

TRADE OF INDUSTRIAL GOODS WITH INDIA: OPPORTUNITIES AND CHALLENGES FOR PAKISTAN

TRADE RELATED TECHNICAL ASSISTANCE PROGRAMME



THE TRTA II PROGRAMME IS FUNDED BY
THE EUROPEAN UNION



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The study was commissioned under Component 1 of the European Union (EU) funded Trade Related Technical Assistance (TRTA-II) programme. The TRTA II programme is implemented by the United Nations Industrial Development Organization (UNIDO) in collaboration with the International Trade Centre (ITC) and World Intellectual Property Organization (WIPO). The Component 1 is about trade policy capacity building and is implemented by the International Trade Centre (ITC).

ACKNOWLEDGEMENTS

This study was carried out as part of the Trade Policy Capacity Building Component, implemented by the International Trade Centre (ITC), of the European Union Trade Related Technical Assistance (TRTA II) Programme, which aims at strengthening the capacity of Pakistan to participate in international trade.

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Andrew Huelin was the editor and managed the production of the final version, and Isabelle Jouve, Associate Programme Adviser, Business and Trade Policy, ITC, carried out formatting including designing of the cover page and desktop publishing.

Finally, we thank PITAD for their overall support as well as active involvement in a public private consultative process, for which the findings of this study informed.

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EXECUTIVE SUMMARY

Report Summary

This is a brief summary of the report that assesses the probable impact of normalization of Pakistan-India trade on certain sectors of Pakistan's industry. These industries have been selected on the basis of their defensive or offensive interest or for their importance in value chains. Included in the study are i) passenger cars, ii) tractors, iii) motorcycles, iv) auto parts, v) electrical fans, vi) surgical instruments, vii) pharmaceuticals and viii) chemicals. The report also looks at the current level of trade facilitation across the Wagah-Attari border and how that can be improved.

This study concludes that expanded trade with India can bring substantial benefits for industrial sectors in Pakistan, including building value-chains, savings on freight, and lower prices for consumers and access to a large market. Further benefits include improved infrastructure, creation of employment and improved utilization of resources. Direct industry contribution and empirical evidence suggests that opportunities for exports would increase worldwide. Even those industries in Pakistan that are likely to be put at a disadvantage, will have opportunities for sustainability and growth in the long run if managed trade is appropriately negotiated. Pakistan's overall import bill is not likely to be adversely affected by the normalization, though the trade balance may continue to remain in India's favour or even increase substantially.

This is a preliminary study and further research and guidance would be indispensable through the transition process that is proposed. Moreover, there are numerous other industries not discussed in this report that would present opportunities for expanding Pakistan's exports. The prospect of industry consolidation as a response to a new emphasis on bilateral trade with India is also an area where further research and technical expertise is needed. It is necessary for Pakistani manufacturers and Government to come out on the front foot and actively seek mergers and joint venture opportunities with their Indian counterparts.

As Pakistan and India increase their volume of bilateral trade, land border stations such as Wagah-Attari border are expected to become major trading hubs, especially due to lower freight costs. Therefore greater focus has to be placed on trade facilitation measures not only at the border but also beyond the border such as different standards, customs valuation, and non-transparent application of trade defence measures. This paper partially touches on some of the practical steps that can be taken immediately. Several studies show that addressing trade facilitation measures results in a greater economic and trade benefit than reduction in tariffs. Furthermore, there are a number of misconceptions about the normalization of trade between Pakistan and India that need to be cleared up through an extensive awareness campaign.

In order to receive industry feedback, two strategies were taken. First, industry agents were directly approached and asked to compile a document illustrating their concerns. Second, where no direct contact was available, questionnaires tailored to each industry were distributed through contact details attained from industry websites. Certain industries had industry organisations. These organisations were consulted for their feedback as well as information on the leading producers in each industry. The below recommendations are derived from a combination of analytical research and stakeholder consultations.

Report Recommendations

These policy recommendations are addressed to the stakeholder agencies, which include the Ministry of Commerce, Ministry of Industries, Planning Commission, and Federal Board of Revenue.

Challenge	Policy solution / recommendation	Proposed concrete initiatives	Timelines
What steps could be taken to make the auto industry more competitive?	<ul style="list-style-type: none"> • Phase out Tariff Based System so that the auto industry can procure cheaper components • Encourage auto-industry association to seek bilateral agreements with its Indian counterpart • Ensure compliance with Euro II and other latest global emission standards 	<ul style="list-style-type: none"> • Reduce customs duty on auto-parts to that prevalent in India i.e., 10% or less • Allow import of CKD kits from India • Gradually reduce duty on cars and motor cycles • Review the current import policy for import of used cars and bring it at par with India, taking account of WTO rules • Negotiate removal of tariff on tractors in India • Set up a joint public-private sector body to implement the recommendations of various tariff reforms reports including this one 	Three to five years for passenger cars. Trade in others like tractors, motorcycles, and auto-parts could be normalized over the next 1-3 years.
How to make electric fan industry more competitive and gain market access in India?	<ul style="list-style-type: none"> • Improve manufacturing practices • Improve capacity utilization • Negotiate reduction of tariffs and nontariff barriers in India 	<ul style="list-style-type: none"> • Make local skill development centers more efficient • Enforce quality standards • Reduce customs duty on import of raw and packaging materials 	1-2 years as Pakistani fan manufacturers are relatively competitive Budgetary proposals should be adopted at the time of next budget
How to enhance exports of surgical goods to India?	<ul style="list-style-type: none"> • Improve technologies • Increase productivity • Shift production from the lower end market to higher value sophisticated products 	<ul style="list-style-type: none"> • Explore setting up joint ventures with developed countries to be able to export higher end goods to India • Set up Public-Private sector testing and standards mechanism • Allow duty free import of raw materials 	1-3 years but budgetary issues should be resolved at the time of next budget
How to make pharmaceutical industry more competitive and compete against the Indian industry?	<ul style="list-style-type: none"> • Improve quality • Review the policy of fixing prices for all drugs • Seek approvals of international regulatory bodies 	<ul style="list-style-type: none"> • Set up a public-private sector regulatory enforcement body to monitor quality • Encourage joint ventures with Indian pharmaceutical companies 	2-3 years
How to increase bilateral trade in plastics and chemicals?	Consider building supply chains as chemicals and plastics are raw materials for use by other industries	<ul style="list-style-type: none"> • Negotiate mutual reduction of tariffs and nontariff barriers in the context of SAFTA • Special storage and handling infrastructure be built immediately 	1-2 years
How to improve trade facilitation across land borders?	<ul style="list-style-type: none"> • Reduce turn-over time • Eliminate multiple checks • Rely on risk-profiling 	<ul style="list-style-type: none"> • Open new border crossings • Replicate customs procedures applicable at sea ports • Establish single window operations 	Start implementing immediately and monitor progress over the next 2 years

SECTIONAL SUMMARIES

Passenger Cars

Within the automotive industry, the major problems arise in the case of passenger cars. There are two significant obstacles facing assembly of passenger cars. First, there are the concerns raised by the local car manufacturers. These include the following:

- a. The playing field is not level as India has many non-tariff and tariff barriers.
- b. Indian manufacturers enjoy greater economy of scale
- c. India's policy of homologation (the process of certifying that a particular car is roadworthy and matches certain specified criteria) is time consuming and complex.
- d. Some models of cars produced in India are much cheaper than those in Pakistan
- e. Pakistani government's frequently changing policies regarding import of used cars makes it difficult to have long-term policies

Secondly, there are other general issues, which are normally not raised by a majority of the auto industry but they become obvious when the auto policies of both countries are compared. These include the following.

- a. The Pakistani car industry has limited sources from which it can procure its components. Under the Tariff-Based System (TBS) for the auto-sector, assemblers have to source most of their components (other than CKD kits) from local sources. Otherwise they have to pay high tariffs ranging from 35 to 50%. Indian assemblers, on the other hand, can pick their supplier, and thus pay a reduced price and only 10 % duty. This duty has been further reduced under the Indo-Asean Free Trade Agreement (FTA) to 5% from January 2013 and will be completely eliminated in December 2013.
- b. Since all three major car assemblers (Suzuki, Honda and Toyota) depend on their parent company for import of CKD kits, any decision taken by the parent company impacts local production in Pakistan. For example, when Suzuki moved its production from Japan to India, Pak-Suzuki was unable to source its CKD kits and other components from India. It therefore had to stop producing its best-selling Alto model. A similar situation could arise with other models, as India is becoming a manufacturing hub.
- c. Another implication of high dependence on sourcing components from Japan is that due to the rise of the Japanese yen against Pakistani currency, prices of local cars have to be periodically adjusted upwards. In order to check this rise in prices, the Government allows import of used cars. This adversely impacts production capacity, which is already rather low at 50%.
- d. With the current levels of tariff and non-tariff barriers in both countries, there is not likely to be much trade between the two countries. They would have to negotiate lowering of tariffs and non-tariff barriers under the SAFTA framework.

Tractors

Pakistani tractors can compete in quality and price with global players. Also they are better suited for local market conditions. It is unlikely that Indian tractors would be able to penetrate the Pakistani market to any significant degree. Pakistani tractors are already being exported to several countries on the basis of their cost competitiveness. If Pakistan were to expand the production of tractors and meet Euro II emission standards, it may have an opportunity to export to India.

Motorcycles

Branded motorcycles in India and Pakistan are of similar price and quality. As a result, there would be little potential for India or Pakistan to make a significant foray into each other's markets through motorcycles of Japanese brands at the current tariff levels. Pakistan does have a competitive advantage over India for motorcycles assembled with Chinese parts and consequently could penetrate the Indian market. This is especially true for Indian rural consumers who may opt for more economical smaller engines such as the 70cc.

On the other hand, Indian manufacturers may be able to export larger engine motorcycles if duty-free exports were allowed. At the current rates of duty, this would not be feasible. The findings would suggest that Pakistan would stand to benefit from opening up of trade in motorcycles with India and it is worthwhile to pursue a more offensive strategy. They would however, need to meet Indian emission control standards.

Auto Parts

Pakistani auto-parts manufacturers can successfully compete and capture a share of the vast Indian market. For this an enabling environment would have to be created. This would mean rationalization of tariffs on import of raw materials, parts that are often incorporated in the finished products, dies, and machinery for producing high quality parts. Also there will have to be more quality control. A public-private auto sector-testing centre should ensure that only parts of the highest quality are exported.

Recommendations

The following approach is suggested:

- First, rationalisation of Pakistan's taxation policies is needed, in particular its customs tariff and other auto-related policies, including import of used cars. More specifically, the following policy decisions are recommended:
 - Phase out SRO 693(I)/2006, dated the 1st July, 2006 regarding Tariff Based System
 - Reduce customs duty on auto-parts to less than 10% so that the auto-industry is in a position to import them from the most economical sources
 - Remove CKD kits and from the negative list for imports from India
 - Gradually reduce import duty on cars and motor cycles to make them more competitive
- Secondly, there is a need to look at some successful models of regional and bilateral agreements involving auto trade, and encourage local industry to negotiate similar agreements with their Indian counterparts.
- Finally, prioritisation of those sub-sectors of auto-manufacturing that have a comparative advantage must be carried out. This would have to be a collaborative effort between the Government of Pakistan and the manufacturers.
- Set up a joint public-private sector body to control quality of exported goods

Electric Fans

Pakistan has successfully built a fan industry to meet all of its local demands. It has also significantly grown in exports to its major markets in Africa and the Middle East. However, it has not made any headway in the Indian market. Pakistan's seasonal manufacturing cycle results in a semi-specialized labour force and plenty of unutilized capacity. Opening up trade with India would drive increased

investments in technology and labour training by Pakistani manufacturers. It may also lead to industry consolidation as a way to build an economy of scale.

Pakistan's main competitors in the Indian market would be Chinese and Indian manufactures. Pakistan should be able to effectively compete and win a large share of the market from Chinese and Indian manufacturers on the basis of better quality and competitive prices. If duty-free import of electric steel sheets and plastics is allowed for fan-manufacturing and if they were given duty free access to the Indian market, Pakistan could easily export fans worth \$50 - 100 million yearly to India over the next 3-5 years.

Recommendations:

- Reduce customs duty on import of raw materials including electric steel sheets, enamelled copper wire, steel rods
- Negotiate with India for removal of tariffs under the SAFTA framework
- Make local skill development centers more efficient
- Provide funding for R&D
- Assist the local manufacturers, particularly small and medium enterprises, in design making
- Extend financial support for meeting one-time costs of various certifications
- Improve facilities for material testing
- Trade Development Authority of Pakistan (TDAP) should organize trade fare in India focusing on light engineering goods such as fans and surgical goods. TDAP should also facilitate participation of Pakistani manufacturers in the Indian industrial expositions
- Enforce quality standards through a public-private sector bodies

Surgical Instruments

Pakistan is one of the major exporting countries in the global surgical hand-held goods market. Pakistan's surgical instruments industry has shown steady growth in exports in recent years, reaching US\$300 million in 2011-2012. However, the industry is underutilized and generates far below its potential. Pakistani manufacturers lose out on significant revenues to middlemen in Germany who, after branding and marketing, make substantial mark ups. The industry is focused on the lower end of the market and it requires less investment in technology and specialised labour.

Pakistan's manufacturers have satisfied international quality requirements and have a flexible manufacturing process that can cater to different specifications. Pakistan has the opportunity to significantly grow its industry through exporting to a growing Indian market. Sialkot's proximity to the Indian border and the manufacturers' ability to make direct contacts, eliminating middlemen, should be an incentive for Pakistan to pursue trade negotiations for surgical instruments with India.

Recommendations:

- Allow duty free import of raw materials particularly electrical steel sheets
- Negotiate with India for removal of tariffs under the SAFTA framework
- Explore setting up joint ventures with developed countries to be able to export higher end goods to India
- Set up Public-Private sector testing and standards mechanism

Pharmaceuticals

Although a majority of Pakistani manufacturers remain apprehensive about opening trade in pharmaceutical goods with India, the fact is that over the years the government of Pakistan has allowed imports from countries that produce some of the cheapest medicines. These include China, Bangladesh, and Hungary. Despite their lower prices the share of medicines from these countries has remained low. For instance, the share of Chinese pharmaceutical products in Pakistan is less than 1%. It is likewise unlikely that products from India will capture any significant share of the Pakistani market.

Furthermore, some Pakistani pharmaceutical manufacturers have recently been successfully competing against their Indian counterparts in many foreign markets. Finished medicines are liable to customs duty of 10% when imported into Pakistan. In some cases such as ampicillin, amoxicillin and cloxicillin, (capsules or syrups), the duty rate is 25%. There is currently no concession under SAFTA on medicines. Thus adequate protection is available against imports from India. In order to retain its domestic share and also be able to capture some share in their market, the following suggestions are being made.

Recommendations:

- Set up a public-private sector regulatory enforcement body to monitor quality
- Encourage the industry to seek approvals from the international regulatory bodies
- Encourage joint ventures with the Indian pharmaceutical industries
- Review the policy of fixing prices for all drugs
- Normalization of trade for pharmaceuticals be done in a phased manner by first removing them from the negative list and then over time considering any tariff reduction

Plastics and Chemicals

Enhanced trade in chemicals and plastics provides another opportunity for Pakistan's industry to become more competitive. Amongst plastics, polyethylene and polypropylene are crucial for many industries making plastic goods, particularly those located in Punjab. Currently these plastics, worth about US\$ 1 billion are mostly imported through sea from the Middle East and then transported by road upcountry. These can be procured at more competitive prices from Indian units located near the Wagah border. On the other hand, Pakistan has recently enhanced its PVC production whereas India is unable to meet its own demand. Pakistan can export its surplus quantity of 70,000 tons to India.

Major organic chemicals where there is a significant potential for trade include p-xylene, o-xylene, ethylene dichloride and phthalic anhydride. Whereas p-xylene and o-xylene are imported in Pakistan, ethylene dichloride and phthalic anhydride are produced in surplus quantities and are in demand in India. As for inorganic chemicals, there is a significant potential for exports of caustic soda, soda ash and hydrogen peroxide from Pakistan while aluminium hydroxide, dithionites, sulphoxylates and chlorates have a significant potential for the Indian side.

Recommendations

- Negotiate with India on mutual tariff reductions on plastics and chemicals. For example, Pakistan can offer to reduce duty on polyethylene and polypropylene and in return seek lowering of tariffs on PVC.
- Trade in chemicals needs special safety and handling requirements. There is an urgent need to have the requisite infrastructure.

Trade Facilitation

Of the measures to improve bilateral trade between India and Pakistan, the most important is trade facilitation. The two countries have a common border of about 3000 km but there is only one crossing, Wagah-Attari, through which legal trade of only 137 items is allowed. The total value of trade passing through this point in 2012 was US\$323 million, of which US\$266 million was imports from India and US\$57 million was exports to India. The bulk of the remaining bilateral trade estimated at US\$2.06 billion in 2010-2011 took place through seaports.

As India and Pakistan increase trade through land, the Wagha-Attari border is expected to become a major hub of their trade, especially due to lower freight costs. However, barriers in trade facilitation remain a major hindrance. Some of the major anachronisms which can easily be observed at this border are the following: multiple agencies overlapping, lack of advance clearance, lack of risk profiling, truck changes, duplication, avoidable fees, and manual processing.

Most of the bottlenecks can be addressed through regulatory measures without any costs. In fact, there would be considerable savings. Trade facilitation measures that can be adopted unilaterally include simplification of processes (remove multiple checking by different agencies, introduce single window concept) and harmonization of clearance processes, advance processing of documents, automation of processes and facilities for payment of taxes in advance. Trade facilitation measures that need to be negotiated and implemented bilaterally include: introducing joint one-stop border systems, allowing transhipment of goods, allowing multiple entry passes for drivers, increasing opening hours from the recently increased 16 to a full 24 hours, introducing risk-profiling, and opening of other border points such as the Hussainiwala-Sialkot crossing.



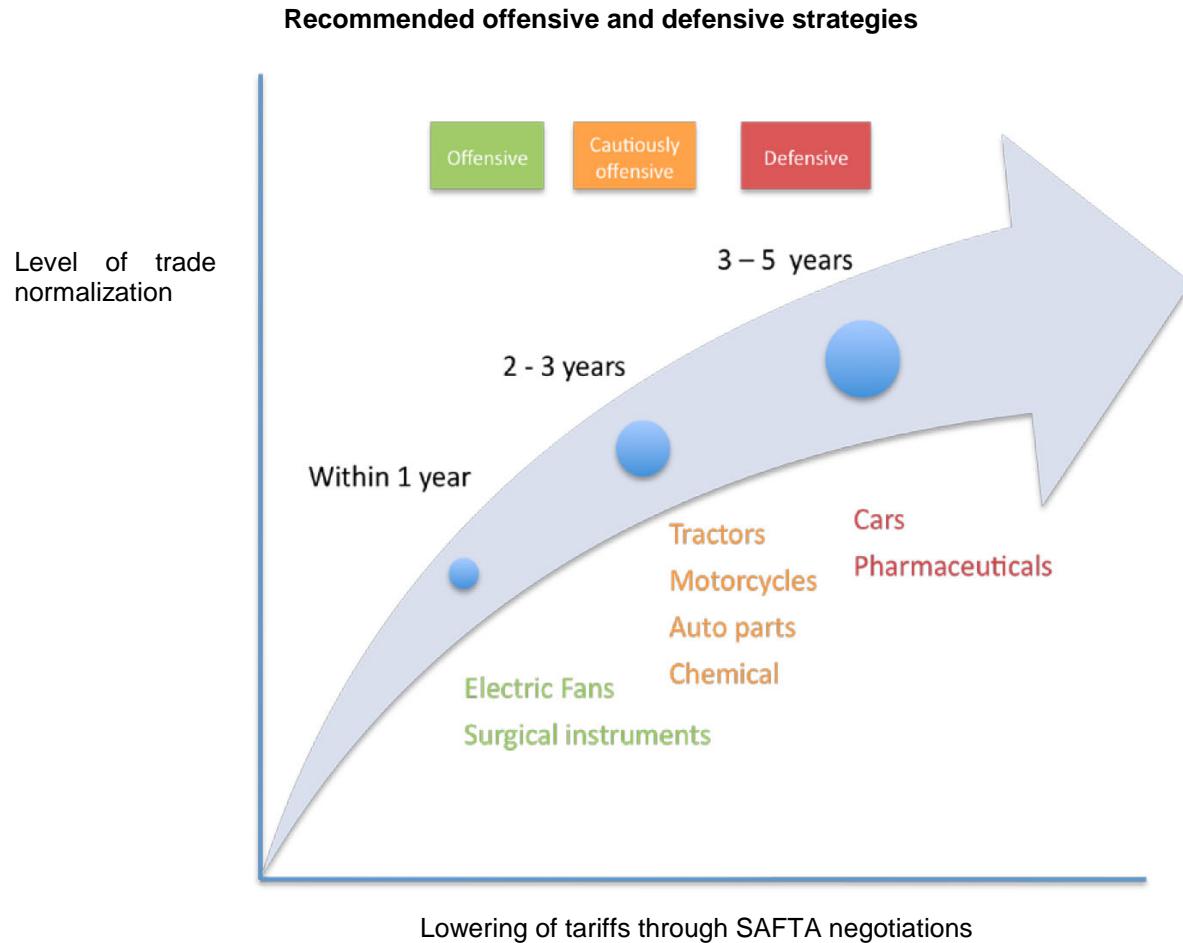
Stakeholder Consultations

In order to receive initial industry feedback two strategies were taken. First, industry agents were directly approached and asked to compile a document illustrating their concerns. Second, where no direct contact was available, questionnaires tailored to each industry were distributed through contact details attained from industry websites. Certain industries had industry organisations. These organisations were consulted for their feedback as well as information on the leading producers in each industry. The list of tailored industry questionnaires is included in the main report.

