A STUDY OF PAKISTAN'S TRADE AND ECONOMIC RELATIONS WITH THE EUROPEAN COMMUNITY IN THE CONTEXT OF EC'S TRADE AND DEVELOPMENT POLICIES

by

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ABSTRACT

The study presents the evolution of Pakistan's trade and economic relations with the EC and endeavours to investigate the effects of the EC's special and preferential trade as well as development cooperation regime on their relations over the years. First, it examines the changing character of Pakistan's global trade and economic relations and manifests the importance and significance of the EC for Pakistan. It also attempts to identify the principal instruments of the EC's trade and development cooperation regime which regulate trade and capital flows and explores their nature and application towards developing countries in general and Pakistan, in particular.

The study then investigates the effects of the EC's special and differential trade regime on the trade flows of Pakistan with the EC. In this regard, it considers trade and economic relations of Pakistan with the EC conducted through Generalised System of Preferences (GSP), bilateral agreements concluded within the framework of Multifibre Arrangement (MFA) and bilateral cooperation agreements. It also explores the price raising effect of the MFA restraints and estimates the quota rent accrue to Pakistan for its textile and clothing exports to the EC. Further, the study meditates to provide empirical evidences of how far Pakistan has fared in the EC market in relation to its competitors consistent with the EC's trade regime. This study further enquires into the possible trade implications of the EC's enlargement towards Southern Europe for Pakistan.

Finally, the study explores the ways and means by which Pakistan can become an attractive site for foreign direct investment in future. In this regard, it identifies and analyses the effectiveness of various factors which have motivated and are likely to motivate the flow of foreign direct investment in Pakistan in general and from the EC, in particular.

CHAPTER 1

INTRODUCTION

The aim of this study is summed up in its title. It endeavours to examine the evolution of trade and economic relations of Pakistan with the EC and investigates the impact of the EC's special and preferential trade as well as development cooperation regime on their relations over the years.

The level of tariff protection in the EC has continued to fall in the post-war years as a result of successive tariff cutting rounds and the spread of preferential tariff arrangements. This liberalisation has been offset by an extension of non-tariff import barriers (NTBs)- for instance, quantitative restrictions, technical controls and anti-dumping and countervailing actions. Many observers argue that, on the whole, this 'new protectionism' has not entirely offset the liberalisation gains in tariff protection, but others see it as a major discouragement to the manufactured exports of developing countries. There is a similar belief which is widely conferred in the business and official circles in Pakistan. This study attempts to contribute to the debate on this belief.

Examined in this context, the main hypothesis of this study is that whether the EC's discriminatory trade treatment and new protectionism have jeopardised the expansion of Pakistan's exports to the EC market; or on the contrary, Pakistan has benefited from this restrictive market owing to the provision of trade concessions granted by the EC under its Generalised System of Preferences (GSP) and financial and technical assistance provided through bilateral agreements.

In order to test the hypothesis, the following main issues are addressed in this study.

a) The EC's external trade policy regime is highly complex and complicated. The very complexity of the trade regime governing access to EC market can be seen as a form of trade barrier in itself. The study describes the various trade barriers which attempt to restrict the level of EC imports from the developing countries.

Offsetting these restrictive provisions, the EC has instituted preferential arrangements with the aim of encouraging additional exports from developing countries including Pakistan. Both these aspects of the EC's trade regime are considered in this study. The study also sheds light on the instruments of EC's development cooperation policy towards developing countries in general and finds its relevance and importance for Pakistan, in particular, both at the multilateral and bilateral levels.

b) The EC's trade policy barriers have proliferated in recent years, most markedly against exports from developing countries including Pakistan. Various instruments of non-tariff barriers have been introduced by the EC, such as the Multifibre arrangement (MFA), bilateral import quotas, orderly market arrangements (OMAs), voluntary export restraint agreements (VERs), safeguard measures, the restrictive application of standards, antidumping laws, the granting of subsidies to domestic producers, etc. Of these, from the standpoint of Pakistan, the MFA restrictions are regarded as the most prominent example of the use of bilateral arrangements to regulate the volume of Pakistan's exports to the EC market by mutual consent. This study deals with the effects of MFA and explores its impact on the country's textile and clothing exports to the EC market.

c) Some EC trade policies such as the Generalised System of Preferences (GSP), the Global Mediterranean Policy (GMP) and the Lome Convention are designed to provide developing countries with a margin of preferential access to help them overcome some of the structural disadvantages they face in trying to compete in the EC market. The EC's differential trade arrangements with its trading partners add up to a hierarchy of trade preferences what has been called the 'pyramid of privilege'. This study enquires into whether these 'special and preferential treatments' have caused any trade diversion from Pakistan in favour of the developing countries having 'special' trade arrangements with the EC at the cost of Pakistan's exports.

d) In the light of static and dynamic effects of a customs union, the second enlargement of the EC from nine to twelve is likely to have strengthened trade within the EC and to have weakened it with other countries outside the EC including

Pakistan. As a general rule, to the extent that their exports compete with those of three new members, they will find themselves at a different disadvantage position in selling their exportable items to the EC market. How has this enlargement affected Pakistan's exports to the EC market? Has the enlargement resulted in diversion of EC's imports from Pakistan a traditional source of supply in favour of its new members (i.e, Greece, Portugal and Spain)?. What are the long term dynamic implications of the EC's recent enlargement for Pakistan's exports to EC market? The study meditates to provide empirical evidences in this regard.

e) In view of neoprotectionism (NTBs), it is argued that improving market access for developing countries' exports is no longer simply a matter of further reducing tariffs, because trade policy barriers operative in the EC as well as in other industrialised countries are increasingly complex. Past experiences have demonstrated that trade liberalisation of trade approach has not proved to be a very effective instrument of development. This is because firstly, production is needed in order to have goods to trade with. Secondly, NTBs have reduced the relative importance of tariffs. Thirdly, international trade is increasingly becoming a result of long-term technological cooperation contacts. All these factors, as well as the debt problem of Pakistan, necessitate to focus on alternative measures like foreign investment promotion ones. This study sheds light on the role of foreign assistance both as a source of foreign capital and improved technology in the country's economic development and explores some ways and means in which further development cooperation between Pakistan and the EC member countries might be strengthened. Joint-Ventures are supposed to be an important instrument of such cooperation among partners. The study focuses on this issue and investigates how Pakistan can become an attractive site for foreign direct investment in future. In this regard, it identifies and analyses the effectiveness of various factors which are likely to motivate foreign direct investment in Pakistan in general and from the EC both at the multilateral and bilateral levels, in particular.

In order to achieve this desired aim and objective, the framework of the study is arranged as follows.

Chapter 2 provides an overview of Pakistan's trade and economic relations in the context of the changing character of its economy. It also manifests the importance and significance of the EC in the framework of Pakistan's global trade and economic relations. In this framework this chapter serves two objectives. First, it provides basic information to those not familiar with Pakistan's experience of economic development. Second, it outlines a general framework within which one can comprehend Pakistan's subsequent economic development.

Chapter 3 describes the principal instruments of the EC trade and development cooperation policy regime and explores their nature and application which regulate trade and capital assistance flows. The ambiguous nature of EC's trade policy is highlighted. On the one hand, through various formal instruments such as quantitative restraints, anti-dumping, countervailing actions, etc., the EC attempts to restrain market access for imports from developing countries. On the other hand, through the Generalised System of Preferences and other preferential arrangements, it attempts to encourage increased manufacturing exports from the developing countries. This chapter considers both these aspects of the EC's external trade policy regime with special reference to Pakistan. Finally, this chapter identifies the main instruments of the EC's development cooperation policy towards developing countries and examines their availability for Pakistan both at the multilateral and bilateral levels over the years.

Chapter 4 examines the effects of the EC's special and differential trade policy regime on the trade flows of Pakistan to the EC market in regards to its competitors. This chapter provides empirical evidence on whether the EC's discriminatory trade treatment and new-protectionism (NTBs) have threatened the expansion of Pakistan's manufactured exports to the EC market, as Pakistan has been at the bottom of its hierarchy of external trade relations what has been called the "pyramid of privilege". This chapter also appraises the argument whether the developing countries, including

Pakistan would not be better advised to dispense these preferences and seek reductions in ordinary MFN tariff on products of specific interest to them.

Chapter 5 deals with the effects of voluntary export restraints (VERs) legitimised under the Multifibre Arrangement (MFA) considering its price raising effect and especially on what can be learned from information on quota premia. In this regard, the quota rents accruing for Pakistan's textile and clothing exports to the EC market is estimated. It also highlights the effects of MFA relaxation both for the developed and developing countries using the extent of Pakistan's quota premia. Further, it examines various proposals put forward for ending the MFA mainly with the object, if the MFA is to go, how best it can be done? Finally, this chapter analyses and provides empirical evidences on how far Pakistan has fared in the EC market in relation to its competitors consistent with the EC trade regime under the MFA restrictions and how she is likely to perform in a world without the MFA.

Chapter 6 endeavours to explore the possible implications of the EC's enlargement for Pakistan. In this regard, it first examines the theoretical implications of the enlargement for member and non-member countries. It attempts to draw an exact picture of the institutional links between Pakistan, the European Community and its new member countries both before and after the enlargement and compares the two situations and predict the direct trade effects of the enlargement derived from these revised institutional arrangements. Then this chapter embarks on an empirical investigation of trade implications for Pakistan's exports in the EC market and explores such implications for Pakistan in the enlarged EC and in the new EC Member countries as well. This is done suitably by adopting the framework of trade creation and trade diversion for Pakistan's major export items (around twenty) at the disaggregated level (i.e. 8 digit).

Chapter 7 attempts to answer the question why is it more important to concentrate on foreign direct investment (FDI) today than yesterday, as compared to trade liberalization orientation. Keeping in mind the importance and role of FDI in the country's economic development, this chapter is devoted to explore the ways and

means by which Pakistan can become an attractive site for such investment in regards to its competitors in general and from the EC member countries, in particular. It mainly embodies the results of the case study based on the evaluation of the primary data obtained through a questionnaire which was sent to the EC firms those already invested in different sectors of the economy in Pakistan. The aim of case study was to identify and analyse the effectiveness of various factors which have motivated and are likely to motivate FDI in Pakistan in general and from the EC, in particular.

Finally, chapter 8 presents a summary and statement of conclusions.

CHAPTER 2

AN OVERVIEW OF PAKISTAN'S TRADE AND ECONOMIC RELATIONS

The purpose of this chapter is twofold. First, to analyse the changing character of Pakistan's trade and economic relations over the years. Second, to find out the significance of the EC in the framework of Pakistan's global trade and economic relations. To this end, section 2.1 provides an overview of Pakistan's development experience and shows the changing pattern of its economy over the years. Section 2.2 describes the commercial Policies and management of Pakistan's foreign trade. Section 2.3 focuses on the composition of country's foreign trade and traces the source of growth or decline of the economy at the commodity level thus showing the links between internal development and international trade. Section 2.4 and 2.5 explore the importance and significance of the EC for Pakistan both in the areas of trade and foreign capital assistance over the years.

2.1 Development Experience and the changing character of Pakistan's Economy

The pattern and experience of the economic development of Pakistan has not been much different from that of other developing countries. As with most market-oriented economies, international trade and investment played an important role. In earlier years, the agriculture sector accounted for a significant proportion of the gross domestic product (GDP), exports and employment. During the last two decades, the structure of Pakistan's economy has undergone significant change and it has now become more industrialized. It witnessed a rapid transformation in its economic structure, with the share of agriculture in GDP declining steadily. In contrast, the share of non-agriculture sectors increased over time (see Table 2.1). For example, in 1949, the agriculture accounted for 60% of GDP, manufacturing only 6%, mining and quarrying 0.11%, public administration and defence 4% and wholesale and retail

trade 11%. A discernible trend towards diversification of the economy emerged during the last four decades. The economic growth of Pakistan has been quite impressive and among the low income countries is listed in "three top growth performers (i.e., Sri Lanka, China and Pakistan)" (see, Yousuf and Peters, 185 and Stern, 1989).

Table 2.1 DISTRIBUTION OF GROSS DOMESTIC PRODUCT

[Share percentage]

Sectors	1949	1965	1970	1975	1980	1985	1990
GDP	100	100	100	100	100	100	100
Agriculture	60	37	35	32	29	26	24
Industry	6	15	17	15	17	19	21
Others	34	48	48	53	54	55	55

Source:Calculated from Economic Survey of Pakistan 1992-93.

Compared with other developing countries having similar levels of income, Pakistan was rather late to develop its industrial sector and to exploit the international trading environment which was liberalized after World War II. The country heavily relied on exports of primary commodities and exports of manufactured goods were negligible. Until 1960 a number of state enterprises through Pakistan Industrial Development Corporation (PIDC) were set up to produce a wide range of manufactured goods. However, the attempt to develop the manufacturing sector turned out to be a failure as most of these enterprises were inefficiently operated and there was widespread corruption in their management which led to substantial losses. Furthermore, private investors were reluctant to invest in the manufacturing sector to compete with the state enterprises. Private investment in manufacturing was thus mostly confined to small-scale production. The major industries with private investment were rice and saw milling, textiles and wearing apparel, and household handicrafts [1].

It was not until the 1960s that Pakistan sought to actively promote industrialization through the free-enterprise system relying on private initiatives. Especially, with the launching of Second Five Year Plan (1960-65), the

government began to reduce its direct involvement in the manufacturing sector and instead switched to playing a supporting role for private enterprises by dismantling the government machinery of economic controls over prices, imports, and industrial investment and by granting investment incentives and providing public infrastructure.

The 1960s saw a rapid growth of the economy. Numerous import-competing industries (particularly fertilizer, cement, edible oil, chemicals, machines and tools industries, etc.) were set up, the inflows of foreign direct investment were accelerated and a modern industrial sector was created. The agriculture sector also underwent diversification and there was a rapid expansion of cropping area and in the use of high yield varieties (HYVs) of seeds and other inputs. The non-agriculture sectors such as construction, banking, trade and services also grew rapidly as the economy expanded as is evinced from Table 2.1. In the 1960s the economy was able to grow at an annual average rate of 7 per cent.

Despite reasonable growth and diversification of the economy, there were a number of problems created by rapid industrialization. In the industrial sector in particular, the problems identified included inefficiency of some import-competing industries as a result of tariff protection, heavy reliance on imported inputs, limited employment absorptive capacity and heavy concentration of manufacturing activities in big cities. These problems were considered to be partly due to the promotion of import-substituting industries catering for the needs of urban upper income groups, and the investment incentive structure which favoured capital-intensive rather than labour-intensive industries that encouraged the utilization of imported materials.

During the 1970s, some attempts were made to correct the distortions in the investment incentive structure. Emphasis was placed on the reduction of tariff protection, simplification of trade regime, promotion of manufactured exports and promotion of small-scale and provincial industries. But due to various reasons, most of these policies were not implemented effectively. Among other things, the government was largely preoccupied with solving the problems arising from nationalisation and land reforms and from external shocks and instability in the

domestic financial market. The long-run objective of structural adjustment was thus neglected.

In the first half of the 1970s, Pakistan was rather fortunate at first to be able to withstand the onslaught of the first energy shock. It seems that the following factors contributed to this better situation. First, a substantial increase in exports combined with a decline in imports caused partly by success in import-substitution. Second, the massive devaluation (56% in May 1972) contributed significantly towards boosting and restoring the competitiveness of exports and curtailing expensive imports. Third, exports were channelled into new markets and were also increased due to the diversification of exportable surplus from East Pakistan (now Bangladesh). Fourthly, the world wide shortage of food and the rise in the international prices of primary commodities of great interest to Pakistan during 1972-74 also played a key role in softening the impact of the first oil shock.

As the effect of massive devaluation exhausted itself and necessary adjustments in domestic prices, wages and costs to new exchange rates took place, the non-viability of the economy began to manifest itself. The growth of agricultural and industrial sectors during the first half of the 1970s decelerated and the rate of inflation reached at double-digit level. Furthermore, as export commodity prices moderated in the mid-1970 and the ensuing world inflationary impact started to be felt through more costly imports, the deficit in Pakistan's balance of trade increased sharply. It rose from only Rs.124 million in 1971 to Rs.9212 million in 1975 and as percentage of GNP it jumped from 0.2% to about 7% during the same period. Table 2.2 summarise the different aspects of Pakistan's balance of trade since 1970.

Significant improvements are witnessed in the growth rates of all sectors of the economy during the first half of the 1970s. The economy was able to grow by 5%, and most of the growth was contributed by the service sector rather than agriculture or industry. As a result, the share of services in the GDP composition increased significantly (see, Table 2.1). Agriculture sector grew

Table 2.2 PAKISTAN'S BALANCE OF TRADE:1970-1990

[Rupees Million]

Year	Exports	Imports	Balance of Trade	Exports as % of Imports	Deficit as % of GNP
1970	1998	3602	-1604	55.5	3.2
1971	3371	3495	-124	96.5	0.2
1972	8551	8398	153	101.8	--
1973	10161	13479	-3318	75.4	3.7
1974	10286	20925	-10639	49.2	9.5
1975	11253	20465	-9212	55.0	6.9
1976	11294	23012	-11718	49.1	7.5
1977	12980	27815	-14835	46.7	7.9
1978	16925	36388	-19463	46.5	9.3
1979	23410	46929	-23519	49.9	9.3
1980	29280	53544	-24264	54.7	8.7
1981	26270	59482	-33212	44.2	9.5
1982	34442	68151	-33709	50.5	8.3
1983	37339	76707	-39368	48.7	8.6
1984	37979	89778	-51799	42.3	10.1
1985	49592	90946	-41354	54.5	7.4
1986	63355	92431	-29076	68.5	4.8
1987	78445	111382	-32937	70.4	4.7
1988	90183	135841	-45658	66.4	5.7
1989	106469	148953	-42484	71.5	4.7
1990	138342	171052	-32710	80.9	3.1

Source:Calculated from Economic Survey of Pakistan, various issues.

by only 2%, while manufacturing sector grew by 4% as depicted in Figure 2.1. It also indicates the growth rates of GDP, gained by the economy during the last two decades. However, the 1970s saw a surge in public sector investment and a rapid expansion of manufactured exports. The most dynamic area of exports growth was the small-scale manufacturing industries, including carpets, garments, leather, footwear, sporting goods, surgical and electrical goods as we shall see latter. The emphasis on export promotion has since continued.

It was not until the early 1970s that the government started to actively promote the export of manufactured products. There were several factors which led to a change in the industrialization strategy toward export

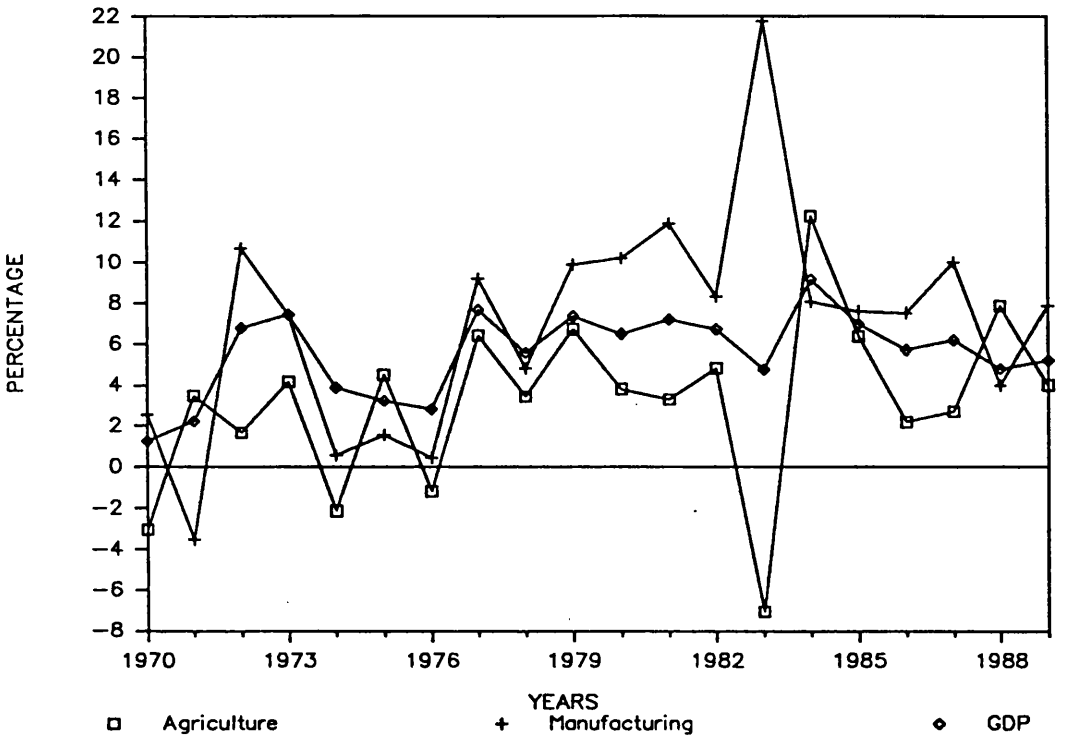


Fig: 2.1 GROWTH RATES OF GDP, AGRICULTURE AND MANUFACTURING.

promotion. Among these were the slowing down of growth of a number of import-competing industries, the realization of the adverse effects of an import-substitution strategy that relied heavily on imported inputs and the concentration of industrial activities around big cities. The successful experience of the Asian Newly Industrializing Economies (NIEs) in achieving high economic growth through the adoption of outward-looking strategies might also have influenced the change in the industrialization strategy [2]. Manufactured exports expanded rapidly in the 1970s. The share of manufactured products in merchandise exports rose dramatically from 28% in 1970 to 43% in 1979. On the other hand, the share of primary commodities decreased in country's total exports. Figure 2.2 depicts the shares of primary commodities, semi-manufactures and manufactured goods in the country's total exports since 1971.

