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Indo-Pak Trade
A Visit to Historical Relations

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India Pakistan trade relations have traversed through numerous oscillations and phases over the last six decade period. While during the early years of independence, India's share in Pakistan's exports was about 24 percent and its share in imports over 50 percent; in recent years, it has declined significantly to a very low level. In between, trade relations (trade volume) were minimal as a result of strained political relations. In the recent past, especially since 2011, trade relations between the two countries appear to be taking a positive turn.

This Briefing Paper aims to analyse in phases the historical trade relations, gather highlights of so far constrained India Pakistan trade relations, and suggests measures to increase trade volumes between two countries to a reasonable level.

Overview

Indo-Pak economic ties have for long been held hostage to political acrimony between the two countries. In the recent past, however, both countries have made some headway in this realm and there seems to be an unequivocal commitment to greater economic engagement. This is visible from the recent economic and political engagements and Pakistan's path breaking decision to grant India Most-Favoured Nation (MFN) status – despite some opposition from certain sections in the country – and the inauguration of an Integrated Check Post (ICP) at the Attari in April, 2012. Two more developments are on the anvil – the opening of more trade routes, and the removal of tariff and non-tariff barriers (NTBs) – something Pakistan has been demanding for long.

What is especially significant apart from the above developments is the fact that the Pakistan leadership seems to be keen on emulating the 'China Model' which implies the de-hyphenation of politics and economics.[1] This paper aims to analyse in phases the historical trade relations between the two countries, capture some important events which have marked the constrained India Pakistan trade relationship, and finally make recommendations for increasing trade volumes between the two countries.

Indo-Pak trade: The important phases

First Phase (1947-1965): During the beginning of this period, the two countries and their economies were reasonably integrated buoyed by an India and Pakistan standstill agreement under which goods from one country to another were exempted from customs duty. In addition, there were few visa restrictions. The closeness of ties is reflected by the fact that, in the immediate aftermath of independence, the volume of trade was quite high. The high volume of trade is mirrored in a high shares in total import and export of the two countries (Table 1).

This can be attributed to a reasonable level of people to people contact (than what was observed during the latter periods), a shared history, cultural similarities, close proximity, relatively open and accessible land routes to cross either side of the border and relatively low accessibility to foreign markets.

Existence of a number of land routes was perhaps the most important factor that facilitated easy movement of people and goods across the border that translated into high trade volumes. It is observed that at least four land routes in India and five in Pakistan

Table 1: India's share in Pakistan's global Exports and Imports (in %)

Year	*Share in Exports*	*Share in Imports*
1948-1949	23.60	50.60
1975-1976	1.30	0.06

Source: D.G.C.I. & S., Kolkata; and Federal Bureau of Statistics, Islamabad

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were operational for movement of goods across borders till 1965 (Table 2).

Land routes appear to have direct impact on volume of trade. Data show that in the year 1948-49, India's share in Pakistan's exports was over 23 percent while share in imports was nearly 51 percent. More importantly, out of the total trade between the two countries, according to estimates, 70 percent of India's imports from Pakistan and 40 percent of India's exports to Pakistan during this period were by land trade rather than seaborne.[2]

Table 2: Important Trade Routes *(before 1965)*

India	Indian States	Pakistan	Pakistan States	Train Services
Munabao	Rajasthan	Khokhrapar	Sindh	Train service started in 2005, but the route is yet to re-open for trade
Attari	Punjab	Wagah	Punjab	Re-opened
Hussainiwala/ Ferozepur	Punjab	Ganda Sindhwan/ Kasur	Punjab	Closed since 1965

Source: http://irfca.org/docs/international-links.html

Gradual closing of land routes resulted in drastic decline in trade volumes. Trade between the two countries started declining drastically resulting from two reasons: deteriorating political relations; and the second one which is relatively lesser known, Pakistan's refusal to devalue its currency, something which India did.[3]

Further, two noteworthy facts are observed during the first phase: firstly, the balance of trade during 1951-1963 was skewed in favour of Pakistan; secondly, in early 1957, an India-Pakistan trade agreement which was the equivalent of granting MFN status, was signed between both countries. The agreement clearly stated that "treatment no less favourable than that accorded to the commerce of any third country". The agreement initially valid for three years was extended for another three years by the then President Ayub Khan, a military dictator. The agreement, however, lapsed in 1963.[4]

Second Phase (1966-2004): As a consequence of the 1965 armed conflict, trade between the two countries was disrupted for a decade.[5] Between 1965 and 1975, there was no trade agreement between the two countries. As a result of this, by 1975-76 the share in exports dipped to 1.30 percent while share in imports declined to a dismal low of 0.06 percent. In addition, the most important trade (land) route turned out to be the least preferable in the later years, as a very high percentage of trade got routed through the sea route between Mumbai and Karachi.

