Source : www.thehindu.com Date : 2019-02-21

REVOKING PAKISTAN'S MFN STATUS: MORE SYMBOLIC THAN PUNITIVE

Relevant for: International Relations | Topic: India - Pakistan

India’s **decision to withdraw the Most Favoured Nation (MFN) status to Pakistan** means that India will not treat Pakistan on an equal footing in trade as is expected of fellow members of the World Trade Organisation. The move comes after the **attack on a Central Reserve Police Force convoy in Pulwama**, Jammu and Kashmir.

It does not strictly fall under the ‘beggar-thy-policy’, often used in international trade through which one country tries to resolve its economic problems by means that worsen the economic problems of its neighbours or trade partners. The moot point therefore is the sensitivity of the impact of the MFN status on Pakistan in terms of its trade with India. It can only be a pressure tactic and do little unless stringent actions are taken to stop informal trade that has been going on between the two countries for long.

Besides China, India and Pakistan are the two largest economies in the South Asian region. Being dominant constituents of the South Asian Association for Regional Cooperation, both countries have immense potential for intra-regional trade. Trade now takes place using three channels: the official route; the illegal (informal) route, through smuggling along porous India-Pakistan land borders and also Afghanistan, which may not be accounted for in the national income; and lastly, through mainly Dubai and Singapore, which have free ports and accommodate legal agents of traders from India and Pakistan.

Informal trade generally takes place due to restrictions on import of specific items on grounds of health and religious beliefs; ‘high tariff barriers or transportation costs, making it cost effective to smuggle goods in the country; imposition of non-tariff measures (NTMs)’; weaknesses in the ‘rules of origin’ resulting in ‘trade routed through a third country; leakages in transit trade; and distortions in domestic policies such as the absence of or relatively low indirect taxes, creating an incentive to transport items illegally to neighbouring countries. Traders carry out informal trade between Pakistan and India through the exchange of goods at the border as well as through the personal baggage scheme’ through “green channel” facilities at international airports or railway stations. ‘Informal trade has also taken place through Afghanistan where goods are exported officially from India and later smuggled into Pakistan. Indian-made goods smuggled into Pakistan include cosmetics, liquor, stainless steel utensils, ayurvedic medicines, videotapes/CDs, confectionery/cashew nuts, tea, coffee, live animals and spices’.

From 2011-12 to 2017-18, India’s formal trade with Pakistan increased from $1.94 billion to $2.41 billion. Of this, the share of exports stands at almost 80% and has been fairly stable over the years (Ministry of Commerce and Industry, India). In 2012-13, informal trade between India and Pakistan — estimated in a study (ICRIER, N. Taneja and S. Bimal, 2016) — was $4.71 billion, which was double when compared to formal trade. India’s informal export share to Pakistan was again much higher at $4 billion while its import share was low at $0.71 billion.

After the Pulwama attack, the follow-up measure to raise tariff duty on imports to 200% can again be trivial. So would be the NTMs, if increased, as India’s imports from Pakistan are reasonably low at $0.488 billion. Besides, imports from Pakistan grew at a lower rate (1.04%) compared to exports (1.32%) per annum from 2011-12 to 2017-18. Major exports from India that would hard hit would be cotton (not carded or combed) valued at $0.273 billion, p-Xylene ($0.082 billion), polypropylene ($0.063 billion) and single yarn ($0.088 billion). Pakistan’s loss from major exports to India would be much less — from dates ($0.113 billion), portland cement ($0.078 billion), other petroleum oil ($0.055 billion) and light oils and preparations ($0.028 billion).

Thus Pakistan is an important export destination for India but not vice-a-versa. This is despite the fact that Pakistan imposes a large number of NTMs (143) on Indian exports, the major ones being export related measures (25.2%); technical barriers to trade (24.5%); and sanitary and phytosanitary measures (22.4%). These are ‘concentrated on agriculture, plants, and food-related products and operate as bans that shut competitors out of its market. Pakistan’s NTMs are blunt instruments; it is difficult to use them to provide targeted protection to the strategic industries. In contrast, India’s NTMs are soft barriers which operate as delays or bureaucratic hurdles rather than bans. Pakistan’s NTMs focus on general categories of goods whereas India’s NTMs are on particular industries and trading partners. The widely used NTMs India uses include defence procurement procedure, preference to domestically manufactured electronic goods in government procurement’ and a ban on goods largely manufactured within the country.

The sense is that Pakistan may not face an exacerbating situation with India withdrawing the MFN status and raising the import duty. Informal trade may proliferate, which might not be in India’s interest and an appropriate strategy is required to bring it to a halt. Also, under the South Asia Free Trade Area Agreement (SAFTA) 2004, Pakistan’s share in external trade is less than 10%, while India’s share is more than 70%. Such steps may propel Pakistan to look for new markets beyond SAFTA, corroborated by the recent meeting held with Saudi Arabia and growing prospects of trade through a third country, mainly via Dubai.

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Pakistan’s identity crisis, going back to the debates since its creation, remains unresolved

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