The 1980s have been a period of stark contrast. After facing serious economic problems and low economic growth in the first half of the decade a dramatic turnaround took place in the latter half. The second oil shock in 1979 brought about a significant slow down in the domestic economy in the first half of the 1980s. This was compounded by declining prices of agricultural commodities which were Pakistan's major exports. The unfavourable terms of trade led to the largest trade deficit the country has experienced. As a proportion of GNP, the trade deficit rose from 7% in 1975 to 10% in 1984 (See Table 2.2).

The problems in the early 1980s were accentuated by the inflexible policy of fixing the value of Pakistani rupee to the US dollar. As the value of the dollar rose in the early 1980s, the value of the rupee rose which had a negative impact on Pakistan's exports. The country's trade deficit and foreign exchange reserves reached a critical stage and government was forced to take serious action. As a result, a major policy shift took place by delinking the rupee from U.S. dollar and adopting the Managed Floating Exchange Rate System. The Pakistani rupee would no longer be strictly tied to the dollar, although the dollar was given the largest weight in the central bank's currency basket used in determining the value of

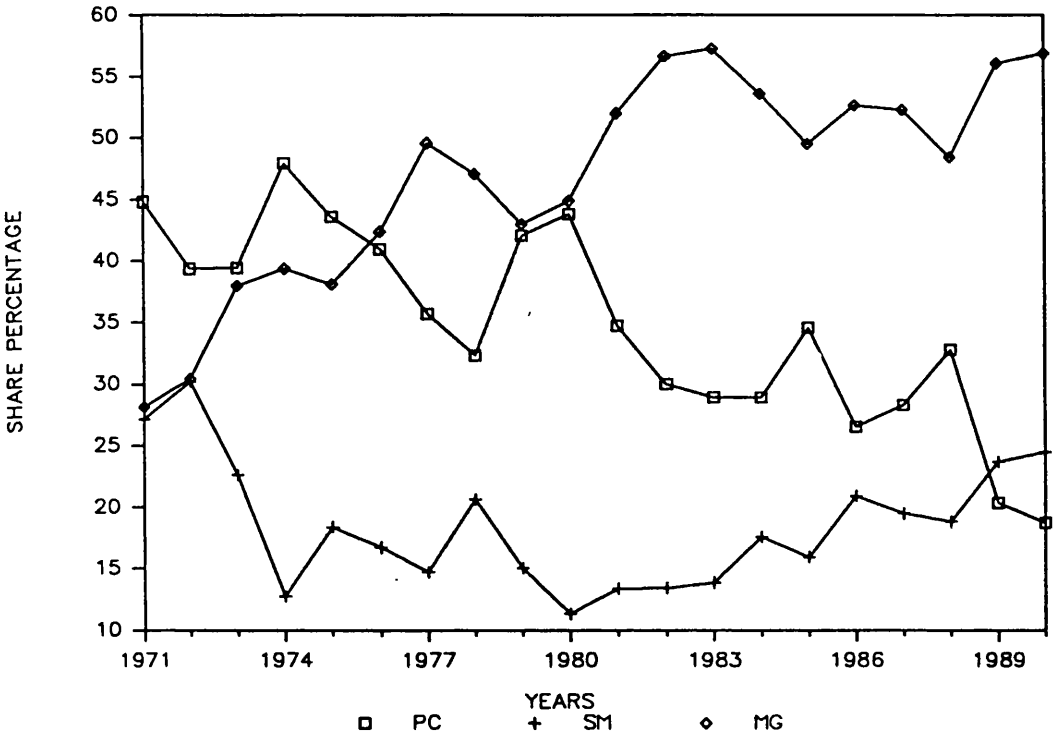


Fig 2.2 EXPORTS BY ECONOMIC CLASSIFICATION.

Abbreviations:

PC - Primary Commodities
SM - Semi-Manufactured and
MG - Manufactured Goods.

the rupee (Pakistan Economic Survey, 1982-83).

In contrast to the 1970s, economic growth during the 1980s was accelerated and the economy obtained impressive growth rate except in 1983 when the economy grew by only 3%. On the other hand, the economy experienced one of its strongest recoveries with the growth rate reaching 10% in 1982, the highest in the last two decades. Several factors contributed to the reversal of the economic trend.

Firstly, the decline in oil prices since 1982 has benefited the country significantly, reducing the trade deficit substantially and therefore helping to moderate foreign borrowing. Manufacturing industries have also benefited from large cost reduction from lower energy prices while consumer purchasing power increased due to better terms of trade as a result of the reduction in oil prices.

Secondly, the adoption of the Managed Floating Exchange Rate System in 1982 and consequently the depreciation of Pakistani rupee created an environment which has been supportive of export industries. The exchange rate policy has helped to open up the world market to local industries. Exports started to pick up rapidly, growing at around 25% in 1980, 28% in 1986 and 30% in 1990.

Thirdly, the recovery of commodity prices also contributed to rapid growth in the agricultural and industrial sectors which stagnated during the 1970s. Since the majority of the county's population is in the agricultural sector, the better commodity prices contributed to increased purchasing power of the masses.

It is obvious from above discussion that global economic trends have had a significant influence on the economy of Pakistan. In the early 1980s, prolonged recession in developed market economies, increased energy prices, high interest rates and depressed commodity prices led to the slowdown of Pakistan's economy. These world economic trends also influenced domestic economic stability in terms of increased trade, current account deficit and debt-servicing burden, higher rates of inflation, larger government fiscal deficits, instability in the domestic financial market as interest rate increased. In the latter half of the 1980s, however, the turnaround in the situation helped to stimulate the domestic economy which, in turn, helped the

government to collect more revenue from taxation and thus its fiscal condition has significantly improved in recent years.

Although the world economic environment had a significant impact on Pakistan's economy, several measures adopted by the government since 1978 contributed to the economic upturn in the 1980s. Among others, the adoption of more flexible management of the exchange rate and the devaluation of rupee have been particularly helpful to continued export expansion. Further, the increased inflow of workers remittances earned the necessary foreign exchange to finance industrial development and development of resource-based industries, the availability of low-cost labour for the development of labour-intensive industries and the stable economic environment made possible by prudent management.

Further, foreign exchange earnings from services, direct investment and foreign capital assistance also played an important role in financing the provision of necessary infrastructure and the import of capital equipment vital for economic development. Above all the encouragement of private investment (which was reluctant to invest during the first half of 1970s due to nationalization) and avoidance of direct government involvement in manufacturing and other economic activities since the 1977 helped the development of industries which relied on market forces and were consistent with the country's comparative advantage. Although there were government interventions and various distortions in the trade and production regime, the distortions were not as severe as in some developing countries.

2.2 Commercial Policies and Management of Foreign Trade

Pakistan's commercial policies are a combination of sub policies administered by different government agencies. These includes: (a) the Foreign Exchange Control Policy administered by the Foreign Committee of the Ministry of Finance which regulates the inflow and outflow of foreign exchange and allocates foreign exchange between the public and private sectors; (b) the Import-Licensing Policy dealing with the disbursement of foreign exchange allocated to the private sector between various

uses and users and which is supervised by the Chief Controller of Exports and Imports; (c) the Export Promotion Policy devised by the Ministry of Commerce most often concentrated on providing the incentives needed to maximize exports and (d) Tariff policy enforced by the Ministry of Finance mainly as a revenue raising device. These policies have altogether assumed the shape of tariff barriers, non-tariff barriers (NTBs) and export incentive schemes.

Tariff and Non-Tariff Barriers: Pakistan's tariff structure is quite complicated and is a mixture of a number of tariff/taxes. The average tariff rate is now about 30%. The highest average import taxes were levied after the 1965 war with India when these taxes were on average above 50% for three consecutive years. Even today Pakistan's average (nominal) tariff rank at the top, along with India's, among developing countries (World Bank 1988, p.68). Individually for different kinds of items these rates varies from zero to 200%. Tariffs do not tell us the whole story of trade as other impediments exist.

Many NTBs to import exist in Pakistan. Some of these are so high as to be prohibitive. They take many forms: very high tariffs, import quotas, licensing, administrative guidance, state purchasing monopolies, domestic content rules, religious requirements, and outright import bans (see, NEDO, 1986). However, the introduction of a positive list in terms of explicit import quotas and list of commodities which could be imported can be regarded as major forms of NTBs in Pakistan. Till 1983 there was a positive list of imports which were allowed to be freely imported. All other items needed explicit approval from the government in terms of an import licence for the import of a commodity. In June 1983, the government switched from a positive to a Negative List system which explicitly listed banned and restricted imports. This list has been revised many times downwards in order to liberalize imports. However, Pakistan continue to depend on import bans and restrictions for protection of import substitution industry. For example, in July 1987, about 52% of consumer goods, 22% of intermediate, and 11% of capital goods were on the Negative List. According to the World Bank (1988, p.64) estimates in 1980

when Pakistan's import regime reached its most restrictive stage, about 41% of the domestic industrial value added was protected by import bans and another 22% by various form of import restrictions. With the introduction of the Negative List system and some other import liberalization measures, the equivalent percentages were 29% and 3.7% in 1986. The official position on import bans and restrictions, as expressed in Import Policy Orders (1986), states that Pakistan's tariff and non-tariff barriers serve two purposes: to provide "assured" protection to import competing industries, and to restrict imports of luxury consumer goods.

Export Incentives: In 1954 for the first time an Export Incentive Scheme was introduced but it was not successful in promoting exports. In order to stimulate exports in view of changing policy environment a new scheme know as Export Bonus Scheme (EBS) was introduced in 1969. Under this scheme, exporters were entitled to retain a certain percentage (usually between 20% to 40%) of their exchange earnings (called bonus) in the form of "import bonus vouchers". The effectiveness of the EBS was all the most remarkable and is considered to be one of the most successful export promotion schemes in Pakistan. Since the licenses command a high premium in the open market, this served as a strong incentive to export activity. In effect the scheme mounted to a selective devaluation of rupee or (alternatively) to a system of selective export subsidies and therefore, had the implicit effects of multiple exchange rate [4]. After the devaluation of Pakistani rupee in 1972 the scheme was abolished.

Currently exports from Pakistan are subject to a number of incentives which include: i) rebates of sales and excise tax (paid on domestically produced goods), ii) rebates of custom duties (paid on imports) used in the manufacture of exports, iii) export subsidies and rebate of corporate income tax, iv) duty free import of machinery for balancing, modernisation and replacement (BMR) and under Pay-As-You-Earn Scheme (PAYE) and provision of concessionary credits for exports [5].

Exchange Rate Policy: At the time of independence Pakistan's rupee was linked with the Pound Sterling. The first major crises in the foreign exchange control policy came in 1949 when the pound Sterling was devalued by 31%. While other

members of Sterling areas followed suit, Pakistan decided to not to devalue its currency. This decision particularly disrupted the trade with India who refused to recognise the exchange rate of its currency in terms of the Pakistani rupee. As a result, Pakistan's exports substantially declined because at that time India was a major trade partner of Pakistan. In 1956, as a late response to the pound's devaluation, the Pakistani rupee was also devalued and its new exchange rate was changed from Rs.2.80 to Rs.4.76 per US dollar.

The exchange rate of Rs.4.76 per US dollar was maintained for quite a long time. The rupee was devalued second time in 1972 by about 56%. The new exchange rate in the beginning was Rs.10.47 per US dollar. Following the devaluation of dollar itself in February 1973, the par value of Pakistani rupee was somewhat improved to Rs.9.90. The new exchange rate was kept fixed for another eight years. In 1982, Pakistan delinked its rupee from the US dollar and adopted the managed floating exchange rate system. This was by far the most important decision in the history of the exchange rate regime of Pakistan, because the delinking of rupee and consequently its depreciation proved to be an effective tool for restoring the competitiveness of Pakistani exports which resulted in an improving the country's balance of trade significantly.

2.3 Composition and Trends of Pakistan's Foreign Trade

The rapid economic growth and structural changes in the economy over the years as examined above have resulted in significant changes to the structure and composition of Pakistan's foreign trade. Table 2.3 reveals Pakistan's net composition of trade by Standard International Trade Classification (SITC) sections presented as a percentage of its total trade. It is important to note that originally data for Pakistan's exports and imports was available broad commodity-wise rather than SITC. The data has been converted to the SITC by the author according to the list of products: SITC revised 3 published by Eurostat and every care has been taken while

converting and estimating the data according to SITC. Table 2.3 points out the net position of Pakistan as a net exporter or a net importer of categories of traded goods.

Table 2.3 NET COMPOSITION OF PAKISTAN'S FOREIGN TRADE
[Selective years]

[Net exports by SITC as a percentage of total trade]					
SITC	1971	1975	1980	1985	1990
(0) Food, Live animals	-0.89	1.72	5.02	-0.62	0.03
(1) Beverages & Tobacco	0.36	0.50	0.07	0.14	0.04
(2 Materials Crude	3.72	0.13	3.22	1.80	0.64
(3) Minerals Fuels	-13.15	-11.20	-16.33	-11.58	-11.94
(4) Veg.Oil and Fats	0.15	0.11	0.07	0.07	0.10
(5) Chemicals	-3.83	-4.58	-8.68	-8.23	-8.90
(6) Manufactures Basic	9.13	4.82	4.94	6.12	16.93
(7) Machines, Transport Equipments	-6.61	-8.01	-7.97	-8.75	-5.29
(8) Manufactures Misc.	-5.24	-5.23	-1.80	-6.82	-3.77
(9) Unclassi-fied Goods	-5.45	-7.31	-3.83	-1.56	1.65

Source: Compiled and calculated from PES 1991-92.

Goods in SITC 0-4 are generally regarded as natural resource-intensive products. Goods classified as chemicals SITC 5, and machines and transport equipment SITC 7 and Misc. manufactures SITC 8 are generally considered as relatively capital-intensive products. Finally, goods in SITC 6 and SITC 9 are treated as labour-intensive products [8]. Human capital requirements may be high in many of these categories, especially manufactures (SITC 5-8). For instance, miscellaneous manufactures (SITC 8 includes highly differentiated goods which require considerable entrepreneurship as well as basic labour inputs. Also, chemical and machinery industries often use advanced technology and employ highly trained labour and professional engineers. Finally, even for more advanced industries, it should be understood that the production of certain manufactures

may still involve considerable basic labour inputs. For example, the manufacture of many advanced electronics products (included in SITC 7) often involves the labour-intensive assembly of product components, with the result that countries relatively abundant in basic labour services can sometimes be greatly involved in manufacturing advanced technology products.

Of particular interest in the data presented in Table 2.3 are the patterns of positive and negative net exports by category of traded goods and the relationship of these patterns with the factor endowments of Pakistan. In the absence of significant policy-induced distortions to trade patterns, by definition Pakistan may be regarded as having a "revealed comparative advantage" in resource-based and labour-intensive and, conversely, comparative revealed disadvantage in capital-intensive categories [6].

Broadly speaking, despite significant policy distortion, the net composition of Pakistan's trade seems to be consistent with the above line of argument. Pakistan exhibits strong comparative advantage in SITC 1 beverages and tobacco, SITC 2 crude materials, SITC 4 vegetable oil and fats and SITC 6 basic manufactures and comparative advantage to some extent in SITC 0 food and live animals. This suggests that the primary sources of comparative advantage for Pakistan are agricultural natural resources and basic labour services. On the contrary, data shows that Pakistan has a strong comparative disadvantage in all the categories of capital intensive goods like SITC 3 mineral fuels, SITC 5 chemicals and SITC 7 machine, tools, transport equipment, SITC 8 misc. manufactures, etc.

An important conclusion to be drawn from above discussion is that a country's pattern of foreign trade, the composition of exports, and the direction of exports depend on both supply and demand conditions and the determinants of supply and demand are continually changing, because resources are depleted or made obsolescent by technological change. Capital, both physical and human, accumulates, changing the relative costs of production, and is made obsolescent by technological changes (and changed factor endowments) elsewhere. Costs fall as output expands and

experience is gained. Knowledge accumulates, bringing innovations or technological breakthroughs. Changes in the size, age and sex composition of the population also alter the relationship between labour and physical capital and the stock of different kinds of human capital. Finally, policies and institutions change. The upshot is that comparative advantage or disadvantage of a country is ever-changing. The analyses of Pakistan's net composition of foreign trade clearly points out the changing comparative advantage and comparative disadvantage as well as its changing pattern of foreign trade. It divulges that the acquisition of capital goods and technology have been enabling Pakistan to decrease its comparative revealed disadvantage in capital-intensive categories of traded goods. These findings should be treated with cautions because these findings result from the highly aggregate trade categories considered. More disaggregate trade statistics should be examined [7].

The rapid economic growth leading to structural changes in the economy have resulted in changing the structure and pattern of Pakistan's foreign trade over the years. The major import items of Pakistan included machinery, iron and steel, petroleum and products, transport equipment, tea, edible oil, fertilizers, electrical goods, grains, pulses and flours, and medicaments. They accounted for more than 70% of the country's total imports during the 1970s and 1980s. Figure 2.3 presents the changing pattern of Pakistan's imports broadly defined by economic classification i.e., consumer goods, intermediate goods and capital goods over the last two decades.

On the import side, there has been a significant fall in the share of capital goods during the 1970s mainly due to nationalization and drop of in private investment. As a result, the share of capital goods declined from 42% in 1971 (47% in 1969) to 28% in 1980. In contrast, in the 1980s, the share of capital goods rose significantly as a result of the investment boom which required increased imports of capital goods. Similarly, the share of intermediate goods and raw materials imports rose as a result of liberalization of imports from 34% in 1969 to 41% in 1972 before levelling off due to the energy shocks in the 1970s which increased the import of oil and petroleum products significantly. As a result of these oil shocks the share

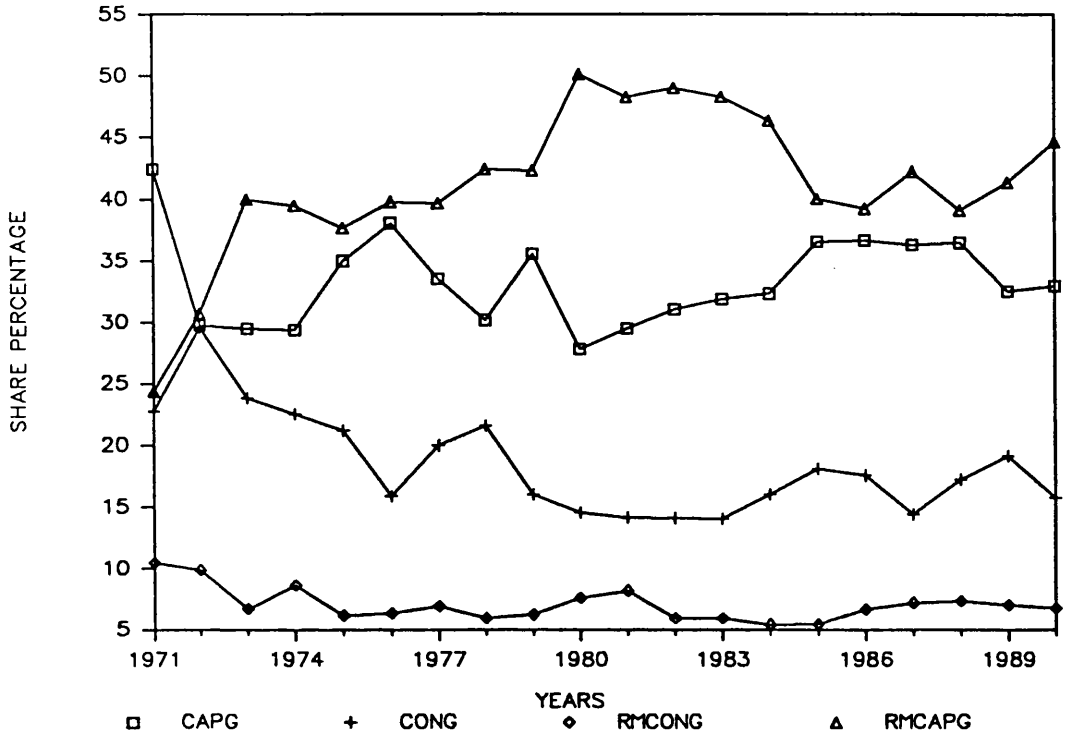


Fig 2.3 IMPORTS BY ECONOMIC CLASSIFICATION.