The year 1975 witnessed a major development in India Pakistan trade relations: trade resumed after a hiatus of a decade, following signing of a trade agreement between the two countries. The resumption of trade was important in view of inconsequential 1974 protocol for the restoration of commercial relations on an inter-government basis, signed by the two countries.

Both countries traded in a limited number of items, put up by each country and referred to as the positive list. The trade agreement signed in 1975, however, expired in January, 1978. The political relationship during this period was extremely vicissitudinal. Interestingly, bilateral trade that resumed in 1975-76, was carried on for more than two decades without any agreement. In July 1982, Pakistan declared a list of 40 items in which private sectors of the two countries could trade.[6]

Despite the unfavourable situation and short-sighted measures taken by both the countries, trade followed its own path of progress during the later years. It is observed that the periods from 1990-01 to 2001-02 encountered numerous short-term oscillations. In the twelve year period, there are four instances, when trade declined after experiencing an increase in the preceding year (Table 3).

The decline in trade volumes might have resulted from numerous factors, including but not limited to political issues. However, if one considers a longer period, trade is observed to have increased during this period from US$88mn in 1990-91 to US$209mn in 2001-02, realising a compound annual growth rate of over 7 percent.

Table 3: India's Trade with Pakistan from 1990 to 2002 *(in US$mn)*

Year	*Exports to Pakistan*	*Imports from Pakistan*	*Balance of Trade*	*Total Trade*
1990-1991	41	47	- 6	**88**
1991-1992	40	87	-46	**127**
1993-1994	64	44	20	**108**
1994-1995	57	53	4	**110**
1995-1996	77	45	32	**122**
1996-1997	157	36	121	**193**
1997-1998	143	44	99	**187**
1998-1999	106	214	- 108	**321**
2000-2001	187	64	123	**251**
2001-2002	**144**	**65**	**79**	**209**

Source: Gill and others

The period is also characterised by another major development, especially in terms of trade facilitatory measures. In 1996, the hopes for more meaningful trade relations between both countries were rekindled when India granted MFN to Pakistan. This gesture was unrequited, even though significant sections of the Pakistani business community were not averse to reciprocating the same. In fact in 1996 itself, a report by the Karachi Chamber of Commerce and Industry (KCCI) advocated granting India the MFN status, particularly after Pakistan had liberalised its regime and signed up to WTO in 1995. The fear was, besides the political issue, mainly on the ground of Pakistani market being flooded with Indian products, leading to increased competition for local products.

It needs to be stated here however, that in spite of all the differences between the two countries during this period, both sides, especially the business community, continued to explore vistas for increasing trade. Irrespective of domestic pressures, governments in both countries have pitched for more harmonious ties.

Third Phase (2004-2011): This phase may be terms as a phase of renewed efforts to promote trade. The signing of the South Asian Free Trade Agreement (SAFTA) in 2004 at the 12th SAARC Summit in Islamabad served as a booster to India Pakistan trade relations. All the developing countries in the SAARC countries, namely Sri Lanka, Pakistan and India agreed to reduce their tariffs to 0-5 percent by 2013 to promote intra-regional trade. For India and Pakistan, this summit coincided with the resumption of dialogue between both countries.

The period following the 2004 SAARC Summit witnessed an improvement in bilateral trade relations between the two countries. Data show significant increase in trade volumes (Table 4). In addition, the phase also witnessed granting of permission by the Pakistani government to foreign direct investment (FDI) from India in the manufacturing of CNG buses. Continuous engagement between the political leadership of both countries and a steadfast commitment to finding solutions to vexed issues appear to have sent right signals to the business community in both countries.

