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TARIFF LIBERALISATION IS THE KEY TO BOOSTING EXPORTS' AN INTERVIEW WITH DR MANZOOR AHMAD

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Dr Manzoor Ahmad has previously served as Pakistan's Ambassador to the World Trade Organisation, Geneva (2002-08). He started out his career in Pakistan Customs as an Assistant Collector (1977) and later became Member Customs, FBR (2000-2002). Dr Manzoor Ahmad has also served as Director, FAO Liaison Office, Geneva (2008-10) and as Regional Trade Advisor for Deloitte Consulting, Islamabad (2013-14). Dr Manzoor is currently working as the CEO of World Trade Advisors, as a senior fellow at the International Centre for Trade and Sustainable Development, Geneva and Chairman, Pakistan LNG Ltd. Currently; he is also serving in several honorary positions at think tanks, such as Institute for Policy Reforms (IPR), Lahore; and Evian Group at IMD Lausanne.

BR Research sat down with the distinguished trade professional to find out his views on boosting Pakistan's export competitiveness. Selected excerpts are produced below:

BR Research: Exports have picked up this fiscal. But for the decade ending FY17, Pakistan's GDP nearly doubled but exports remained at almost the same level. Why do you think is it that exports now matter less and less to GDP growth?

Dr Manzoor Ahmad: I think it is a very worrying sign that exports are almost at the same level as they were a decade ago. But Pakistan has been doing poorly on the exports front for the last forty years. Back in the late 60s, Pakistan's exports were more than the combined exports of East Asian countries. From there on, it has been downhill. There were small periods when exports shot up - one such period was from 2002 to 2007. Apart from such exceptions, we have been losing market share for the last forty years. We lost all of the nineties; and the last ten years were also lost.

There are many factors, such as law and order, and the energy crisis, that have hit

exports. But one major factor has been our lack of reforms. Our competitors moved fast and we stayed where we are. That has hurt our competitiveness. Trading patterns have changed in the last two decades. Previously, countries used to deploy import substitution policies, make things all on their own and then export them. Now it is about the global value chains (GVCs). Countries, based on their competitiveness, tend to export components that are part of the GVCs. These GVCs account for 70 percent of world's exports, but unfortunately Pakistan has no share in that.

BRR: Why is Pakistan not able to become a part of the GVCs?

MA: Energy availability used to be an issue hurting exporters, but not anymore. The culprit is our policies. One of them is the lack of effective import tariff liberalisation, which is the key to boosting exports. We depend too much on import taxes, which are about 40 to 45 percent of FBR's taxes. Compare Pakistan with any other country and we are collecting three to four times more on import-related taxes. Our Customs duty rates are at least three times the Asean countries and at least twice the global average. Moreover, we tax on top of tax through additional custom duties, sales tax, withholding tax, etc. The politicians feel it easier to collect taxes indirectly, as our tax machinery is completely broke.

As countries become more and more involved in trade, they realize they are becoming competitive through opening up. Look at the examples of China, Korea and other Asian economies, including India. We also did some opening up in the nineties, but that was mostly driven by donor agencies. The country is still living in the past, thinking that we should be making everything ourselves, with policies like import substitution. Such thinking is behind Pakistan not being able to be a part of GVCs.

The protection to different sectors has also played a role in them not being able to break out internationally. Look at the auto sector, which still hasn't gained a critical level of production and has not been able to export a single car. Till today, we insist on localisation and promote deletion programmes so we can promote domestic parts. What happens in the process is that if you have a good car and if you don't have good tires or other parts, you bring down the quality of that whole car. And then to insist that a new company that comes in has to have 30 to 50 percent local parts acts as a barrier. Last year, the government opened up a little bit. But the

import substitution is largely still in place.

The other thing is the geo-strategic location. You hardly find a country at the junction of so many regions: Central Asia, South Asia and the Middle East. But we have made minimum use of it. Our regional trade is less than five percent. Other countries have taken their regional trade to at least forty percent. Maybe it's politics, but if it is politics, then it needs to be kept aside. China, despite its differences with India and Taiwan, is trading with them more and more. We have politics in front and then we determine the trade.

BRR: What do you say to the argument that lowering import tariffs would further undermine domestic manufacturers? The Pak-China FTA is often cited as Exhibit A.

MA: I feel that the Pak-China FTA was unfortunate and we should not have rushed into it. Pakistan should have noticed that China, over the years, had brought down their tariffs significantly under their WTO commitments. So any advantage that Pakistan could have had at the time the FTA was signed would not exist, but China would have had a lot of advantage as our tariffs were high. So that's why a lot of our trade was diverted towards China. What we should have done was reform the tariff structure for other countries as well, so that the Chinese imports would have competition in Pakistan.

It's a logical thing that when you lower your tariffs, imports will increase. But so will your exports. There is a relationship between tariff liberalisation and exports. Without tariff protection, local producers have an incentive to become more competitive. Before Turkey signed the customs union agreement with the EU, its industrial import tariff was much higher compared to the EU. It gradually lowered its tariffs in line with the EU, became competitive, and then entered the customs union.