Abbreviations:

CONG - Consumer Goods.
CAPG - Capital Goods.
RMCAPG - Raw Material for Capital Goods.
RMCONG - Raw Material for Consumer Goods.

of this category of imports increased to 58% of total imports in 1980. However, with the fall in energy prices in the past few years, the share of intermediate goods and raw materials imported decreased marginally in the following years.

A prominent feature of Pakistan's external trade has been the country's heavy dependence on imports of consumer goods. However, during the 1980s, government endeavoured to reduce such a dependence on imports of consumer goods through import substitution and rapid industrialization. With concerted efforts, the volume of imports of consumer goods has been contained to a great extent. It became possible by vigorous and successful import substitution measures in respect of wheat, tea, sugar and edible oil as discussed earlier. As a result, their share in total imports declined considerably from 23% in 1971 to 18% in 1979 and further to 15% in 1990. During the 1970s, the share of consumer goods was considerably higher mainly due to the poor performance of the agricultural sector. The reasons given for poor performance of the agricultural sector were the abnormal weather conditions (a combination of floods and droughts) and the non availability of water from the Tarbela Dam.

Similarly, the export structure has also undergone a significant change. The diversification of exports resulted from rapid growth made relatively wide fluctuations in the behaviour of individual commodities and helped in changing the composition of Pakistan's exports drastically. There has also been a much wider range of exports. Table 2.4 reflects the changing composition and behaviour of Pakistan's principal exports and their share in the country's total exports since 1971. Broadly speaking, the positive impact of trade policies and export incentives provided over the years is clearly reflected in the changing behaviour of the country's exports. As discussed earlier, various changes in the export regime were introduced in the early 1970s. The overall policy was shifted in favour of small-scale sector relative to the large-scale sector. A component of these favourable policies was a sharp increase in bank advances. Simultaneously, various incentives and facilities were provided to the exporters in the form of rebates, tax concessions, etc.

Table 2.4 PAKISTAN'S PRINCIPAL EXPORTS

(Share %)

Item	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990
1. Fish & Fish Prepar.	3.3	2.7	2.7	1.5	2.5	3.4	2.6	2.7	2.3	1.9	3.0	2.6	2.7	3.2	2.7	3.0	2.8	2.3	1.9	1.9
2. Rice	8.1	13.3	20.6	22.4	22.0	21.9	18.6	20.0	17.9	19.1	15.7	10.7	15.2	8.8	11.1	8.1	8.2	6.6	4.8	5.7
3. Hides & Skins	0.6	0.2	0.2	0.4	0.3	0.0	0.0	0.0	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
4. Raw Wool	0.7	1.0	0.6	0.2	0.6	0.7	0.6	0.6	0.4	0.2	0.4	0.5	0.5	0.7	0.6	0.5	0.4	0.4	0.4	0.1
5. Raw Cotton	28.3	13.6	3.6	15.0	8.7	2.6	8.5	3.9	14.2	17.8	11.2	11.3	4.7	11.5	16.7	12.1	13.7	20.0	9.0	6.9
6. Cotton Waste	0.8	0.4	0.3	0.2	0.1	0.2	0.1	0.1	0.1	0.1	0.0	0.2	0.5	0.4	0.2	0.2	0.2	0.3	0.6	0.9
7. Cotton Yarn	17.6	22.7	17.8	8.3	12.6	10.4	8.2	11.6	8.7	7.0	7.9	9.1	7.8	10.5	9.1	13.7	12.1	12.9	16.8	19.3
8. Cotton Thread	0.4	0.4	0.5	0.6	0.4	0.4	0.5	0.3	0.3	0.3	0.3	0.5	0.3	0.2	0.1	0.1	0.1	0.1	0.1	0.1
9. Cotton Cloth	11.5	14.6	13.9	12.8	12.1	14.2	13.4	12.6	10.3	8.2	11.2	10.4	13.0	12.2	10.2	9.4	10.9	9.9	11.3	11.0
10. Leather	5.2	6.4	4.1	3.6	5.3	5.7	4.9	7.4	5.4	3.0	4.4	3.5	5.3	6.1	5.8	6.4	6.4	5.2	5.6	4.5
11. Petroleum & Products	1.2	1.5	1.7	1.4	1.7	2.4	4.8	3.6	7.5	5.7	7.8	2.9	1.5	1.4	1.0	0.7	0.6	0.4	0.2	0.6
12. Synthetic Textiles	0.4	0.7	0.6	0.2	0.3	0.3	1.2	0.4	0.2	4.3	0.9	8.1	3.9	1.7	1.6	4.3	4.4	2.5	4.3	5.6
13. Foot Wear	1.2	1.0	0.9	1.2	0.6	0.8	0.6	0.6	0.5	0.3	0.4	0.4	0.6	0.7	0.5	0.4	0.5	0.4	0.5	0.5
14. Animal Casings	0.3	0.2	0.3	0.2	0.3	0.3	0.2	0.2	0.2	0.2	0.2	0.2	0.1	0.2	0.2	0.2	0.3	0.2	0.2	0.2
15. Guar & Products	1.2	1.1	1.6	1.6	1.8	1.6	1.6	1.6	1.4	1.0	1.2	0.8	0.9	0.9	0.9	0.9	1.2	0.8	0.8	0.5
16. Paints and Varnish	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
17. Tobacco Raw & Manufac.	0.7	0.6	1.0	1.3	1.4	1.5	1.0	0.6	0.3	0.2	0.4	0.4	0.4	0.4	0.4	0.3	0.4	0.0	0.2	0.1
18. Garments and Hosery	1.1	1.1	1.6	2.4	2.9	3.7	1.1	2.2	3.1	2.5	4.9	5.9	7.9	7.0	8.5	12.2	10.9	10.7	13.5	13.5
19. Drugs and Chemicals	0.3	0.4	1.0	1.1	1.2	1.2	1.1	0.8	0.5	0.5	0.5	0.4	0.4	0.3	0.2	0.2	0.3	0.3	0.4	0.3
20. Surgical Instruements	0.7	0.5	0.8	1.3	1.2	1.2	1.2	1.2	1.0	0.9	1.0	0.8	1.2	2.0	1.7	1.5	1.3	1.4	1.4	1.4
21. Carpets and Rugs	3.2	3.3	4.5	4.4	6.4	8.1	9.0	10.4	9.4	7.7	6.4	5.6	6.2	5.3	5.4	5.4	5.7	4.9	4.6	3.6
22. Sports Goods	1.5	1.6	1.9	2.0	1.7	1.8	1.5	1.3	1.0	1.1	1.2	1.3	1.8	1.8	1.6	1.6	1.5	1.5	2.2	2.2
23. Other Exports	11.6	12.6	19.2	17.9	16.0	17.7	19.3	17.9	15.2	17.8	20.9	24.5	25.0	24.7	21.4	18.6	18.3	19.0	21.2	21.1
Total Exports	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

Source: Calculated from Economic Survey of Pakistan, various issues.

Further, the revision of the import licensing system in 1972 also helped the small industrialists. As a result, the share of traditional major exports raw cotton, cotton yarn, cotton thread, cotton waste and cotton cloth, which accounted for 59% of the country's total exports in 1971 declined to 40% in 1990. It is important to note that the greatest fall is in the share of raw cotton whose share declined from 28% in 1971 to 7% in 1990. Although, the share of cotton and cotton related export items decreased due to diversification of exports and rapid growth of other export items resulting from rapid industrialization on the one hand, it declined also due to the quota restrictions imposed by the EC and other developed countries as well (see, Adam and Sabiha, 1983).

The most striking visible change which Table 2.4 reflects is the increased relative importance of manufactured export products including carpets, leather goods, sporting goods, petroleum and products, surgical instruments, cotton made-ups, fish and fish preparations as opposed to traditional ones. Many of these products were nonexistent or accounted for a very small part of the country's exports in the 1960s. It seems that alongwith other factors, the adoption of positive policy measures played an important role in stimulating the export of these items. As a result, they surged as main contributors to country's export earnings. This is especially true in the case of cotton garments and cotton made-ups and synthetic textiles. The share of these items rose from only 1% and 0.4% to more than 13% and 5.6% in 1990 respectively between 1971 and 1990 as Table 2.4 indicates.

To sum up, the steady increase in manufactured exports and capital imports indicate the progress of the industrialization, since the faster the pace of industrialization, the faster is the rise in manufactured exports and imports of capital goods. In the 1960s, however, Pakistan was not able to establish export-oriented industries more rapidly because of its emphasis on import substitution strategy. In the 1970s, there has been a significant shift of industrialization strategy from import substitution to export expansion. The emphasis on export promotion has since continued. Pakistan has begun, as data suggest, to emphasise manufactured exports,

despite its large domestic market allowing for a continuation of industrialization strategy based on import substitution.

2.4 Pakistan's Global Trade Relations

The world economy has a strong impact on the economy of Pakistan because of its relatively small size and openness. Its openness has increased significantly over the last two decades. For example, its openness (exports and imports as percentage of GNP) has increased from about 5% in 1970 to 15% in the case of exports and from 8% to 19% in the case of imports. Nevertheless, the country's contribution to world trade is still small around 0.28% due to the relatively small size of the economy. However, the rapid growth of exports in the 1970s and 1980s, together with the large amount of investment in export-oriented industries, made relatively wide fluctuations in the distributive pattern of its trade to world markets.

The rapid economic growth and structural changes in the economy over the years have resulted in changing the structure and composition of Pakistan's foreign trade. Similarly, there has been a significant visible shift in the destinations of its exports and the sources of its imports. Table 2.5 presents the distributive pattern of Pakistan's foreign trade over the last two decades. It mainly indicates that in the 1970s, the share of developed countries decreased and that of the share of developing countries increased sharply. This change manifests the combined effects of higher oil prices, stagnation in the industrialized countries, swings in exchange rates and interest rates, and the growth of protectionism in the industrial countries.

From Pakistan's viewpoint there were three main factors responsible for this major change: i) the sharp increase in oil prices in 1973 and 1977, ii) the drop in private investment activities in Pakistan due to nationalization and political instability, iii) the demand for capital goods created by the public sector was shifted towards CMEA member countries and China. Furthermore, the distribution of Pakistan's trade to the developed countries had also suffered from the fact that Pakistan has not been and is not a member of any regional

Table 2.5 DIRECTION OF TRADE AS PERCENTAGE OF TOTAL TRADE: 1973-1990

	Developed Countries			Developing Countries									
Year	EC	Others	Total	OIC	SAARC	ASEAN	Central America	South America	Others Asian	Others African	Others	Total	CMEA
	1	2	3(1+2)	4	5	6	7	8	9	10	11	12(4+11)	13
1973	24.58	31.06	55.64	15.83	2.08	7.07	0.17	0.50	8.01	3.02	2.29	39.78	4.58
1974	22.27	30.91	53.18	20.32	2.74	4.61	0.19	0.16	6.99	4.14	1.72	43.86	2.96
1975	23.14	29.75	52.89	22.70	4.24	4.27	0.28	0.13	7.74	2.63	0.64	42.62	4.49
1976	24.12	30.76	54.88	24.11	4.26	4.20	0.20	0.31	5.87	1.59	0.80	41.34	3.78
1977	24.90	26.93	51.43	23.28	6.01	5.24	0.17	0.42	6.77	2.58	0.67	45.15	3.42
1978	25.90	29.90	55.80	20.66	3.74	5.16	0.13	1.29	6.97	2.34	0.60	40.88	3.32
1979	23.76	24.93	48.70	27.10	3.64	4.93	0.19	1.59	8.64	1.43	0.55	48.08	3.22
1980	20.01	22.67	42.69	31.19	3.74	4.13	0.50	1.56	9.88	2.32	0.56	53.88	3.43
1981	19.71	24.85	44.56	32.47	3.22	5.13	0.28	0.66	8.24	1.60	0.46	52.06	3.38
1982	19.58	25.28	44.86	34.75	2.42	4.59	0.36	0.57	7.56	1.52	0.54	52.31	2.83
1983	20.61	27.93	48.54	31.98	2.35	5.23	0.18	0.84	5.23	1.51	0.65	47.96	3.50
1984	20.44	31.68	52.12	25.31	2.59	6.34	0.04	1.05	6.54	2.82	0.45	45.14	2.74
1985	24.14	32.64	56.74	20.56	2.81	5.42	0.11	1.31	6.54	2.50	0.69	39.95	3.26
1986	27.04	32.05	59.09	17.80	2.36	4.91	0.18	0.88	8.64	2.85	0.71	38.32	2.59
1987	28.13	31.92	60.05	16.96	3.05	4.92	0.12	0.65	8.71	2.17	0.62	37.20	2.75
1988	27.34	31.24	58.58	16.62	2.72	6.20	0.19	0.73	10.25	2.15	0.58	38.45	1.97
1989	27.80	31.17	58.97	16.97	2.59	6.35	0.15	0.69	9.87	2.58	0.52	38.31	2.73
1990	27.69	30.70	58.39	16.56	2.40	7.21	0.17	1.00	10.83	2.42	0.67	39.26	2.35

Source: Compiled and calculatedfrom Economic Survey of Pakistan 1992-93.

trading bloc and had limited bargaining power and industrial countries adopted a series of new protectionist measures in the early 1970s.

Within the developed countries, the EC has been Pakistan's single largest trading partner since 1973. Today, the EC accounts for around one third of Pakistan's total trade. The share of EC trade with Pakistan has fairly increased over the years. The corresponding figure in 1973 was 24%. The more significant trading partners within the EC include FRG, UK, Italy, France and Belgium. In 1990, they together accounted for around 23% of Pakistan's trade with the EC. The individual relative importance of these countries was 8%, 6%, 4%, 3% and 2% respectively. The USA and Japan are other important trading partners of Pakistan within the developed countries. They together accounted for around 22% (11% respectively) of the country's two-way trade in 1990. It is important to note that over the years Japan has superseded the USA. The share of Japan in Pakistan's total trade rose from 7% in 1973 to 11% in 1990, while the share of USA declined from 17% to 11% during the same period. The examination of Pakistan's trade flow between the EC, USA and Japan show similar trends when their shares are compared within the developed countries. The share of the EC increased from 42% in 1973 to 47% in 1990. In contrast the share of the USA dropped from 30% to 20%, while the share of Japan rose substantially from 13% to 20% during the same period. Overall these three countries accounts for around 50% of Pakistan's total trade and 87% of Pakistan's trade with the developed countries.

Textiles and garments, leather and leather products are among the major export items to the EC as well as to other markets of industrialized countries. Pakistan's textile and garment exports to the industrialized countries including the EC are strictly regulated by the MFA which is regarded as the most prominent example of the use of bilateral arrangements to restrict the volume of exports by mutual consent. Keeping in view Pakistan's potential, exports of these items need to be increased through the encouragement of Pakistan's economic development by the industrialised countries. This reflects the fundamental importance of trade relations of Pakistan with

these countries and particularly with the EC which are accordant with the country's development requirements. Within the industrialised countries the EC's importance for Pakistan is more pronounced. It should be kept in mind that despite the rapid expansion of exports to the EC as well as Japan and the United States, Pakistan's imports from theses countries have grown even faster mainly due to imports of capital goods required to support the investment boom. The country has experienced large trade deficit with these countries which is compatible with the country's overall trade deficit over the years as examined earlier.

Among the developing countries, the Organisation for Islamic Countries (OIC) [8] has been an important trading partner of Pakistan. Pakistan's trade with these countries expanded significantly during the last two decades. It seems that the dramatic increase in oil prices and the steady increase in Pakistan's manufactured exports contributed to this increased trade with these countries. As a result, their share in the country's total trade rose sharply from 15% in 1973 to 35% in 1982. However, in the subsequent years, their share in the country's total trade continuously declined to 16% in 1990. The decline in oil prices has been responsible mainly for this decline. Within the OIC countries, Pakistan's major trading partners were Saudi Arabia, UAE, Kuwait and Iran. These countries are major oil supplier and Pakistan has large trade deficit with these countries. The major exports items to these countries include rice, carpets and textiles products. Pakistan's trade with ASEAN and other Asian countries including China, Hong Kong and Korea is also significant and increasing their share in the past few years. However, Pakistan's trade relations with the CMEA countries remained unstable during the last two decades. Their share in the country's total trade declined throughout the 1970s and 1980s. Similarly, Pakistan's trade relations with other regions/markets remained less important.

2.5 International Financial Inflows

It is obvious from the above discussion that, Pakistan like many developing countries, experienced deterioration in its balance of trade. Its imports tended consistently to exceed exports resulting in a considerable deficit in its balance of trade, because its export earnings arise mainly from primary commodities which are subject to fluctuations in prices and to a tendency for secular deterioration in the terms on which export goods are exchanged for imports. On the other hand, Pakistan's imports consist mainly of capital goods vital for its development which experience secular upward trends in their prices. The shift in Pakistan's composition and structure of exports from primary goods to manufactured goods is gradual. To hasten the change in the composition of trade, domestic industry needs huge resources for investment.

A consistent feature of Pakistan's development plans had been the setting of investment targets above the level permitted by domestic savings and relying on external borrowing. As mentioned earlier, Pakistan followed the import substitution and rapid industrialization policies from the very beginning. In order to import capital goods/machinery and technology needed for setting up the proposed industries, rapid industrialization required a much higher level of investment, a sufficient surplus in agricultural products, raw materials and minerals. In contrast, Pakistan has been unable to provide all necessary financing from its domestic resources. To bridge the increased two-fold gap between investment and saving on the one hand, and imports and exports on the others, Pakistan started receiving foreign assistance as early as 1950s. Foreign capital assistance has played a key role in the economic development of Pakistan and occupied a critical position in determining the strategy and the pace of economic development of the country. It is now financing around 32% of the total investment which was above 50% till 1975. It mounted US $2779 million in 1989. Table 2.6 shows trends and different aspects of foreign capital assistance received by Pakistan from different sources over the years.

Table 2.6 TRENDS OF FOREIGN CAPITAL ASSISTANCE IN PAKISTAN
[SELECTIVE YEARS]

[US $ million]

	1972	1975	1980	1985	1990
Total FCA Inflow:	355	1064	972	1528	2156
As % of Total Investment:	50.6	51.8	28.5	32.7	31.5
Of Which (share %):					
(1) Consortium	93.6	83.8	88.8	98.5	93.8
Bilateral	66.1	51.9	44.6	29.6	32.2
EC	22.4	32.6	47.0	39.4	36.5
Multilateral	27.5	31.9	44.2	69.1	61.6
(2) Non-Consortium	6.4	1.3	3.6	0.0	3.4
(3) Islamic Count.	0.0	14.9	7.6	1.5	2.8
Grants (%)	15.1	19.3	24.0	21.9	8.3

Source:Computed from Pakistan Economic Survey 1991-92.