Table 4: Indo-Pak bilateral trade
(2003-04 to 2008-09, in US$mn)

Year	*Exports to Pakistan*	*Imports from Pakistan*	*Total Trade*
2003-04	283	96	379
2004-05	505	158	664
2005-06	689	180	869
2006-07	1349	323	1672
2007-08	1944	288	2232
2008-09	1440	370	1810

Source: D.G.C.I. & S., Kolkata and Ministry of Commerce, Government of India

Fourth Phase (2011 and beyond): This phase is referred by many as the phase of consolidation of improving economic relationships. If one were to return to the larger context, it is the most productive phase for bilateral trade not only in numerical terms, but in terms of policy decisions. Just as January 2004 gave a fillip to better relations between both countries, it was the revival of economic engagement between the two countries in April 2011 when the two Commerce Secretaries met at Islamabad, and identified areas where they could proceed which paved the way for progress which has been made so far.

It is observed that a number of positive developments have occurred during this short phase. A chronology of positive development is given in Box 2.

The phase has witnessed setting up of clearer and

Box 1: Chronology of Developments (2011 and 2012)

Date	**Important Developments**
April 28, 2011	Commerce secretaries of India and Pakistan issue a joint statement with the objective of boosting trade
September 26, 2011	Pakistan Commerce Minister assures progress on MFN status to India, seeks removal of NTBs
November 02, 2011	Pakistan Cabinet approves MFN status to India, but later retracts and gives in-principle approval for 'trade normalisation' with India
November 13, 2011	Pakistan Commerce Secretary visits India, assures a shorter negative list and removal of positive list
February 29, 2012	Pakistan announces transition from positive list to negative list and says the negative list would be removed by December
March 20, 2012	Pakistan notifies negative list with India, banning 1,209 items and opening more than 7,500 tariff lines
April 13, 2012	ICP inaugurated at Attari

concretised targets by both the countries. While the Pakistani side assured the Indian side that concrete steps would be taken towards giving India MFN status by taking the following steps: (1) In the first stage, Pakistan will move from the current positive list approach to a negative list. Thereafter, all items other than those on the negative list can be freely exported from India to Pakistan; and (2) in the second stage, the negative list will be phased out. It is expected that complete phasing out will be completed before the end of 2012.

In sum, Pakistan's consent to grant MFN status to India is definitely an important decision taken by the Pakistani government and would pave the way for enhanced cooperation in trade and other areas between the two countries. Reports indicate that Pakistan has now a negative list of 1,209 items which it cannot import from India. As a result, India can now export more than 7,500 tariff lines to Pakistan.

The initiative to grant MFN status to India was followed by another major development – inauguration of the Integrated Check Post (ICP) at Attari in April. As a result of this more trucks can now plough between Attari-Wagah and also the trading hours have increased with the setting up of the ICP.

India on its part has shown willingness to address the legitimate grievances of Pakistani businessmen with reference to both tariff and NTBs. It is argued that the issue of tariff in two specific sectors, the agricultural and textile sector has been hampering trade between the two countries. In the case of the agriculture sector, the applied tariff rates for agriculture exports at approximately 40 percent, one of the highest in the world. This is a major barrier that Pakistani exporters of agricultural products face in terms of expanding trade with India. In a number of sectors, specific tariffs and regulatory duties outside statutory MFN tariff rates are levied. Potential textile exports from Pakistan are subject to specific duties which can go as high as 50-100 percent in equivalent terms.

Apart from high tariffs, there are specific barriers for commodities such as leather and cement. These barriers are argued to be tedious apart from logistical problems such as stringent visa regimes and no direct banking arrangement between both countries.

Future Outlook and the Way Forward

Indo-Pak trade has immense potential. Opening up of the integrated check post at Attari-Wagah border and Pakistan's granting the MFN status to India can increase the bilateral trade to US$8bn a year in the next two years from the current level of US$2.6bn, according to a study released by industry chamber ASSOCHAM. In addition to direct gains in trade volumes, consumers in both the countries are likely to gain significantly from increased trade.

A study conducted by CUTS[7] has estimated the net gain to consumers, arising from increased intra-regional trade in South Asia, at about US$2bn. Pakistan and India will be the two most important beneficiaries in such a situation.