Road map to Pakistan's industrial sector

Automotive sector	Electric fans Surgical instruments	Pharmaceuticals Chemicals	Trade facilitation Stakeholder consultation
<p>Automobile industry may still need some time to adapt to the opening of trade but a start has to be made immediately.</p> <p>Tractor manufacturing has become a success story.</p> <p>Motorcycle industry is another success story.</p> <p>In the engineering sector, auto-parts hold the most promise for Pakistan.</p>	<p>Pakistan's electric fan industry is well placed to benefit from normalization of trade with India.</p> <p>Pakistan's surgical instruments is one of the few that exports over 95% of its output to developed partners such as the US and EU.</p>	<p>Pakistan has a well-established pharmaceutical industry.</p> <p>Cheaper imports of chemicals polymers (polypropylene and polyethylene) and increased export of inorganic chemical (caustic soda and ash soda).</p>	<p>Of the measures to improve bilateral trade between India and Pakistan, the most important is trade facilitation.</p> <p>Questionnaires tailored to each individual sector were sent to the respective stakeholders, including company CEOs, associations and their members, government officials, customs official, importers/exporters, and others.</p>

The chart below provides a summary of offensive and defensive strategies Pakistan can employ through the transition process. These consider Pakistan's comparative advantage to India in each sector.



The objectives of this report were clear at the outset, with the ITC Terms of Reference articulating exactly the expected outcomes of the report. These objectives are outlined below from the original document provided by the ITC.

OBJECTIVES OF THE STUDY

The International Trade Centre under the terms of reference outlined these objectives. The purpose of the research is to analyse Pakistan's certain industrial sectors is to identify potential opportunities and threats for trade with India as well as policy reforms needed to enhance exports to India in the industrial sector. Analysis should consider how the improved trade relations with India and full implementation of SAFTA can maximise business opportunities.

The study is specifically required to address the following objectives:

Overall

- Analysis of the existing trade regime and market access opportunities with India in the industrial sector with a view to recommending policy reform for enhancing to enhance exports to India

Offensive strategy

- Identification of potential Pakistani product clusters / sectors for exports to India where Pakistan has a comparative advantage
- For selected product clusters / sectors, comprehensive identification of the challenges at the border, behind the border and beyond the border; challenges and issues for Pakistani exports to India.
- Clearly set out and articulate recommendations for domestic policy and regulatory reforms to enhance the competitiveness and boost exports to India in the above (identified) potential industrial sectors.
- The recommendations should provide long term and short-term strategy and should address challenges faced behind the border, at the border and beyond the border.
- The recommendations should be derived from a combination of analytical research and stakeholder consultations.

Defensive strategy

- Identification of industrial sectors which may require protection along with recommendations for policy reform to make them competitive
- For both offensive and defensive strategy to a great extent the study should suggest how aim to reach a stakeholder common position for the final recommendations, but where clear divergences exist in stakeholders views on the recommendations (and underlying challenges), such divergences should be tracked, opined upon and represented by the consultant. This point must be re-written
- For both offensive and defensive strategy any laws, regulations and policies, which may need to be changed, should be identified, and proposals furnished to amend those.

AUTOMOTIVE SECTOR



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Global Scenario

The global automotive industry is highly competitive. Industry players engage in a constant search for new ways and means to remain ahead of their competitors. The recent prolonged global financial crisis has only made this race even fiercer. In order to survive, many players have looked to mergers, acquisitions, and divestments. Others have formed strategic alliances and entered into joint ventures.

As a result, certain global manufacturing hubs have emerged which are better equipped to meet new challenges. They make use of novel concepts such as 'just-in-time', which favours delivery of parts to the assembly line in a continuous flow, rather than stockpiling large volumes at the plant, with an emphasis on a flexible production line. These changes enable manufacturers to produce several different models on the same assembly.

Shifting the place of production has a two-fold advantage, the first being lower costs. For example, the shift of labour-intensive operations, such as assembly, to places such as the Czech Republic and Romania in Eastern Europe, to Mexico and Brazil in the Americas, and to Asian countries such as Korea, Malaysia, Indonesia and now increasingly to China and India has resulted in far more flexible and efficient manufacturing. As production has grown, other more capital-intensive operations have also been moved (engines, gearboxes, body panels, etc.). Secondly, these shifts allow actors to take advantage of fast growing domestic markets for vehicles and to produce parts and components in global supply chains. The steep rise in some currencies has also made certain countries less competitive in the industry. For example, the rise in the value of the yen has contributed to Japan moving many of its production facilities to other countries.

These global factors are having a significant impact on Pakistan's auto industry, irrespective of its opening trade with India. Like auto-industries elsewhere, Pakistan's industry must now reflect on how to adapt itself to these changes. The players must be aware that, despite having a long history spanning over 60 years, the industry has not made the kind of progress that many of its global competitors have achieved. Analysis is, therefore, needed as to what lessons can be learnt from other successful developing countries and what policy changes are needed to put the auto-industry on par with them.

In order to understand the current challenges, it is useful to turn, briefly, to a profile of the auto industry in Pakistan and how it has evolved over time.

Pakistan's automotive industry

There are over 100 companies assembling various other vehicles including buses, trucks, tractors, rickshaws, and motorcycles. In addition, there are around 1,700 automotive parts manufacturers, including sole enterprises. These manufacturers can be grouped under four categories:

- i. Passenger cars;
- ii. Tractors;
- iii. Motorcycles and
- iv. Auto-parts

As they are structured differently and each has its own challenges and opportunities, these sectors are discussed separately. Other automotive industries such as light commercial vehicles, buses, and trucks were not included in this study.

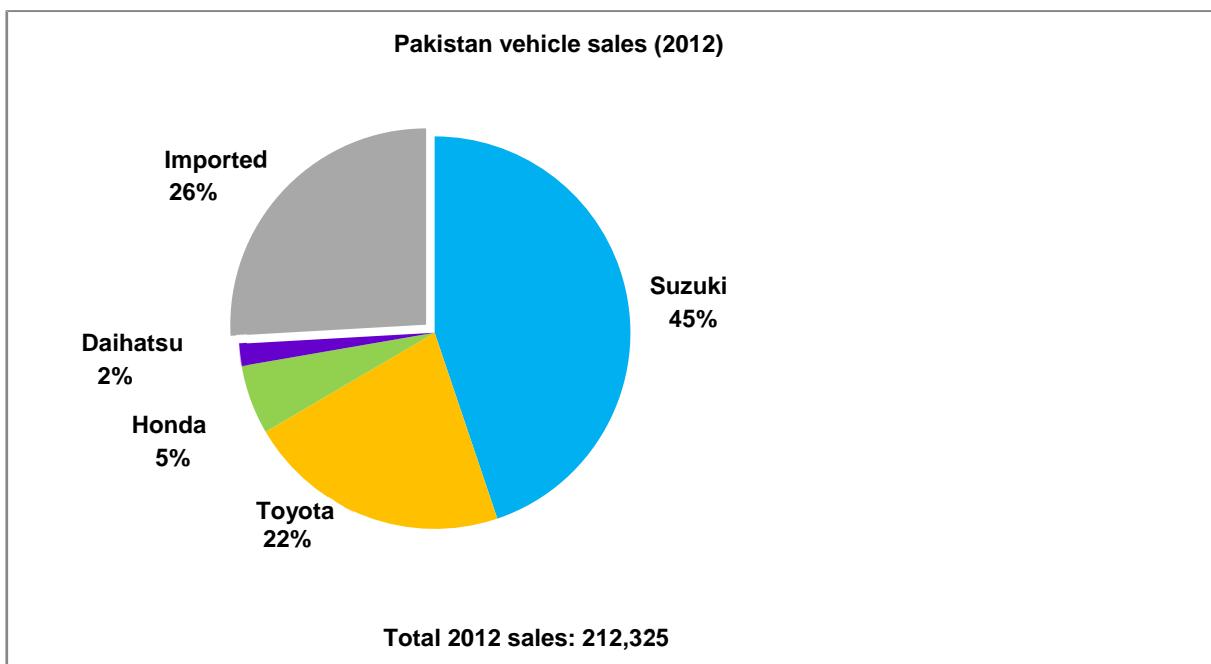
Passenger cars

Industry dynamics

Following independence, the automotive industry was one of the pioneering sectors in Pakistan. Starting with the establishment of a Bedford trucks assembly plant by General Motors in 1953, it then expanded to production of British Ford and Vauxhall passenger cars. In the 1960s, Rover started producing jeeps and Massey Ferguson started assembling tractors. However, with the nationalization of all industries in 1972, the auto-industry started to lose its momentum and there was limited investment and development.

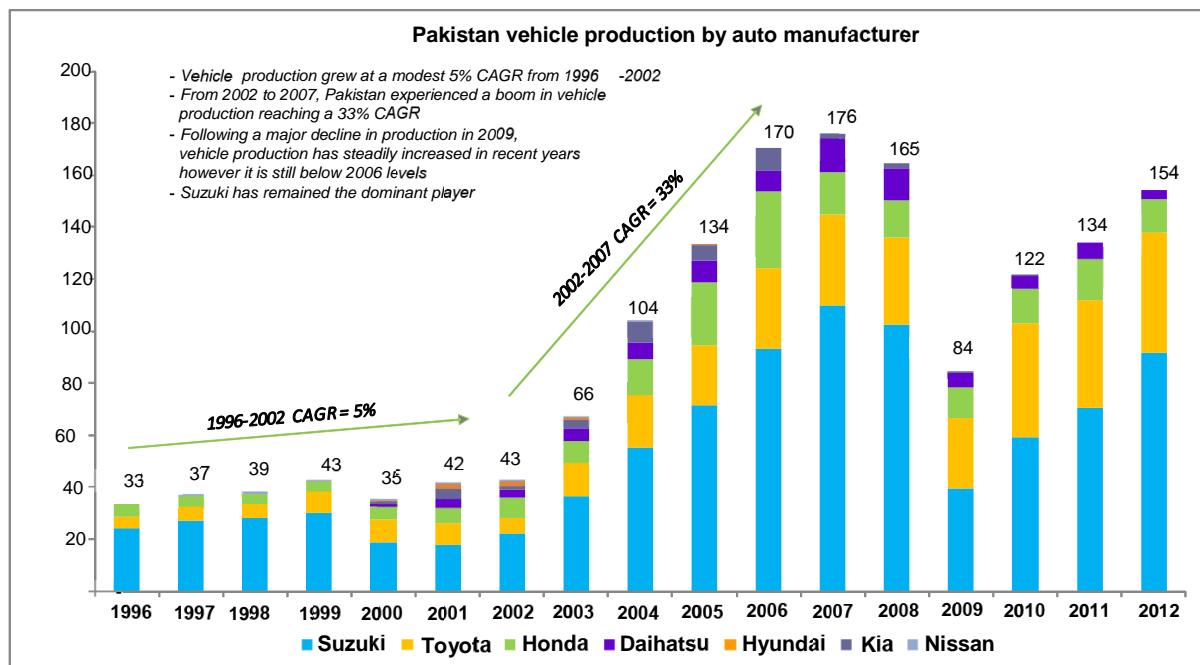
With the easing of nationalization in the early '80s, private investment started to flow in once again. One of the first such collaboration was between Suzuki Motor and Pakistan Automobile Corporation (PAC), which led to the establishment of PAC Suzuki Motor. This joint venture started manufacturing all types of vehicles including passenger cars, pickups, vans, and jeeps. Success of this joint venture encouraged others like Honda, Toyota and Daihatsu to also start the local assembly of passenger cars. Hino followed suit with the manufacture of buses and trucks while Isuzu started producing trucks.

When the auto-industry was fully privatized in the early 1990s, a number of new companies emerged. Suzuki acquired the majority of Pak Suzuki's shares and in 1992 became Pak Suzuki Motor Company Limited. Toyota and Habib Group established Indus Motor Corporation for production of the Corolla, as well as Hi-Lux and Daihatsu Cuore. Honda and local Atlas Group set up Honda Atlas Cars Pakistan Limited and started manufacturing Honda City and Civic models. Another Japanese assisted assembly plant is Ghandhara Nissan Limited (GNL) but this does not have any equity from Nissan Motors. The only non-Japanese plant is Dewan Farooq Motors Limited, which was jointly established by Hyundai Motor (Korea), Kia Motors (Korea) and Dewan Farooq Group (local). Hyundai and Kia provide technical assistance for Dewan Farooq Motors without equity participation. Production at Dewan Motors is currently suspended and GNL also is not active. As a result, Pak Suzuki, Indus Motors and Honda Atlas share 99% of the domestically produced passenger car market share and 72% of all Pakistan vehicle sales in 2012.



Source: PAMA (June - July 2012)

TRADE OF INDUSTRIAL GOODS WITH INDIA: OPPORTUNITIES AND CHALLENGES FOR PAKISTAN

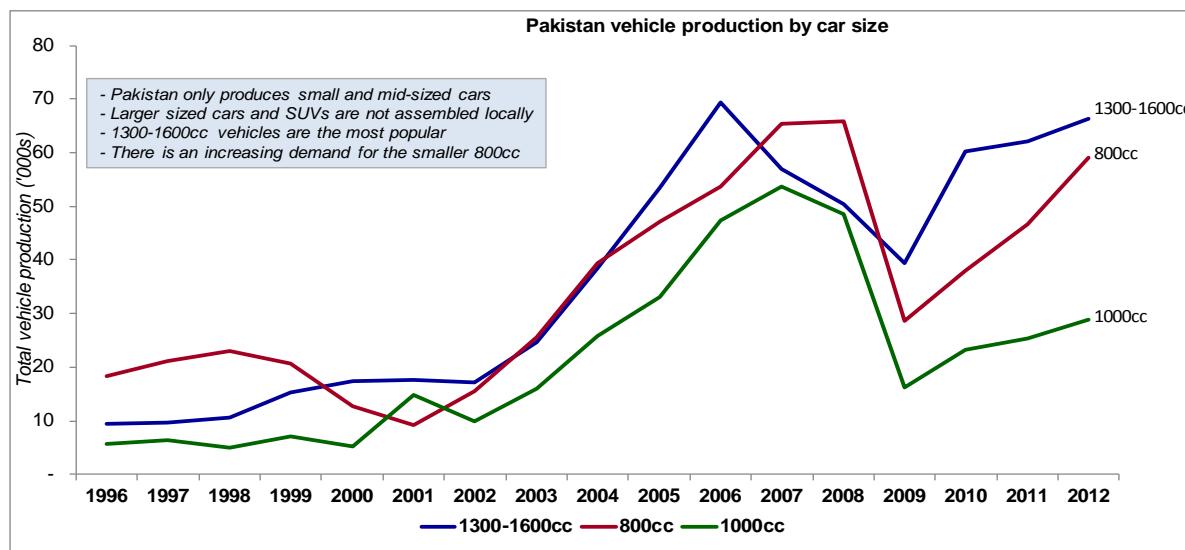


Notes: Toyota is parent of Daihatsu but it is shown separately. Figures as of June to July year end.

Source: PAMA (Includes figures from PAMA members only), July 2012

The assembling capacity for passenger cars is 270,000 units but capacity utilization is no more than half. In 2011-12, domestic industry produced about 157,325 cars while imports of 55,000 units met the remaining needs.

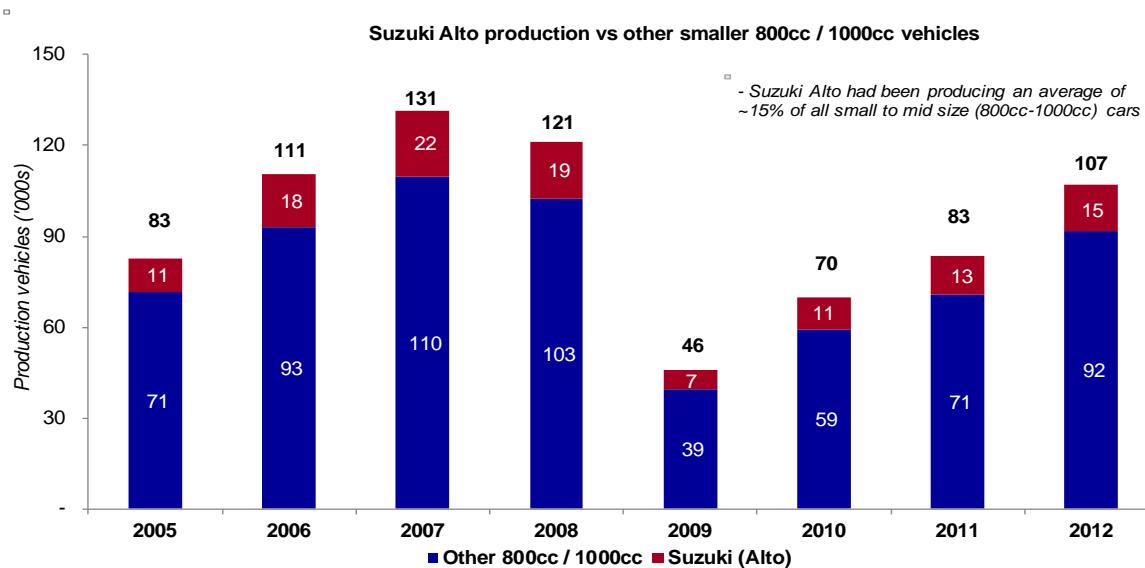
While Suzuki specializes in small cars, Toyota and Honda produce mid-sized compact cars. Larger sized cars and SUVs are not assembled locally.



Source: PAMA July 2012

All major manufacturers of passenger cars in Pakistan are subsidiaries of Japanese multinational auto-manufacturers. As such, any policy decisions by their parent companies have an immediate impact on the local car industry. The following two recent case studies explain how decisions taken by the parent company adversely affected Pakistan's auto-industry.

Until recently Suzuki Alto was the best-selling small car in Pakistan. When the Japanese parent company moved its production from Japan to India, they could not adjust to this change as auto-parts are on the negative list and could not be imported from India. Pak Suzuki Motor Company had to stop producing this model. If the industry had been able to adjust its sourcing, it would, not only, still be producing Alto cars but making them more economically.



Note: Other smaller vehicles include Suzuki (Cultus, Mehran, Bolan, Margalla), Hyundai (Santro Plus), and Daihatsu(Cuore)

Source: PAMA (June - July 2012)

Since Pakistan's passenger car industry is entirely dependent on import of CKD kits, any rise in the Japanese yen has immediate repercussions for Pakistan's auto-industry. Over the last three years, the prices of all Pakistani cars were raised several times to keep up with the rise of Japanese yen against Pakistani rupee.

So far Pakistan's passenger car industry has been highly protected through high tariffs. In addition, import substitution policies such as deletion programmes have discouraged new entrants in the market. But with the global changes, high tariffs and other protective policies are not sufficient to keep Pakistan's auto-industry immune to the ramifications of these exogenous changes. It is therefore essential that the auto-industry looks to its long-term future and starts taking the necessary measures. The implications are to make the industry more nimble so that it is able to adjust with the changing patterns of trade and technology.

In fact, Pakistan is not unique in protecting its auto industry through high tariff and import substitution policies. Other developing countries followed similar policies. It was particularly so for India. Until 2001, new entrants in the Indian market were required to use no more than 50% imported content in their passenger car production by the end of their third year, and no more than 30% imported content by the end of the fifth year. They were also required to balance their imports of auto kits and components into India with exports of cars or car parts of at least equal value of those imports. But these requirements were subsequently abolished in 2002 following the European Community and the United States successful challenging at the World Trade Organization (WTO).

On the other hand, Pakistan has continued to use local content programmes (officially referred to as indigenization policies) to date. First, it continued to seek an extension for its deletion programme from the WTO, as they were inconsistent with the WTO rules. It was given four years after the expiry of grace period of five years allowed to all WTO members when the Trade Related Investment Measures (TRIMs) agreement entered into force. At the end of this period, instead of phasing out the deletion programme, Pakistan replaced it with a Tariff Based System (TBS). This system essentially keeps the deletion programme intact. Under this regulatory scheme, imports in CKD condition are allowed only to those assemblers who are registered by the relevant Federal Government Agency. Furthermore, parts/components indigenized by June 2004 have been placed at a higher rate of customs duty and those that had not been indigenized are allowed at CKD rate of custom duty.