Table 2.6 also proclaims the major sources of Pakistan's foreign capital assistance. Since its inception, Pakistan has been receiving foreign capital assistance from three main sources: Aid-to-Pakistan Consortium, Non-Consortium and Islamic Countries. Of these, the Aid-to-Pakistan Consortium, organised by the World Bank in 1960, has been the largest source providing more than 80% of total foreign capital assistance. It provides assistance to Pakistan both through bilateral (country to country) and multilateral (financial institution to country) arrangements. The Consortium bilateral comprises Belgium, Canada, France, Germany, Italy, Japan, the Netherlands, Norway, Sweden, the UK and the USA. It provided around 94% (US $2022 million) of total capital assistance to Pakistan in 1990. Of which 33% (US $667 million) was provided through bilateral and 67% (US $1355 million) through multilateral arrangements. The remaining 6% of Pakistan's foreign capital assistance was shared by the non-consortium and Islamic countries. It is worth mentioning that within the Consortium bilateral, the EC member countries have been an important source of foreign capital assistance for Pakistan. Their share in the Consortium bilateral fairly increased over the years as is evident from Table 2.6.

The important change within the Consortium over the years is the shift from bilateral to multilateral arrangements and a significant fall in the share of USA in the total capital inflow to Pakistan. The share of USA declined from 65% in 1972 to 19% in 1990. In contrast, the share of EC member countries increased dramatically, especially during the 1980s which is evident from Table 2.6. Their share increased from 22% in 1972 to 47% in 1980 then declined to 37% in 1990. The multilateral arrangement of Consortium assistance consists of International Bank for Reconstruction and Development (IBRD), International Financial Corporation (IFC), International Development Association (IDA), Asian Development Bank (ADB) and International Fund for Agricultural Development (IFAD). The increase in the share of Consortium multilateral assistance points towards a decline in the share of concessionery transfers (see Table 2.6). It is so because Consortium multilaterally through financial institutions have historically transferred large amount of resources to Pakistan in the form of loans whose financial terms and conditions in some cases have been equivalent to commercial loans. Nevertheless, the overall trends, terms and conditions of foreign capital assistance in Pakistan are consistent with the "graduation theory" which stipulates that terms and conditions should reflect the stage of economic and social development of the recipient country as measured by per capita GNP or other economic indicators.

2.6 Concluding remarks

This chapter has examined Pakistan's global trade and economic relations in the context of its economic development experience. The analysis reveals that the pattern of Pakistan's development experience has not been much different from that of other developing countries. The economy of Pakistan witnessed a rapid transformation in its economic structure, with the share of agriculture in GDP declining steadily and increasing the share of manufacturing and other sectors rapidly. As with most market-oriented economies, international trade and investment financed

through domestic and foreign resources has played an important role. Nevertheless, the economy of Pakistan has experienced several critical periods in reaching its present stage of development, and there are many economic problems that are yet to be resolved.

Turning to the country's composition of trade, there has been a continued shift in the composition of exports from primary commodities to manufactured exports. More importantly, the relative importance of manufactured export items increased substantially as opposed to traditional ones. Overall industrial exports are becoming rapidly more diverse which seem to be consonance with the changing pattern of the economy of Pakistan.

This steady increase in manufactured exports and capital imports indicates the progress of the industrialization and acquisition of technology, since the faster the pace of industrialization, the faster is the rise in manufactured exports and imports of capital goods. It also indicates the fundamental importance of trade relations of Pakistan with the developed countries in general and EC in particular. Within the developed countries, the EC member countries appeared to be the single largest trading partner and donor of capital assistance which is vital for industrialization and transformation of the economy. In the following chapters the evolution of Pakistan's trade and economic relations with the EC and the impact of EC trade policy regime for Pakistan's exports in the EC market will be explored.

Notes to chapter 2

1. For the economic development of Pakistan before 1970, see Breacher Irving and Abbas S. A., (1972).

2. International organizations, particularly the World Bank and the Asian Development Bank (ADB), might have also influenced the shift of policy toward export promotion. Export promotion has been advocated in a number of publications by the World Bank and the ADB. See, for example, Hla Myint, Southeast Asia's Economy in the 1970s (New York: Praeger Publishers, 1975), a study commissioned by ADB.

3. For further detail see, World Bank Report No.7005 Pak, November 1987.

4. For a more extensive introduction and application of Export Bonus scheme see, H. J. Bruton and S. R. Bose (1963).

5. See, John Adam and Sabiha Iqbal, (1984).

6. The notion of "revealed comparative advantage" was first introduced by Balassa with the view to representing the trade performance of countries across commodity categories in such a manner as to gain an insight into source of comparative advantage. See Bela Balassa, (1967).

7. Though numerous studies have been conducted for industrial countries, particularly the United States, few studies have been conducted for developing countries. But no pure study conducted for Pakistan is available. Some recent empirical evidence for Asian countries, however, is presented in Leamer, (1984), op. cit.

8. See, John Adam and Sabiha Iqbal, (1983), p. 56 and Asian development bank, (1986), p. 27.

9. The following countries are included in the OIC: Afghanistan, Algeria, Bahrain, Cameroon, Egypt, Iran, Iraq, Jordan, Kuwait, Labanon, Libya, Oman, Qatar, Saudi Arabia, Sierraleon, Somalia, Turkey, UAE, South Yemen, Syria, etc. For further detail see, Economic Survey of Pakistan 1989-910, pp. 168-171.

CHAPTER 3

EC'S EXTERNAL TRADE AND DEVELOPMENT COOPERATION POLICY REGIME

The purpose of this chapter is to describe the instruments of the EC's trade and development cooperation policy and explore their nature and application towards developing countries in general and for Pakistan, in particular. Access to the EC market for imports from third countries is governed by the EC's common commercial policy which is inherently complex, multi-faceted and multi-dimensional. Its untidy collection of regional and national trade agreements makes generalisation difficult. Some have gone so far as to conclude that the EC has not yet managed to develop a coherent policy in its external economic relations (Yannopoulos, 1985, p.451).

In considering the EC's approach to external trade and development cooperation, the background and preoccupations of the Community policy maker must be kept in mind. Economic and political ties with former colonies go far to explaining the complex series of preferential arrangements both in the spheres of trade and cooperation with the developing countries. Section 3.1 describes the instruments of EC's external trade policy, while section 3.2 explores the way in which the various instruments operate to regulate market access for imports from the developing countries. In this regard both aspects of EC's trade regime which restrain imports and preferential arrangements which are designed to favour imports from developing countries are considered. Section 3.3 presents the evolution of the EC's development cooperation policy towards developing countries and examines its relevance for Pakistan. Section 3.5 identifies the relative importance and significance of the EC's assistance available to Pakistan through the formers development cooperation instruments like financial and technical assistance, food aid, etc. both at the multilateral and bilateral levels.

3.1 EC's External Trade Policy Regime

The principles of EC's external trade policy are put into effect by means of certain trade policy instruments. The main trade policy instrument affecting trade in manufactured and semi-manufactured goods from third countries is the Common Customs Tariff (CCT), also known as Common External Tariff (CET).

The CCT endorses the non-discriminatory principle by the status it accords to the conventional duty as opposed to autonomous duties, stipulating that the conventional duties shall take precedence over the autonomous duties where they are more favourable than the latter. Indeed, the CCT takes the principle of non-discrimination a step further by extending most-favoured-nation treatment even to goods from countries which are not GATT members. The fact that goods are placed on the same footing from whatever country they come does not mean, however, they are necessarily likely to be imported: that depends on the rate of duty and hence the level of protection enjoyed by the Community industry concerned. For instance, the CCT contains no protective devices sufficiently flexible to meet the special needs of the agricultural sector. Its function has largely been taken over by the system of agricultural levies with the purpose to raise the prices of imports to the higher level of EC prices guaranteed by the common market organisations by a mechanism designed to make up the exact difference between the two prices.

In addition to tariffs and levies, the EC possesses a variety of instruments for curbing imports which it regards as being trades on unfair terms or as being harmful to its domestic producers. These include, anti-dumping and anti-subsidy measures, safeguards and surveillance procedures and voluntary export restraints (VERs).

Where a product is sold at a lower price (net of tax) in an export market than its normal price in its domestic market, Article VI of GATT allows an importing country to take safeguard action. This can take the form of anti-dumping duties set no higher than the 'dumping margin' on the goods concerned. If the exporting country has granted a subsidy to help its exporters, then the importing country can impose a

countervailing duty. In both cases, it must be shown that the imports causes or threaten to cause economic difficulties for the industry in the importing country. The first anti-dumping regulation, defining dumping and laying down the procedures for dealing with it, came into force on 1st July 1968 (see EC's Official Journal of Legislation (OJL) No.305 of 19.12.1968), at the same time as the CCT, thus providing the Community with a back-up weapon to be used against the threat of unfair competition from imports.

Among the instruments designed to back up the CCT in regulating the flow of imports from outside the EC, quantitative restrictions stand out as one of the most effective. Where industrial goods in particular are concerned, they offer the only means of curbing imports which threaten seriously to disrupt EC's domestic production by reasons of the quantities involved. Article XIX of GATT stipulates that quantitative restrictions should usually be applied across the board to all countries supplying the product in question.

The regulatory trade instruments described above, with the exception of anti-dumping and countervailing duties, were designed, at least initially, to apply to all imports irrespective of their country of origin or consignment. However, with the passage of time and with the possibility of association agreements with non-member countries (Article 238 of the Treaty of Rome) more discriminatory application of the common commercial policy has been explored. At present, the CCT proper applies virtually only to trade with North America, Japan, Australia, South Africa and the Eastern bloc countries. In trade with the rest of the world, at least as far as industrial goods are concerned, CCT has been displaced by a number of preferential trade arrangements.

Such differential treatments now play quite an important role in trade relations between the EC and non-member countries. It is generally argued that the differential treatments based on political considerations involve protecting the EC's vulnerable industries against fierce pressure from certain imports. In this case the differential element lies in the conclusion of selective 'voluntary export restraint' (VERs) or

orderly market arrangements (OMAs) with particular countries, which undertake to limit imports. The difference between these two types of restrictions is a technical/legal one: OMAs are arrangements between two governments, while the VER is negotiated directly with the foreign export industry. Instead of the importing country imposing a quota or raising tariffs, the exporting country 'voluntarily' agrees to restrict its exports to a certain amount or to a maximum rate of growth. One incentive for the restrained country to agree to restrained is that it obtains higher prices for its remaining exports than before.

Quantitative restrictions may be imposed either at Community level or at national level, reflecting the current state of the common commercial policy. Some quantitative restrictions are community-wide and negotiated under the Commission's auspices, but regulated by Member States, for example, restrictions with respect to textiles (the MFA) and steel [see, Alan Mathews, 1991]. Where the situation is critical, temporary restrictions may be imposed by the Commission or by the Member States on an individual basis. But quantitative restrictions are still imposed fairly frequently as national measures to protect individual Member States.

The trade policy instruments discussed above are used by the EC to restrict market access for manufactured imports from the developing countries. In addition to various measures to curb imports, the EC has also adopted measures aimed at increasing imports from the developing countries. The most important instrument is the special tariff preferences provided to developing countries under the Generalised System of Preferences (GSP). Under this scheme, the EC waives customs duties on imports of manufactures from developing countries (with the exception of so-called 'sensitive' products) as well as reducing duties on imports of agricultural and food products which do not compete with the Common Agricultural Policy (CAP). Some 124 developing countries and 23 dependent territories in Asia, the Far East and Latin American countries are now covered by the EC's GSP scheme [see, TARIC, 1990].

Another instrument is the conclusion of preferential and economic cooperation agreements with former colonies due to economic and political reasons (Table 3.1).

Table 3.1 EC'S MAJOR TRADE AGREEMENTS WITH DEVELOPING COUNTRIES

Countries/Region	Range of Trade Agreements
1. ACP: African, Caribbean & Pacific countries.	Lome Convention
2. Northern Mediterranean: Cyprus, Malta, Turkey, Yugoslavia & Israel	Association Agreement Preferential Trade & Cooperation Agreements
3. Southern Mediterranean: Mashreq (Egypt, Jordan, Lebanon, and Syria) and Maghreb (Algeria, Morocco, and Tunisia) countries.	Preferential trade and Cooperation Agreements
4. Asia: Pakistan, India, China, & Sri Lanka.	Non-preferential Commercial Cooperation Agreements
5. Latin America: Argentina, Brazil, Mexico, Uruguay, and Andean Pact countries.	Non-preferential Commercial Cooperation Agreements
6 ASEAN:Indonesia, Malaysia, Philippines, Singapore, Thailand.	Regional framework Agreement
7. Central America: CACM member countries.	Regional framework agreement
8. Near East: Gulf States: Saudi Arabia, UAE, Kuwait, Oman, Qatar, Bahrain.	Gulf Cooperation Agreement
9. North Yemen, China & Romania	Non-preferential Trade Agreements

Source: Compiled from the Europe World Yearbook, 1991, The Middle East & North America 1991, Western Europe 1989: A Political and Economic Survey and Europe Information External Relations, EC Commission, No.37/80, October 1980.

The EC has signed such agreements with African Caribbean and Pacific (ACP) States, and allows free access to the EC market for all goods originating in those countries except for products coming under the common agricultural policy (CAP). As part of its 'global approach' towards the Mediterranean Basin, the EC signed preferential trade and cooperation agreements with many individual Mediterranean countries. These agreements permit duty-free and quota-free imports of manufactured goods except certain products such as textiles and agricultural products. The EC has also concluded non-preferential trade agreements with a number of Asian and Latin American countries bilaterally (meaning no trade preferences apart from those available under the GSP) and has signed some regional framework agreements with ASEAN, Central American and with the Gulf States. In fact, the preferences given to the ACP and Mediterranean countries are considered more generous than GSP preferences in many cases. Their exports are either exempt from non-tariff barriers or the restrictions are imposed more sympathetically that apply to GSP beneficiary countries or MFA suppliers. The Multifibre Arrangement regulating trade in textile, for example, is not applied either to the ACP or to a number of Mediterranean countries as we shall see.

3.2 Operation of the EC's Trade Regime

A recent survey of the Community's trade policy towards developing countries conducted by Pelkman (1987) suggests that the EC's tariff protection rarely, if ever, presents developing countries with a genuine obstacle to market access. The substantial reduction in most-favoured nation (mfn) tariffs resulting from successive GATT rounds and the introduction of EC's GSP may be considered responsible factors for this improved situation. It would be wrong to conclude from this that tariff barriers no longer pose any impediment to developing countries' exports to the EC market. However, the main problem areas of EC trade policy concern NTBs which have become the major focus of attention over the years. Accordingly this section will

focus on EC's trade relations mainly with the developing countries considering the NTBs rather than tariff ones.

The EC's economic relations with many industrial countries have been based on strong political and cultural ties as well as common economic interests and in theory are governed by the rules of General Agreement on Tariff and Trade (GATT) [1]. On the other hand, EC's trade relations with the EFTA countries have been remarkably free of friction and in the origin of a free trade agreement (Table 3.2). The Luxemburg Declaration of 1984 extended cooperation into other related areas with the aim to create a 'homogeneous and dynamic European Economic Space'. With the advent of the single market, the main concern of EFTA countries has been to ensure that they do not lose out from the creation of a more integrated EC (Pintado, et al., 1988).

Trade relations with the developing countries at the Community level has been conducted through a number of different channels, principally with the ACP states through the Lome Convention, Mediterranean countries through the Global Mediterranean Policy (GMP) and with certain countries in Latin America and Asia through the GSP and non-preferential cooperation agreements. This is reflected in the complex network of discriminatory tariffs through generalised and country-specific or regional-specific trade preferences. It is generally argued that these different channels of EC trade policies affect the access to markets by both the privileged and non-privileged developing countries and in absolute as well as relative terms.

Table 3.2 provides detail indication of the range of EC's external trade arrangements concluded not only with the developing countries but also with the developed countries. It is often commented that the EC's different trade arrangements with its trading partners add up to a hierarchy of trade preferences. Stevens (1981, p.60-82) refers it to the 'pyramid of privilege. At the top of this hierarchy comes trade between the EC member states, which is completely free of tariffs and quantitative restrictions. The same is true of trade in manufactures, though not in agricultural goods, with the EFTA countries. Next come the ACP countries with

Table 3.2 EC'S EXTERNAL TRADE RELATIONS

Countries/Group	Agreement	Trade Provision
(1) EC (Belgium, Denmark, France, Germany, Ireland, Italy, Luxembourg, the Netherlands, UK, Greece, Portugal & Spain).	Treaty of Rome (1957) Treaty of Accession (1973,1981 & 1986)	Free trade in all goods Common external tariff on imports from third countries
(2) EFTA (Austria, Finland, Iceland, Norway, Sweden, & Switzerland).	Free trade Agreements (1972 & 1973 for an unlimited period)	Free trade in industrial goods & setting up an industrail free trade area.
(3) Turkey, Malta & Cyprus,	Association Agreements providing for full customs union with the EEC (1964, 1971 & 1973 for an unlimited period)	Duty-free access for industrial products & concessions on agri-cultural products. Cotton products subject to VERs.
(4) 69 African, Caribbean and Pacific countries (ACP)	Lome Convention (1975, 1981, 1985, and 1989).	Trade cooperation: duty-free access to EEC for ACP goods. Provisions for stabilization of export earnings.
(5) Maghreb (Algeria, Morocco, Tunisia) & MaShreb (Egypt, Jordan, Lebanon, Syria) & Yugoslavia and Israel.	Preferential trade & Cooperation Agreements (1976, 1977 & 1980 & 1975 for an unlimited period	Free access to the EEC market for industrial goods and preferential treatment for agricultural products.

cont'd overleaf

Table 3.2 · EC'S EXTERNAL TRADE RELATIONS - cont'd

Countries/Group	Agreement	Trade Provision
(6) Other LDCs (except Taiwan).	Non-preferential Commercial Cooperation Agreements (1976, 1974, 1976 & 1975)	These countries receives no preferences in addition to those available via GSP. The scheme provides
i. South Asia*: Bangladesh, India, Pakistan & Sri Lanka		
ii. ASEAN: Indonesia, Malaysia, the Philipines, Singapore & Thailand	Single framework agreement (1980)	for duty-free entry of all otherwise dutiable manufactured and semi-manufactured industrial products, inc-
iii. Latin America: Argentina, Brazil, Mexico & Uruguay.	(1972, 1974, 1975 & 1974 respectively)	luding textiles- but subject in certain circumstances to preferential
iv. China, Romania, Yemen Arab Republic.	(1979, 1980 & 1984)	limits. Tariff reduction preferences are also offered to agri. products.
(7) Other Developed Countries signatories of GATT plus Taiwan.	General Agreement on Tariff and trade	Most-favoured-nation treatment.
(8) CMEA member countries excluding Romania & Yugoslavia.		Least-favoured-nation treatment

* The EC has signed Development and Commercial Cooperation with India and Pakistan.

Source: Compiled from the Europe World Yearbook 1991, The Middle East & North America 1991, Western Europe 1989: A Political and Economic Survey and Europe Information External Relations, Commission of the European Communities, No. 37/80, October 1980.

unlimited duty-free access for exports of manufactures and (almost all) agricultural goods not covered by the CAP. The Mediterranean countries with which the EC has signed association or preferential trade agreements are in the next most favoured position. The next tier consists of the non-ACP developing countries which qualify for GSP treatment. Below the GSP beneficiaries come the other GATT signatories which qualify for most-favoured-nation status. This is quite a small group which comprise those Western developed countries outside the EC or EFTA. Finally, at the base of the pyramid, with least favoured nation status, are the state trading countries of Eastern Europe. It is likely these countries will improve their status within the hierarchy of preferences in the light of the EC's willingness to negotiate more favourable trade arrangements following the establishment of a market economy regime there.

The most important and systematic part of the EC's trade policy toward developing countries has, however, been conducted through the Lome Convention [2]. In essence, the Lome Convention have sought to promote trade, to stabilize-or at least attempt to stabilize-export earnings, and to encourage industrial cooperation and the economic development of the ACP countries. In terms of trade, the EC has given preferential access to some 99% of ACP exports without demanding reciprocity. Lome Convention also provided special treatment for products covered by the CAP, including special quotas for sugar and beef. Its trade provisions were supplemented by special aid and technical cooperation arrangements like STABEX, SYSMIN, [3]. Thus, the Lome Convention encompasses more than tariff reductions. It also includes the relaxation of NTBs, less stringent enforcement of trade regulations, and exemptions from multilateral trade arrangements such as the MFA.

