

## ISSUE PERSPECTIVE



“Unlocking the full potential  
of the U.S.-India relationship”

Vol. 3, Issue 1

March 2013

**India-Pakistan: Is Trade Key to Everything?**

Stephen Engelken

India and Pakistan must expand their bilateral trade significantly if South Asia is to remain peaceful over the coming 20 years, according to the National Intelligence Council’s recently published study, *Global Trends 2030: Alternative Worlds*.<sup>i</sup> NIC experts reason that Pakistan’s economy must grow fast enough to provide meaningful employment to the large number of youth who will enter the workforce or face growing militancy and reinforcement of the militants’ links with the army. Renewed efforts to stir rebellion in Kashmir and to radicalize Muslim populations in India would inevitably follow, and India could find its progress dragged down by regional unrest. In the NIC’s view, the only plausible way that a Pakistani economy now in crisis can generate the growth needed is by expanding trade with India. The economic benefit to an India experiencing its own growth slowdown would also be significant. The question is whether leaders in each country are far-sighted enough to see the opportunity and take it. The NIC’s analysts fear they will not.

Much of the NIC’s reasoning is spot on and will have South Asia experts nodding in agreement. I worked on South Asian issues for many years, most notably as deputy chief of the U.S. Embassy in Islamabad in 2010-11 and acting consul general in Peshawar in 2012 and left the region convinced that trade provides the best path for Pakistan and India to escape the trap of old enmities. Progress on the political and security issues identified in their Composite Dialogue has been and will likely continue to be painfully slow. Creative thinkers in both countries have proposed solutions for most of them, but there is little incentive for risk-averse officials in both capitals to depart from long-standing positions. Solutions to issues like Siachen, Sir Creek, and—above all—Kashmir may be the last steps, not the first, in a process of gradually normalizing relations.

The NIC’s experts fear that the same conservatism will cause officials in both countries to drag their feet on trade and fail to reap the real benefits. They are right to worry. Pakistanis are uneasy with a trade-only approach that they fear could allow India to put off discussing political issues. As long as India is willing to keep such topics on the agenda, however, there is a real chance for the two countries to expand their economic relationship in ways that benefit both and contribute to regional stability.

The potential for greatly expanded trade is widely acknowledged. The regions that became India and Pakistan were close trade partners before conflict led them to redirect their trade elsewhere, and commerce has already bounced back from a low-point in the mid-1970s when it was almost negligible. In 2010, the total value of trade between the two South Asian giants came to \$2.6 billion, and it could grow far more in the near future.<sup>ii</sup> India’s Associated Chambers of Commerce and Industry recently forecast that bilateral trade could grow to \$6 billion annually by 2014, and a background report prepared for the Pakistani Parliament assessed that trade could rapidly rise to \$10 billion a year.<sup>iii</sup>

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Even more important, the allergies to doing business with each other are not as great as many would expect. Despite threats from extremists like Lashkar-e-Taiba founder Hafiz Saeed, I found Pakistani businessmen wary of opening the door to large competitors but perfectly open to doing business where the mutual benefit was clear. Those who had visited India remarked on how much easier it was to do business in a place that was linguistically and culturally similar. I have heard Indians say much the same about doing business in Pakistan.

Most important of all, both governments have in the past two years shown courage and taken steps to follow up. Pakistan began in November 2011 by announcing that it would apply Most Favored Nation (MFN) treatment to goods coming from India by the end of 2012.<sup>iv</sup> (India granted Pakistan MFN in 1996.) In February 2012, both countries announced the conclusion of agreements on customs cooperation, mutual recognition of standards, and redressal of trade grievances.<sup>v</sup> This was followed in March 2012 by the Pakistani Commerce Ministry's announcement that it would replace the relatively short "positive list" of less than 2000 items that could be imported from India with a "negative list" of 1200 prohibited items thereby effectively freeing up trade in almost 6800 previously banned product areas.<sup>vi</sup> Finally, in September 2012, both governments announced a new visa agreement that included provisions designed to facilitate business travel.<sup>vii</sup>

These steps are having an impact. The Indian Ministry of Commerce & Industry's statistics show Pakistan's exports to India grew 66 percent to \$460 million during the April-December 2012 period, while India's exports to Pakistan rose 16 percent in the same period.<sup>viii</sup>

However, it would be too soon to proclaim victory. In recent months there have been worrying signs both governments could fall back into old habits. Citing concerns from Pakistani agriculturists, the Pakistani government did not begin to apply MFN to Indian goods on December 31 as it had undertaken to do.<sup>ix</sup> And in early January a series of small but brutal incidents between the two armies along the Line of Control cast a pall. The Indian public was especially affronted by reports that an Indian soldier had been beheaded. Trade across the Line of Control was suspended for 10 days. More recently, terrorist bombings in Hyderabad have renewed Indian suspicions about Pakistani backing for terrorism.