As a result of continuation of these policies, a large gap has developed between the Indian and Pakistani auto-industry. Not only India has been able to attract foreign investment, it also makes its industry more dexterous and competitive. It is time for Pakistan to learn by example as to how it was able to adjust to liberalization and put the industry on firmer ground.

Through consolidations and concentration of production facilities, those countries that can produce a critical mass are much better placed to sustain themselves in the long run. Pakistan's production of passenger cars has not even touched 200,000 units. It is thus fairly small as compared to other Asian car producers such as South Korea: 3,866,206, India: 3,038,332, Iran: 1,413,276, Indonesia: 561,863, Thailand: 554,387, Malaysia: 522,568, and Taiwan: 251,490. It, therefore, has to expand to achieve a critical mass. It would not be easy to find export markets as exports of foreign brand cars is governed by the parent company's global strategy.

RCA and NRCA

The Revealed Comparative Advantage (RCA) and Normalised Revealed Comparative Advantage (NRCA) calculate the extent of advantage one country has over the other. These have been worked out on the basis of TRADEMAP from ITC. A detailed explanation of the calculations is shown in Annex 1.

Passengers cars

HS Code	Product description	Year: 2011, Unit: Million USD			RCA		NRCA	
		Pakistan exports to world	India exports to world	World exports	Pakistan	India	Pakistan	India
8703	Cars (including station wagon)	2.6	3,624.9	634,189.1	0.00	0.34	(0.99)	(0.49)
	All products	25,343.8	301,483.3	17,855,727.0				

This shows that India has significant advantage over Pakistan. However, since passenger cars are on the sensitive list of Pakistan and no tariff concessions have been agreed, trade is not likely under the current levels of tariff rates which range from 50 % and higher (depending on the engine capacity). On the other hand, India has allowed concessionary rate of 10 % as against MFN rate of 100 %. If Pakistan is able to assemble cheaper cars, it would stand a comparatively good chance of exporting to India. This is quite possible if Pakistan was to use CKD kits and some other components from India.

The Way Forward

The automotive industry as well as the Government of Pakistan must take full cognizance of various developments around the world. Over the last decade, the Government of Pakistan commissioned three studies to see how it could adjust its tariff and trade policies to make the automotive industry more competitive. The three reports by the World Bank (2004), Dr A.R. Kamal (2004) and Garry Pursell et al (2011) made several concrete recommendations but no serious efforts have been made to implement them.

It is clear that reforms cannot be delayed for too long. The opening of trade with India should be taken as an opportunity rather than a threat, representing a step forward. The auto industry may still need some time to adapt to the opening of trade but a start has to be made immediately.

To this end, a three-pronged approach is suggested. Firstly, rationalisation of Pakistan's taxation policies is needed, in particular its customs tariff and other automotive-related policies. Secondly, is the application of best practices through the analysis of previously successful models of regional and bilateral agreements involving automotive trade, and adapt those models to the local requirements. Finally, prioritisation of those sectors that have a comparative advantage must be taken. This would have to be a collaborative effort of the Government of Pakistan with the auto-manufacturers.

Tariff Rationalization

The best option for the Government is to review the recommendations for tariff rationalization already made in the three studies listed above. While two of the studies were made in 2004, the recommendations therein are still very relevant. In any event, these studies were reviewed in 2011 by an independent team of international and national experts led by Garry Pursell, who reiterated those recommendations.

The key recommendations of the three studies were:

- Removal of the *de facto* deletion programs;
- Reduction of the auto customs duties to a considerably lower uniform rate;
- Unification of tariffs on CKD packs, original equipment components and replacement parts at a single rate (for example at 25%),

Review of Successful Models of Regional Automotive Agreements

While there are many successful models of regional or bilateral trading arrangements, the two most relevant are those of MERCOSUR and Canada/United States. In both cases, a smaller economy was entering into a free trade agreement with a much larger one and had to negotiate some safeguards to preserve its market share and also to benefit from exporting its cars.

The agreement negotiated by Argentina and Brazil while forming Mercosur (Mercado Común del Sur or Southern Common Market of Argentina, Brazil, Paraguay and Uruguay) in 1991, which became effective on January 1, 1995 is more relevant for Pakistan. As in case of SAFTA where only India and Pakistan have automotive industries, in case of Mercosur it was Brazil and Argentina.

In terms of size of economies, population and geographical area, there are many similarities between Argentina vs. Brazil as with Pakistan vs. India. More specifically there are many similarities in the auto-policies. Up to the 1990s, both Argentina and Brazil not only provided high levels of protection but also resorted to various import substitution schemes. Their companies were also mostly joint ventures of foreign multinationals with domestic firms as is the case with India and Pakistan.

Just as Pakistan is apprehensive about its ability to compete with the Indian automotive industry, so was Argentina worried about its capacity to compete against Brazil. Although Argentina had a long history of auto production, it was worried that free trade would not only result in the shifting of the existing manufacturers to low-cost Brazil and that new entrants would also invest preferentially in that country.

In case of Argentina and Brazil, the main automotive lobbies negotiated the basic agreement, ADEFA in Argentina and ANFAVEA in Brazil, representing the two countries. The agreements main provision was "Compensated Trade Clause" (CTC) which provided for managed auto trade regime. Although the agreement evolved over time the basic premise was that the exports of Brazil were restricted to what the country would import from Argentina. For example, Brazil was originally permitted to export \$265 of duty free products to Argentina for every \$100 of duty free Argentine exports to Brazil. This limit was later revised to \$195 for every \$100 of automotive products it imports from Argentina. An "Automobile Commission" was formed to enforce the agreement. It is composed of members from the auto industry and the governments. Its most important functions are to regulate the compensation mechanisms of the accord.

It has been a win-win result for both countries but particularly so for the Argentinean industry. Before the agreement, Argentina's automotive industry was suffering a long period of decline. Its production of 300,000 units in 1980 had gone down to 100,000 in 1990 owing to deep economic crisis. Its exports were less than 1% of its production. After the implementation of Mercosur, its auto industry not only restored its earlier growth but has also taken an even higher trajectory. Its current annual production is reaching one million units with almost 60% being exported to 44 countries. The intra-industry trade between the two countries reveals even more impressive numbers with Brazil buying four/fifths of total exports of Argentina. Automobile overseas sales are equivalent to 13% of Argentina's total exports. The Brazilian auto industry also showed solid growth. In 1990 it produced

914,466 units. By 2011, it was producing 3,406,150 units or roughly increasing its production by 350% and becoming the fourth largest vehicle producer in the world. More recently it is the Brazilian automotive industry, which is finding it difficult to compete against the Argentinean industry and is trying to renegotiate some licensing arrangements to limit the number of cars entering their market.

Another good example is that of US-Canada Auto Pact, 1965. The Canadian auto industry had the same players as US but it was 1/10th the size. Resulting from lower economies of scale, it was uncompetitive. When the Agreement became effective, duties were eliminated on autos and parts, but the Canadian industry was protected through various safeguards. The agreement provided that for every car sold in Canada, one has to be built there. And each vehicle built in Canada has to have 60 per cent Canadian content in parts and labour. If the conditions were not met then tariffs were to be applied. Manufacturers were required to maintain a certain ratio between the net sales value of vehicles made in Canada and the net sales value of vehicles sold in Canada.

Prior to the signing of the Auto Pact, Canada produced 671,000 vehicles. By 2007, this number had reached 2.56 million. Meanwhile, OEM (Original Equipment Manufacturer) parts production improved from less than \$500 million to roughly \$35 billion. Canada's vehicle production to sales ratio increased from 1:1 in 1964 to 1.53:1 in 2007. At the same time, its share of North American production has grown to just under 16% in 2007 from 7.1% in 1964.

These examples show that when the automotive industries of neighbouring countries combine, they can develop synergies and both can benefit from such arrangements. Normalization of trade with India provides a good opportunity for this purpose. The governments of both countries can facilitate their automotive industry Associations to negotiate an agreement similar to that Argentina negotiated with Brazil or Canada agreed with the United States. Till such time that such an agreement is worked out, some tariffs may have to be maintained but gradual movement towards achievement of SAFTA should be made.

It should also be mentioned that there is a need to determine whether there is any justification in the fears of Pakistani auto-industry that they are not competitive against the Indian industry because of economy of scale. In a recent study, Garry Pursell compared the prices of locally assembled cars with similar Indian models¹. His key findings were that domestic ex-factory prices of the inexpensive car (the 796 cc Suzuki Mehran) exceeded Indian prices by about 32% in 2011. The price difference for the more expensive model (the Honda City) seemed to be about zero. If Pakistan was to source some of its components or CKD kits from India instead of Japan, it would considerably reduce the costs for the assemblers. This could mean that the price difference between the Indian and Pakistani manufacturers could be eliminated. Also this would allow higher capacity utilization, which at present stands at less than 50%.

Determine Long Term Priorities

Finally, it needs to be carefully examined where the Pakistani industry is best placed to have long-term comparative advantage in exports. Is it passenger cars, light commercial vehicles, buses and trucks, tractors, two and three wheelers or auto-parts? It is apparent that where passenger vehicles present many obstacles, other sectors provide a much more significant opportunity. As such the long term priority should be managed trade for passenger cars whilst a more rapid integration for tractors, motorcycles and auto parts where there may be more competitive.

The Next Steps

As a first step, a high level committee consisting of government and auto-manufacturers should be set up to consider the issue. The committee could consist of the following:

- Deputy Chairman, Planning Commission (Chairman)

¹ http://www.theigc.org/sites/default/files/Pursell%20et%20al_Pakistans%20trade%20policies.pdf
Auto industry with the support of the government should be encouraged to start negotiations with their Indian counterparts for an agreement along the lines of MERCOSUR and Auto Pact Agreements between Canada and the United States.

- Secretaries of Ministries of Commerce, Industry and Board of Investment
- Chairmen of FBR, National Tariff Commission and Engineering Development Board
- Representatives of Pakistan Automobile and Pakistan Auto-Parts Manufacturers
- The Committee should examine the main recommendations of the reports that it commissioned in 2004 and 2011 and try to facilitate their implementation. The Committee should also agree on what collaborative efforts can be done to boost the productivity of our auto industry.

This may involve the following steps:

First, the Pakistani auto-industry should look to diversify its sources of raw materials such as steel plates and plastic resins. It will be much cheaper to import them from India than from far off sources.

They can also consider sourcing components and CKD kits from India. This should be voluntary and left to the choice of each assembler. Currently Pakistan's auto-industry is highly dependent on Japan and Thailand for this purpose. This has given rise to a number of problems in the recent past. For example, as noted earlier when Suzuki's parent company decided to move its production to India, Suzuki-Pakistan motors had no choice but to close down its best-selling Alto car. India is the only country in the region that produces Euro-II compliant parts for Suzuki.

If Suzuki were allowed to import parts from India, Suzuki Pakistan would not only be able to export its best-selling Alto cars as they would become cheaper to produce and also they would meet the international Euro-II emission standards. When floods hit Thailand in 2011, there was an acute shortage of parts for assembling of Honda cars in Pakistan and they had to suspend their production for a while. The recent rise of yen against the dollar has been having a disproportionately large impact on prices of cars in Pakistan.

Auto-manufacturers should be allowed to procure new dies (molds) and other equipment duty free for replacement of old equipment.

Some framework agreement should be worked out with the Indian auto industry to allow use of technical training facilities.

With the reduction of these constraints, cost of producing automobiles will come down substantially. This would not only be good for the consumers but also for the assemblers who will be able to raise their production. With managed trade, imports can be limited to the level of present imports, which were approximately 55,000 cars last year. This would save considerable amount of foreign exchange and instead of old vehicles new could be imported.

Tractor industry

Industry dynamics

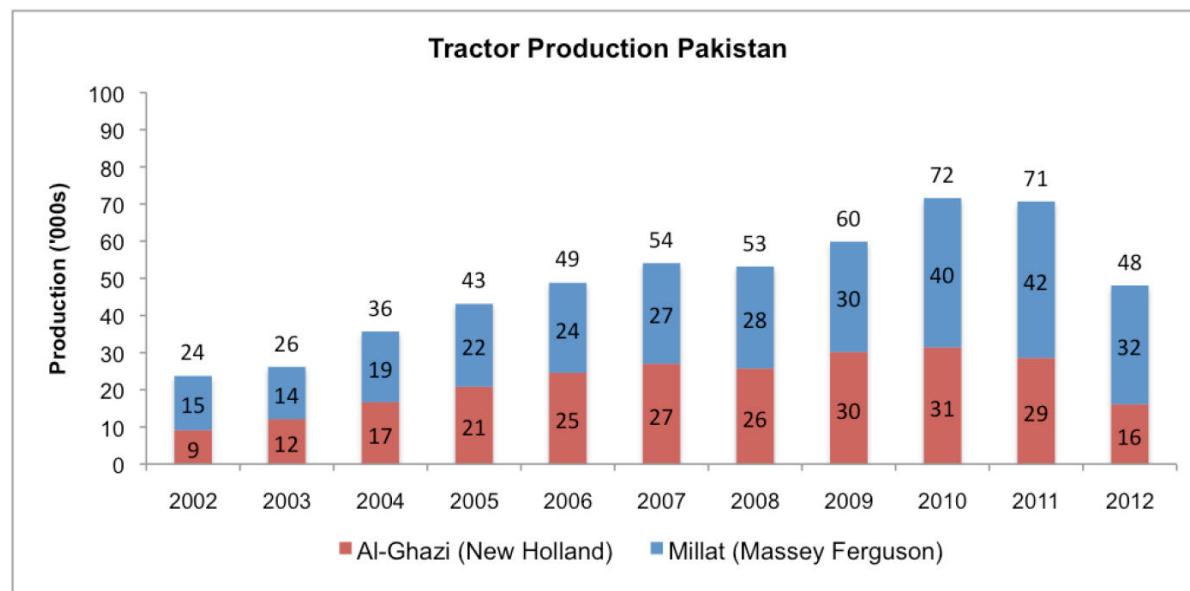
Tractor manufacturing has become a success story. Over the last five years, the industry has shown a compound annual growth rate of more than 9%. They work at full capacity and sell whatever they can produce. It is one of the very few industries that are not protected through any tariffs or other regulatory measures.

There are two major tractor-manufacturing companies, Millat Tractors Limited (MTL) and Al-Ghazi Tractors Ltd (AGTL). In addition, there are several small manufacturers such as John Deere (Agro tractors Ltd), Foton (Dewan group), Euro-F (PM autos), Belarus like tractor (Hero Motors, Hyderabad, Changfa Ali Corporation) and Ursus (Farmall Technology, Lahore).

MTL is the largest producer of tractors with a market share of almost 55%. It was established in 1964 for assembling and marketing Massey Ferguson Tractors. The company was nationalized in 1972 but was privatized through a management buy-out in 1992. After privatization, MTL set-up a modern plant and increased production capacity to 16,000 tractors per year on a single-shift basis. Its production has been increasing over time and in 2010/11, it produced its highest ever number of 42,000 tractors.

AGTL, the second biggest tractor manufacturer, was established by joint venture of PACO, Habib Group, and FIAT of Italy in 1983. Al-Futtaim Group of Dubai took over its management control in 1991. They manufacture New Holland (Fiat) tractors in technical co-operation with Case New Holland, the foremost manufacturer of agricultural tractors in the world. Their current annual production is about 32,000 units and is well supported by a widespread network of dealers and 3,000 mechanical workshops spread all over the country.

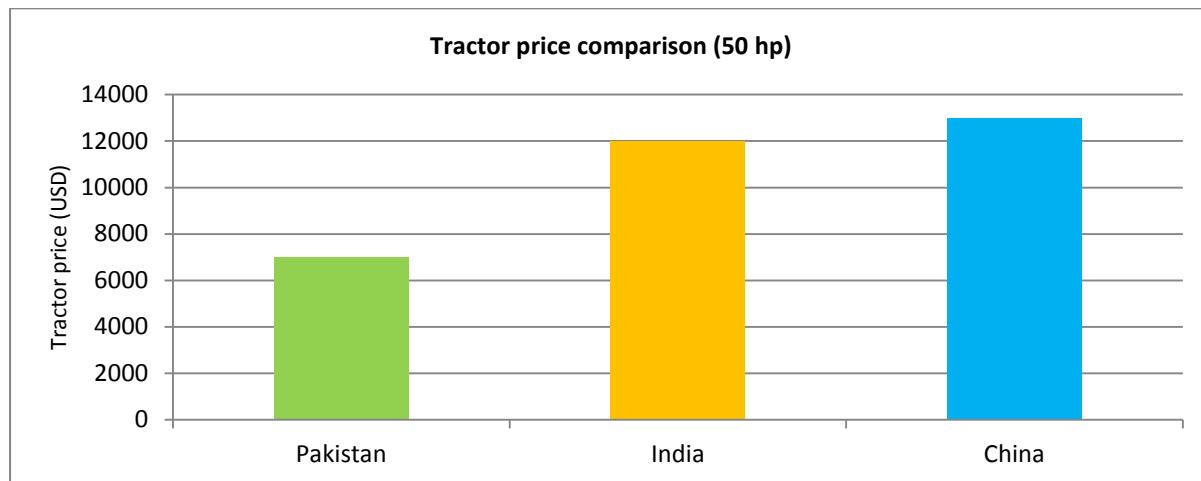
Both industry leaders, TML and AGTL, have experienced steady growth in production in Pakistan. From 2002 to 2011 they grew at an 11% and 12% CAGR respectively. Tractor production fell drastically in 2012 after the government imposed a 16% sales tax which has since been reduced to 5% and production resulting in production starting to ramp back up.



Source: PAMA 2012

Pricing

Massey Ferguson 240 (50 hp) is one of the most popular and economical tractors in the world. MF 240 is regarded as having easily available parts and services. Pakistan is the price leader in these tractors. In India, 31-40 HP tractors dominate the market followed by 41-50 HP.



Would the Indian tractor manufacturers be able to compete in the Pakistani market?

India is one of the largest manufacturers of tractors in the world. On an average, it produces 400,000 units, of which about 60,000 are exported. The Indian tractor industry has 13 national and a few regional participants. This market share is, however, concentrated amongst the top-five manufacturers, accounting for over 90% of total volumes. The four major manufacturers are M&M with a share of 41.4%, TAFE at 23.4%, Escorts at 11.4% and John Deere 7.5%.

Since tractors are importable free of duty and India is an established exporter of tractors, it would want a share in this market. However, it is likely to face several hurdles in breaking into the Pakistani market for the following reasons:

1. Indian manufacturers would need to establish a distribution network, which is not economical for a limited number of tractors that it may export initially;
2. Quite often the purchase of Pakistani made tractors is assisted through financial support such as low-interest loans from Agricultural Development Bank or other support through Benazir scheme;
3. Pakistani producers make cheap tractors and have an established market. It has not been easy for the Chinese or other manufacturers to get any substantial share in the local market;
4. So far the major Pakistani manufacturers, due to licensing arrangements with their principals, are not exporting any tractors. However, the private exporters are not covered by such licensing agreements and have been able to compete in many African markets due to the low cost of local tractors. The other reason for not exporting substantial numbers is that the local manufacturers can only meet the local demand and do not have enough surplus for exports.

It is therefore not likely that Indian tractors will flood in the Pakistani market. However, there may be opportunities for technical cooperation.

Would the Pakistan tractor manufacturers be able to compete in the Indian market?

Pakistani tractors and tractor parts are of competitive quality and of better price compared to the Indian manufacturers. Further, they are well-suited for the Indian Punjab terrain which is similar to that on the Pakistan side. However, Pakistan tractor manufacturers would face two major problems. First, currently their tractors do not meet Euro II emission controls. Secondly, tractors are on the sensitive list of India and it also levies a duty of 10% on import of tractors. If Pakistan was able to improve emission controls and also get this duty eliminated, it would be able to compete in the Indian market.

Tractors

HS Code	Product description	Year: 2011, Unit: Million USD			RCA		NRCA		
		Pakistan exports to world	India exports to world	World exports	Pakistan	India	Pakistan	India	
8701	Tractors (other than tractors of heading no 87,09)	29.2	752.5	54,104.9	0.38	0.82	(0.45)	(0.10)	
	All products	25,343.8	301,483.3	17,855,727.0					

The RCA and NRCA show comparative advantage for India. This is due to the fact that the trade between the two countries was restricted and Pakistani assemblers were not producing tractors meeting global emission standards. Furthermore they were only focusing on the local market.