The EC's Global Mediterranean Policy (GMP) in fact consists of a series of preferential trade and cooperation and association agreements that have been concluded at various times in the Mediterranean basin except Libya and Albania. The agreements therefore cover such diverse countries as Tunisia, Algeria and Morocco (the Maghreb), Egypt, Lebanon, Syria, and Jordan (the Mashreq), Malta, Cyprus,

Israel, and Turkey (Spain, Portugal and Greece had cooperation agreements with the EC prior to their accession). The trade and cooperation agreements all had a similar structure, and had much in common with the main provisions of the association agreements [4]. These agreements provides free access for their exports of industrial goods (although with a number of safeguards) and concessions on agricultural imports into the Community, both without reciprocity [5].

Access to the EC market for other developing countries' exports is facilitated by the EC's GSP scheme and conclusion of commercial cooperation agreements using a variety of instruments, to promote trade between the two parties. The GSP scheme was put into effect, by council Regulations (OJL, No.142 of 28.06.1971), from July 1971 which granted non-reciprocal tariff preferences to all finished and semi-finished industrial products originating in the developing countries. Generalized tariff preferences are a form of tariff preference which give their recipients an advantage over products exported by other industrialized countries. The EC's GSP scheme has a three-fold objective, to increase the export income of poor countries, to help their industries, and to speed up their rate of economic growth. The preferences consist of a total suspension of customs duties, for a limited quota or ceiling, which have been reviewed every year taking into account the development of international trade.

Since 1971 the EC has made a new GSP offer each year by stressing always that the offer was not a binding commitment, but an arrangement that was temporary and could be withdrawn. Nevertheless, those who hold that tariff preferences given under the GSP are continually being eroded are making a valid point, in that the general level of customs duties was considerably reduced following the Keneddy Round multilateral negotiations and was further cut during the Tokyo Round, thus lessening the margin of advantage enjoyed by preference-receiving countries. Moreover, privileges given under the GSP are considerably less generous than provided under the Lome Convention or to the countries of Mediterranean Basin. Their impact on the recipient countries has been less favourable, in terms of export

expansion, export diversification, and foreign investment effects as opposed to the latter (Ann Weston, 1982, pp.73-86).

Up to 1980 the EC's GSP scheme had four categories of industrial products each governed by a different regime. The first category covered fifteen 'sensitive products' with each of which the Community industry was experiencing particular difficulties [6]. These were governed by a system of quotas shared out in specific maximum limits for each member country in the Community. Once the limit was reached the member state concerned reintroduced normal customs on all imports coming from GSP countries. The second category contained twenty-eight 'semi-sensitive' products known as 'hybrid'. These were governed by a system under which the Commission reintroduced customs duties at Community level for all GSP imports once the Community ceiling was reached. In addition under certain conditions each member state could reapply customs duties at its own borders for products considered to be particularly endangered. The third category comprised eighty-one of the semi-sensitive products governed by a single system of Community ceiling, with the re-establishment of customs duties taking place at Community level only and applying to all GSP countries. Finally, non-sensitive products were also governed by ceilings but the reintroduction of customs duties when those ceilings were reached was a theoretical possibility only [see, Anne Weston, 1980 and 1982].

The EC's GSP treatment for agricultural products was quite different from that of manufactured goods. In this case preferences consists in a reduction of the CCT customs duty or of the levy applied within the framework of the CAP [7]. There were no system of quotas or ceilings but preferences varies from product to product and may go as far as complete exemption. However, these products were subject to safeguard clause [8]. Only 310 products (chapter 1-24) of common tariff were covered under the GSP. But only 73 products were granted duty-free entry, the rest were given partial, often small, tariff reductions ranging from 20 to 50%. With exception of items- preserved pineapples, soluble, coffee, cocoa, Virginia tobacco

and other unmanufactured tobacco- all other products could enter the EC within the limits of fixed, global amounts [EC Commission, 1992, No.DOC 1/34.90].

In order to qualify for duty exemption under the GSP, however, exporting countries were required to comply with certain rules regarding the origin of goods, in particular, by providing certificates of origin. However, towards regional economic groups, the Community adopted a cumulative system of exports entering the EC from Common markets such as ASEAN (Singapore, Thailand, Indonesia, Malaysia and Philippines), CACM (Costa Rica, El-Salvador, Guatemala, Honduras and Nicaragua) and the Andean Pact Countries (Colombia, Bolivia, Ecuador, Peru and Venezuela).

The first period for the application of the EC's GSP ended on 31 December, 1980. On 16 December the Council agreed to continue the scheme for a further period of 10 years. For the years following 1980 the scheme was intended to ensure a better balanced use of the preferential benefits. To this end, a number of adjustments were made in the operation of the system, and the method of calculating ceilings or quotas has been changed. The original formula, based on quantity plus an additional amount, has been subject to more and more exceptions because the overall statistical figures did not contain any feature which reflected the degree of sensitivity regarding the sector in question. Thus, to make it possible to differentiate between beneficiary countries the overall quotas and ceilings were abolished. Preferential quantities were established on an individual basis, and the reintroduction of duties after the ceiling had been reached were applied to the single beneficiary country whose exports had reached this ceiling.

From 1981, in order to simplify the management of the GSP scheme, the subdivision of the industrial products other than textiles into four categories: sensitive products (fifteen customs headings), Hybrid (twenty-eight customs headings), Semi-sensitive (eighty-one customs headings), and non-sensitive (about 1700 customs headings) was ended. In the new GSP scheme, the Community adopted only two categories of products namely 'sensitive products' and 'non-sensitive products' [9]. There were 128 sensitive products out of which 64 industrial products were strictly

controlled in the form of quotas for certain origins on account of the difficulties which they posed to the Community industry. On the other hand, non-sensitive products were subject only to statistical supervision.

Inspite of quotas and ceilings, a number of supplementary controls were therefore devised, mainly for the purpose of a fairer distribution of GSP benefits. For this purpose 'Community maximum amounts', or 'butoirs' as they were called determined the volume of a particular product any one beneficiary could export under the GSP. These Community maximum amounts, may be set at 15%, 20%, 30%, 35%, 40% or 50% of the ceiling depending on the degree of spread desired [OJL, No.370 of 31.12.1990]. Another instrument namely 'burden sharing' among preference-giving countries i.e., the EC Member States was also introduced with the aim not to allow any GSP beneficiary to concentrate its exports on any EC Member State's market. Burden Sharing is shown in Table 3.3.

Table 3.3 DIVISION OF EC QUOTAS BY EC MEMBER STATES
[Burden Sharing Formula]

Country	Per cent	Country	Per cent
West Germany	25.5	Denmark	2.7
United Kingdom	21.0	Greece	1.5
France	16.5	Portugal	1.5
Italy	13.5	Irish Republic	0.8
Benelux	9.5		
Spain	7.5	EC (12)	100.0

Source:European Community, OJL, No.255 of 05.09.1987.

In order to spread the GSP benefits more evenly among preference-receiving countries, some of which had become a great deal more competitive than others, the EC introduced some positive measures especially the poorest developing countries, giving them a greater advantage than the other developing countries. List annexed to various GSP regulations identify some thirty least-developed countries whose exports can enter the EC market free of all the limits imposed in the form of quotas, ceilings,

maximum country amounts or quota shares, entitling them generally to unrestricted duty-free access [see, OJL 370 of 31.12.1990].

The EC's GSP for textiles came into force on 1st January 1980. Until 1980, textile products were treated broadly as other industrial products with 30 in the sensitive category, 16 semi-sensitive and 50 non-sensitive. The major differences were, first, that for non-sensitive products the formula for calculating ceilings was less generous than for other industrial products, and second, that there was a more concerted effort to restrict GSP for the major suppliers (by means of separate tariff quotas or tighter butoirs). In 1980 the GSP was changed significantly for those textile products falling under the MFA. The major innovation was that each developing country was given its own fixed share of the tariff quotas admitted duty-free to be entered into the EC market. Tariff quotas were based on the country's GNP per capita, past exports of that product to the EC market, and its quota under the MFA. For the very sensitive products the shares of exporting country were subdivided between the EC member states. Product falling outside the MFA continued to be treated as in the past. Imports from the least developed countries (provided they met the rules of origin) were duty free throughout the year.

As mentioned above, the scheme was introduced for products covered by the MFA [10]. Nevertheless, benefits from the GSP preferences granted in the form of CCT tariff concessions, tariff quotas and tariff ceilings were restricted to developing countries only which signed VERs or undertook similar commitments vis-a-vis the EC (see, OJL, NO.370 of 31.12.1990). The volume of exports enjoying duty-free entry was fixed in the form of quotas or ceilings individually for each country. Tariff quotas and tariff ceilings were increased year by year at a rate of growth which varied according to the 'sensitivity' of the product. The net affect of tariff quotas or tariff ceilings has not been to stop the imports after the limits have been reached but only to apply the full most-favoured nation tariff rates of duty. Preferences were granted for products not covered by the MFA within global ceilings.

There is no doubt that significant improvements have been made from year to year in the GSP scheme since it was first introduced in 1971. The improvements introduced in the new GSP scheme in 1980 are of great importance. Previously, a lion's share of the benefits, in terms of GSP imports, had gone to seven countries- Yugoslavia, Malaysia, Hong Kong, India, South Korea, Brazil and Romania. The new GSP scheme extended greater security to the beneficiary countries through the system of "guaranteed quotas". It has also been simplified in the sense that now there are only two categories of manufactured products (sensitive and non-sensitive). The non-sensitive products are subject only to statistical surveillance . The sensitive ones are subject to quotas and to EC country-wise limits. There is no gainsaying the fact that the new GSP made an advance over the preceding one.

Despite these improvements , the EC scheme entering into a third decade of its existence as a whole, and in particular the mechanism for administering preferential imports from developing countries outside the Lome Convention, has remained highly complicated, inadequate and riddled with uncertainties. Furthermore, it has come to be used as a political tool to divide developing countries by turning the less developed against the more developed, and persuade the latter to liberalise their imports from the EC (Anne Weston 1982, p.85). It seems that till now the EC has given more emphasis on redistribution of GSP benefits between developing countries, rather than solving their export problems. If the GSP is to meet its original objectives namely to promote development by expanding the demand for (largely manufactured) exports, further changes are required in the EC's GSP scheme to make it more simple, more transparent and more stable.

3.2.1 Voluntary Export Restraint Agreements (VERs)

Granting tariff preferences to developing countries gives them a competitive advantage which is usually justified by the structural weakness of their industries. But experience has shown that industries located in some developing countries are not invariably in a position of weakness, particularly where the type of goods in question

has a high labour content. A country with low wage costs can be extremely competitive on the international market. Usually, however, this state of affairs is consistent with the industrialized countries' efforts to assist developing country's development. But their views may undergo a change when the accessibility of their markets to low-cost imports jeopardizes important economic interests. The open-door policy then gives way to strict import controls.

There are various ways of looking this problem. In theory although it has never happened, a country could cease to be eligible for the Generalised System of preferences and instead become liable for normal tariff treatment again. In practice, however, since this type of problem tends to be confined to limited areas of industry, the system is manipulated from within by means of various specific restrictions (quotas and ceilings) to limit the impact of tariff preferences on the import of products regarded as sensitive.

On textiles, however, a more radical approach has been taken, since it was not thought that the difficulties arising from low-cost imports into the EC could be properly dealt with by tariff measures. The need was for a tighter system of controls more along the lines of quantitative restrictions. The discipline imposed by the EC on textile imports has been based on 'voluntary export restraint agreements' (VERs) under which the textile-producing countries undertake to keep their exports to the EC market within certain limits. Such bilateral agreements were concluded by the EC with some 40 low-cost developing countries including Pakistan within the framework of the Arrangement regarding International Trade in Textiles- the Multifibre Arrangement (OJL, No.118 of 30.04.1974 and OJL, No.348 of 30.12.1977). They are aimed at avoiding disruption of both the importing countries' markets and exporting countries' trade, and lay down quantitative export limits which the supplier countries undertake to respect. The quantitative limits allow for an annual import growth rate which varies according to the 'sensitivity' of the product involved. The basic idea behind this has been to limit exports of all low-cost developing countries to an acceptable total import level.

A central issue in the political economy of VERs is the extent to which they are in fact voluntary. The possibility that they are voluntary arises from the fact that the exporting countries in effect are offered a choice between a VER and an Article XIX safeguard action. The attraction of VERs is that they bypass the non-discriminatory requirements for the use of GATT's Article XIX. Exporting countries agree to VERs because their losses in market share are partially compensated by greater profits on the quantities they are allowed to export. Thus restriction on the quantity exported is likely to raise the prices (and create scarcity premia, so-called quota rents) of the remaining exports to the restricted market. The higher profit per unit sold implies the possibility that exporting country will gain as a result of a restraint, and therefore the possibility that its government will be willing to voluntary restrain exports. The main examples affecting the developing countries are the textile arrangements under the MFA; consumer electronics (covering imports from Singapore, South Korea and Taiwan); and shoes and cutlery (Cable, 1983).

These rents make VER expensive instrument for developed countries (as we shall see in chapter 5). Then it is interesting to know why importing countries ask for them and why they prefer VER than Article XIX. Some governments of developed countries claim that their neglect of Article XIX is due, first to its requirement that exporters affected by Article XIX actions be compensated and, second, to the requirement that Article XIX actions must apply to all exporters of a particular product, which means that "disruptive" exporters cannot be singled out for special treatment. That's why these developed country governments often go on to suggest that a relaxation of these requirements would lessen their temptation to seek VERs. The attraction of VER is that it provides a possible means of avoiding arduous negotiations when a number of different countries are sources of relevant imports and all exercise their right to equivalent concession allowing discriminatory actions.

Beyond that technical problem, however, lies a more important political one. Nondiscrimination means that action taken under Article XIX must be taken against powerful trading partners as well as against weaker ones. Thus, for example, using

Article XIX, the United States and the EC would have to act against one another's exports when an expansion of competitive imports from a newly industrialised country has "created" the problem. Tension in a central political relationship may be threatened as a result of economic events in a relationship that may be politically peripheral.

Seen from another vantage point, however, the fundamental problem lies in the decision to protect the import-competing industry. This may explain why the most common defense of selectivity lies neither in the technical problem of the equivalent tariff adjustment nor in the political problems of relations between trade superpowers. The most common defense lies in the ethical proposition that importing country governments have a right to prevent "market disruption". The VER provides the right to the importing country governments to take action against "disruptive" imports without reference to the exporting country government (Hindley (1979) gives a fuller discussion of this contention). This is not to say, of course, that there are no losers from a VER in the countries directly. In particular, buyers in the importing country are worse off. They pay the rents that make the restraint acceptable to the exporting country government (This issue will be dealt in chapter 5).

To sum up, the above discussion indicates that the EC's external trade policy regime has been highly complicated and discriminatory in its nature and operation. This is reflected in the hierarchy of EC's external trade relations or so called pyramid of privilege. The reasons for the EC's hierarchy of preferences are complex. Some preferences were introduced on foot of GATT obligations (e.g. the GSP). Others reflect foreign policy considerations and the EC's attempts to maintain close relations with countries it deems important to it either for security considerations (the Mediterranean Agreements or as providers of important raw materials (the Gulf States). Others reflect previous colonial ties (the Lome Convention). Whatever the motives, the existence of this hierarchy is now an important factor which must be taken into account in evaluating the impact of EC's trade policy on developing countries in future.

3.3 The Place of Pakistan in the EC's Cooperation Policy towards Developing Countries

The EC was established by the Benelux states, France, Federal Republic of Germany and Italy with the signing of the Treaty of Rome in 1957. The Treaty of Rome confined itself to setting the legal foundations of close association with only those developing countries which had special links of a colonial nature with the member-states of the EC. With the passage of time, however, the EC has slowly but surely worked out its own particular relationship with the (other) developing countries.

The enlargement of the EC in 1973 to include three members states- Denmark, Ireland and the United Kingdom-brought the EC into direct and privileged contact not only with the English-speaking countries of Africa, but also with countries of Asia, such as India, Pakistan, Sri Lanka etc. One direct result of this widening the EC's horizon was the conclusion of the Lome Convention which replaced the Yaounde Convention. It was signed in 1975 between the EC and forty (40) countries belonging to the African, Caribbean and Pacific region [see, Richard Bailey, 1983, pp.187-199]. This phenomenon of growing EC relations with the developing countries was not limited, however, to countries in Africa. With the passage of time it coincided with a number of fundamental changes in the EC's cooperation policy. Today, the EC's development cooperation policy towards developing countries covers two closely associated and complementary aspects:

i) the continuation and extension of cooperation with developing countries in a regional context, i.e. the Lome Convention and association agreements with the countries of the Mediterranean and the Mashreq and the Maghreb.

ii) the implementation of an overall policy at world level, including such instruments as GSP scheme, provision of financial and technical assistance, food aid, etc.

In regard to the operation of these instruments towards developing countries other than the Mediterranean and the ACP, the following three considerations seem to

be useful for our further analysis. The first is that, with the exception of the GSP, these instruments were not of exclusive relevance. What is meant here is that the member-states continue to operate in the same fields (this is particular true of financial aid), and this poses the question of coordination and harmonization on the basis of national and Community cooperation in these fields both at the conception and at the operational stages. The second is that, the EC's global policy is characterized by an intensely evolutive nature, not only in quantitative but also in qualitative terms. In fact, on a par with the internal constitutional evolution of the EC, its cooperation policy grew slowly from a limited range of traditional sectors (trade cooperation, food aid, towards a wider sphere of more sophisticated activities (industrial cooperation, scientific cooperation, transfer of technology, etc.).

The third consideration is that, in spite of its global nature, the EC's cooperation has not been applied in the same way to all developing countries. This does not mean that it was discriminatory or selective, but simply that each instrument was applied according to the different needs of the various developing countries as compared with the size of the EC resources devoted to that instrument [11]. While access to the EC market through GSP and trade co-operation were open to all, only a few developing countries received food aid and financial aid from the EC.

If one tries to find out the place of Pakistan in the EC's policy of cooperation on a world-scale, the following two remarks are of paramount importance: (i) Pakistan is not included in the EC's regionalistic approach i.e., Lome Convention or the Mediterranean Global Policy, but (ii) Pakistan appears to be at the forefront of the EC's interests within the global approach. All the instruments of EC's cooperation policy towards developing countries have been intensively employed in relation with Pakistan.

As far as the first of these two elements is concerned, one might wonder why the countries of the sub-continent including Pakistan were not included in Protocol No.22 of the Act of Accession which listed the independent, developing Commonwealth countries to which the regionalistic approach (Lome) was extended.

The main historical reason might well be that, unlike the other Commonwealth countries situated in Africa, in the Indian Ocean, in the Pacific Ocean, and in the Caribbean, the countries of the sub-continent had already established extensive relations with the EC by the time of the first enlargement. Pakistan had already established diplomatic relations with the EC in 1962 and had a series of bilateral agreements with the EC for exports of silk, fabrics and handicrafts. Bilateral agreement on textiles was also concluded in the larger framework of the long-term agreement (LTA) negotiated in GATT between the textile-exporting and importing countries [12]. Finally, since July 1971, Pakistan became a beneficiary, like all other South Asian countries, of the EC's GSP scheme. Stimulated by these developments of the EC in its original composition, Pakistan was able to diversify its export market, so as to both improve its balance of trade and lessen the impact on its exports on Britain's entry into the EC. This produced a widespread confidence that the trade of Pakistan would not suffer as a result of the enlargement.

With the accession of the UK into the EC, it became difficult for the enlarged EC, having agreed to accommodate the developing Commonwealth Countries outside Asia within the framework of the existing association agreement with French-speaking Africa, to refuse to enter into an agreement with South Asian countries including Pakistan. The search for a new type of agreement was therefore undertaken by the EC with India to begin with. As a result, they invented the Commercial Cooperation Agreement (CCA), which came into force on 1 April 1974. As it was the first of its kind, the EC took it as a model for its relations with the other South Asian countries. Consequently, a Commercial Cooperation Agreement between Pakistan and the EC was signed in 1976. The central instrument for putting 'flesh on the bones' of the CCA was the Joint Commission. The Joint Commission was required to explore ways and means for an efficient and coherent utilization of all available instruments (GSP, food aid, financial and technical assistance, etc.).

The CCA sought to provide the institutional machinery which allowed the EC to help Pakistan, both to take full advantage of the GSP and develop new trade

opportunities. In spite of its limited economic scope, the CCA constituted a big step forward by the EC and had a great significance. The existence of historical links with one of the member-states, the long tradition of close relations with the EC, even before its enlargement, by the number and extent of special trade preferences, sectoral agreements, the CCA and finally the conclusion of the new Commercial, Economic and Development Cooperation Agreement (CEDCA) in 1986 affirms that Pakistan enjoys a special status in the EC's relations with the developing countries. These relations tends to place Pakistan in an intermediate position between the associated ACP countries and the others.