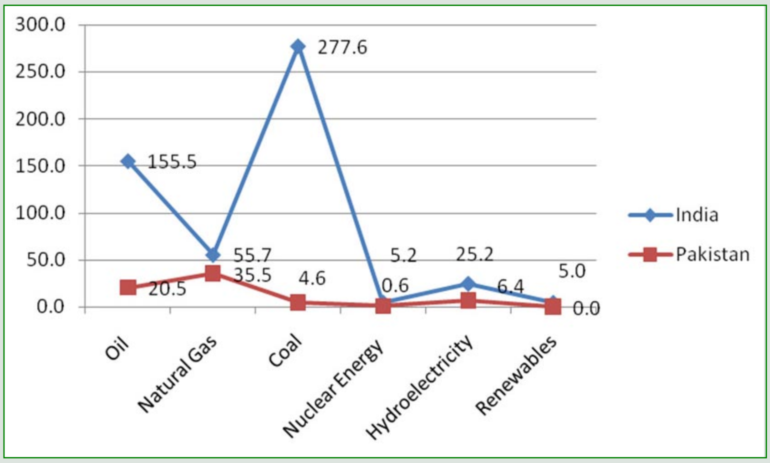
Some issues need to be addressed immediately to ensure that both countries can build on the new cooperative momentum and initiatives:

- Opening more trade routes such as Hussainiwala-Ganda Singh is imperative as these would save immense time and transactions costs for businessmen on both sides. This route was an important trade route in the pre-1971 period. Nearly 100 trucks carrying dry fruit and other fruits from Afghanistan and Pakistan used to pass through the Hussainiwala check post before 1971. This route was used by the Indian traders to export rice-shelling equipment and farm machinery to Pakistan and beyond. With the inauguration of the Bathinda oil refinery, this could be an important route for importing petroleum products to Pakistan, as Hussainiwala is closer to Bathinda.
- There is immediate need for improving infrastructure on both sides to facilitate greater trade through the Wagah-Attari land route. Currently only 137 items have been allowed for trade through this route as a consequence of the inadequate infrastructure on the Pakistani side.
- For making the ICP at Attari more effective and useful it is imperative to integrate the railway line at Attari into the former. For achieving this it would be necessary to have a small extension of the 120-acre ICP onto the rail track. Unless the extension to cover the railway line is carried out, rail cargo, including perishables such as gypsum and cement, shall continue to remain stored in the open and lie for months due to the paucity of warehousing space. It is observed that even in the aftermath of the inauguration this problem persists.
- India needs to address Pakistan's concerns with regard to tariff and NTBs, especially in the textile and agriculture sectors. Until these are dealt with a large section of Pakistani businesses will be apprehensive about opening up their markets to India.
- With regard to FDI in India, and liberalising of the visa regime, there are a lot of apprehensions within the security establishment. For building on the foundations which have been built so far it is imperative that these apprehensions are amicably addressed.

Box 2: Increased cooperation can help both countries to achieve energy security

Both India and Pakistan are energy insecure and, therefore, growth of both can be challenged in the coming periods. Energy tie-ups between India and Pakistan have been completely lagging. The recently signed Turkmenistan-Afghanistan-Pakistan-India (TAPI) gas pipeline deal undoubtedly provides a huge opportunity. It is expected that the natural gas markets of both India and Pakistan will benefit from this. This is because, natural gas markets in India are still in evolutionary phase and there is also a fall in natural gas production of India's largest private sector enterprise, Reliance Industries Limited's Krishna Godavari basin (KG-D6 basin), which has been a cause of concerns for natural gas industries in India.

Figure 1: Trend in Primary Energy Consumption in India and Pakistan (mtoe)



Source: BP Statistical Review of World Energy 2011

Inauguration of the Bathinda Oil Refinery in April 2012 presents another opportunity for the two countries. The unit, which can process 9 million metric tonnes a year of crude oil will help boost India's exports and may open fuel sales to Pakistan. It may be recalled that Pakistan has allowed imports of fuels including gasoline and diesel from India after removing NTBs late 2011.

The possibility that India rejoining the Iran-Pakistan-India gas pipeline is the third opportunity towards energy security of the two countries. What is needed is a combination of strong political will on both sides and meticulous implementation of these projects will be critical for long term energy security of the two countries.

Considering that most of the primary sources of energy presently produced and used by the two countries are exhaustible in nature. Accessibility of these energy sources need to be guaranteed for a sustained economic growth. The cooperation in energy, therefore, will not only help to ensure energy security for the two countries, but will also help in saving costs of production. Various such sectoral examples can be cited, in which both countries will gain immensely by cooperating with each other.

Endnotes

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