Conclusions

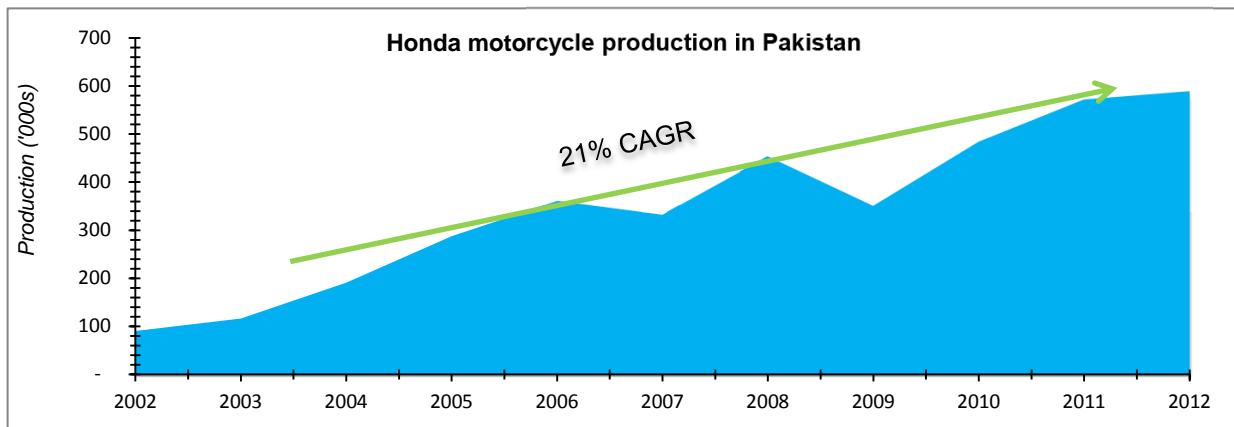
Pakistan appears to have some edge in tractor production. Pakistani tractors and tractor parts are of competitive quality and of better price compared to global players. Further, they are better suited for local market conditions. It is unlikely that Indian tractor manufacturers would be able to penetrate the Pakistani market to any significant degree. Pakistani tractors are already being exported to several other markets on the basis of their cost competitiveness. If Pakistan were to expand the production of tractors and make them compliant with the global emission standards, it may be able to export to India. It is therefore recommended that Pakistan should negotiate the elimination of duty on tractors as Pakistan already allows duty-free import of tractors.

Motorcycle industry

Industry dynamics

Motorcycle Industry is another success story. There are currently 72 manufacturers producing about 1.6 million motorcycles in Pakistan in June – July 2012. This represents an increase of almost sixteen fold during the last ten years. No other engineering industry has seen such a phenomenal growth. Both Japanese branded as well as local motorcycles shared this growth.

Honda which currently enjoys ~37% of the total market saw its production grow from 90,111 units in 2001-2002 to 588,106 units in 2011-12 or 21% CAGR.

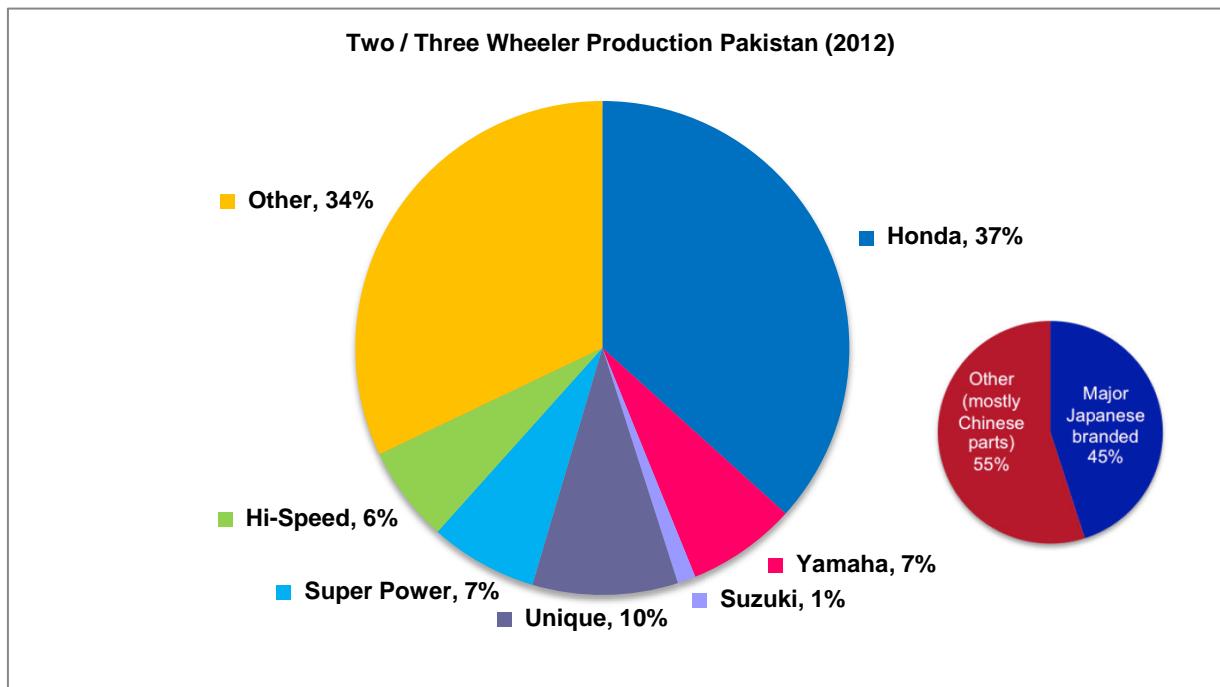


Source: PAMA (July 2012)

The distant second Japanese brand Yamaha, which currently enjoys ~7% of the total market, also saw its production grow to 114,845 units in 2012. Another Japanese well-known name in automotives, Suzuki (21,389 units), is also producing motorcycles but its share in this sector is negligible. Locally manufactured motorcycles assembled with Chinese components now have about ~55% market share.

Pakistan has a unique advantage in that a single type of engine (70cc), with essentially the same body parts and design, dominates its market. The 70cc motorcycle accounts for over 80% of Pakistan's domestic market. The Indian market is predominantly based on 100 to 125cc engines, which account for approximately 65% of its domestic market. India has a much larger market with over 13.3 million units sold in 2010-2011. Hero Motor Corp accounted for 55% of India's market share.

In 2010-2011, Pakistan had an installed capacity of 2.5m whereas India had an installed capacity of 18.7m. This equated to 64% and 80% of capacity utilization in 2010-2011. Two wheeler penetration per 1000 persons in Pakistan is 12/1000 and 48/1000 in India (2010-2011).



Source: Motor World (2012)

Pricing

Prices of local brands are about 2/3 of the Japanese branded motorcycles. For example, prices of the most common model Honda CD 70 are Pak Rs 65,900 (US\$ 689) as against Rs 44,000 (US\$440) for a local 70cc brand.

Pakistani manufacturers have the competitive edge in 70cc engines from Indian makers but in 125 cc engines they are about the same price. For example, Honda CG125 in Pakistan is Pak Rs 96,500 (US\$ 1,010) versus a comparable Honda Shine 125cc is Ind Rs 52,000 (US\$ 986). Pakistan does not produce medium or big sized (beyond 250 CC) motorcycles.

Industry feedback

In response to a survey, a sample of major motorcycle manufacturers in Pakistan showed that Pakistani manufacturers see a huge market potential in India. However, they remain apprehensive about softening trade barriers with India without ensuring that the playing field is levelled. The concerns lay in both non-tariff and tariff barriers.

India has a homologation policy that states that all imported vehicles and parts coming into India must meet certain requirements. The process generally takes more than nine months for certification of a part manufactured in India. Noting the experiences of other foreign manufacturers in India, Pakistani manufacturers see little chance in meeting these standards. Other non-tariff barriers include the cost of approvals, need for permissions, certification requirements, and emissions standards.

Combined with the high tariffs, these measures make trade in two/three wheelers for Pakistani manufacturers prohibitive. Pakistan manufacturers do however; see a win-win situation given a pragmatic and step-by-step approach is undertaken for opening up trade with India.

Will there be any bilateral trade in motorcycles?

Branded motorcycles in India and Pakistan are of similar price and quality. As a result, there would be little ability for India or Pakistan to make significant foray into each other's markets through branded motorcycles. Pakistan does have a competitive advantage for non-branded motorcycles versus India but it will face two problems. First, it may not be easy to meet the Indian homologation requirements as most of the Pakistani non-branded motorcycles do not meet the Euro II emission standards. With the right marketing strategy and improvement in emission controls, Pakistan can likely penetrate the Indian market. This is especially true for Indian rural consumers who opt for smaller engines such as the 70cc.

Pakistan assemblers also enjoy comparative advantage in terms of higher duty rates. Whereas Pakistan charges a duty of 45%, India's duty rate for SAFTA countries is only 10%. Therefore, while it would not be feasible for India to export to Pakistan because of high tariffs, Pakistan does not face this problem. Pakistan can afford to gradually reduce duty on motorcycles, as they are competitive even without such high tariff levels.

Motorcycles

HS Code	Product description	Year: 2011, Unit: Million USD			RCA		NRCA	
		Pakistan exports to world	India exports to world	World exports	Pakistan	India	Pakistan	India
8711	Motorcycles, side-car	11.7	1,230.7	20,036.2	0.41	3.64	(0.42)	0.57
	All products	25,343.8	301,483.3	17,855,727.0				

These numbers show a major comparative advantage for India but this is mostly due to the fact that Pakistani assemblers have so far been focusing on meeting domestic demand. Since they have built a good domestic base, Pakistan should now be looking for export markets.

Conclusions

Pakistan is well placed to compete with the Indian assemblers. With the right marketing strategy, Pakistan should be able to export substantial quantities to the Indian market. However, Pakistan needs to rationalize its tariffs and also make efforts to meet international emission standards if the industry is to continue on its growth path and enter the export market.

Auto parts

Industry dynamics

In engineering sector, auto-parts hold the most promise for Pakistan. Due to the indigenization policies followed over the year, the local auto-parts manufacturers have developed capacity to produce automotive parts that are of international quality. Well-known brand names such as Suzuki, Toyota, Honda, Massey Ferguson, New Holland, Hino, Isuzu, and many OEM have been heavily relying on these parts. The fact that international brand tractors and motorcycles are assembled mostly (over 90%) from local auto-parts shows that the local industry is highly developed.

A large range of auto parts and accessories are being produced in Pakistan. These include air conditioners, lead-acid batteries, tires and tubes, radiators, rims, break-drums, wheel-hubs, assembly brackets, pistons, engine valves, gaskets, crankshafts, camshafts, shock-absorbers, struts, steering mechanism, cylinder head, bumpers, gears, cylinder liners, electrical instruments and panels, blinkers, lights, doors and door-locks.

Normalization of trade with India provides a big opportunity to tap into that market. There are many reasons for optimism as Pakistani vendors could successfully get a considerable share of that market. Some of these factors are listed below:

Pakistan's competitive factors	
1	Local manufacturers already producing quality auto parts meeting global standards
2	Globally competitive in prices
3	Kept pace with phenomenal growth of motorcycles production over last 10 years
4	More than 1,600 vendors producing auto-parts including over 400 registered vendors
5	Almost 10% of vendors in the organized sectors are also successful exporters. Export markets include many developed countries such as USA, Italy, UK, Germany, Spain and many developing countries such as the UAE, Sri Lanka, Bangladesh, Malaysia, Brazil and Turkey
6	Exports are picking up momentum and have grown more than three-fold over the last 6 years from US \$25 million in 2005 to US \$80 million in 2011
7	Demand for auto-parts is growing many folds in the neighboring countries. Indian auto-parts markets is estimated to grow to US\$60 billion by 2015 and US\$100 billion by 2020
8	Pakistan has geographical proximity to major emerging markets
9	Due to opening of trade with India, auto-parts manufacturing clusters which are mostly located in Lahore and Gujranwala can have access to cheaper and quality raw-materials such as pig iron, coal, coke, silicon manganese, aluminum and foundry chemicals
10	There will be many more opportunities to form joint ventures with international companies that may want to benefit from Pakistan's SAFTA status

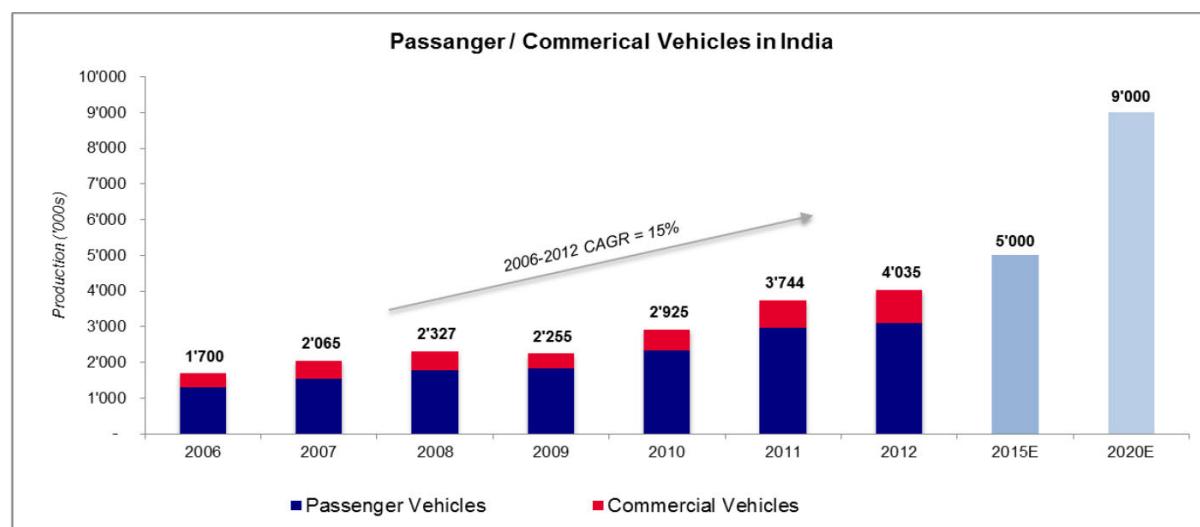
Already some exporters are successfully exporting auto parts to India. However, in all these cases there were strict requirements to meet quality controls and it often took months to do so. For many SMEs it may not be possible to bear the expense of going through a long testing phase. It would therefore be advisable that SMEDA, PAAPAM, TDAP and Engineering Development Board set-up a facilitation centre or an independent technical testing center to check quality standards and only those meeting the required quality be allowed to be exported. Earlier when the government wanted to encourage use of ISO 9000 standards, it provided direct financial subsidization.

As a first step, potential auto-parts exporters should be encouraged to get certified for ISO/TS 16949 standards. Some of the costs for doing so could be met by the proposed center or through Export Marketing Development Fund available with TDAP. ISO/TS 16949 standard was developed by the International Automotive Task Force (IATF) and the "Technical Committee" of International Standards

Organization and goes a long way in harmonizing the country-specific regulations of Quality-Management-Systems.

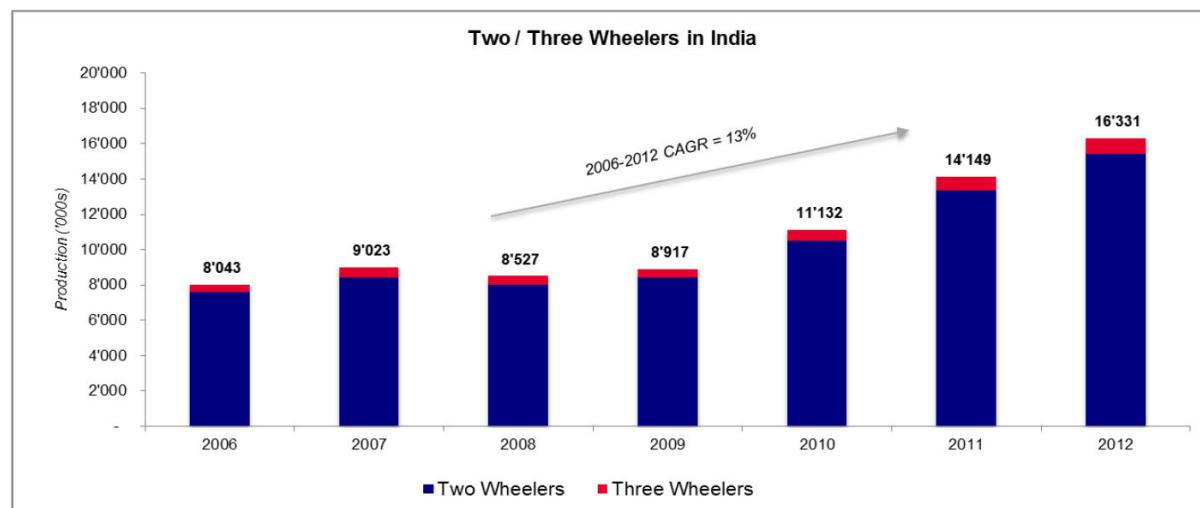
Automotive Sector in India

The Indian automotive industry is one of the largest in the world, with approximately 50 million vehicles on the road. It is also the fastest growing in the world with SIAM forecasting India's annual vehicle sales to increase to 5 million by 2015 and more than 9 million by 2020. From March 2001 to March 2012, India produced 3.1 million passenger and 912,000 commercial vehicles. According to a 2011 study by PAAPAM, the Indian auto parts industry has appropriately 500 firms in the organized sector producing practically all parts and more than 10,000 firms in small unorganized sector.



Source: SIAM 2012

India's automotive industry is dominated by two wheelers (motor cycles), which in 2012 produced nearly four times than the amount of vehicles. Of the total Indian automotive market share, two wheelers account for 76% and passenger cars at approximately 15%. Commercial vehicles and three wheelers share about 8% of the market between them.



Source: SIAM 2012

India exports automobiles around the world, of which its top 5 markets are US (~9%), Italy (~6%), UK (~4%), Sri Lanka (~4%) and South Africa (4%). India is aiming to grow its export market from US\$3.8 billion in 2009 to US \$27.5 billion by 2020. During the same period, its domestic aftermarket is

expected to grow from US\$4.3 billion to \$12.8 billion². Pakistani auto vendors should keep these estimates in view and try to get a percentage of this growing market.

Will there be any significant bilateral trade in auto-parts?

The local auto-parts manufacturers have developed capacity to produce automotive parts that are of international quality. Already some vendors are successfully exporting auto-parts that are well accepted by the Indian assemblers. These include Millat Equipment Ltd. (tractor parts e.g. counter shaft and carrier planetary pinion), Adamjee Engineering Ltd. (oil pump gears), Mannan Shahid Forgings Ltd. (gearbox support parts) and KSB Pumps (centrifugal pumps).

While customs duty rates in Pakistan are rather high - ranging between 35 to 50%, they are relatively low at 8 -10 % in India. This duty has been further reduced under the Indo-Asean Free Trade Agreement (FTA) to 5% from January 2013 and will be completely eliminated in December 2013. In India, there is an additional charge of CVD of 16% (on those products that are produced in India), special CVD of 4% and educational fess of 3% but these additional charges are adjustable for the local assembler. If Pakistan could rationalize its tariff rates and negotiate removal of non-tariff barriers in India, both countries could substantially increase their bilateral trade in auto-parts.

Parts and accessories for motor vehicles

HS Code	Product description	Year: 2011, Unit: Million USD			RCA		NRCA	
		Pakistan exports to world	India exports to world	World exports	Pakistan	India	Pakistan	India
8708	Parts and access of motor vehicles	26.4	2,756.6	112,900.0	0.16	1.45	(0.12)	(0.28)
	All products	25,343.8	301,483.3	17,855,727.0				

Although RCA and NRCA show that India has a substantial edge, its market is huge and growing. Pakistani exporters should target at least 5 % of the market that could result in export of \$5 billion by 2020.

Conclusions

Pakistani auto-parts manufacturers can successfully compete and grow many-fold in the vast Indian market. However, they would only be able to do so if they are provided with enabling environment. This would mean rationalizations of tariffs on import of raw materials, parts that are often incorporated in the finished products, dies, and machinery for producing high quality parts. Also there will have to be more quality control. A public-private auto sector-testing centre should ensure that only parts of the highest quality are exported.

² Full details can be seen at http://acmainfo.com/docmgr/Press_Releases/ACMA_ppt_Feb_8_ver_4_0_Edit.pdf

ELECTRIC FANS



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Industry dynamics

Pakistan's fan industry is well placed to benefit from normalization of trade with India. There are 450 manufacturing units with an estimated production capacity between 9.5 to 10 million fans. On average approximately 8 million fans are produced annually of which 90% are for domestic use and just 10% exported. Pakistani fans are primarily manufactured around Gujrat (70-75%) and Gujranwala (30-35%).

Pakistan's fan industry is highly fragmented with the six largest companies responsible for around 70% of the total annual production. These companies are large scale manufacturing units that have composite integrated system i.e. from motor winding to high-pressure dies casting.