3.4 Commercial Cooperation Agreement (CCA): the Framework for the evolution of Pakistan-EC Trade Relations

Pakistan's formal contacts with the European Economic Community date back to 1962, when Pakistan opened a diplomatic mission accredited to the Community. Pakistan was one of the leading developing country to establish such relations with the EC. These relations became closer with the accession of Pakistan's traditional major trading partner Britain , to the EC in 1973. The Joint Declaration of Intent (JDI) issued jointly with Britain (in 1972) annexed to the Treaty of Accession committed the Community to extend and strengthen its trade relations with the Asian countries of the Commonwealth, especially seeking appropriate solutions to the trade problems that might arise for these countries as a result of the Britain's accession to the Community.

In line with this JDI to promote trade relations between Pakistan and the EC a Commercial Cooperation Agreement (CCA) was signed in June 1976 [see, EC Commission OJL, NO.168 of 28.06.1976]. The conclusion of the CCA provided a legal framework for the evolution of Pakistan's trade and economic relations with the EC on the basis of comparative advantage and mutual benefits so as to contribute to their economic and social progress and to the improvement of the balance of their mutual trade to as high a level as possible.

The CCA was based on the recognition that the economies of Pakistan and the member-states of the Community complemented, rather than competed with, each other. The agreement provided for the grant of the most-favoured-nation (MFN) treatment in their commercial relations in accordance with the provisions of the GATT. Provisions were made for the promotion of development and diversification of their mutual trade to the highest possible level on the basis of comparative advantage and mutual benefits and development of their economic cooperation in the light of developments in their economic policies. It also provided provision for special sectoral agreements between Pakistan and the EC on cotton textiles, handicrafts and silk and hand-loom cotton fabrics.

The CCA's principal operative instrument, therefore, was a Joint Commission whose task was to ensure the proper functioning of the agreement, devise practical measures for achieving its goals, and discuss and pursue effectively all matters which may arise in the course of its implementation. Clearly, the Joint Commission's terms of reference was a key element of the CCA. The Joint Commission was required to (i) seek ways and means of encouraging economic and commercial cooperation with a view to promoting trade expansion and diversification; (ii) study and devise ways and means of overcoming trade barriers especially non-tariff barriers; (iii) examine and recommend ways and means of progressively adopting the advantage of economic complementarity, and (iv) facilitate exchange of information needed to promote cooperation on mutually advantageous terms.

The Joint Commission established under the CCA as an institutional mechanism worked for developing closer commercial cooperation and facilitating a large volume of complementarity trade. The Trade Promotion Program (TPP) undertaken at the instance of the Joint Commission provided Community assistance for Pakistani participants in European trade fairs and sales missions, organising seminars and workshops for them, visits by Pakistani trade delegations to the member-countries of the EC, visits by European businessmen delegations to Pakistan,

and visits by European Experts to Pakistan, etc. [see, Amanullaha Hussain, 1981, p.13].

The CCA marked a departure from the classical type of trade agreement, which normally provide for a most-favoured-nation (MFN) in trade matters between the signatories. It was a different in its scope and conception from the classical trade agreements. The two principal objectives enshrined in it were "the development and diversification of the Community's imports from Pakistan and Pakistan's imports from the Community". Through its main instrument, the Joint Commission, a number of programmes were devised to promote "economic cooperation limited to trade" as mentioned above. As the agreement was non-preferential, Pakistan relied on the EC's GSP scheme to facilitate its manufactured and semi-manufactured exports. At the same time, Pakistan's Economic Mission in Brussels co-ordinated the efforts of the Joint Commission in the member-states of the Community so as to make a determined attempt to achieve a balance in trade exchange between Pakistan and the EC.

In spite of above mentioned activities, however, the CCA was much too general in scope and quality. There was nothing specific about trade and the impression was given that this was the kind of general cooperation agreement that the EC could have signed with any country. Keeping in view their expanding trade and economic relations, upon the expiry of the old agreement, Pakistan and the EC entered into negotiations with a view to arriving at a new agreement by taking into account the experience of the old CCA. After protracted negotiations, an agreement was reached and a new Commercial, Economic and Development Cooperation Agreement (CEDCA) was signed which came into force on 1 May 1986 [see, EC Commission, OJL NO.168 of 25.04.1986]. Although the said agreement between Pakistan and the enlarged EC was concluded for a period of five years expiring on 22 April 1991, it is automatically renewed from year to year unless it is denounced by either party six months before expiry.

The new Commercial, Economic and Development Cooperation Agreement reflects the importance of Pakistan-EC trade relations. The scope of the new

agreement is summed up in its title. It provides a framework and ways in which commercial and economic cooperation can be encouraged between Pakistan and the EC. In comparison, the new agreement is both broader in scope and deeper in quality. It defines specific areas of mutual interest. Cooperation in the field of trade is reinforced and extended to take in economic and development cooperation. In this context the EC and Pakistan undertook to encourage industrial cooperation and the transfer of technology between their economic operators and to promote scientific and technological cooperation. Provision is also made for development cooperation, with the EC undertaking to intensify its support for Pakistan's development programmes.

The immediate benefit of the conclusion of the CEDCA agreement was apparent in granting special preferences for Pakistan's major agricultural item i.e., basmati rice which accounted around 20% of the country's total exports in 1978. In 1976 under CCA provisions, the EC specifically undertook the responsibility to explore possibilities for facilitating the exports of basmati rice, but little was done under the 1976 cooperation agreement. Attempts to do this through the GSP did not succeed as this Pakistan's major exportable item remained uncovered even under the EC's new GSP scheme. However, in 1987 the EC allowed Pakistan to export basmati rice into the Community by reducing the normal levy by 25% for a quantity of 10000 tonnes (instead of 50% levy cut for 15000 tonnes as proposed by the EC Commission) falling within heading No.ex 10.06 of the CCT. Whereas the average offer price for basmati rice was well above the price for other long-grain rice and was even above the Community threshold price for long-grain rice. In spite of the small quantity involved, this was major advance made under the new 1986 Commercial, Economic and Development Cooperation Agreement.

Pakistan surely benefited from this arrangement and has increased its overall earnings from the export of basmati rice in the EC market over the years. However, it is important to note that the effects of the above mentioned EC's policy in regard to export of basmati rice from Pakistan are twofold. First, Pakistan is allowed to export a certain amount (10000 tonnes) of basmati rice at the higher price in the EC market.

Second, Pakistan's export of basmati rice above the allowed limit is restricted by imposition of import levies at MFN rates [EC Commission, OJL, NO.357 of 19.12.1987]. It would be useful here to estimate the extent of these two effects. Table 3.4 illustrates the effects of EC's policy regarding the export of basmati rice from Pakistan. It also indicates the movements of Pakistan's unit values of rice which have declined both in the EC and world market over the years. This evidence seems to underline the fact that the producers and exporters of primary commodities have been more vulnerable as prices of these commodities were fluctuated dramatically during the last two decades (Kohli and Ali, 1987, pp.45-49).

Table 3.4 reveals the fact that Pakistan's export of basmati rice has benefited in the EC market with the provision of 10000 tonnes quota at higher prices. It also discloses Pakistan's total export earnings from the export of basmati rice if (a) all the basmati rice had been exported to the non-EC market and (b) the basmati rice had been exported to the non-EC and EC market (up to the allowed limit) supposing that export to the EC market is diverted from non-EC markets. Pakistan's total export earnings to the non-EC market stood at US $672.18 million during 1987 and 1990. After the provision of EC quota, Pakistan's export earnings both from the EC and non-EC sources increased to US $682.57 million (US $646.39 + US $36.18 million) during the same period. Pakistan's net gain from the provision of quotas, being able to export to the protected but high priced EC market, amounted to US $10.39 million (US) $682.57 - US $672.18 million) between 1987 and 1990. However, it should be borne in mind that this is a more or less informative rather than actual situation as the data for this purpose have been obtained from different sources. For example, the data for basmati rice export in the case of EC market was obtained from Eurostat expressed in ECUs and for Non-EC market from Pakistan Economic Survey expressed in Rupees both were converted into US$.

In our above example, we assumed that export of basmati rice to the EC market was diverted from the Non-EC market, while in practice this increased amount may be have been met from three sources: a) full diversion from

Table 3.4 PAKISTA'S EXPORT OF BASMATI RICE TO THE EC AND NON-EC MARKETS

Year	Quantity Tonnes	Unit Value (US$)	Total Value (US$ million)
Total Export to the NON-EC Market:			
1987	221187	725.90	160.56
1988	215462	699.15	150.64
1989	207972	685.33	142.53
1990	466391	468.38	218.45
Total Export Earnings:			672.18

Trade after Quota given by the EC:

	Non-EC Market			EC Market		
	Qty*	UV*	TV*	Qty*	UV*	TV*
1987	211187	725.90	153.30	10000	1126.14	11.26
1988	205462	699.15	143.65	10000	869.94	8.70
1989	197972	685.33	135.68	10000	850.15	8.50
1990	456391	468.38	213.64	10000	717.98	7.72
Total Exports:			646.39			36.18

Total Export Earnings from Basmati Rice:

Non-EC: 646.39 US$ million
From EC: 36.18 US$ million
Total Earnings: 682.57 US$ million

Pakistan's Net Gain: 682.57 - 672.18= 10.39 US$ million.

* Qty= Quantity in Tonnes; UV= Unit Value in US$ per Tonne and TV= Total Value in US$ Million.
Source:Calculated obtaining data from Eurostat and Pakistan Economic Survey.

Non-EC market as supposed earlier; b) full adjustment from domestic resources with increased production or reduced consumption; and c) a combination of (a) and (b).

In view of Pakistan's total exports of basmati rice, there seems to be a need for further trade liberalization of basmati rice in the EC market. As India is Pakistan's only competitor in the export of this variety, it is not impossible for the EC to increase Pakistan's quota limit (as previously quota with the reduction of 25% import levy was given to Pakistan not to India in 1987). None the less, further liberalization of basmati rice import will depend on the scope for increasing consumption of basmati rice in the EC market. It is beyond the scope of this thesis to make an estimation of the scope for increasing the consumption of basmati rice in the EC market. However, a separate study in this regard may be revealing.

3.5 EC's Economic Assistance to Pakistan

Economic and political relations between Pakistan and the EC take place at two levels, at multilateral (Pakistan-EC) level, and at a bilateral (Pakistan-EC Member State) levels. The EC Commission is responsible for the trade relations of the individual Member States vis-a-vis third parties. Here, one may say that each EC member country has transferred most of its sovereignty concerning trade policy to the Commission. This fact is underlined by the Commission's role as the negotiator for the whole Community in international trade negotiations and by the acceptance by EC Member States of the inclusion of a "Community-Clause" in all trade agreements.

There are still areas like culture, economic and technological activity that are still much more the responsibility of the individual Member States than of the EC. Indeed, in the specific fields of cultural affairs and capital investment, the EC has defined no policy for third parties. Through the passage of time, however, the EC has developed a number of instruments to implement its cooperation policy towards developing countries. This section will examine the implementation of these instruments both at multilateral and bilateral levels in the case of Pakistan over the years.

3.5.1 Multilateral Assistance

In spite of greater responsibility of the individual Member States, the EC has been successful in developing a number of instruments for implementation of its overall development policy at world level. The main instruments of its policy includes the GSP, food aid and financial and technical assistance [see, EC Commission, 1976]. We have examined the EC's GSP scheme earlier; the present section will focus on the aspects of transfer of resources from the EC to Pakistan via these instruments i.e., food aid, financial and technical assistance.

(i) Food Assistance

Food assistance was initiated by the EC in 1968 and is recognised today as an important instrument of overall EC development policy. Its importance is growing given the food shortages and the growing requirements for food in the developing countries. The EC's food assistance is given in the form of donations directly to states or through international organisations. It falls into two categories: emergency and nominal food assistance. Emergency food assistance is reserved for famines following natural catastrophy (drought, floods, earthquakes, etc.). In such situations the EC takes responsibility for supplying the goods, the cost of transport and free distribution to the affected population.

Nominal food assistance consists of food supplied free of charge and sent to the EC's port or to the border of the recipient country in exceptional cases. The cost of transport and distribution remains the responsibility of the beneficiary country. The products supplied are destined either for free distribution by the government concerned or for sale at the local markets. In the latter case, the government has to use the "counterpart" funds it receives from the sales to finance development projects [for more detail see, EC Commission, 1988, DE 56].

Between 1976 and 1992 the EC provided directly and indirectly nearly ECU 68 million (between 1976-85 ECU 58 million) for food assistance to Pakistan. During

this period, food assistance to Pakistan has fluctuated. It was about ECU 9 million in 1981, ECU one million in 1983 and was ECU 3 million in 1985. Until 1985 EC assistance consisted of food grains (35,000 tonnes that year), skimmed milk powder and butter oil. Since then no food grains have been supplied as direct food aid, although small quantity of edible oil (500 tonnes) were included in 1984 and 1985 [see, EC Commission, 1986,No. 86/86].

Since 1980, in addition to direct food assistance to Pakistan, the EC has provided food and, on concession, medical aid to Pakistan to share the burden of more than 3 million Afghan refugees. Between 1980 and 1985, for example, the EC provided ECU 110 million and assistance mainly consisted of cereals but included skimmed milk powder, butter oil, vegetable oil and sugar. The food package for 1986 included 45,000 tonne of cereals, 2,000 tonne of sugar and 1,000 tonne of butter oil, worth ECU 12 million. On the whole, EC's food assistance amounted to ECU 174 million during 1980-88 [see, EC Commission, (1989), Telex Development, No.482, pp.13-14]. In fact, the EC accounted for about one-third of the food assistance the Afghan refugees have received from all sources.

In the case of Pakistan, EC's food assistance has played a modest role in the country's development effort and share the burden of more than 3 million refugees. It is easily conceivable that, in the absence of food aid, the magnitude of food shortages and associated problems of starvation and death would have assumed tragic proportions. This role of food aid, although prima facie humanitarian, also has growth implications. Food shortage is a highly sensitive, political issue and one which the government can ill afford to ignore.

This means that, in the absence of food aid, Pakistan would have to use a large part of its scarce, foreign exchange earnings to import food, thereby reducing the amount available for importing necessary capital equipments, raw materials and intermediate goods. The effect of curtailing imports of investment goods would be to reduce the rate of growth. In sum, food aid has not only prevented deaths from

starvation but has also worked as a lubrication in the process of structural transformation.

(II) Financial Assistance

In addition to food assistance, the EC , since 1976 has been implementing a programme of direct financial and technical assistance for the "non-associated" developing countries of Asia and Latin America [see, OJL, No.52 of 27.02.1992]. In line with its development policy, the EC provides financial assistance either directly or through co-financing with EC member countries or with multilateral or regional bodies.

In the case of Pakistan, the EC provided financial assistance mainly through co-financing. For example, in 1979, the EC together with the Asian Development Bank (ADB) financed a livestock development project in Pakistan. The EC contributed $9.2 million (ECU 6.7 million) and the ADB also provided an equal amount. Further in 1984, the EC approved both a vocational training and a rural electrification project. Under the first, to be co-financed with the World Bank and the International Development Agency (IDA), 11 new vocational training centres were to be built in North-West Pakistan. The second project relates to the electrification of 176 villages [Luigi Boselli, 1984, p.26]. Table 3.5 enlists major projects and commitments of the EC to finance these projects in Pakistan [13].

Table 3.5 MAJOR PROJECTS IN PAKISTAN FINANCED BY THE EC

Name of Project	Commitments
1. Baluchistan Livestock	6.7 million ECUs
2. Karachi Fish Harbour	12.0 million ECUs
3. Baluchistan Integrated Area Development	9.4 million ECUs
4. Rural Electrification	10.0 million ECUs
5. Buner Development Projet	10.6 million ECUs
6. Tharparker Roads Project	10.0 million ECUs
7. Chitral Project	8.0 million ECUs
8. Primary Education Project	15.0 million ECUs
9. Road Project in Buner	5.0 million ECUs

Source: EC Commission.

Apart from project assistance mentioned in Table 3.5, in 1987, the EC's guaranteed for ECU 18 million (out of total ECU 28 million cost) loan for the establishment of Agricultural College at Quetta (capital of Baluchistan province). Further 5 proposals from Pakistan to invest in projects such as motorcycle assembly, two agro-industry projects, a road project and a housing finance project amounting to value of around 584,000 ECUs were under consideration [see, EC Commission, 1989, pp.13-14].

To sum up, in view of the EC's overall development cooperation policy, the EC has financed a large number of important projects in Pakistan. Unfortunately, data for disbursement of EC's financing provided for projects in Pakistan are not available. It is generally believed that on the whole the EC's disbursement in relation to its commitment has been low in the case of Pakistan [14]. Factors like the paucity of matching funds in local currency, the lack of matching partner in the cases of co-financing and insufficient infrastructural facilities can be considered responsible for the low level of EC's disbursement to Pakistan. This dilemma could be resolved in future by common efforts of Pakistan and the EC. Pakistan should look for new opportunities for raising the funds required in the local currency. While the EC should help in finding a matching partner in the case of co-financing projects. In this regard EC should finance projects wholly if possible or the matching partner should be within the EC and EC should help actively in finding matching partners.

(iii) Technical Assistance

The opening up of markets under the GSP is not always sufficient to enable developing countries to make full use of the opportunities provided by the EC under its GSP. This is essentially because tariff barriers are not the only barriers to the expansion of developing country trade. Developing countries like Pakistan also suffer from deficiencies in their marketing networks, lack of adequate information and contact between firms and finally, insufficient knowledge of consumers' requirements. Keeping in view the difficulties, the EC launched in 1974 marketing

and trade promotion schemes to help developing countries to overcome such barriers and to benefit from "market access" measures provided under the EC's GSP scheme. It may be noted that the EC is the only industrialized entity to implement trade promotion schemes to help developing countries sell more efficiently in its markets. The EC action in this sector was initially limited to the organization of training courses and seminars, but has been greatly diversified since then [for more detail see, EC Commission, 1984].

As mentioned earlier, the CCA was signed between Pakistan and the EC in 1976. Under the provision of this agreement a Joint Commission was set and an important role was assigned to it. Since its first meeting in 1977, the Joint Commission has promoted a wide range of activities, principally with a view to helping Pakistan to increase and diversify its exports and take maximum benefits from the GSP scheme. To facilitate the successful implementation of the agreement, EC launched a Trade Promotion Programme (TPP) for South Asia. Pakistan has been an important beneficiary of this programme.

For the implementation of TPP, EC has allocated some ECU 500,000 a year on average during 1980-86 to help Pakistan develop its exports not only to the EC but also to the Middle East and Gulf States [see, Pakistan and Gulf Economist, 1986 and Pakistan Economist, 1988]. Initially, these funds were used to finance a series of disparate activities- participation of Pakistani firms in European trade fairs, buyer-sellers meetings, visits by business delegations, workshops and seminars. However, after the inclusion of the new agreement in 1986, the emphasis has been shifted towards a more integrated approach, in which marketing of the finished products is the last in a chain of events which begins with conception and design of the product. The EC now tries to help at each stage, by providing consultants specialising in design and product development, manufacturing and finally marketing.

Three sectors are already under examination, leather garments, jewellery and light engineering. Between 1983 and 1992, EC has provided assistance ECU 590,000, ECU 250,000 and ECU 300,000 for these projects respectively. Apart from these

projects, EC has also provided ECU 250,000 million for assistance to the Export Processing Zone at Karachi (KEPZ) and ECU 270,000 for the horticultural sector during the same period [15]. In the case of leather garments, the project concerns technical assistance in tanning, garment design, quality control, business management and marketing. In the jewellery sector, it is envisaged to assist selected firms with product design and quality control as well as with the marketing of finished products. In the light engineering sector the EC extended technical assistance to selected firms at every stage of the process from product design to marketing.

3.5.2 Bilateral Assistance

Unlike trade foreign capital and investment flows mainly in one direction, from the richer (developed) to the poorer (developing) countries. The developed countries tend to have the ownership advantage required for investment by virtue of their capital abundance, technological lead and marketing know-how, while the developing countries offer the locational advantages of abundant, low-wage, unexploited natural resources, etc. This pattern of foreign investment, from the developed to the developing countries, is well illustrated in the case of Pakistan.

