensive efforts should be made at the highest level to attract Chinese companies to relocate their ventures that are becoming uncompetitive due to rising labor costs in Special Economic Zones. This exercise should begin by examining the factors that have impeded the efforts in the past. These zones should be provided all the facilities, amenities and utilities and be made completely free from all bureaucratic hassles and administrative hurdles. The prospective benefits of this relocation would be training and development of skilled manpower , improved managerial practices which would transmit best practices and raise the productivity of our industries. Similarly, the Chinese experience and expertise in Agriculture crops, Livestock and Fisheries in developing and diffusing new varieties that are resilient to climate change and conserve the use of water resources should be tapped to minimize the vulnerabilities and extreme weather shocks we are likely to face. Research-Training-Extension would have to be integrated in a continuous value chain to achieve this.

Afghanistan

The bilateral cooperative arrangements between the wo countries are critically dependent upon the establishment of cordial and trusted political relations and the acceptance of the Taliban regime by the rest of the world. Assuming that this happens, and it is big if, the economic relations between the two countries are mutually beneficial to both . Pakistan is one of the largest trading partners of Afghanistan and its exports of goods and services had touched $3 billion annually a few years ago and is also the main conduit of imports from elsewhere through the Karachi port. More recently, Afghan coal has substituted the supplies from South Africa and others .

To promote further trade, tariff rates should be reduced on essential commodities, non-tariff barriers lowered and trade facilitation eased to remove the obstacles faced by Afghan businesses and lower the cost of transactions. Concessionary export refinancing facilities should be made available to Pakistani exporters for incremental flows of goods to Afghanistan beyond the present threshold. Pakistan provides Afghanistan with the shortest access to the sea but rail and road freight services have not been fully developed to leverage this locational advantage. Liberalisation of the transportation sector by allowing the entry of newcomers and promoting competition among the carriers, expanding the existing highways and rehauling the railway subsector would go a long way in facilitating both bilateral and transit trade. Exports of the mining sector from Afghanistan would require that the transport corridors be functioning for evacuation to the ports. Connecting Kandhar with Gwadar through the Western Corridor can be a possible route that needs to be explored. Afghanistan can also earn substantial revenues from transit trade and energy to and from the Central Asian Republics.

Government of Pakistan should revive the proposal for the establishment of industrial zones for Pakistani investment. As Afghanistan enjoys an LDC status Pakistani private investors can set up export-oriented industries in these zones in joint ventures with Afghan partners attracting preferential lower tariffs in the advanced countries. These zones would bring foreign exchange earnings badly needed by Afghanistan substituting the volume of foreign aid that has since 2021 evaporated. Pakistani investors, to be successful, would require better infrastructure in the form of highways, railways, integrated border crossings etc. Several other border posts should be opened and the missing infrastructure put in place. A tripartite agreement between China, Afghanistan and Pakistan under CPEC should assign the responsibilities for execution of this plan. China can take the lead in building the necessary infrastructure; Pakistani private investors can set up the industries and bring skilled manpower and Afghanistan can set up a one-stop shop to facilitate investment flows and resolution of problems and create jobs for the youth and supply chains.

In addition to industrial zones, Afghanistan offers investment opportunities in construction, food processing and retail. Pakistani investors should take first-mover advantage as their transportation costs would be low and they understand the consumer tastes and preferences better.. The EXIM Bank that has recently been approved by the Parliament will be the ideal vehicle for scrutinizing investment proposals and furnish a range of funding and non-funding instruments (eg guarantees) to those whose proposals are found to be feasible.

In the area of trade in services, Pakistan has earned a good reputation in banking and insurance, telecommunications, IT enabled services, engineering consultancy, architecture and accountancy. Afghanistan would need expertise in these areas both for current operations and ‘on the job’ training of their own young professionals. Well-reputed hospitals, medical laboratories, clinics, nursing training institutes, general and specialised universities and colleges, vocational and technical training institutes from Pakistan can enter into partnerships and agreements with their Afghan counterparts. After all, the youth bulge has to be gainfully employed for which quality education is a pre-requisite. The affordability to this kind of education would be a major consideration for which the Pakistani experience would come in handy. In the coming years, Pakistan should negotiate free trade and bilateral investment agreements with Afghanistan. The trade agreement can have sensitive lists that protect vulnerable items and these lists can be gradually phased out over a given period. In the medium term, the two countries should form a common customs union with the external tariffs at ports of entry and thereafter the goods can move freely between the two countries. This will mitigate the curse of illegal imports into Pakistan through the diversion of the present Afghan transit trade, generate tax revenues to be shared by the two and reduce the transaction cost of doing business.