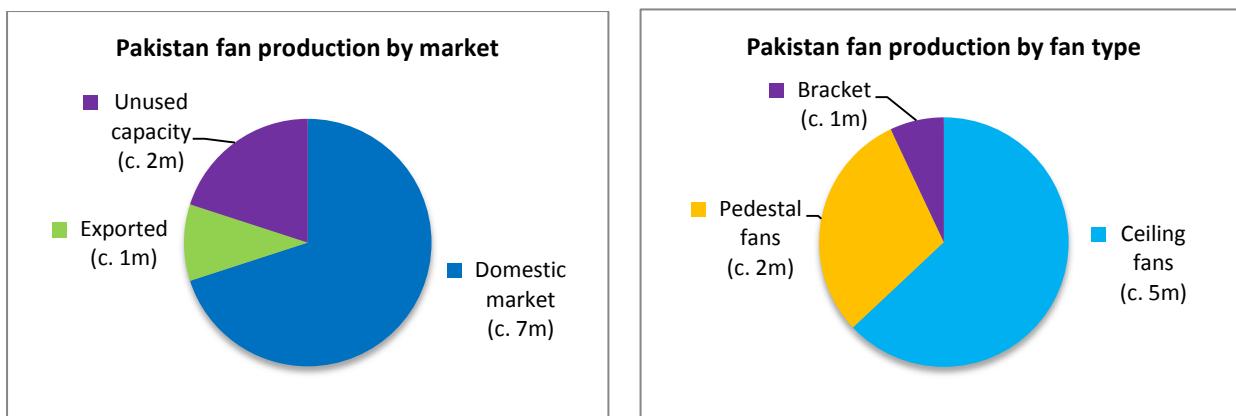
A brief description of each of these six large brands is given below:

Company name	Comment
	<ul style="list-style-type: none"> One of the largest manufacturers of quality electric fans in Pakistan Exports c. US\$12 million annually, nearly 1/3 of total fan exported from Pakistan, to more than 30 countries Has won 12 Export Trophy Awards in Pakistan and is certified by UL (Underwriter Laboratories, USA) to export fans in USA and Canada
	<ul style="list-style-type: none"> Established in 1975 as a washing machine manufacturer, now is the market leader for washing machines Produces fans, room air coolers, heaters, water dispensers, motorcycles, insulation and packing materials, microwave ovens, air conditions, automotive parts, three-wheelers, and gas stoves Strategic partner of Procter and Gamble in Pakistan Has won FPPCI export trophies and recently granted the Brands of the Year Award
	<ul style="list-style-type: none"> Wahid Industries, a private medium sized fan manufacturer, operates under the "Pak Fans" brand Has diversified into washing machines, driers, enamelled copper wire and room air coolers Exports to mainly the Middle East, Europe and Africa, with increasing growth in export sales yearly Has won Pakistan's highest export trophy award for the last 11 years consecutively
	<ul style="list-style-type: none"> Rafiq Engineering, a private medium sized fan manufacturer, operates under the "Royal Fans" brand Manufactures washing machines and room coolers. Exports 10 different category of fans (120 models) with an efficient packaging system that allows minimum freight cost per piece ISO9001 certified
	<ul style="list-style-type: none"> Has over 35 years of manufacturing experience Manufactures electric fans, washing machines, energy saves, voltage stabilizers and other home appliances
	<ul style="list-style-type: none"> S.M. Younus Electrical Industries (Welco Fans and Washing machine) was established in 1980 Manufacturing is specialised in fans and washing machines ISO9001 certified

Source: Company websites

Although these firms enjoy local branding power, none of them have been able to create an international brand name. The exported products are normally just branded as "Gujrat Fans".

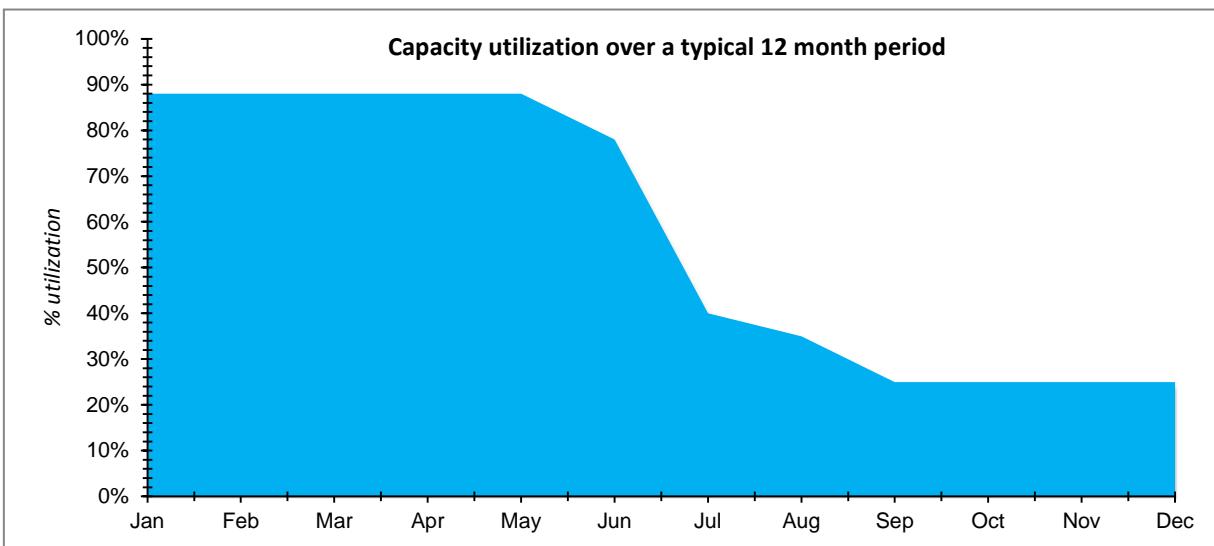
Most production is of domestic fans i.e., those consuming less than 125 watt of energy as against Industrial Fans (HS 8414.59) that consume more than 125 watts. Approximately 63% of production is of ceiling fans, 30% to pedestal fans and remaining 7% to bracket fans.



Source: TDAP (2011)

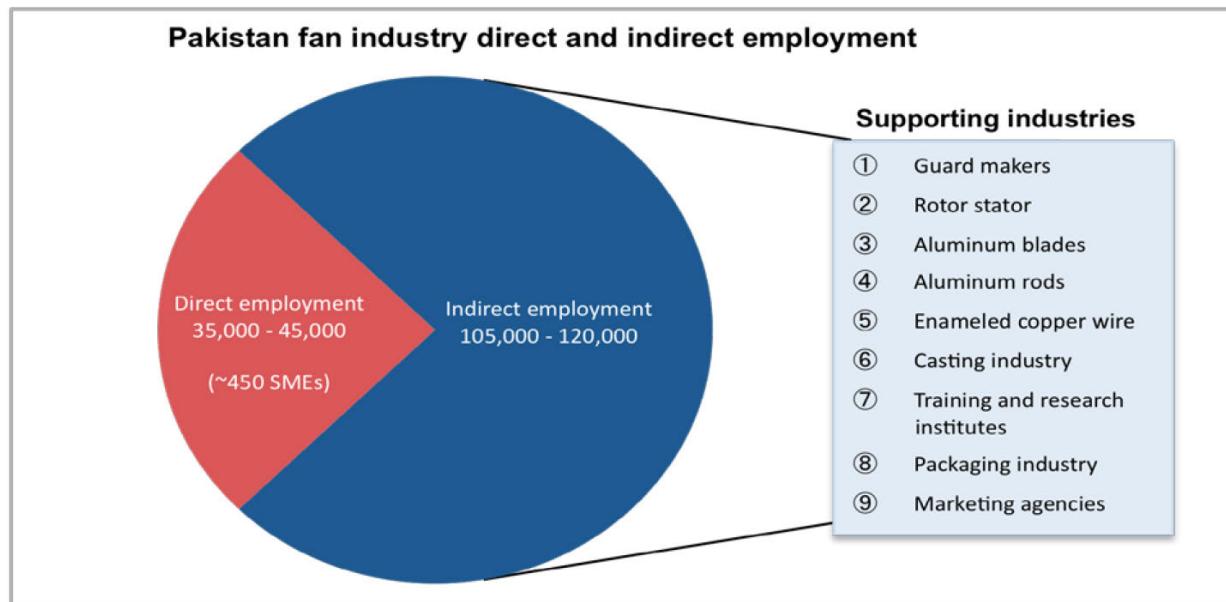
Seasonality

As the majority of sales are made to the local market, where the demand only exists between January to early July, a large number of factories have to shut down operations in the remaining months. As a result, their capacity is underutilized and many workers are not willing to specialize in the fan industry because of these cyclical job prospects. Few firms do manage to keep employees engaged throughout the year by shifting production into related industries. If additional export markets become available, the capacity can be easily doubled without significant additional financial expense. Additionally, this would lead to a more efficient and competitive fan industry.



The total direct employment within the fan industry is thought to be between 35,000 and 40,000 workers, mostly semi-skilled in light engineering works. If production could be continued throughout the entire year, it would not only lead to an increase in a specialised labour force but also create significant employment opportunities.

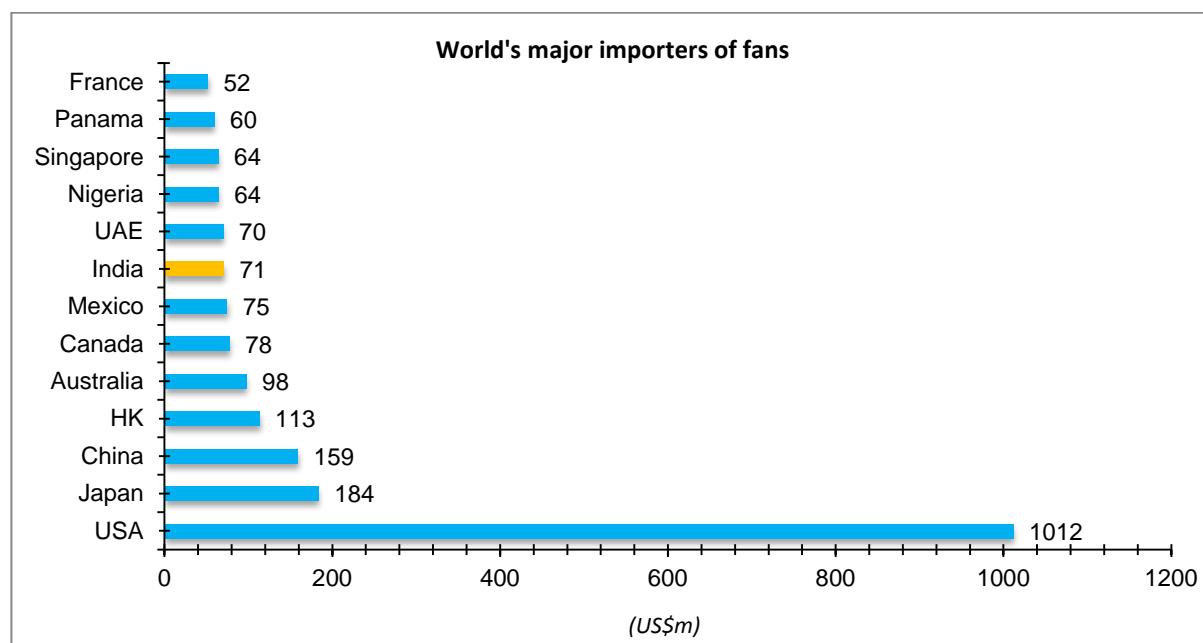
Furthermore, the Pakistan Electric Fan Manufacturing Association (PEFMA) projects that for every one person directly employed in the fan industry, another three indirect opportunities are created elsewhere. Given the fan industry relies on a wide range of supporting industries, many other indirect employment opportunities will also benefit. Currently direct employment in the fan industry is 0.4% of the total manufacturing employment (formal sector), and with indirect employment it makes up to 1.5% of total manufacturing employment.



Sources: TDAP (2011), LUMS (2010), PEFMA

Global markets

With the construction boom in India, demand for fans is growing at more than 10% annually. At present, its market is quite large and is estimated to be at c. 30 million fans per year. In 2010, in addition to its own domestic production, India imported fans worth US \$71 million. China has the majority share of exports to India, followed by Vietnam.



Note: Includes both consumer and industrial fans. 2010-year end figures

Source: TDAP (2011)

Chinese fans are considered (by some retailers) to be of lower quality compared to Pakistani fans. This is mostly because Pakistani fans are comprised of usually pure metals whereas China has shifted to using cheaper composite and adulterated materials. In terms of productivity, China has a large economy of scale advantage to Pakistan. A medium sized factory in Pakistan produces on average 500 fans a day. This is extremely low compared to Chinese manufacturers that produce, on average, 35,000 fans per day.

As a result of its cheap pricing, high productivity and aggressive push into world markets, China has been able to capture around 70% of the total world market for fans. However, Pakistan is able to effectively compete in pricing with China in the lower end of the market; and may even increase market share given its quality advantage in relation to China. Pakistani fans are considered better in terms of their air blow capacity and coverage than their Chinese counterparts. Furthermore, Pakistan's fan industry has successfully warded off competitive threats from Chinese and other foreign manufactures in its own domestic markets.

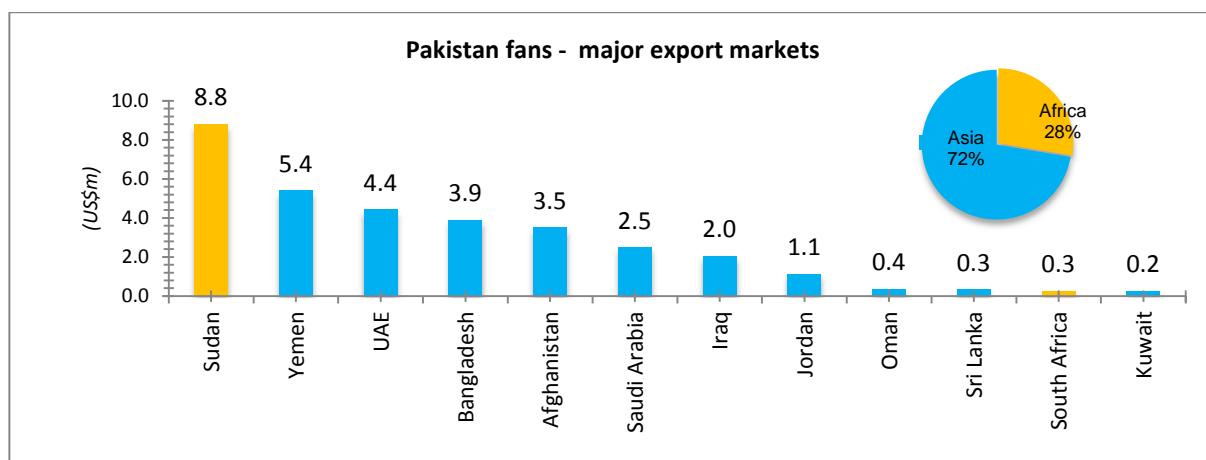
Entering the Indian Fan Market

Pakistan has not yet been able to make any inroads into the Indian market although it has a significant price advantage. For example, a ceiling fan sized 56" is available for retail sale in Pakistan at US\$25 (Pak Rs 2370) whereas the same size Indian-made fan is available in the Indian market for US \$40 (Indian Rs 2149). Since the poorer segment of the society normally uses fans, this difference in price provides substantial incentive for the largest market to preferably purchase Pakistan made fans.

Pakistani manufacturers have an advantage of lower freight costs as well. They are already exporting fans to several countries in the Middle East and Africa. The above mentioned six main companies are familiar with the technicalities involved in exports and meeting international standards. Moreover being located near to the Indian border, their cost to export is much less than their competitors.

Another advantage for the local manufacturing units is that the vast majority of them are located in a cluster around Gujranwala and Gujrat. Therefore, they have easy access to trained labour, raw materials and well-developed infrastructure. There are also a number of technical institutes to provide training. Several export facilitation agencies and banking facilities are also available locally.

Currently Pakistan is exporting fans to several countries but mostly to the Middle East and Africa. Its exports during 2010/11 were worth US\$38 million. Although in overall terms this is not significant but the export growth has been quite substantial over the last ten years. During 2000/01, the export was a mere \$3.9 million and it has grown almost tenfold since then.



Note: Includes both consumer and industrial fans. 2010-year end figures
Source: UN Commodity Trade Statistics, TDAP (2011)

Fans are charged a 10% customs duty in India. Pakistani exporters currently do not have any tariff advantage over other countries as fans are on the Negative List of SAFTA. However, this is likely to change soon as the scope of SAFTA agreement expands and duty rates are coming down. There is also a CVD of 16%, additional CVD of 4% and education cess of 3% but these taxes are also charged on domestic products. Thus on this account, Pakistani fans do not suffer any additional penalties.

RCA and NRCA

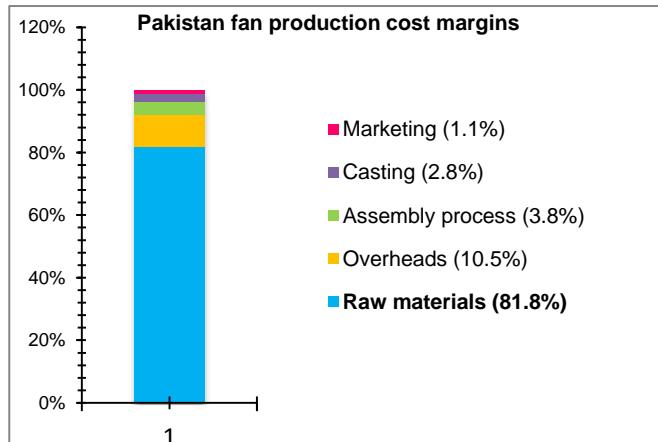
Electric fans

HS Code	Product description	Year: 2011, Unit: Million USD			RCA		NRCA	
		Pakistan exports to world	India exports to world	World exports	Pakistan	India	Pakistan	India
841451	Fans: table, roof etc w a self-cont elec mts or an output nt excde 125 W	35.6	36.6	3,353.6	7.47	0.65	0.76	(0.21)
	All products	25,343.8	301,483.3	17,855,727.0				

The above figures show Pakistan has a considerable advantage over India in exporting fans.

Currently approximately 82% of the cost of producing fans in Pakistan is from raw materials. Almost 50% of these raw materials are imported, which not only significantly increases the cost margins of fans; it also adds an element of cost variability.

The most important raw material is electric steel sheets. Since the imported steel sheet is almost five times more expensive, most the manufacturers use local scrap steel (including oil drums) to produce the rotor. These impact upon the quality of the product.



Source TDAP (2011)

If the steel sheets were imported from India, it would be economical for most of the manufacturers to use imported steel sheet. It would not only improve the quality of fans but would also make them even more competitive.

Conclusions

Pakistan has successfully built a fan industry to meet all of its local demands. It has also significantly grown in exports to its major markets in Africa and the Middle East. However, domestic demand has slowed down while global demand has increased, especially from neighbouring India. Pakistan's seasonal manufacturing cycle results in a semi-specialized labour force and plenty of unutilized capacity. Opening up trade with India would drive increased investments in technology and labour training from Pakistani manufacturers. It may also lead to industry consolidation as a way to build an economy of scale.

Pakistan's main competitors in the Indian market would be Chinese and Indian manufactures. Pakistan should be able to effectively compete and win a large share of market from Chinese and Indian manufactures given its better quality and competitively priced fans. It is estimated that if Pakistan is given duty free access to the Indian market and also it can import duty free electric steel sheets, it can easily export fans worth \$50 - 100 million to India over the next 3-5 years.

SURGICAL INSTRUMENTS



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Industry dynamics

Pakistan's surgical industry is one of the few that exports over 95% of its output to developed partners such as the United States and the European Union. The city of Sialkot produces over 99% of all Pakistani-made surgical instruments. Along with Tuttlingen in Germany, Sialkot ranks as one of the world's two leading centres for the manufacture of hand held stainless steel surgical instrument. Korea, France, Hungary, Poland and England also manufacture surgical instruments but their exports are negligible.

Pakistan's surgical industry comprises of over 2,300 companies. These companies can be categorized into four main segments – large sales (30 firms), medium sales (50 firms), low sales (150), and vendors (2,000).

Over 300 of these firms have ISO-9002 Certification and about 250 have Certification of Good Manufacturing Practices.