So far both sides have tried to prevent tensions from disrupting trade. Pakistan's Commerce Minister Makhdoum Amin Fahim publicly reiterated Pakistan's intention to implement MFN "soon,"<sup>x</sup> and Anand Sharma, India's commerce minister, told a business conference in Agra in late January that "India is of the considered view that there is no alternative way other than building an atmosphere of confidence and trust . . . and for that the only way is economic partnership."<sup>xi</sup>

Looking forward, the most important thing both governments must do is to keep reassuring their businessmen that they have

the political wind at their back when they consider doing business in the other country. The barriers to trade are fundamentally political and psychological. Merchants must feel that it is safe to do business and that they have fair ways to resolve disputes if any arise. Pakistani businessmen, in particular, must look over their shoulders at all times and wonder whether they will be accused of aiding the enemy by militant groups or the security services. All involved will need regular assurances that carefully constructed business arrangements will not be suddenly disrupted by political crises.

Reassurances will be especially necessary over the next 12-18 months as first Pakistan and then India go to elections. Each government will be especially wary of seeming "soft" in this period. This may make big, new initiatives that require action by national parliaments difficult. Tackling the significant non-tariff barriers to trade could be very hard now. However, there are many steps the two governments could take quietly to facilitate trade that might have just as big an impact as formal changes in law and regulation. Pakistani businessmen, for example, complained strongly to me that the near impossibility of making payments or obtaining financing was the biggest hindrance to trade across the Line of Control in Kashmir. The two governments have announced their intention to permit each other's state banks to operate in the other's territory, but this effort is still in its infancy and should be expanded rapidly. Similarly, facilities at the border for the trans-shipment of goods could be expanded, as India has recently done at Wagah. Opening of another crossing point between the countries would help as well.

Ultimately, the two governments must get to the point where they can allow properly screened trucks to haul goods directly from one country to the other without requiring costly and inefficient trans-shipment at the border. For now, this is likely to be a bridge too far. Both sides would have to satisfy important national security concerns and offset damage to local economic interests but the reward would be significant, particularly in Pakistan, where the trucking industry is heavily concentrated in the Peshawar region, precisely the area of the country most threatened by Taliban groups. As executives of trucking firms pointed out to me, the more goods hauled to Wagah or beyond, the more jobs they could provide. Expanded trade with India would thus have a positive impact all over Pakistan and not just in areas close to the Indian border.

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<sup>i</sup> Global Trends 2030: Alternative Worlds, National Intelligence Council, December 2012, p. 75

<sup>ii</sup> “Background Paper: Trade Relations between Pakistan and India,” Pakistan Institute of Legislative Development and Transparency, January 2012, p. 17.

<sup>iii</sup> Ibid., p. 17

<sup>iv</sup> “Pakistan Grants India Most Favored Nation Status,” The Guardian, 2 November 2011.

<sup>v</sup> “Pakistan, India Sign Three Trade Agreements,” Aftab Maken & Obaid Abrar Khan, *The News*, Lahore, Pakistan, February 16, 2012.

<sup>vi</sup> “Pakistan Implements ‘Negative List’ for India Trade,” Bridges Weekly, Volume 16, Number 12, International Center for Sustainable Trade and Development.

<sup>vii</sup> “India, Pakistan Activate New Visa Agreement,” Arun Rajnath, *The News*, Lahore, Pakistan, December 15, 2012.

<sup>viii</sup> “Pakistan’s Export to India Grew 66% during Apr-Dec,” Nayanima Basu, *Business Standard*, New Delhi, India, January 30, 2013.

<sup>ix</sup> “Delay in MFN Status to India due to Agri Lobby in Pakistan,” Nayanima Basu, *Business Standard*, New Delhi, India, February 5, 2013.

<sup>x</sup> “Pakistan Set To Award India MFN Status: Fahim,” *Dawn*, Pakistan, January 31, 2013.

<sup>xi</sup> “Economic Ties Only Way Forward for India-Pakistan: Anand Sharma,” *The Times of India*, January 29, 2013.