GULF STATES

Pakistan has enjoyed very friendly relations with the Gulf states. The first generation of the rulers of the Emirates were very favourably disposed towards Pakistan as they received a lot of cooperation in the journey towards the modernisation of the country. Saudi Arabia and UAE have absorbed a large number of workers in their labour force and are the two top sources of remittances. UAE is one of the major trading partners and Saudi Arabia and Kuwait suppliers of petroleum products and crude oil while Qatar has long term contracts for LNG. These countries have been coming to Pakistan's rescue whenever it has been struck with balance of payments crises. However, the future relationship , to be dependable and sustained , has to be recalibrated so it is not perceived as a one way street. Both UAE and Qatar in their recent dialogue with the Pakistani authorities have expressed the desire to invest or acquire projects in Pakistan rather than providing cash , commodities or place deposits . These states have plans to invest 22 billion dollars in Egypt which has also been a traditional recipient of Gulf states' aid flows. The same seems to be the new strategy for Pakistan too. This , in my view, is a preferable option that it would create assets and expand the productive capacity of the country. Saudi Arabia had announced in 2019 that they would set up an oil refinery

and petrochemical complex in Gwadar but even after three years the progress on this project is not visible. Bureaucratic red tape , convoluted and time consuming procedures and coordination failures among the federal and provincial governments have been the main stumbling blocks in the way of Foreign Direct Investment. The mindset of politicians and civil servants has to change dramatically from finding faults with the proposals from foreign or domestic investors to that of a facilitator and enabler.
The Economist Magazine has reported that the gulf states would earn $3.5 trillion in the next five years in response to the reengineering of global energy flows arising from the Western sanctions , climate change and remaking of geopolitical alliances in the Middle East. Saudi Arabia and UAE aim to raise output from 13 million barrels per year to 16 million. Qatar is planning to expand its North Field project at a cost of $ 30 billion in the next five years and would raise LNG output annually from 77 million tons to 126 million tons further increasing its present share of 33 percent in LNG traded worldwide . A new look Gulf that is destined to remain pivotal for decades to come should trigger a response capacity from Pakistan in strengthening its economic ties in form of trade flows, attracting investment from Sovereign Wealth Funds and reserves (at present $ 3 trillion) in long gestation infrastructure projects and exports , ensuring energy security , participate in the development projects of these states and continuing to supply skilled and semi skilled workers to augment their domestic labour force. The competition from Egypt, India, Bangladesh, Iran and other countries in the neighborhood is going to be tough and Pakistan has to work hard to win its place.

SOUTH ASIA

Economic historians and analysts have been faced with a conundrum for quite some time as they find it hard to comprehend that South Asia, which was a single large market until a few decades ago with goods, services, capital investment and skilled labor flowing freely and the newly independent countries inheriting a common historical, legal, cultural and administrative background and a very well linked infrastructure was the least integrated region in the world while East Asia with countries having such diverse background and very little in common historically had become the most integrated region second after the European Union. Moreover, there was almost a consensus among academic economists in both the countries that the normalization of trade relations would bring substantial economic benefits evenly. Among many reasons responsible for this puzzle, the political tension and rivalry between the two major countries of the region – India and Pakistan - stands out as the main explanatory variable. There is very little doubt in the minds of Pakistanis that India has emerged as a leading economic power during the last decade and Pakistan, which was ahead until 1990, has slipped behind for the reasons well known and amply documented. This change in the economic equilibrium calls for a fundamental review of Indo-Pakistan relations. The dark clouds of mutual mistrust, suspicion, blaming each other cannot evaporate overnight. It will take time and perceptible actions on the part of both the countries. However, there is a huge asymmetry in the power relationships where India with 80 percent of the population and 85 percent of GDP dominates the region and thus holds disproportionately heavy responsibility to lead the way out of the present stalemate.

India, in its quest to continue its journey towards economic ascendancy needs safe and secure borders, peaceful and prosperous neighbors and a dynamic regional institutional framework in which the smaller countries can have a voice. Its aspirations will be thwarted by constant distractions caused by insecure, discordant and fearful neighbours. As the predominant player in South Asia its responsibilities, responses and behaviour must be commensurate with its size and status. Past tradition of strict reciprocity, tit-for-tat or equal measured response have to give way to a more asymmetric behavioral pattern in which it shows magnanimity, large heartedness and broad mindedness by being more accommodative of the economic and political imperatives of other countries in the region . Despite this, the cost benefit calculus will favour India in the medium to long term and this is the only sure way to achieve its economic goals.

For a country that has some of the most progressive entrepreneurs, leading intellectuals, professionals, innovators and scientists, globally competitive human resources at the top end, high in demand natural resources it is not comprehensible as to why it can not take the initiative to normalize trading relations with Pakistan and unshackle the huge potential that the regional trade offers for growth, poverty reduction and food security .

Pakistan and India have been observing the Indus Water Treaty for over 60 years despite the wars and skirmishes. It is a high time that they should together examine the impact of glacial melting of HKH range which both of them would be affected adversely. They should develop joint strategies to minimize the adverse damage to our agricultural crops, water availability and energy security. This is a regional public good that transcends boundaries of the two countries and is above the narrow considerations of bilateral relationships however tense they may be. It is in fact an existential threat for survival and sustenance .

To sum up, resetting Pakistan's foreign economic relations to shift towards Geo economics rather than Geopolitics would require Pakistan's domestic economic policies, management and governance to be put on a sound footing. Macroeconomic stabilization and resumption to sustained growth are the prerequisites for this agenda to be executed.Continued political instability, uncertainty about policies and frequent economic crises would not bring in any change from the present status quo in which we would remain a marginal player losing our dignity by constantly asking for bail outs. The major problem we face is not lack of diagnostics or prescriptions to solve those problems but an inward looking narrow mindset where processes are given precedence over outcomes and results. Unless we remove the in built disdain for anything foreign including the Overseas Pakistanis we would become more insular and disconnected from the tide of progress that is benefitting other emerging and developing countries. We should have South Korea, China , Indonesia , Malaysia and Vietnam as role models to follow rather than drift towards the closed economies of the world.