Segment	No of firms	Annual Revenues (US '000)	Investment in Equipment (US '000)
Large sales	30	600 – 1,000	500-1,000
Medium sales	50	100-600	100-250
Low sales	150	10-100	10-50
Vendors	2000	10 - 15	na

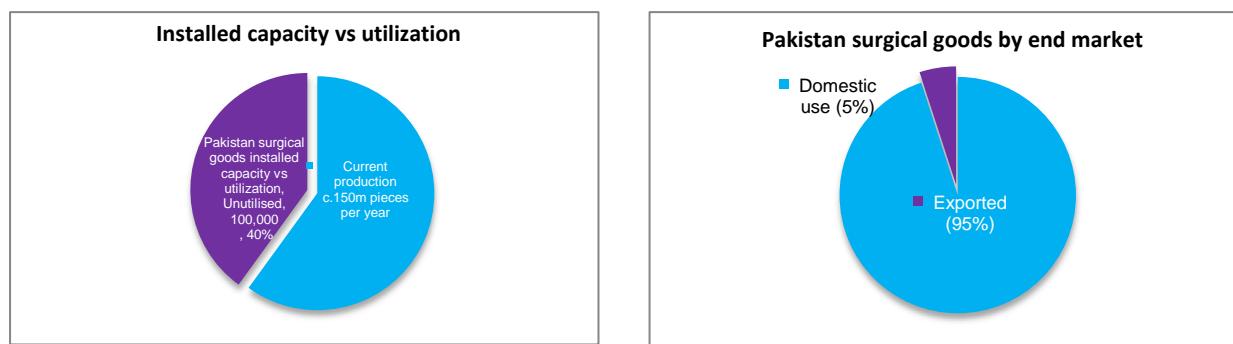
Surgical instruments manufactured in Pakistan	
Diagnostic	Instruments
Anesthesia	Suture
Vaccination	Plaster
General	Bone Surgery
Neurology	Oral Instruments
Tracheotomy	Tonsil
Cardiovascular	Sterilization
Lung Surgery	Urology
Dermatology	Gynecology
Ophthalmology	Obstetrics
Otology	Intestinal & Stomach
Rhinology	Rectum

Note: Aside from all of the above, there are 800 – 1,000 traders who do not have their own production facility

Source: Rawalpindi Chamber of Commerce and Industry

The sector employs between 100,000-150,000 direct and 400,000-450,000 indirect employees. The workers can be mostly classified as skilled and semi-skilled, however employment is unstable as there is high number of temporary jobs. A large portion of the work force is comprised of second, third or fourth generation workers from the same family.

Pakistan's surgical industry is estimated to have the capacity to produce 250,000-275,000 million pieces per year of which only 150 million pieces per year are produced. Revenues have been growing each year totalling approximately \$300 million in exports for 2011-2012.



Source: TDAP (2011) Source: SIMAP (2012)

Strategic rationale	Comments
Quality	▪ Quality of surgical goods produced at Sialkot is high and accepted throughout the world
Manufacturing flexibility	▪ The industry is already producing over 100,000 instruments of 1,000 different varieties and can easily adjust to any specific Indian requirement
Globally competitive	▪ Most of the manufacturing units are clustered in a limited area of about 30 sq km which makes it easier to access raw materials, trained labour and engineers
Location	▪ Sialkot is located near the Indian border resulting in much lower transport costs for Indian importers than from rest of the world
Reduced tariffs	▪ Customs duty on import of surgical instruments in India is 8%, which is likely to come down as implementation of SAFTA makes further progress ▪ There is an additional CVD of 16% and an education cess of 3% but those taxes are also applied to domestic manufacturers in India
Eliminate middle-men	▪ Most exports to the EU, especially for reusable instruments, go through middlemen in Germany ▪ As a result even those instruments which are comparable to those made in Tuttlingen are sold at a fraction of the price of German-made instruments ▪ In case of India, the profit of the middleman can be reduced substantially
Growing demand	▪ India is developing medical tourism and thus its demand for medical instruments is growing fast which Pakistan can easily tap into
Technical advancement	▪ The local industry could benefit from India sharing its information technology, in which it is regarded as a world leader
Sales distribution	▪ It is much easier for the local manufacturers to establish contacts with importers in India as compared to its current markets

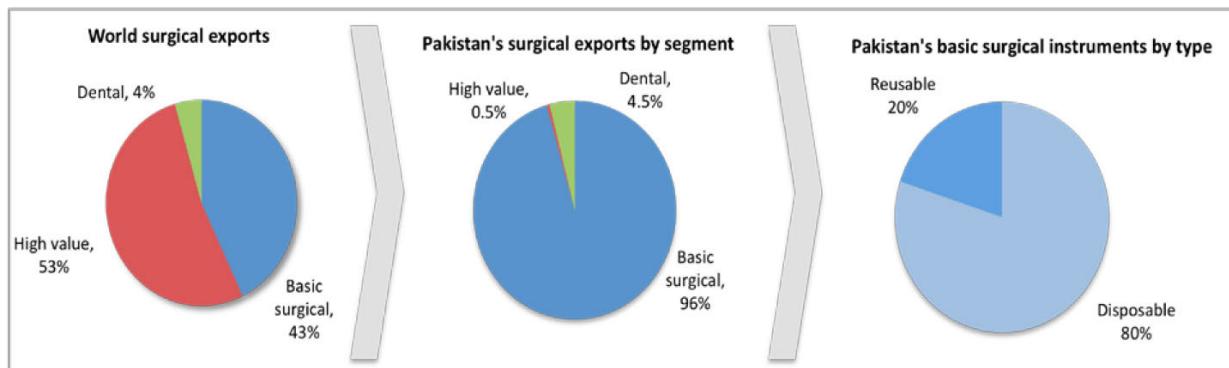
Export markets

Most Sialkot based firms subcontract the initial production of instruments to workers employed in small workshops. They then bring production in-house for finishing and quality checking against EU or USA standards before exporting. These exports are often sent to German firms in Tuttlingen who act as middlemen and trade with end users.

The German firms then brand and package the products and market them to other large markets in the USA or Western Europe, usually at a considerable mark-up. For example, a pair of fine surgical scissors will cost \$1.00 to produce in Pakistan, be exported to Germany at a price of \$1.25, and then can be sold to a hospital for close to \$67.00. Pakistani products do fetch higher prices than their Chinese counterparts (e.g. Chinese disposables are c. US\$ 0.35). However, a substantial profit margin is lost, as manufacturing firms in Pakistan do not have the infrastructure or marketing presence to allow direct trade with the end users.

The world export market for surgical instruments is estimated to be over US\$30 billion. More than half of this is for high value products: c. 43% is for basic surgical products and remaining 4% for dental products. Approximately 96% of Pakistan's surgical instruments production falls under the basic surgical category of which c. 80% is disposable and c. 20% is reusable. Basic surgical instruments are in the lower end of the market where the instruments are often commoditized. However, quality, pricing and branding remain a major driver of sales.

TRADE OF INDUSTRIAL GOODS WITH INDIA: OPPORTUNITIES AND CHALLENGES FOR PAKISTAN



Sources: TDAP, SIMAP, exports as of 2010-2011

Pakistan's exports of surgical instruments have shown healthy growth over the last seven years. Exports grew from US\$95 million in 2004-2005 to around US\$300 million in 2011-2012 - a compound annual growth rate of 18%. Pakistan exports in broadly three categories that include:

- HS Code 9018 – Instruments for medical, surgical and dental
- HS Code 9021 – Orthopaedic appliances
- HS Code 9022 – Equipment using X-rays, alpha, beta, gamma rays

The majority of Pakistan's exports fall in the 9018 category.



Source: SIMAP (2012)

The leading buyers of Pakistani surgical instruments are the USA, Germany, and the United Kingdom (UK). Exports to each of the major emerging developing countries such as India, China and Brazil were around \$5 million each. Pakistan has continued to rely on the EU and US for the majority of its exports, which has its own set of challenges as the quality standards and other requirements are much higher.



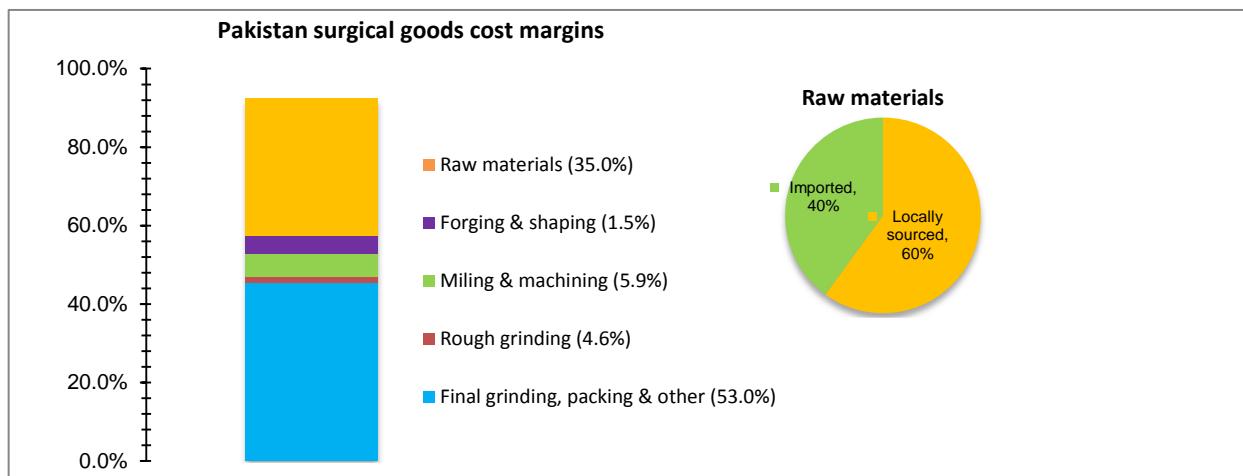
Source: SIMAP (2012)

Industry challenges

Pakistan is earning far less than its potential from surgical good exports for several reasons. One of the biggest contributing factors is the lack of marketing and branding. Pakistani made surgical exports serve developed markets around the world, which demand precise and high quality products. However, most times the end-users do not even know that the instruments are Pakistani made. The instruments are often stamped for example, "Made in Germany" if made with German raw materials and then marketed at elevated prices. Although Pakistan has been producing surgical instruments for over six decades, it still does not have an international distribution network or a globally recognised firm brand name.

Other challenges for the industry in Pakistan are a lack of adequate technologies, a lower level of productivity, a shortage of skilled employees, and an inability to shift production from the lower end market to higher value sophisticated products. Pakistani manufacturers will need to address compliance, testing and certifications to move up the value chain.

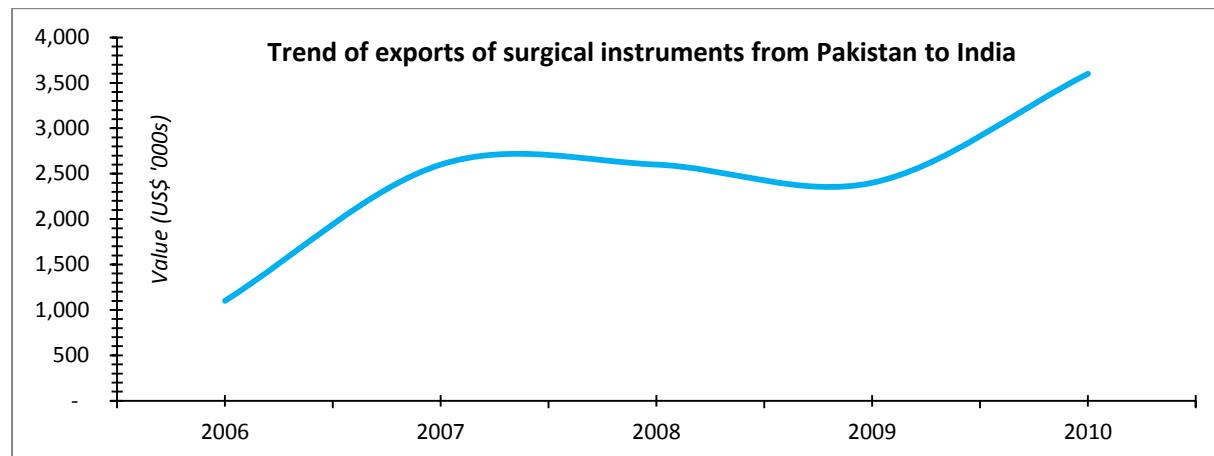
Pakistan is also facing a squeeze in the margins as the costs from raw materials continue to rise. Approximately 35% of the cost of manufacturing is from raw materials, of which 60% is sourced locally and the remaining 40% imported, mostly stainless steel from Germany.



Source: TDAP (2011)

Opportunity in India

The normalization of trade with India provides a good opportunity to expand markets in emerging economies. Exports to India have been steadily growing in recent years but they are well below its potential. Pakistan already exports surgical instruments to India via Germany. It is estimated that if Pakistan traded surgical instruments directly with India, it could earn an additional \$200 million.



Source: SIMAP

Indian tariffs average 8%, while Pakistan imposes tariffs on raw material range from 5 to 25%. These discourage trade across the borders. However, there is considerable scope for expanding the exports:

Surgical instruments

HS Code	Product description	Year: 2011, Unit: Million USD			RCA		NRCA	
		Pakistan exports to world	India exports to world	World exports	Pakistan	India	Pakistan	India
9018	Electro-medical apparatus (electro-cardiographs, infra-red ray apps. Sy)	291.6	487.9	95,420.2				
9021	Orthopedic appliance (crutche/surgical belts and trusse)	0.3	38.0	45,076.0				
9022	Apparatus based on the use of X-ray/of alpha, beta/gamma radiations	0.1	160.7	21,952.9				
Total surgical instruments		297.0	686.6	162,449.1	1.27	0.25	0.12	(0.60)
	All products	25,343.8	301,483.3	17,855,727.0				

The above figures show a clear competitive advantage for Pakistani fans.

Conclusions

Along with Germany, Pakistan is one of the only two major exporting countries for the large global surgical hand-held goods market. Pakistan's surgical instruments industry has shown steady growth in exports in recent years, reaching US\$300 million in 2011-2012. Nevertheless, the industry is underutilized and generates far below its potential. Pakistani manufacturers lose out on significant revenues from middlemen in Germany who, after branding and marketing, make substantial mark ups. The industry is focused on the lower end of the market which results in low-priced goods also requires less investment in technology and specialised labour.

Pakistan's manufacturers have satisfied international quality requirements and have a flexible manufacturing process that can cater to different specifications. Pakistan has the opportunity to significantly grow its industry through exporting to a growing Indian market. Sialkot's proximity to the Indian border and the manufacturers' ability to make direct contacts, eliminating middlemen, merit Pakistan to pursue trade negotiations for surgical instruments with India.

PHARMACEUTICALS



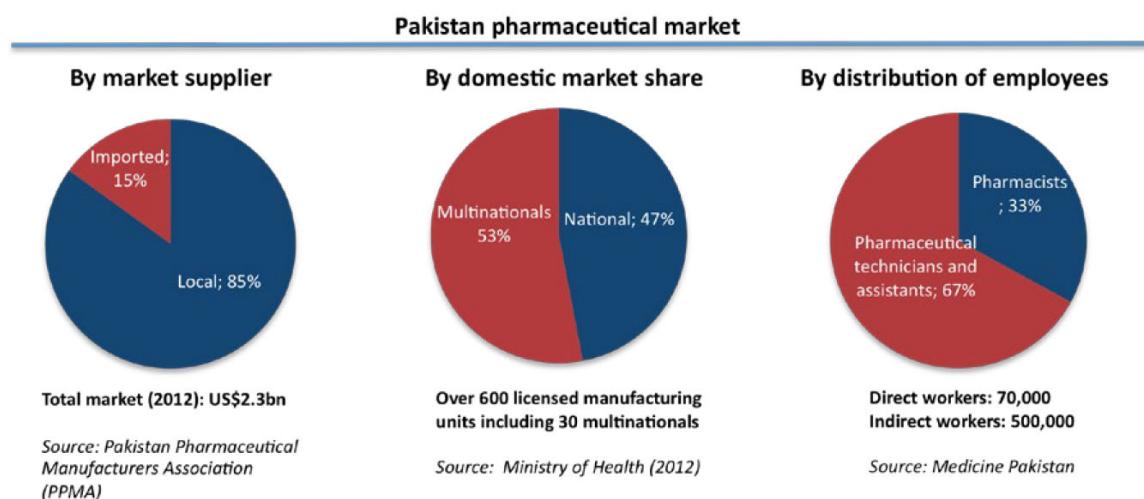
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Industry dynamics

Pakistan has a well-established pharmaceutical industry. With over 600 licensed manufacturing units including 30 being operated by multinationals, the domestic market share for pharmaceutical products is almost evenly divided between national (53%) and multinational (47%) companies. Of the top 10 companies operating in Pakistan, six are multinational and four are national.

The consumption of medicines in the country is expected to exceed \$2.3 billion by 2012, 85% of this is manufactured locally whereas the rest (15%) is imported.³ Pakistan is therefore amongst the few countries with a well-developed pharmaceutical industry.

Exports of pharmaceuticals from Pakistan have seen a substantial increase during the past decade from US\$3.0 million in 2001-2002 to US\$ 170 million in 2010-2011.



The industry provides direct employment to more than 70,000 and indirect employment to around 500,000 people. The pharmaceutical industry is considered to be the largest employer of university graduates in the smaller towns of Pakistan.

Despite an impressive growth, the pharmaceutical industry in Pakistan faces a number of issues.

³ PPMA, Pulse Islamabad, Abbott Laboratories Pakistan

Issues and the Way Forward

Issues	The Way Forward
Access to modern medicine	<ul style="list-style-type: none"> ▪ In order to achieve its Millennium Development Goals (MDGs) it is imperative that access to modern medicine within Pakistan is universal ▪ The pharmaceutical industry needs to work with the government in devising strategies to improve access to the basic health (including essential drugs of standard quality) at affordable prices especially in the rural areas.
Drug pricing	<ul style="list-style-type: none"> ▪ The government fixes the prices of all the 70,000+ drugs registered in Pakistan. ▪ This extreme level of control is arguably the highest in the world and creates aberrations between products in Pakistan as well as in comparison with drugs in India/Bangladesh ▪ Moreover due to unrealistic pricing many essential drugs are no longer freely available driving patients to expensive alternatives ▪ A pragmatic transparent and uniformly implemented pricing policy (at the same time ensuring that drug prices are similar to those in India and Bangladesh) is needed
Quality of Drugs	<ul style="list-style-type: none"> ▪ Since 2001, the government has not allowed an across-the-board adjustment to offset the increase in cost of manufacture/import of drugs ▪ Eroding margins have deterred companies from making significant investment to improve quality of products (plant/equipment, Human Resource and systems) ▪ Additionally poor enforcement of Current Good Manufacturing Practices (cGMPs) by the Regulatory Authorities has contributed and increase in sub standard spurious and counterfeit medicines in the country
Antiquated Regulatory Framework	<ul style="list-style-type: none"> ▪ Since 1976 (Drug Act) there has been no significant change in the regulatory framework even though the environment has changed ▪ In the wake of the 18th Constitutional Amendment with Health becoming a provincial subject, the Drug Regulatory Authority of Pakistan (DRAP) was established and passed by the Assembly/Senate ▪ Unfortunately despite recommendations from technical experts (including from the WHO) the framework was not modernized. The DRAP is therefore a continuation of the erstwhile Federal Ministry of Health ▪ In order to improve the access and quality of Drugs in Pakistan and to facilitate the industry into becoming a global player, the recommendations of the technical experts need to be adopted
Exports of Drugs	<ul style="list-style-type: none"> ▪ There is no manufacturing unit in Pakistan that has been approved by the WHO, US FDA, EMEA or MHRA of the UK. ▪ Therefore medicines manufactured in Pakistan cannot be exported to any country with a Stringent Regulatory Framework ▪ A regulatory framework that encourages investment into Quality Facilities is needed in Pakistan

Comparison with the Indian pharmaceutical industry

As compared to Pakistan, the Indian pharmaceutical industry is much larger in terms of its size and output. It is one of the world's largest and most developed, ranking 4th in volume terms and 13th in value terms, accounting for 10% of global production in 2010.⁵

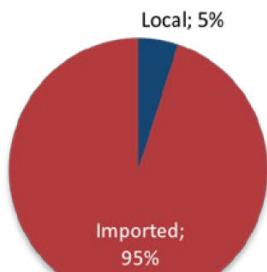
India has a total of 24,000 pharmaceutical companies, of which 250 organised units control c. 70% of the market. About 75% of the top 20 pharmaceutical companies are Indian owned.⁴

There are 74 USA Food and Drug Administered (FDA)-approved manufacturing facilities in India. Indian companies are making significant inroads in the USA domestic market. Thus e.g. in 2007-2011 over 30% of all Abbreviated New Drugs Applications (ANDAs) approved by the US FDA was for products from Indian companies.

⁴ Invest India

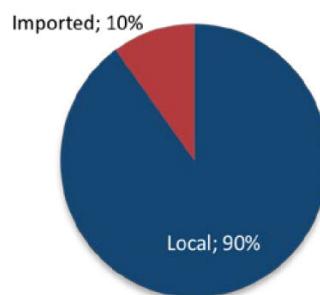
Pharmaceutical raw materials

Pakistan manufacturing



Source: Atlantic Council

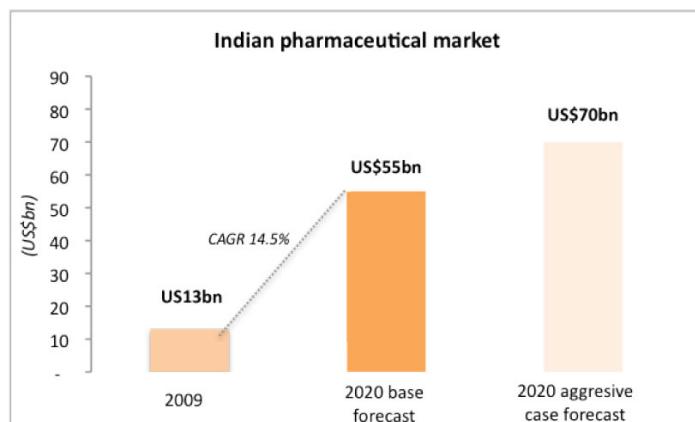
India manufacturing



Source: Abbott Laboratories Pakistan

Whereas Pakistan produces only 5% of its raw materials, the Indian industry meets 90% of its needs locally.