The main purpose of this section is to explore and evaluate the development cooperation of EC Member States with Pakistan at bilateral level. The scope of our analysis is limited to the United Kingdom, the Federal Republic of Germany, France and Italy only. These four EC member countries not only have been Pakistan's major trade partners absorbing more than 80% of its trade with the EC, but also in the areas of investment, joint ventures, provision of financial, technical assistance, etc. Table 3.6 summarises the trends and share of EC capital assistance provided to Pakistan through Consortium bilateral in the forms of loans and credits since 1970. It indicates that the share of EC Member States in the provision of loans and credits between themselves has fluctuated widely and declined from 60% in 1970 to 37% in 1990. This shift coincides with the overall changes which occurred within Consortium arrangements over the years as discussed in chapter 2, section 2.5.

Table 3.6 BILATERAL CAPITAL ASSISTANCE OF EC MEMBER STATES TO PAKISTAN
[Total Loans & Credits]

[US $ million]

	Belgium		France		West Germany		Italy		Netherlands		UK		EC share % in	
Year	V	S %	V	S %	V	S %	V	S %	V	S %	V	S %	CB	TL&C
1970	1.5	1.0	30.6	19.8	24.9	16.1	23.1	15.0	4.4	2.8	69.9	45.3	60.4	19.9
1971	0.0	0.0	0.0	0.0	2.5	15.4	4.4	27.2	3.4	21.0	5.9	36.4	19.9	19.9
1972	2.5	3.4	21.7	29.6	24.8	33.8	3.8	5.2	4.9	6.7	15.6	21.3	22.4	14.8
1973	12.7	7.3	23.9	13.8	61.3	35.4	0.3	0.2	6.5	3.8	68.3	39.5	45.9	14.4
1974	4.2	2.9	26.1	17.9	22.8	15.6	9.3	6.4	11.0	7.5	72.6	49.7	45.5	14.4
1975	4.3	2.9	64.6	43.9	39.3	26.7	7.7	5.2	31.2	21.2	0.0	0.0	32.6	16.9
1976	4.0	3.1	51.5	40.2	35.6	27.8	9.6	7.5	17.5	13.7	10.0	7.8	27.5	13.8
1977	4.8	4.5	45.7	42.7	27.0	25.2	10.6	9.9	0.0	0.0	18.9	17.7	25.1	12.9
1978	5.0	2.2	41.3	18.5	108.9	48.8	20.0	9.0	26.7	12.0	21.2	9.5	41.1	18.8
1979	5.2	2.0	58.5	22.4	92.6	35.4	32.8	12.5	19.4	7.4	53.0	20.3	52.7	18.6
1980	0.0	0.0	60.2	38.0	35.3	22.3	16.6	10.5	14.9	9.4	31.4	19.8	47.0	21.0
1981	0.0	0.0	0.0	0.0	20.5	27.3	15.0	20.0	15.8	21.0	23.8	31.7	19.6	6.3
1982	0.1	0.1	26.2	14.1	52.6	28.2	23.4	12.6	12.8	6.9	71.1	38.2	38.9	15.2
1983	7.2	3.5	22.8	11.0	104.7	50.7	18.9	9.1	18.7	9.0	34.4	16.6	39.1	14.0
1984	7.5	3.5	25.4	11.8	64.4	29.9	21.5	10.0	4.6	2.1	92.0	42.7	33.4	11.9
1985	0.0	0.0	56.0	26.8	60.8	29.1	65.0	31.1	0.0	0.0	27.0	12.9	39.4	11.6
1986	0.0	0.0	143.0	42.5	188.0	55.9	2.2	0.7	0.0	0.0	3.3	1.0	59.3	20.2
1987	0.0	0.0	0.0	0.0	79.2	39.2	113.6	56.2	9.4	4.6	0.0	0.0	31.0	10.0
1988	29.6	23.1	0.0	0.09	8.6	76.9	0.0	0.0	0.0	0.0	0.0	0.0	11.4	4.7
1989	0.0	0.0	198.0	57.9	44.3	12.9	0.0	0.0	7.9	2.3	91.9	26.9	37.6	12.3
1990	0.0	0.0	111.1	43.3	145.6	56.7	0.0	0.0	0.0	0.0	0.0	0.0	36.5	11.4

Note: V= Value, S%= Share percentage in CB , CB= Consortium Bilateral and TL&C= Total Loans and Credits contracted.

Source: Computed from Economic Survey of Pakistan, various issues.

(I) Pakistan and the United Kingdom

The government-to-government aid- known as bilateral- from the United Kingdom is managed by the Overseas Development Administration (ODA), part of the foreign and Commonwealth Office [16]. A large proportion of British aid has been used to finance the purchase of a mixed bag of capital goods and industrial raw materials like buses, railway rolling stock, electrical equipment, steel, billets, chemicals, dye-making machinery, and so on. Table 3.6 exhibits trends of bilateral UK assistance provided to Pakistan in the form of loans and credits since 1970. It mainly indicates that up to 1974, the UK accounted for the lion's share of total capital assistance provided to Pakistan through bilateral arrangements. Since then, the UK's share declined sharply while the share of other EC Member States increased. However, it is important to note that since 1976 British bilateral aid to Pakistan has been mainly in the form of grants, relieving Pakistan of interest payments and repayment of capital. For example, between 1970 and 1990, the UK provided total aid to Pakistan worth US $919 million. Out of which around 48% ($441 million) were provided in the form of grants [see, PES, 1977-78, p.123 and 1990-91, pp.219-221].

Britain's aid programme, in the case of Pakistan, was targeted on those sectors which are a high priority in terms of Pakistan's needs, where real progress can be made and in which Britain has been specially able to help. In this regard Britain's aid has mainly concentrated in sectors like energy, industry, agriculture (including irrigation, drainage and water), water supply and sanitation, education, health and population. Several projects of particular importance to Pakistan's infrastructure and economy have been funded by British aid.

Major completed and on-going projects funded by the UK aid since 1974 are the provision of equipment for the Pakistan railway, the development of port Qasim, agriculture and earth-moving machinery for land levelling in Sind, land drainage for agricultural development in the Punjab, supply of operating and maintenance equipment for the Chashma, Mangla and Tarbela hydroelectric dams, provision of plant and machinery for Kamalia Sugar Mill, provision of equipment for Kakul

Phosphate Mine and rehabilitation of the gates of the Sukkur and Kotri Barrages in Sind. Technical co-operation included assistance to establish the Allama Iqbal Open University, the development of links between universities in Pakistan and Britain, various training programmes in Britain managed by the British Council, and some important projects were also provided by the UK in other fields [see, ODA, 1988].

The UK is the biggest investor in Pakistan. In 1985, the UK's direct investment was worth of Rs.1209 million, while joint ventures accounted for Rs.386.5 million. This does not take into account the non-repatriable investment by overseas Pakistanis living in the UK. They have invested in a variety of projects ranging from engineering to paper factories. The entire investment comes to more than Rs.429 million. Among the major direct UK investment in Pakistan was ICI's new polyester stable fibre plant amounting to Rs.30 million. This was the single largest British investment in Pakistan for more than a decade which began to operate ahead of schedule [see, Dawn, March 16, 1985].

As far as joint ventures are concerned, in the beginning of 1985 Ford entered into partnership with a local company to manufacture tractors in a plant near Karachi. Massey Ferguson supplied their licence to Millat Tractor of Lahore, with 12000 units in 1984 from their Coventry plant in the north of England. Likewise Morris Motors signed (1984-85) a Rs.549 million deal with Associated Motors (Lahore) to assemble taxis [Dawn March 16, 1985].

In spite of financial and technical cooperation, the British government not only strongly supported Pakistan's point of view on the Afghan crisis but also shared the burden of Afghan refugees which came to Pakistan after Soviet invasion. By April 1986, Britain provided aid for Afghan refugees to the tune of £30 million. Furthermore, Britain has also provided over £60 million in assistance through the United Nations High Commission for Refugees, the International Red Cross Committee and the European Community, to relieve the plight of about three million Afghan refugees who fled to Pakistan following the Soviet invasion of their own country in 1979 [ODA, 1988, p.21].

(II) Pakistan and the Federal Republic of Germany

The Federal Republic of Germany's (FRG) direct official assistance is channelled through the Aid-to-Pakistan Consortium which was established by the World Bank to coordinate international aid for Pakistan. The FRG has been the third largest donor of economic assistance to Pakistan since the 1950s after the USA and Japan and the largest donor country within the EC. Its share in the country's total capital assistance received through Consortium bilateral increased significantly over the last two decades as Table 3.6 delineates. Between 1970 and 1990, the FRG provided total capital assistance worth $1371 million mainly in the form of loans and credits. The share of grants in the total capital assistance was less than 3% or US $41 million. Roughly 92% of the FRG's capital assistance (including export credits) provided to Pakistan between 1970 and 1990 was allocated to specific Pakistani projects. Most of these involved the development of energy resources, industry, agriculture, transportation, rural infrastructure, improvement of water supplies and expansion and modernization of telecommunication.

Development loans have made up the greatest part (about 68%) of the FRG's total assistance provided to Pakistan during the last two decades. They were normally tied to FRG source of supply. The terms of FRG's assistance have been softened in consideration of Pakistan's difficulty in repayment of debts. For example, during this period, the repayment period has been extended from 30 to 50 years and interest rates have been reduced from 3% to 0.75% [see, PES 1990-91, pp.207-217].

Several FRG firms are engaged in business in Pakistan. Among the FRG's firms, the German Financing Corporation for Participating in Developing Countries (DEG) has participated in industrial development in Pakistan, alongwith such firms as BASF, Bayer, Hoechst, Klockner Humboldt-Deutz, Schanzline Becker, Deutsche Perlite Gmbh, Siemens, etc. The DEG which functions strictly in accordance with private business principles has been involved in the financing of specific profitable projects. The Corporation mostly gave priority to "joint venture" projects. In this regard, the DEG has participated in a milk processing plant and a plaster factory. In

terms of financial corporation, a large proportion of funds has been channelled towards the purchase of defence materials, food and industrial spare parts [see, Mehrunisa, 1984, pp.75-83].

Besides development cooperation mentioned above, the FRG has been an important source of political as well as financial support to Pakistan on the Afghanistan crisis. The FRG has rendered significant financial, medical, and food assistance for the maintenance of Afghan refugees directly and through various international agencies and the EC [17]. All these aspects of FRG's cooperation with Pakistan provides an evidence to conclude that development cooperation between Pakistan and the FRG has widened considerably. At present, it represents a successful example of bilateral cooperation between developed and developing countries.

(III) Pakistan and Italy

Pakistan's relation with Italy, established soon after independence, are the most long outstanding, meaningful and consciously pursued. This achievement was a direct result of: (i) Italy being an industrially advanced country with no direct political interest in this part of the world, and (ii) Pakistan's need to achieve economic viability and rapid development. In the very beginning, Pakistan's policy makers realized that Italy was in a position to extend much needed financial and technical assistance to Pakistan with no political interests whatsoever.

Italy became a member of the Aid-to-Pakistan Consortium in May 1963. Italy's membership of the consortium marked the beginning of an important relationship, which is essentially economic in nature. Since then Italy has made valuable contribution to Pakistan's progress and development, by way both of financial and technical assistance as well as the transfer of technology and investment. Apart from consortium pledges Italy extended bilateral assistance in the form of project loans and export credits. Pakistan received Italian assistance in the form of an assurance by the Government of Italy, under the Martenella Law, which

provided that if an Italian exporter was willing to sell capital goods to Pakistan on credit the Italian government would allow the sale.

Between 1970 and 1990, Italy provided total assistance to Pakistan worth US $397.8 million (excluding $30 million as grants) as indicated in Table 3.6. Out of which 58% were provided as capital aid/ project aid and 42% as export credits. The export credits granted, during 1970-82, were for a period not exceeding 10 years at the interest rate of 6% to 7.5%. After 1982, Italy not only reduced the interest rate but also reduced the period of amortization. For instance, Italian capital aid amounted to US $105 million between 1983 and 1987. It carried an interest rate of 2.5% to 7.5% with an amortization period of 10 to 15 years. In 1987, Italy set a record by extending to Pakistan a soft loan of US $113.6 million for a period of 30 years at the interest rate of only 1.5% [see, PES 1990-91, pp.207-217]. The examination of Italy's assistance to Pakistan reveals the fact that Italy provided capital aid to Pakistan mainly between 1983 and 1987.

The most important development projects undertaken by Italian assistance are the Tarbela Dam and its repairs, the Fiat Tractor Plant, the Fertilizer Plant, the Kot Addu Power Plant, the electrification of the Sibbi railway section, the expansion of the liquid petroleum gas industry and establishing a centre for training in the maintenance and repairs of agricultural machinery. Italy also provided financial and technical assistance to the farm extension service of the Fauji Fertilizer company which was the first of its kind in Pakistan.

The Italian Institute of Middle East and Far East has made, in the field of archeology, pioneering efforts in excavations and exploration of ancient Ghandara civilization in Pakistan. Under the leadership of Professor Guiseppe Tuici, an Italian archeological mission carried out an excavation in Swat and on various Buddhist sites. This Italian contribution has given impetus to the tourist industry in Pakistan.

In the area of investment Italian cooperation has been and is insubstantial. Italian investment in Pakistan began very late. However, whenever it has been available, it has proved beneficial to the country's development. The first Italian

investment was made in 1963 in collaboration with a Pakistani party to set up a pharmaceutical concern (Opel Laboraties). In 1977 a private Italian loan was made available for the manufacture of Vespa two-wheeler and three-wheeler to a local concern. Other important ventures launched with Italian investment are Al-Ghazi Tractors- with licence from Fiat, Elko for manufacture of PVC bags and Sitara Chemicals. Several other joint ventures with Pakistani companies- particularly in the high technology sectors like power generation and distribution, agro-based industries, petroleum and gas, telecommunication, etc.- are under consideration [for further detail see, Tufail Ahmed, 1985].

(IV) Pakistan and France

Although France is a major Western donor, the bulk of its development efforts have been concentrated in the "Zone Franc". Consequently, French capital assistance to Pakistan has been modest. French aid administration has undergone much refinement over the years. Since 1966, all executive and administrative powers in this field have been regrouped within the Ministry of Foreign Affairs, under the Secretary of State in charge of 'cooperation'. Funds for countries of the `Zone Franc' are usually channelled through special agencies like the 'Food d' Aid et de Cooperation' for French Africa and the Malagasy Republic. The 'Caisse Central de Cooperation Economique' handles non-zone franc' countries that have special relations with France, such as Tunisia and Morocco; while grants and loans to other countries, like Pakistan, are proceeded directly by the 'Director General de Cooperation Technique et Culturelle' in the Ministry of Foreign Affairs. France has established permanent aid missions in countries which receive a substantial portion of French assistance; in other countries the French Ambassador is usually assisted, as in Pakistan, by an aid attache who is a full-fledged member of the diplomatic service [see, OECD, 1969, p.308].

In the case of France, Table 3.6 manifests that the flow of loans and credits remained highly unstable during the last two decades reflecting the influence of

political relations. Between 1970 and 1990, France provided to Pakistan total capital assistance worth US $1014 million ($1006 million as loans and credits and only US $8 million as grant). The provision of state credits was the main instrument of French assistance to Pakistan. It accounted about 50% of total French assistance. Similarly, the second largest share was accounted by bank credits around 35%, while capital aid accounted only 15% of total French assistance to Pakistan. A number of French credits were extended to finance the development of various sectors of Pakistan's economy like energy, telecommunication, transportation, etc. Most of credits were tied, most carried interest rate of 3%, and the repayment periods ranged between 25 to 34 years. While the bank credits provided by France carried high interest rates and were provided for a maximum period of ten years [see, PES 1990-91, pp.207-217].

The area of joint ventures is still desirous for both countries. During French Foreign Minister Claude Cheysson's visit in 1983, proposals for the building of electric substations, telegraphs and transport projects and the establishment of various industries came under discussion, but no announcements were made. Similarly, in 1984, a French delegation of industrialists visited Pakistan. During their meetings with federal secretaries they identified five major areas of cooperation, viz: engineering, transportation, oil and gas, electricity and nuclear technology. Joint ventures in the field of agro-based industries in order to cater to the Middle East markets was pointed out as an other area of interest. The two countries had already signed an agreement for mutually promoting and protecting each others investment in the two countries. Recently Pakistan has awarded a $128 million contract to the French firm Alsthom for the supply of four gas turbines of 400 megawatt capacity for Kot Addu-the first power project awarded to a French firm in Pakistan and the biggest project since 1978 [18]. In the field of technical cooperation, the french organization ACTIM is responsible for organizing all technical cooperation programmes between the two countries.

The development cooperation between Pakistan and France in the areas of capital assistance, direct investment, joint venture and technical cooperation has been

very meagre and began pouring in very late due to historical reasons. Nevertheless, this limited contribution has been of value to development and is noteworthy as evidence of France's aim to extend assistance well beyond the 'Zone Franc' to countries like Pakistan.

In spite of Pakistan's encouraging policy towards foreign capital assistance and investment, Pakistan's relations with other EC Member States viz., Belgium, Luxembourg, Denmark, Ireland, Netherlands, Greece, Portugal and Spain remained "cordially distant", despite the early establishment of diplomatic relations. Trade forms the major links with these countries. These countries together, today, represent around 20% of Pakistan's trade with the EC. The lack of interest of Pakistan's policy makers in trying to forge close, fruitful relations with these countries was due to the economic and political conditions prevalent both in Pakistan and these countries. With the inclusion of the new agreement with the enlarged EC, it is expected that the areas of development cooperation will be expanded. Under this agreement the EC Member States have undertaken responsibility to provide Pakistan scientific and technical assistance and cooperation in the economic field with a view to extending maximum benefits by their experience in various areas of agriculture, industry, technology, etc.

3.7 Concluding remarks

This chapter has outlined the main instruments of the EC's external trade and development cooperation policy towards developing countries and has commented on their use. It concentrated on both aspects of instruments which restrain imports and preferential arrangements which favour imports from developing countries. These instruments fall broadly into the two categories i.e., tariff and non tariff barriers. Non-tariff barriers apparently seem much more important in restricting access to the EC market for developing countries' exports than tariff barriers.

The EC's preferential trade arrangements for developing countries consists of a generalised system of preferences available to all developing countries and special

preferential schemes for particular groups of countries i.e., the ACP and the Mediterranean countries. These schemes differ in the context of products covered and the size of the concession offered. Together, they form a hierarchy of its trade preferences system what has been called the "pyramid of privilege".

The EC's development cooperation policy, as in the case of trade policy, does not rule out differences of emphasis to take account of historical, geographical or economic circumstances, but its characteristic feature today is its global scope. The circle of countries which have concluded agreements with the EC has widened considerably. In the case of Pakistan, EC's all development cooperation instruments i.e., GSP, financial and technical assistance and food aid were implemented frequently both at multilateral and bilateral levels over the years. However, Pakistan-EC development cooperation has been mainly concentrated with its four EC member countries i.e., the UK, the FRG, Italy and France. They proved to be Pakistan's major partners not only in the field of trade (absorbing 80% of Pakistan's trade with the EC), but also in the areas of investment, joint ventures, provision of financial as well as technical assistance.

The analysis of the EC's development cooperation policy reveals the fact that capital investment flows are still the prerogative of the individual Member States of the EC and this area is conducted on a bilateral-nation basis. Nevertheless, the involvement of the EC through implementation of cooperation instruments and financing some projects marks the beginning of a real EC presence in the field of capital investment in Pakistan. Chapter 7 will focus to identify some ways and means how their relations in these fields can be strengthened, while next 3 chapters would concentrate on trade matters and examine the impact of EC's trade policy regime for Pakistan's exports in the EC market.

Notes to chapter 3

1. The General Agreement on Tariff and Trade (GATT), which came into force in 1948, is both a multilateral treaty embodying the ground rules for international trade and a forum in which countries can discuss their trade problems, settle dispute and negotiate the removal of barriers to their external trade. Its first principle is that trade must be conducted on the basis of non-discrimination - all members are on equal basis, whatever the volume of their trade. This cardinal principle of GATT is embodied in the most-favoured-nation clause.