BRR: The policy of using import tariffs as a tax-maximization-tool instead of a trade-policy-tool still exists. Why do you think that reverse of tariff liberalisation is occurring in Pakistan while the world is moving on?

MA: We are going against the international trend. Tariffs, in fact, no longer command the same level of time in trade negotiations like they used to a decade

ago. This is, of course, before the current US President started threatening a trade war. But generally, the conversation has moved, and tariff talks are restricted to only a few items now. The important thing now is "standards", especially in areas of agriculture and component exports. Pakistan has a clear need to reform in this area, too.

BRR: Indeed. GVCs are more than tariffs, and include elements like efficiency in logistics, freight/insurance, IPR, customs clearance, etc. How do you see Pakistan faring on those non-tariff trade areas?

MA: We have already discussed tariffs. The other thing is our procedures. For a GVC to work here, things have to come into Pakistan on time, get processed per schedule, and then leave the port on time. But we are amongst the worst on that count in the Doing Business ranking. For trading across the borders, we are ranked at 171 out of 190 countries; our cost to import a container (not including taxes) is $990 whereas for high-income countries it is $111 and for other South Asian countries, it is $638.

These indirect costs like procedural delays and inefficiencies add something like 13-15 percent to the imported cost. There are multiple agencies looking at the same documents, wasting the importer's time and money.

There is an opportunity to rectify that. The WTO's Agreement on Trade Facilitation came into being in 2014, which serves as a roadmap for developing countries. Pakistan's response so far has been the least ambitious, indicating little or no reform plan for the next five years.

BRR: Let's pivot to CPEC. In your view, what needs to be done to ensure CPEC helps boost Pakistan's export competitiveness in the long run?

MA: Generally, I am very positive on what CPEC could do for Pakistan's economy. CPEC is a huge source of FDI, compared to very low FDI coming in from other countries. One of the reasons for low FDI is the previous experience of many investors. It doesn't send a good signal to investors that Pakistan is contesting major commercial cases in international courts. By contrast, CPEC, in its first few years, has invested a lot in new power projects, something which our own government wouldn't have been able to achieve. There are still problems in the energy sector,

but our total production is now more than the demand.

The other area, besides energy, that can help boost exports is connectivity under CPEC. We can use the CPEC to increase regional trade if this North-South project also includes an East-West corridor. Afghanistan used to import most of its goods through Karachi, until things became difficult and now most of their trade is happening through Iran. For such transit trade to go through Pakistan, railroad transportation is critical. I feel that Railways projects should be a top priority under CPEC for efficient transportation of cargo. It is critical to double the speed of the Karachi-Peshawar Railway line.

BRR: Within the GVCs that China is involved in, what products or assembly lines can Pakistan become part of through CPEC?

MA: The government is working on nine special economic zones, but it still hasn't spelled out which sectors will be its focus. Perhaps it will be the routine industries like textiles, clothing, leather, etc. I would rather that the government focuses on products other than the traditional ones that still constitute bulk of our exports. We are already late in diversifying towards machinery and electronic components.

So, with China and other countries, I would say we need to link up in terms of value-added and knowledge exports. This includes sunrise industries such as electronics or knowledge industries such as software services, pharmaceutical research & development, etc. Services exports really have a potential for Pakistan going forward.

BRR: What are your thoughts on the Commerce Ministry's new trade policy framework?

MA: We need to understand that trade policy should be designed in a different way than it used to be designed a couple of decades ago, allowing certain imports and disallowing others. How we control trade is happening through tariffs. Unfortunately, the Commerce Ministry has no role in that. It has mostly been done by the FBR, whose first consideration is revenue. They don't look at other concerns. With the new STPF, there is a proposal that Commerce Ministry should be responsible for determining tariffs.

The policy documents, which are publicly available, show that the direction is good in terms of making tariffs simpler. But how long will they take to implement? If they have a ten-year horizon, beware that Pakistan is currently losing its share in global trade every year. This budget, too, despite eliminating and reducing custom duties on some export-linked raw materials, has not made things simple.

One of my recommendations is to bring import tariffs down at the same level for all countries. This will make foreign sourcing competitive and help us avoid trade diversion towards one country. And that's what other countries have done. Second thing is, politics aside, regional trade is the way forward. We have to promote trade in the region. And the third thing is that we need to have a powerful Commerce Ministry that can regulate various aspects of trade.

BRR: Lastly, a question on global trade. Do you think the US under Donald Trump is simply litigating with its major trade partners or will the current administration's belligerence lead to a trade war?

MA: I think what is currently happening is unique. This is serious. But for the time being, it is mostly politics. Besides, the fact that China is in a position to retaliate against America's tariff imposition is also a deterrent. Also, as TPP (Trans-Pacific Partnership) has shown, the US can pull out of a trade deal but other countries are still looking to go ahead and sign up. Moreover, globalisation enjoys strong support in developing countries, who can come together to keep the international rules intact. Even in the UK, despite Brexit, there is consensus that free movement of goods within the EU has to be preserved.