The Indian pharmaceuticals market is forecast to grow from \$12.6bn in 2009 to \$55 billion in 2020 according to a recent McKinsey study.⁵ The study states that the Indian pharmaceutical market has the further potential to reach \$70 billion by 2020 if aggressive growth efforts are embraced.



Source: McKinsey and Company — “India Pharma 2020”

Trade-related Aspects of Intellectual Property Rights (TRIPS) and Public Health

Both India and Pakistan face serious and complex public health challenges. Up to 30% of the population has little or no access to modern medicine due to the poor infrastructure (lack of doctors, hospitals, dispensaries) and poverty in rural areas. Their rates of communicable diseases such as tuberculosis, HIV/AIDS and Malaria are second only to those of sub-Saharan Africa. Non-communicable diseases such as cardiovascular disease, respiratory disease, digestive diseases, cancer, and diabetes pose an even more serious challenge and already account for over 50 % of deaths in these countries.

Considering these serious challenges, medicines should not be treated like any other commodity. By normalizing trade, both countries would help their populations to have better access to life-saving medicines. This cooperation, however, need not be at the expense of the pharmaceutical industry, which like any other industry operates in response to economic factors and market forces.

Contrary to common perceptions, the TRIPS Agreement does not prevent members from taking measures to protect public health. Both countries successfully negotiated for the flexibilities in the WTO TRIPS Agreement to facilitate compulsory licensing for medicines for public health crisis. Having successfully obtained these concessions both can cooperate to use those flexibilities (the so-called paragraph 6 mechanism) to address public health problems.

⁵ McKinsey and Company — “India Pharma 2020”

Trade with India

RCA and NRCA show that India has substantial comparative advantage over Pakistan.

Pharmaceutical

HS Code	Product description	Year: 2011, Unit: Million USD			RCA		NRCA	
		Pakistan exports to world	India exports to world	World exports	Pakistan	India	Pakistan	India
30	Pharmaceutical products	150.7	8,259.9	459,717.7				
	All products	25,343.8	301,483.3	17,855,727.0	0.23	1.06	(0.62)	0.03

The majority of Pakistani manufacturers remain apprehensive about opening trade in pharmaceutical goods with India. The reasoning is that Indian pharmaceutical industry is not only large and competitive, but it also has access to local cheaper raw materials and several other institutional advantages. They fear that these could lead to the closure of the local industry.

Others argue that over the past many years the government of Pakistan has allowed imports from countries (e.g. China, Bangladesh, Hungary etc.) that produce some of the cheapest medicines. Yet despite their low prices the share of these medicines has remained low (e.g. share of Chinese products in Pakistan is less than 1%). Some also argue that prices of drugs are in fact less in Pakistan than in India. They refer to the data compiled by IMS Consulting, which shows that on average 63 % of Pakistan's medicines are cheaper than Indian products of the same brands.

It is therefore unlikely that products from India will capture any significant share of the Pakistani market.

Furthermore, Pakistani pharmaceutical manufacturers have been successfully competing against their Indian counterparts in many foreign markets. For example, Pakistan's largest and fastest local manufacturing company Getz Pharma is exporting generic medicines to 18 countries covering most of the East and South East Asia, Africa, and other parts of Asia. It is also likely that Pakistan may be able to gain market access to India at least for those medicines that are being successfully exported to other countries.

Finished medicines are liable to customs duty of 10% when imported into Pakistan. In some cases such as ampicillin, amoxicillin and cloxicillin, (capsules or syrups), the duty rate is 25%. There is currently no concession under SAFTA on medicines. Therefore, adequate protection is available against imports from India.

Also significant is the fact that for a majority of popular drugs such as amoxicillin, atenolol, captopril, ceftriaxone injection, co-trimoxazole, fluoxetine, lovastatin, omeprazole, and salbutamol, prices are very similar in both countries.⁶

Nevertheless considering the apprehensions of the local industry against cheaper imports, the following approach is suggested:

Imports of raw material, medical equipment, packaging material, machinery and those medicines which are not manufactured in Pakistan may be allowed when the negative list is abolished

Import of other medicines may be allowed in a phased manner but no duty concession under SAFTA be allowed so as to offset the cost advantage enjoyed by Indian companies (cheaper materials, machinery and other institutional advantages).

⁶ Survey by the Network for Consumer Protection

PLASTICS AND CHEMICALS



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There are over 80,000 chemicals and plastics used for commercial purposes. The discussion in this paper is limited to a few important products that are either currently being traded or are likely to be traded in significant quantities between India and Pakistan.

Plastics

The two products with most potential are polyethylene and polypropylene. In 2011, Pakistan's imports of these two products were worth almost US\$1 billion, which is two-thirds of the total value of its chemical imports.

Polyethylene

Polyethylene is of two types - low-density polyethylene (LDPE) and high-density polyethylene (HDPE). Because of its softness and pliability, LDPE is used for manufacturing plastic bags, containers, textiles, and electrical insulation and coatings for packaging materials, amongst other similar applications. On the other hand, HDPE is much more rigid and is used for making products such as plastic tubing, bottles, and bottle caps.

In 2011, Pakistan's global imports of polyethylene were US\$506 million. Imports from India were US\$16.04 million or merely 3.2% of the total. Although their value seems negligible at present, they are rising rapidly. Compared to less than US\$1 million in 2010, in 2011 they were worth US\$16 million.

Plans for setting up a polyethylene plant at Karachi with an estimated output capacity of 350,000 tons are in advanced stages. Nevertheless, it will be quite a while before local capacity is built to a level that the local needs can be met only through domestic production.

Polypropylene

The other major imported polymer is polypropylene. Unlike polyethylene it has high melting point of 160°C and is therefore capable of being operational at a very high temperature. Furthermore, due to its lightweight and high tensile strength, it is used in a range of household goods. Amongst its other commercial applications, the most important are for making plastic parts - from toys to automobile products; crates and boxes; furniture; carpeting; reusable products; paper and laboratory equipment.

Pakistan's global imports of polypropylene in 2011 were US\$488 million and those from India were US\$41.57 million or about 8.5%.

As in case of polyethylene, most of the demand is currently being met through imports from Saudi Arabia and Kuwait.

With the growing trade between the two countries, this situation is changing. India has a surplus of propylene and can easily meet the entire needs of Pakistan. Ever since IndianOil set up its Panipat naphtha cracker plant in 2010, it started exporting polypropylene to Pakistan through Wagah border. Until recently imports were restricted through railways and due to paucity of wagons, only limited quantities could be imported. Recently imports have started coming through trucks and in the past few months 1200 tons of polyethylene has been imported. Furthermore, due to the coming into production of HPCL-Mittal Energy Limited, which has built a 9 million ton refinery at Bathinda, Punjab (about 180

Polyethylene

- Polyethylene exists in two forms; soft and pliable low-density polyethylene (LDPE) and rigid high-density polyethylene (HDPE)
- LDPE is used in plastic bags, containers, textiles, and electrical insulation
- HDPE is used in plastic tubing, bottles, and bottle caps

Polypropylene

- Polypropylene is operational at higher temperatures than polyethylene. It is lightweight and possesses high tensile strength
- Polypropylene is used in plastic parts found in toys, automobile products, crates and boxes, furniture, paper and laboratory equipment

Polyvinyl Chloride (PVC)

- PVC is a rigid and brittle in its pure form but through the addition of plasticizers it become softer and more flexible
- PVC has low cost and is valued for its chemical and biological resistance
- PVC is most widely used in the production of pipes
- Also used in electrical cabling insulation, clothing, and as a building material

Polyethylene Terephthalate (PET) resin

- PET is strong and lightweight and can be made to be rigid or semi-rigid. Its impact resistance properties make it suitable material for packaging
- PET is primarily used in the production of synthetic fibers and bottles

Polystyrene

- Polystyrene can be molded into a cheap fairly rigid lightweight plastic. It also exists in an expanded form which is very lightweight and insulating
- Molded polystyrene is used in a wide range of plastic products including CD cases and smoke detectors
- Expanded polystyrene is widely used in packaging and insulation

kilometres from Wagah border), competition will become more intense. It is expected that if the transportation problem is resolved, India's exports of polypropylene may exceed 100,000 tons per year or almost one-third of the total requirement.

Pakistan's imports are likely to increase several folds as the economy grows. The potential demand can be seen from the fact that the consumption of these polymers per capita per population is a mere 3 kg as compared with 7 kg for China and global average of 10 kg. The figure for industrialized western countries is 30-40 kg per capita.

Polyvinyl Chloride (PVC)

PVC resin is another important polymer. It is mainly used to manufacture PVC pipes, artificial leather, shoes, rigid and soft sheets, garden hose, windows and doors etc. In Pakistan, Engro Polymer and Chemicals Limited is the major manufacturer. Its annual production is 150,000 tons, which is currently being increased to 200,000 tonnes/year. Pakistan's domestic demand is estimated at 130,000-140,000 tonnes/year. As such, it will have a surplus of about 60,000 tons per year.

India has the potential to absorb this extra production as it imports large volumes of PVC and will continue to do so for the next few years. During 2010/11, it imported about 650,000 tonnes of PVC, which is about 35% of its total demand. This demand is estimated to rise further as estimates show that India will need 200,000-250,000 tonnes of new capacity every year to keep pace with demand but no new projects are currently being undertaken.

Polyethylene Terephthalate (PET) resin

Because of its strength and lightweight, PET is the most common plastic used for packaging purposes such as bottles for water, carbonated drinks or juices. When it is used for making fibres or fabrics, it is called polyester.

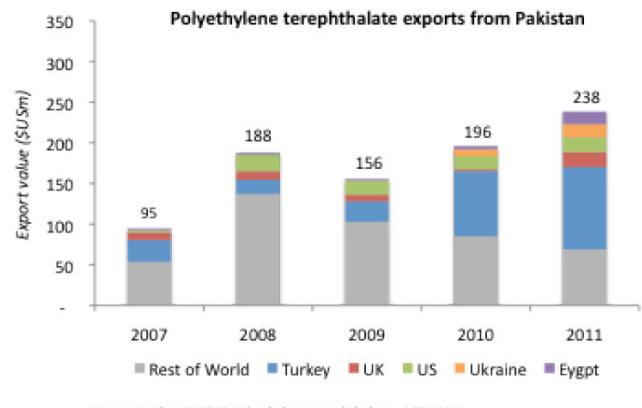
Both India and Pakistan have adequate manufacturing capacity not only for their own needs but also for exports.

According to UN COMTRADE statistics, Pakistan exported PET RESIN valued at US\$238m in 2011, a compound annual growth rate of 26% from 2007.

Pakistan's five largest PET RESIN exports in 2011 were: Turkey (US\$101m), UK (US\$18m), US (US\$18m), Ukraine (US\$16m), and Egypt (US\$15m).

Novatex Limited, along with its sister company Gatron Industries Limited, is the only PET Resin Bottle Grade manufacturer in Pakistan, with the brand name of "Gatronova". According to the company's website, the total PET resin production capacity is 235,000 mt/annum, out of which more than 70% of the quantity is exported to 45 countries.

In India there are three major manufacturers of PET resin. Reliance Industries Ltd (RIL) is the leading producer with a capacity of 290,000 tons/annum while Dhunseri is the second largest manufacturer with a capacity to produce 200,000 tons. It is increasing its capacity by 210,000 tons to become the biggest producer in India. Another major producer is JBF Industries Ltd with a capacity of 110,000 tons/year. It is estimated that Indian production may reach 1.618 m tons by 2016, at a compound annual growth rate (CAGR) of 13.8% from 2011-2016.



Currently Pakistan's PET resin industry is protected through a relatively high customs duty of 20%. In comparison, customs duty rate in India is 10%. While India is a major exporter, it is also importing some speciality PET resin. In 2010, its imports were about US\$40 million.

It seems that Pakistan may have a short-term advantage of exporting PET resin to India as it is more competitive. But the local manufacturers do not see India being an important market for PET resin. On the other hand, they feel that India may be able to capture the Pakistani market if enough protection is not maintained at present levels. They claim that India subsidizes its exports through various schemes whereas no such incentive is available for Pakistani exporters.

Polystyrene

Polystyrene is the fourth biggest polymer produced in the world after polyethylene, polyvinyl chloride and polypropylene. Almost 75% of global production is used for packaging and construction industries. Its everyday uses include housing for computers, hairdryers, TVs and kitchen appliances. It is also used as foam packaging and insulation, and making auto-parts such as radio knobs. Another common use is making drinking cups.

There is one manufacturing unit - Pak Petrochemical Industries – with an annual capacity of 100,000 M. Tons/ annum. Except for some special qualities such as ABS and high-impact Polystyrene, this unit is able to not only meet the local needs but also export about 50% of its production. India is also a major producer of this product. In fact due to its overcapacity in India, BASF recently announced shutting down its plants in India and Malaysia. It is not likely that, aside from some special qualities such as high-impact polystyrene, there would be much trade of this polymer.

Organic chemicals

Other major organic chemicals where there is significant potential for trade include P-xylene, O-xylene, Ethylene Dichloride, Phthalic Anhydride. Whereas P-Xylene and O-Xylene are imported in Pakistan, Ethylene Dichloride and Phthalic Anhydride are produced in surplus quantities and are in demand in India

Inorganic Chemicals

Caustic Soda

Pakistan's capacity is 435,000 tons whereas its domestic consumption for caustic soda is around 300,000 tons. Thus it has surplus of about 135,000 tons. According to the Alkali Manufacturers' Association of India, their annual demand for caustic soda in India is around 2.5 million tonnes, but they still need another 25000 tons to meet their requirements. Exports of caustic soda have doubled during this period for 5000 tons to 10000 tons. This is a healthy sign for Pakistan's chemical industry, which was hardly considered as a potential exporter only two years ago. Pakistan can raise its exports several folds as the Indian industry is not competitive and is also not able to meet its domestic demand.

Soda Ash

There are two units with production capacity of 470,000 metric tons per year. Pakistan's consumption is estimated at 360,000 tons. Thus there is a surplus of 110,000 tons available for exports. Pakistan recently started exporting this product to India. During 2011-12, Pakistan exports reached 11,101 tons to India. Although India is also a major producer of soda ash, its industry is unable to meet the local needs, which are met through imports from various sources. Pakistan has significant price advantage over other countries due to its proximity. Pakistani producers are also cost effective as compared to the Indian manufacturers, which are mostly located in Southern India. The

freight cost from South to Delhi is US\$ 30 per ton while from Pakistan it is US\$ 7-14 per ton. Therefore Pakistan can easily increase its productions many fold from its present levels. Pakistan's exports of soda ash increased almost 5 fold from 2420 tons to 12007 tons during June 2012 to Feb 2013 as compared to the same period last year. This can increase several folds as Pakistan has the necessary raw materials and also enjoys freight advantage.

Other Inorganic Chemicals

There is significant trade potential for Aluminium Hydroxide, Dithionites, Sulphoxylates and Chlorates.

RCA and NRCA

PLASTICS								
HS Code	Product Description	Year: 2011, Unit: Million USD			RCA		NRCA	
		Pakistan exports to world	India exports to world	World exports	Pakistan	India	Pakistan	India
'3923	Plastic packing goods or closures stoppers, lids, caps, closures, plas	36.7	446.5	45,929.1				
'3924	Tableware, kitchenware, toiletery articles, of plastic	27.3	143.0	11,902.2				
'3917	Tubes, pipes & hoses & fittings therefor of plastics	25.6	113.9	21,220.4				
'3926	Article of plastic nes.	9.5	357.7	58,072.0				
'3920	Other plates, sheets, film, foil, tape, strip of plastics etc.	9.0	753.3	56,301.3				
'3922	Baths,shower-baths,wash-basins,bidet etc of plastic	1.2	4.1	3,670.0				
'3921	Plates, sheets, film, foil and strip, of plastics, nes	1.0	253.6	23,646.6				
'3925	Builders' ware of plastics, nes	0.5	15.1	9,913.0				
	Total plastics	110.9	2,087.2	230,654.6	0.34	0.54	(0.49)	(0.30)
	All products	25,343.8	301,483.3	17,855,727.0				

Source for trade data: TRADEMAP

POLYETHELENE								
HS Code	Product Description	Year: 2011, Unit: Million USD			RCA		NRCA	
		Pakistan exports to world	India exports to world	World exports	Pakistan	India	Pakistan	India
'390120	Polyethylene having a specific gravity of 0.94 or more	21.9	327.1	27,058.2				
'390110	Polyethylene having a specific gravity of less than 0.94	13.3	63.0	28,177.3				
'390190	Polymers of ethylene nes, in primary forms	4.2	23.1	14,185.4				
'390130	Ethylene-vinyl acetate copolymers	0.6	1.2	4,277.6				
	total Polyethelene	40.0	414.4	73,698.5	0.38	0.33	(0.45)	(0.50)
	All products	25,343.8	301,483.3	17,855,727.0				

Source for trade data: TRADEMAP

POLYPROPYLENE								
HS Code	Product Description	Year: 2011, Unit: Million USD			RCA		NRCA	
		Pakistan exports to world	India exports to world	World exports	Pakistan	India	Pakistan	India
'390290	Polymers of propylene nes or of olefins nes, in primary forms	0.3	4.8	2,557.4				
'390210	Polypropylene	0.2	1,187.2	26,152.0				
'390230	Propylene copolymers	0.1	8.9	16,042.6				
'390220	Polyisobutylene	-	12.5	796.9				
	Total Polypropylene	0.6	1,213.3	45,548.9	0.01	1.58	(0.98)	0.22
	All products	25,343.8	301,483.3	17,855,727.0				

Source for trade data: TRADEMAP

TRADE OF INDUSTRIAL GOODS WITH INDIA: OPPORTUNITIES AND CHALLENGES FOR PAKISTAN

POLYETHYLENE TEREPHTHALATE (PET RESIN)

HS Code	Product Description	Year: 2011, Unit: Million USD			RCA		NRCA	
		Pakistan exports to world	India exports to world	World exports	Pakistan	India	Pakistan	India
'390760	Polyethylene terephthalate	238.4	530.2	14,131.5	11.89	2.22	0.84	0.38
	All products	25,343.8	301,483.3	17,855,727.0				

Source for trade data: TRADEMAP

Inorganic chemicals : Caustic soda, Soda Ash, other inorganic chemicals

ASH SODA

HS Code	Product Description	Year: 2011, Unit: Million USD			RCA		NRCA	
		Pakistan exports to world	India exports to world	World exports	Pakistan	India	Pakistan	India
'283620	Disodium carbonate	9.86	66.22	2,368.46				
	All products	25,343.8	301,483.3	17,855,727.0	2.93	1.66	0.49	0.25

Source for trade data: TRADEMAP

POLYVINYL CHLORIDE (PVC)

HS Code	Product Description	Year: 2011, Unit: Million USD			RCA		NRCA	
		Pakistan exports to world	India exports to world	World exports	Pakistan	India	Pakistan	India
'390410	Polyvinyl chloride, not mixed with any other substances	7.9	0.9	12,267.8				
'390422	Polyvinyl chloride nes, plasticised	0.2	10.3	1,968.8				
'390440	Vinyl chloride copolymers nes	0.0	0.2	319.3				
'390490	Polymers of vinyl chloride nes, or of other halogenated olefins	0.0	0.6	391.0				
'390469	Fluoro-polymers nes	-	0.1	1,772.9				
'390421	Polyvinyl chloride nes, not plasticised	-	13.1	1,091.1				
	Total PVC	8.1	25.3	17,810.9	0.32	0.08	(0.51)	(0.85)
	All products	25,343.8	301,483.3	17,855,727.0				

Source for trade data: TRADEMAP

POLYSTERENE

HS Code	Product Description	Year: 2011, Unit: Million USD			RCA		NRCA	
		Pakistan exports to world	India exports to world	World exports	Pakistan	India	Pakistan	India
'390319	Polystyrene nes	62.6	85.1	6,654.0				
'390311	Polystyrene, expandible	2.3	0.5	3,284.6				
'390390	Polymers of styrene nes, in primary forms	0.0	12.2	4,266.1				
	Total Polysterene	64.9	97.9	14,204.7	3.22	0.41	0.53	(0.42)
	All products	25,343.8	301,483.3	17,855,727.0				

Source for trade data: TRADEMAP

CAUSTIC SODA

HS Code	Product Description	Year: 2011, Unit: Million USD			RCA		NRCA	
		Pakistan exports to world	India exports to world	World exports	Pakistan	India	Pakistan	India
'281511	Sodium hydroxide (caustic soda) solid	3.5	32.7	617.5				
'281512	Sodium hydroxide (caustic soda) in aqueous solution	0.5	1.2	2,967.8				
	Total caustic soda	4.0	33.9	3,585.3	0.78	0.56	(0.12)	(0.28)
	All products	25,343.8	301,483.3	17,855,727.0				

Source for trade data: TRADEMAP

TRADE FACILITATION⁷

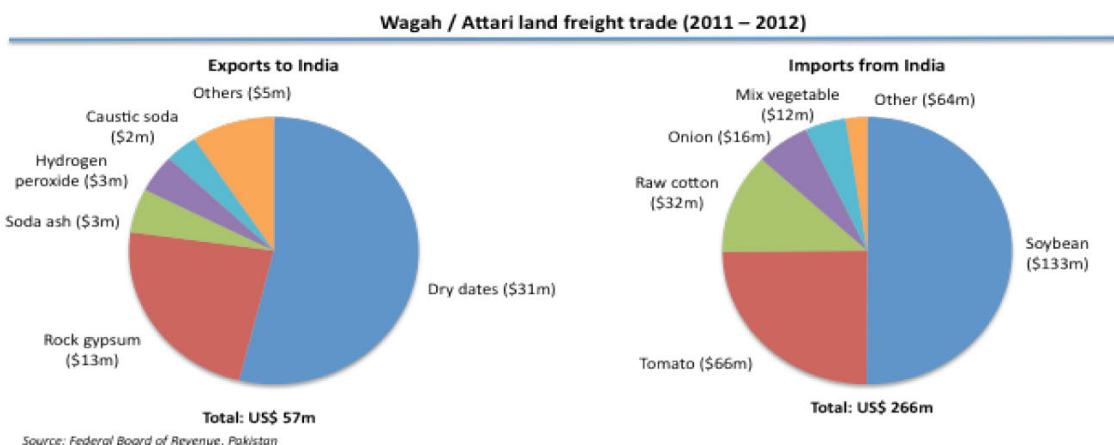
Dynamics

Of the measures to improve bilateral trade between India and Pakistan, the most important is trade facilitation. This includes the streamlining of Customs clearance procedures but also the improvement of transport infrastructure, the removal of multiple government checks and of other non-tariff trade barriers, the modernization of customs administrations, and a renewed emphasis on export marketing and promotion.

Pakistan and India have a common border of about 3000 km but there is only one crossing Wagah-Attari through which legal trade of only 137 items is allowed by Pakistan. The total value of trade passing through this point in 2012 was US \$323 million, of which US \$266 million was imports from and US\$57 million was exports to India.⁸ The bulk of the remaining bilateral trade estimated at US\$2.06 billion in 2010-2011 took place through seaports.⁹

There was an average of 132 trucks per day processed by the Pakistan Customs at the Wagah-Attari border in 2011, of which 95 were Indian and 37 were Pakistani.¹⁰ This daily average has risen dramatically after the recent trade liberalization measures as can be seen by the current 2012 trends - July: 145, August: 168, September: 268 and October: 293.¹¹

At present, 100% of all imports and exports are scanned on the Pakistani side. The Pakistan's Customs have recently increased its working hours from 6am to 10pm. The major products exported through Wagah-Attari by road include dry dates, rock gypsum, and chemicals (caustic soda, soda-ash, hydrogen peroxide, etc). The main import is soybean meal that accounted for almost 50% by value of imports in 2011-2012. Other major commodities are vegetables (tomatoes, onions, garlic, etc.) and raw cotton.



Despite some recent improvements such as electronic linkage of Wagah Customs through One-Customs and construction of new buildings in 2007/08 for processing of passengers overall procedures requires significant logistical and infrastructural improvement to catch up with international standards or even the local standards as are applied at the seaports.

⁷ This Chapter is based on desk-research and personal observations of the author on a visit to the Wagah-Attari border to examine the current clearance procedure from the Pakistani side

⁸ Federal Board of Revenue, Pakistan; USAID

⁹ State Bank of Pakistan

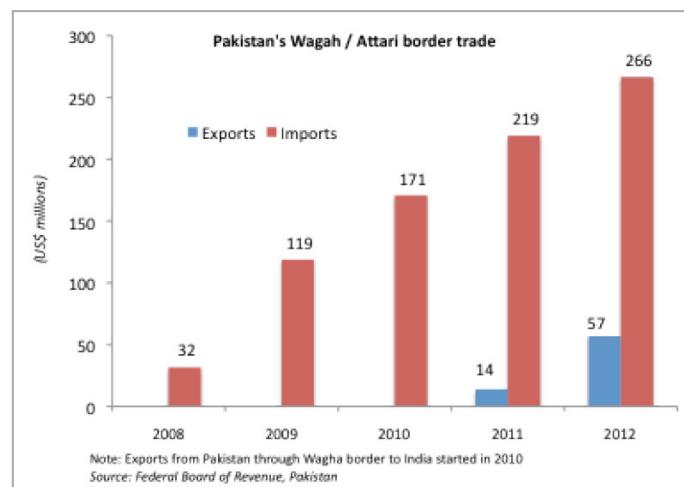
¹⁰ Federal Board of Revenue

¹¹ Pakistan Customs

Exports from Pakistan through Wagha border to India started in 2010. Since then there has been a sharp rise in exports and imports. Pakistani exports to India via the Wagah border grew by 309% in June 2012 to June 2011 whilst imports grew at 22% during the same period.

As India and Pakistan increase the amount of items that are tradeable through the land route, it is anticipated that Wagha-Attari border will become a major hub of trade between India and Pakistan, especially due to lower freight costs.

Before the issuance of the Statutory Notifications (SRO) 280 (1) 2012 dated 20.03.2012 when the positive list of importable items from India was replaced by a negative list of a limited number of products, the main items that were imported from India through Wagah were agricultural products. After March 2012 there has been an increase in the trade volume and industrial goods like newsprint paper and plastic raw-material have started coming in.



Trade facilitation barriers

However, barriers in trade facilitation remain a major hindrance. Some of the major anachronisms, which can easily be observed at the Wagah-Attari border, are the following:

Inefficiency	Comments
Multiple agencies overlapping	<ul style="list-style-type: none"> There are three government agencies overseeing imports and exports at the border. Quite often their work overlaps. For example, Pakistan Customs, Pakistan Rangers and National Logistics Cell (NLC) note particulars of each truck. Thus, in addition to the clearing agent or the importer's representatives, there are at least a dozen government functionaries involved in processing of the entry details (not including customs examination, payment of taxes or other processing involved in clearance of goods) of a truck.
Lack of advance clearance	<ul style="list-style-type: none"> There is no system of advance clearance notification of goods being imported or exported. Thus, unlike goods arriving through seaports, there can be no advance processing of paper work as is allowed under Section 79 of the Customs Act and has been practised at the Karachi port for several decades.
Lack of risk profiling	<ul style="list-style-type: none"> There is hardly any reliance on risk profiling. Almost all trucks are weighed, scanned and physically inspected. The only exceptions are that, due to lack of scanning capacity (there is only one scanner although more are being planned to be installed), some imported trucks were not scanned. However, in case of exports to India every truck was scanned.
Truck changes	<ul style="list-style-type: none"> Goods are off-loaded from the Indian trucks and then on-loaded on the Pakistani trucks after they cross the border. All this is done manually without any mechanical tools. This takes lot of time and financial resources. It also results in wastage and breakage of goods.
Duplication	<ul style="list-style-type: none"> Each agency has its own countercheck. For example, each declaration is first signed by an inspector and then countersigned by a supervisor.
Avoidable fees	<ul style="list-style-type: none"> There is an official fee for each of the services involved. For example, for each weighing or scanning, there is a charge that adds on to the costs. Even empty trucks are weighed. In exceptional cases when trucks are allowed without weighing, a charge is nevertheless collected.
Manual processing	<ul style="list-style-type: none"> Although the processing of documents is supposed to be done electronically, it is mostly manual. Each entry is also posted in various registers. Also there is no system of electronic data interchange

Trade process flows

The USAID Trade Project team also conducted an assessment at the Wagah-Attari Border in 2011 of which they identified the current process flows.

Process flow for imports from India to Pakistan

Step	Process flow	Waiting time (mins)	Processing time (mins)	Total time (mins)
1	Indian truck crosses over the border and enters Pakistan	5	10	15
2	Scanning is Carried Out at the NLC Yard	25	5	30
3	Loaded truck passes through Weighbridge (1st Weighing)	10	5	15
4	Unloading of cargo at NLC Yard	5	55	60
5	Goods Declaration is filed in Customs Office on the OneCustoms system	5	5	10
6	Examination of Goods is carried out	5	25	30
7	Empty truck passes through Weighbridge (2nd Weighing)	5	10	15
8	Goods are Appraised - Cash Number Issued by Inspector	5	10	15
9	Duties and Taxes are deposited in National Bank of Pakistan (NBP) booth	5	10	15
10	Out of Charge	5	5	10
11	Out of Gate	5	10	15
Total		80 mins	150 mins	230 mins (4.20hr)

Process flow for exports from Pakistan to India

Step	Process flow	Waiting time (mins)	Processing time (mins)	Total time (mins)
1	Pakistan Truck enters Inward Export Gate	230	10	4 hours
2	Pakistani truck Enters NLC Yard	None	5	5
3	Truck is Weighed at the Weighbridge	10	5	15
4	Scanning is carried out at NLC Yard	25	5	30
5	Goods Declaration for Exports is filed on OneCustoms system	5	5	10
6	Processing of Export Documentation by Deputy Superintendent	5	10	15
7	Examination of Goods	5	25	30
8	Out of Charge	5	5	10
9	Single Entry Permit issued by Pakistan Customs	25	5	30
10	Out of Gate	5	5	10
Total		315 mins	80 mins	385 mins (6.42hr)

Note: The process sequence is as described by the Pakistan Customs officials at the Wagah-Attari border post. There are, however, variations in the process sequence as some processes or part of processes may be expedited in parallel, given the availability of staff.

Source: USAID

A survey carried out for this study indicates that the time taken by scanning and weighing is now much longer. For example, scanning is reportedly taking more than one hour while weighing could take up to one hour.

Path to efficiency

Most of the bottlenecks can be addressed through regulatory measures without any costs. In fact, there would be considerable savings. Simplification of procedures can be achieved through the following two steps:

1 Trade Facilitation Measures that can be adopted unilaterally	
Simplification	<ul style="list-style-type: none"> i. Multiple checking by different agencies should be stopped immediately and separate roles assigned to each according to its mandate. Thus NLC's role would be comparable to any port operator at Karachi. Given their experience in handling huge amount of goods, it would be preferable if any of the port operators were given the same task in Wagah. Similarly Rangers would only work on any specific security related issue and would not be checking all incoming or outgoing goods. ii. Only one check by an agency would be enough. Currently after checking of a consignment by a customs inspector, it is then countersigned by a Deputy Superintendent. This practice should only apply to higher risk goods. iii. Introduce Single Window concept that allows importers and exporters to submit documents at a single point to fulfill all import, export, and transit-related regulatory requirements
Harmonization	<ul style="list-style-type: none"> i. Simple replication or harmonization of clearance processes with those applicable at Karachi would be a major step forward ii. Allow filing of goods declaration and processing of documents in advance of the arrival of goods as is allowed under the Customs Act and has been practiced at Karachi for several decades iii. Move from the current manual or semi-automated clearance process to a more automated process as is applicable for clearances under PaCCS at Karachi iv. Allow payment of taxes in advance so that the goods are not held up for that purpose

2 Recommendations that need to be negotiated and implemented bilaterally:	
Joint cooperation	<ul style="list-style-type: none"> i. Introduce Joint One-Stop Border systems: Nominated representatives of both governments can inspect the goods jointly. If this is not acceptable at this stage, at least both sides could agree to single scanning or weighing of goods in the presence of the other side (the Indian side does not have a scanner) ii. Allow transshipment of goods to other dry ports or at least clearance should be allowed through Lahore Dry Port instead of unloading at Wagah iii. Currently each time a driver crosses border, he is issued a single entry pass. This could be multiple entry but for a limited period of 3 to 6 months iv. Currently only one border crossing Wagah-Attari is operational. Although processing time has been increased substantially during this year and it works for almost 16 hours but it could be made operational 24 hours as is the case with the airports v. In order to speed up clearances, risk-profiling should be introduced. Instead of 100% scanning, it should be gradually reduced to about 10% vi. Other border crossings that were operational in the past could be made functional without many costs. For example, opening of the Khokhrapar-Munabao route would provide opportunities for businessmen in Gujarat and Rajasthan to trade with Sind and Baluchistan provinces. Similarly opening of Husseiniwala-Sialkot would enable light engineering hubs such as Sialkot and Gujranwala to trade more easily with their Indian counterparts.

STAKEHOLDER CONSULTATIONS

As previously described, input from relevant industries was considered imperative for an informed discussion on the implications of normalisation of trade between Pakistan and India. This feedback was consulted as evidence of threats and opportunities posed by such an adjustment to trade relations. In order to receive this feedback two strategies were taken, firstly, industry agents were directly approached and asked compile a document illustrating their concerns, secondly, where no direct contact was available, questionnaires tailored to each industry were distributed through contact details attained from industry websites.

Certain industries had industry organisations. These organisations were consulted for their feedback as well as information on the leading producers in each industry. A cover letter and a questionnaire tailored to each individual industrial sector were sent to the respective stakeholders. The stakeholders included company CEOs, associations and their members, government officials, customs officials, importers / exporters, and others. Sample surveys for passenger cars and trade facilitation are included in Annex 2.

ANNEX 1: REVEALED COMPARATIVE ADVANTAGE AND NORMALIZED REVEALED COMPARATIVE ADVANTAGE

This measure will show if a given product or sector has a revealed comparative advantage in each other's market.

The following formula has been used for the calculation of Revealed Comparative Advantage (RCA) and Normalised Revealed Comparative advantage (NRCA). Further details can be seen in the book "A practical guide to trade policy analysis, page 26-27" published by WTO and UNCTAD:

$$RCA = [Xpx/Xp]/[Xwx/Xw]$$

Xpx Pakistan exports of product x

Xp Total Pakistan exports

Xwx World exports of product x

Xw Total world exports

Critical value is 1. RCA above one indicates revealed comparative advantage in product x

$$NRCA = (RCA-1)/(RCA+1)$$

Critical value is 0. RCA above zero indicates revealed comparative advantage in product x

The RCA and NRCA are calculated for Pakistan and India from the exports value of year 2011

Pakistan has RCA in the following sectors: electric fans, surgical instruments, PET resin, Polyesterene and Soda Ash

ANNEX 2: SAMPLE SURVEYS FOR PASSENGER CARS AND TRADE FACILITATION

	Put "X" where answer best fits in your opinion.	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
1	Simplification of clearance procedures could considerably cut the cost of doing business with India					
2	It is easier to import/export goods of Indian origin through land as compared to sea					
3	There are more governmental agencies dealing with clearance of goods at the Wagah/Attari border than at Karachi ports					
4	The current physical movement of consignment (exports) from Pakistan into India are cumbersome					
5	The current physical movement of consignment (imports) from India into Pakistan are cumbersome					
6	Both countries should allow movement of trucks till their final destination rather than at the border					
7	There is a lack of alignment of procedures on the two sides of the border					
8	There is a lack of standardization of documents and electronic data requirements					
9.	There are currently transparent and operable rules and procedures					
10	There should be joint examination of goods involving customs officials from both sides					
11	There is no cooperation between the border agencies in operational and technical areas for simplification of trade procedures					
12	Do you think the Customs Cooperation Agreement will help reduce incidences of arbitrary stoppages of goods at each other's ports?					
13	Is the Mutual Recognition Agreement for acceptance of certificates of internationally-accredited laboratories fully effective?					
14	Do you agree that the Redressal of Grievances Agreement has improved trading environment?					

Average time (including queue time) for each consignment

	Put "X" where answer best fits in your opinion	< 30 mins	> 30 mins < 1 hrs	> 1 hr < 2 hrs	> 2 hrs < 4 hrs	> 4 hrs
8	Customs-related formalities					
	For assessment of Customs duties and other taxes					
	For payment of customs duties and other import taxes					
	For examination procedures					
	For completion of all customs formalities					
	Other formalities - time taken					
	For scanning					
	For weighing	< 3	3 - 5	5 - 7	> 7 < 10	> 10
9.	No of consignments in month					
	No of documents required for filing a declaration for clearance of goods					
10	How often you face problems relating to:	Never	Sometimes	Frequentl y	Always	n/a
	Customs valuation					
	Examination of goods					
	Scanning					
	Weighing					
11	How would you rate the below facilities	Poor	Average	Good	Very Good	Excellent
	Cargo handling facilities					
	Computer systems					
	Infrastructure (roads, checkpoints etc)					
	Sufficient number of manning officials					
	Level of competence among officials					
	Physical inspection of cargo					
	Security controls					
	Anti smuggling controls					
	Fair and consistent enforcement					

13. Please rank the trade facilitation barriers from highest to lowest (1 = best, 5 = worst):

Customs Other agencies Tariff barrier (taxes)

Non tariff barrier Infrastructure

		Comments
14	How long have you been trading with India and for what product or service?	
15	How has your experience been with respect to trade facilitation with India?	
16	In your opinion, what are the greatest trade facilitation challenges when trading with India?	
17	In your opinion, what approach should Pakistan take with India with respect to trade facilitation? What are some Pakistani specific trade facilitation barriers from India?	
18	Any further comments	

TRADE OF INDUSTRIAL GOODS WITH INDIA: OPPORTUNITIES AND CHALLENGES FOR PAKISTAN

Put "X" where answer best fits in your opinion.

		Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
1	Pakistan should continue to keep automobile sector on the negative list for imports from India					
2	Pakistan can eliminate the negative list for automobiles but it should continue to maintain the MFN tariffs and not allow any concessions under SAFTA					
3	Pakistan should open trade with India through a managed auto trade regime (e.g. Brazil and Argentina adopted this practice by which exports of Brazil were restricted to what it would import from Argentina)					
4	Pakistan should protect its passenger car industry but can open trade for tractors, motorcycles and auto-parts					
5	Pakistan needs 3+ years to prepare for any liberalization of auto trade with India. It could not effectively compete now					
6	Pakistan's auto industry will be able to effectively compete with Indian auto industry if level playing field is ensured					
7	Pakistan's auto industry will be able to effectively expand in India through competitive exports					
8	Pakistani auto industry would benefit by importing cheaper raw materials from India rather than from far off sources					
9	Pakistani auto industry should be able to source components and CKD kits from India					
10	It would be acceptable if Pakistan imported a limited number of passenger cars from India					
11	Pakistani cars are competitively priced compared to Indian cars					
12	Pakistani cars are of competitive quality compared to Indian cars					
13	Some framework agreement should be worked out with the Indian auto industry to allow use of technical training facilities					
14	Pakistan and India should cooperate in operational and technical areas for developing their auto industries					
15	Pakistan and India should have joint ventures in the auto industry					
16	Non tariff barriers from India to Pakistan would not allow any meaningful exports from Pakistan to India					
17	Pakistan and India meet similar environmental standards for auto production					
18	It is in my own company's best interest to open trade with India					

	Comments
19	In your opinion, what are the greatest challenges to opening up trade with India?
19	In your opinion, if Pakistan were to open up trade in auto sector with India, what approach should it take? What are some of the measures to ensure Pakistani auto-manufacturers benefit from increased trade relations?
20	Any further comments

The International Trade Centre implemented the Trade Policy Capacity Building Component of the European Union funded TRTA II programme. It is aimed at the Ministry of Commerce and Government of Pakistan in developing a coherent trade policy and attendant regulations for export competitiveness. Specifically, it will aim to reinforce the skills of government officers working in trade related ministries and implementing agencies on issues related to trade policy, commercial diplomacy and regulatory reform. The main way in which to achieve this through the institutional capacity building of key local training institutes, which is intended to have an immediate effect on the capacity of government officers working on trade policy issues.

In addition, Component 1 promotes comprehensive, regular and well informed public-private dialogue among the government, private sector and civil society for trade policy development, monitoring and evaluation. To promote local ownership and legitimacy of the dialogue, a steering committee comprising equal representation of the public and private sectors has been established with the formal approval of the Ministry of Commerce of Pakistan. Its mandate is to oversee the planning, implementation and monitoring of public-private dialogue on key issues. To better inform the public-private dialogue process, research studies are commissioned and internationally peer reviewed before dissemination to stakeholders.

The targeted interventions of Component 1 to achieve these goals constitute the following:

Result for Component 1: Coherent trade policy and regulatory reform for export competitiveness

1. The Pakistan Institute for Trade and Development (PITAD) institutional capacity is strengthened.
2. PITAD's and other research institutes' expertise on trade policy strengthened.
3. Government officers' capacity on specific trade policy and international trade negotiations strengthened.
4. Research studies contributing to the development of a national export strategy conducted.
5. Public-private dialogue for a coherent national export strategy is fostered.



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For further information about the ITC implemented Component 1
and the TRTA-II programme visit: <http://trtapakistan.org>