2. When the first Lome Convention was signed in 1975, it was widely regarded as a model for relations between developed and developing countries. More sober judgments have since been expressed. Despite this, some 69 African, Caribbean and Pacific states (the ACP) signed the fourth Lome Convention in 1989, which suggests that even if Lome has not fulfilled all the hopes and promises of 1975, it remains a necessary and important agreement for the ACPs. The Lome II came into force on 1 January 1981. The Lome III came into force on 1 March 1985 (trade provisions) and May 1986 (aid). The Lome IV was signed in December 1989: its trade provisions entered into force on 1 March 1990 and the reminder in 1991. For the EC and its member states Lome remains the focal point of relations with the developing world, particularly with Africa. For further detail see, Commission of the European Communities, European Information Development, No.DE 64, March 1990 & No. DE 69, April 1991.

3. The system of increasing importance for many ACP countries as a result of downward trends in their export earnings has been thoroughly overhaulted and improved by providing loans and grants through STABEX- for agro-based commodities and SYSMIN-for mineral-based ones. For detail see, Marine, A. (1990), pp. 449-453 and EC Commission, Lome IV 1990-2000 Background, Innovations and Improvements, DE 64, March 1990.

4. Association agreement intends to lead to customs union or the eventful accession of the country concerned. For further detail see, Western Europe 1989: A Political and Economic Survey, (1990), pp.60-61 and Coffy Richard (1987), pp.154-156.

5. For more detail see, Western Europe 1989: A Political and Economic Survey, pp. 60 and The Middle East and North America, Europa publications Limited 1990, p. 238.

6. It may be considered paradoxical that, despite the elaborate mechanism within the GSP for limiting preferential access for sensitive products, no overall formula or definition of the term 'sensitive' exists. In practice a sensitive product is one that is produced by domestic industry in a particular member state (or quite possibly in all of them) where that industry is facing difficult times. Several textile items, leather and plastic footwear, and leather goods fits in this category. Sensitive products face tariff quotas, member state shares and butoirs. In contrast non-sensitive products only face tariff ceilings and butoirs. Tariff ceiling-like a tariff quota with the difference that the normal tariff is not automatically reimposed once the ceiling is exceeded but is subject to negotiation between the EC member states.

7. The European Community's Common Agricultural Policy (CAP) is a complex mechanism. The internal prices of major agricultural products are maintained by imposing variable levies on imports when EC production exceeds by government purchases. With the accession of the Mediterranean countries, a much larger share of the EC's consumption of agricultural products will be produced internally and protected from competition from competition from other developing countries. The EC surpluses are in part disposed of as food aid, but the intermittent selling of

surpluses has effects of depressing world prices and displacing established exporters. For further detail of the ACP see, for example, Gary Sampson and Alexander Yeats, (1977), pp. 99-106; Ingeborg Menzler-Hokkanen, (1982), Alberto Valdes and Joachim, (1986) and Valerio Lintner Sonia Mazey, (1991), pp. 94-109 and Alan Mathews (1985).

8. The EC's GSP scheme has been governed by general a "safeguard clause". This clause makes it possible to suspend tariff preferences and restore the customs duty partially or totally if the quantities or prices of imports are deemed to be causing serious disruption of the domestic market. It could also be invoked to prevent the interests of countries enjoying special preferences under agreements with the EC. The duty is restored, for the product and origin concerned, by means of a Commission Regulation.

9. For further detail see, EC Commission, Europe Information, External Relations, DG Information, No.18/79, March 1979, No.28/79, December 1979 and No.41/81, February 1981.

10. The First MFA (1974-77) was negotiated in the GATT as a basis for controlling international trade in textiles. On the basis of the renewed MFA (1977-1981), the EC has concluded bilateral agreements with the "low-cost" developing countries including Pakistan. For further detail see, Ram Khanna, (1991), pp.19-38 and EC Commission, Europe Information External Relations, No. 44/81, April 1981 and Chapter 5 of this thesis.

11. For a thorough discussion of these aspects, see Commission of the European Communities, Bulletin of the EC, suppl. 8/74.

12. For detail of these agreements see, EC Commission, OJL, No.176 of 10.08.1976; OJL No.168 of 28.06.1976; OJL No.289 of 26.11.79; OJL No.245 of 29.08. 1986 and OJL, No.255 of 05.09.1987.

13. These informations were obtained personally from the Director General of Development Cooperation, EC Commission during the author's visit to Brussels in April 1992.

14. These views were expressed by the official of Pakistan's Mission to the EC during discussion with the author.

15. Collected personally from the EC Commission during the author's visit to Brussels in April 1992.

16. The Overseas Development Administration (ODA) is the British Government Department responsible for Britain's aid programme to the developing countries. For detail see, ODA, British Overseas Aid, Annual Review.

17. For detail see, Press Release, Embassy of the Federal Republic of Germany, op. cit., and Dawn, May 14, 1984.

18. For detail see, Dawn, Karachi, March 13, 1983, Morning News, Karachi, March 13, 1984 and Ibid, May 5, 1987.

CHAPTER 4

PAKISTAN-EC TRADE RELATIONS: AN EMPIRICAL ANALYSIS

The EC's trade regime appeared to be complex in its nature and restrictive in its operation. Offsetting the various restrictive provisions, however, the EC has instituted various arrangements with the aim of encouraging additional exports from developing countries including Pakistan. Section 4.1 examines the worth and significance of these preferential arrangements available to Pakistan under the EC's GSP scheme in the context of its competitors in the EC market. It is some time asked whether the developing countries including Pakistan would not be better advised to dispense these preferences altogether with the benefits of the GSP and instead seek reductions in ordinary MFN tariff on products of specific interest to them. Section 4.2 focuses on the examination of this argument. Section 4.3 is devoted to investigate the role of EC's special and differential treatment whether they have retarded trade flows between the EC and developing countries? Finally, section 4.5 explores whether the EC's differential trade treatment and increased new-protectionism (NTBs) have jeopardised the expansion of Pakistan's manufactured exports to the EC market as Pakistan has been at the bottom of its hierarchy of external trade relations what has been called "pyramid of privilege".

4.1 The Worth of EC's Generalized System of Preferences (GSP) for Pakistan

The Generalised System of Preferences (GSP), introduced as an exception to the principle of "most-favored-nation" (MFN) of the GATT, offers to the beneficiary countries the opportunity to enjoy a preferential tariff rate equal to the MFN rate paid by non-beneficiary countries. The GSP preferential treatment however, is seen principally as a means of insuring an increase in the volume of exports from the beneficiary country, due to the trade creation and trade diversion effects The preferences are granted in order to stimulate the expansion of exports (Aitken 1976)

and, consequently, favouring foreign currency earnings (Baldwin and Murray 1977). The purpose of this section is to examine the worth and significance of the EC's GSP scheme for Pakistan.

Pakistan began to benefit from the EC's GSP scheme since its inception 1971. Pakistan's agricultural exports are quite adequately covered in the EC's GSP scheme except for the exclusion of rice and molassess. With the exception of these two items, all other agricultural exports of Pakistan have been either MFN duty free or included in the GSP scheme with duty reduction or duty free treatment. The major agricultural products of Pakistan's exports interest included were shrimps and prawns, chillies and spices, mushrooms, mangoes, fish meal, dried apricots, pickles, food preparations, tobacco and tobacco manufactures (SITC 0,1). Tobacco, an important export item for Pakistan, was covered with a quota of 60,000 metric tonnes whereas Pakistan's total export was around 37,000 tonnes.

Table 4.1 manifests overall benefits available for Pakistan under the EC's GSP for more recent years for which data are available. It indicates that around 80% of Pakistan's total exports to the EC is covered under the EC's GSP scheme. Almost all manufactured exports of Pakistan are considered eligible for the GSP preferences. For example, in 1989, Pakistan was allowed to export up to Ecu 1011 million (which is around 80% of the country's total exports) to the EC under the GSP preferences called butoirs. The butoir determines the total volume of a particular product any beneficiary country could export under the GSP scheme. Other 20% Pakistan's exports (most agricultural and minor MFA products) were charged either MFN tariff or were free of MFN tariffs in the EC market. The examination of data presented in Table 4.1 reveals the fact that Pakistan's preferences under the GSP have been increased by bringing more products under the GSP scheme over the years. This is reflected in the increasing share of total GSP preferences (butoirs) from 73% in 1987 to 80% in 1989 as proportion to the country's total exports to the EC. On the other hand, data indicate that actually 46.5% (Ecu 588 million) of the country's total exports benefited from GSP preferences in the EC market. It means that only 58% GSP preferences were

Table 4.1 THE WORTH OF THE EC'S GSP FOR PAKISTAN

[Million ECUs]

Description	1987	1988	1989
(I) Total exports to EC	1102	1230	1265
(II) Total manufactured exports to EC	806	910	918
(III) Total GSP Butoirs*	803	906	1011
(IV) Total Benefited	464	487	588
Ratio:			
(IV) / (I)	42.1	39.6	46.5
(IV) / (II)	57.6	53.5	64.1
(IV) / (III)	57.7	53.7	58.2
(III) / (I)	72.9	73.7	79.9

* Total amount allowed to be exported under the GSP.
Source: Calculated obtaining data from Eurostat, System of GSP imports, concerned years.

Table 4.2 PAKISTAN'S EXPORTS BENEFITING UNDER THE EC'S GSP BY BROAD CATEGORIES

[Million ECUs]

Description	1987		1988		1989	
	Value	%Share	Value	%share	Value	%share
Sensitive indust. products	190	40.9	190	39.0	229	38.9
Non-sensitive products	46	9.9	50	10.3	60	10.2
MFA Products	208	44.8	225	46.2	273	46.4
Non-MFA products	1	0.2	4	0.8	5	0.9
Non-sensitive Agr. products	18	3.9	17	3.5	20	3.4
Total	464	100	487	100	588	100

Source:Calculated obtaining data from Eurostat, GSP imports, concerned years.

utilized by Pakistan in the same year. The utilization ratio of Pakistan remained more or less the same around 58 % between 1987 and 1989. It seems that the complexity of the EC's GSP as a whole and supply constraints were the contributory factors for the low utilization of GSP preferences.

Pakistan's overall GSP benefits by broad categories for the same years are shown in Table 4.2. Broadly speaking it indicates that the most of the country's exports are considered sensitive in the EC market. Sensitive and MFA products together dominate the list. Their share together in the country's exports benefited from the EC's GSP remained more or less the same around 86% between 1987 and 1989. It is important to note that the share of sensitive products declined from 41% to 39%, while the share of MFA products rose slightly from 45% to 46% during the same period. The share of non-sensitive and non-MFA products rose from 9.9% to 10.2% between 1987 and 1989 respectively, while the share of non-sensitive agricultural products dropped from 3.9% to 3.4% during the same period.

Table 4.3 enlists Pakistan's key twenty products at 6-digit level that benefit from the EC's GSP scheme. These key products are also representative of the key manufactured exports of Pakistan. Most of the items- including those highest in the list - are also relatively labour-intensive. As might be expected from the objectives of the GSP, there are relatively few food products in the list. What is remarkable from this table is the great concentration of GSP benefits in relatively few products. The top seven items make up around 359 million ECUs, almost 80% of the total 20 items' exports to the EC in 1989. These 20 items contributed around 77% of Pakistan's benefited exports and 36% of Pakistan's total exports to the EC market during the same year.

Table 4.3 also manifests the behaviour of major commodities which benefited from the EC's GSP scheme between 1987-1989. The behaviour of major items differ from commodity to commodity and shows a mixed picture. For most commodity declining trends are observable with respect to their utilisation ratios. Only eight commodities show an increase in their utilisation ratio

Table 4.3 PAKISTAN'S MAJOR EXPORT ITEMS BENEFITING FROM THE EC'S GSP SCHEME

[Million ECUs]

Items	1987 1	1987 2	Percentage Share	Percentage Utilization	1988 1	1988 2	Percentage Share	Percentage Utilization	1989 1	1989 2	Percentage Share	Percentage Utilization
100580 Leather garments & similar articles.	82	62	15.7	75.6	83	46	11.9	55.4	100	89	19.6	89.0
400580 Carpets and rugs.	89	82	20.8	92.1	89	78	20.3	87.6	89	79	17.4	88.8
100520 Hides & Skins (Bovinsex).	77	70	17.8	90.9	88	72	18.7	81.8	84	74	16.3	88.1
309500 Toys, etc.	38	28	7.1	73.7	39	32	8.3	82.1	45	36	7.9	80.0
400020 Woven Fabrics of cotton.	58	28	7.1	48.3	74	32	8.3	43.2	90	34	7.5	37.8
100540 Hides & Skins (goat-alike).	28	20	5.1	71.4	34	30	7.8	88.2	38	32	7.1	84.2
520240 Fish & fish preparation.	15	12	3.0	80.0	17	13	3.4	76.5	18	15	3.3	83.3
400350 Woven fabrics of synthetic fabrics.	2	2	0.5	100	3	3	0.8	100	14	13	2.9	92.9
400060 Hand-made & needlework Tapestries, etc.	1	1	0.3	100	17	8	2.1	47.1	22	11	2.4	50.0
100590 Gloves for job protection.	12	12	3.0	100	11	10	2.6	90.9	12	9	2.0	75.0
100680 Footwear.	9	8	2.0	88.9	12	11	2.9	91.7	9	8	1.8	88.9
400033 Woven fabrics of synthetic filament yarn.	72	32	8.1	44.4	81	5	1.3	6.2	69	8	1.8	11.6
100570 Travel goods, hand bags & similar articles, etc.	5	5	1.3	100	6	5	1.3	83.3	8	7	1.5	87.5
400290 Women or girl's suits and ensembles, etc.	7	4	1.0	57.1	9	5	1.3	55.6	10	7	1.5	70.0
401130 Floor cloths, dish cloths and duster,etc.	6	4	1.0	66.7	9	8	2.1	88.9	8	7	1.5	87.5
400010 Cotton yarn.	18	4	1.0	22.2	24	5	1.3	20.8	23	6	1.3	26.1
400390 Toilet and Kitchen linen	13	7	1.8	53.8	11	5	1.3	45.5	13	6	1.3	46.2
400730 Track suits (wool, cotton and man-made fibres).	6	3	0.8	50.0	8	7	1.8	87.5	10	5	1.1	50.0
100530 Hides & skins (D'Ovins)	6	5	1.3	83.3	6	6	1.6	100.0	4	4	0.9	100.0
400040 Woven curtains and other furnishing articles, etc.	13	4	1.0	30.8	15	4	1.0	26.7	17	4	0.9	23.5
Total Export (20 Items).	556	394	100	70.9	637	385	100	60.4	684	453	100	66.2
GSP GAINS (%):												
I. 20 items as % of Benefited			85.0				79.2				77.1	
II. 20 items as % of total exports to the EC			35.7				31.3				35.7	

Note: (1)= Special trade covered under the GSP, (2)= Actual exports benefited from the GSP.
Source: Compiled and calculated from Eurostat, System of the GSP imports, concerned years.

between 1987 and 1989. As a result of poor performance of items like carpets and rugs, bovine leather, protective gloves, footwear, woven fabrics of synthetic filament yarn, toilet & kitchen linen, etc., the utilization ratio of these twenty commodities declined from 71% in 1987 to 60% in 1988, then rose to 66% in 1989. On the contrary, a different picture emerges while comparing their shares. More than half of major commodities show significant increase in their shares in 1989 over 1987. Items like, leather garments, goat-alike leather, woven fabrics of synthetic fabric, handmade and needlework tapestries, recorded significant increase in their exports. The comparison of these 20 items' performance with that of the country's overall utilization situation between 1987 and 1989 shows the similar trends. The poor performance of many of these items in 1988 caused a declined in the country's overall utilization of GSP preferences. As a result, its utilization ratio declined from 58% in 1987 to 54% in 1988. With the better performance of many of these items, Pakistan's utilization ratio rose to 58% in 1989.

More interesting than this static picture is the dynamic picture of the GSP preferences. A dynamic approach suggests, instead, that in the long term, preferences would offer incentives for the diversification of the export base, the substitution of production of primary goods with more finished goods accompanied by the reallocation of resources, an overall push towards development and industrialization. In the case of Pakistan's exports, the impact of dynamic effects of GSP preferences are quite visible. This is reflected in the increased share of country's potential exports like, leather garments, synthetic fabrics, hand-made tapestries, travel goods, track suits, women and girl's dressings, etc., as opposed to traditional ones like, carpets & rugs, cotton yarn, hides & skins, etc. Furthermore, the declining share of these 20 major commodities in the country's preference-receiving imports from 85% to 77% between 1987 and 1989 also seem to be supportive of this view (Table 4.3).

Table 4.4 presents the comparative statistics for the major 14 GSP beneficiaries of the EC's GSP scheme. Broadly speaking, it betrays that a limited number of suppliers receive the bulk of the GSP benefits as a whole. For example, in

1989, these fourteen suppliers accounted for 75% of the total preference-receiving imports in the EC market, while more than 50% of total GSP benefits were gone only to top five countries.

Table 4.4 MAJOR BENEFICIARIES OF THE EC'S GSP SCHEME

[Million ECUs]

	1987			1989		
	Actual Exports	Total Butoirs	Utiliz ation	Actual Exports	Total Butoirs	Utiliz ation
China	1501	3780	39.7	2914	6498	44.8
Brazil	1902	3550	53.6	2453	4403	55.7
India	1128	2667	42.3	1792	2714	66.0
Thailand	784	3408	23.0	1213	2324	52.2
Indonesia	368	938	39.2	930	1715	54.2
Hong Kong	859	4652	18.5	910	3869	23.5
Singapore	454	2086	21.8	883	3536	25.0
Malaysia	478	1245	38.4	822	2042	40.3
Pakistan	464	803	57.8	588	1011	58.2
Argentina	222	472	47.0	465	697	66.7
Philippines	363	832	43.6	440	010	43.6
Colombia	1053	631	166.9	431	885	48.7
S. Korea	1117	5161	21.6	367	968	37.9
Chile	209	348	60.1	277	380	72.9
I.Total	10902	30573	35.7	14485	32052	45.2
II.Total GSP	15584	46834	33.3	19448	47659	40.8
(I/II) %	70.0	65.3		74.5		67.3

Source:Calculated from Eurostat, GSP imports.

Table 4.4 also reveals that Asian and Latin American countries dominate the list, because as examined in the previous chapter, African and Mediterranean countries generally find it more advantageous to use their Lome Convention and bilateral trade preferences as opposed to GSP ones. A comparison of imports receiving preferences (butoirs) with actual imports benefited under the GSP scheme from each country indicates that a high proportion of imports do not qualify for preferences. This is partly due to the fact that some GSP products are not required to pay duty under normal circumstances, so obviously, in these cases, preferences cannot

be given. It is also due to the fact that GSP products which might be eligible for preferences are not granted preference, either because a country has exceeded its tariff quotas in the case of sensitive products, or because the exports do not satisfy the rules of origin requirement, or because the exporter has not applied for GSP status because of the administration costs of so doing. A further reason for the low utilization may be the coverage of products and the allocation of tariff quotas and ceilings where the beneficiary country often does not have decisive comparative advantage as we shall see in the next section. These problems in comparing the preference-receiving countries in utilising the GSP scheme can not be overlooked and should be kept in mind.

Perhaps, one reason for the low coverage of LDCs imports by the EC's is the existence of preferential limits in the case of sensitive products and textiles. The importance of the restrictions imposed by preferential limits depends on the number of products classified in the sensitive categories. It is not possible to tell directly from Eurostat statistics just what proportion of LDC exports to the EC fall into the sensitive category. The statistics do tell the value of imports in each category which actually obtained GSP treatment. The value of EC's imports imported under its GSP scheme from the developing countries as well as from Pakistan is shown in Table 4.5.

What is remarkable from Table 4.5 is the great concentration of LDC as well as Pakistan's GSP benefits in relatively sensitive categories. Around 60% of industrial product's imports from the developing countries and more than 85% of Pakistan's exports in the EC market are considered sensitive. However, it is important to note that Pakistan's exports are highly concentrated in MFA product category than the sensitive ones in comparison with the developing countries. However, in both cases industrial and MFA textile products are dominating the list. Given that not all sensitive imports will have received GSP treatment, it is apparent that preferential limits apply to the great majority of LDC as well as Pakistan's manufactured exports.

Table 4.5 VALUE OF EC'S IMPORTS FROM THE LDC AND PAKISTAN BENEFITING FROM THE GSP TREATMENT IN 1989

(Million ECUS)

Category	LDC		Pakistan	
	Value	%share	Value	%share
Sensitive industrial products	7088	45.5	229	38.9
MFA products	2216	14.2	273	46.4
Non-sensitive industrial products	6067	38.9	81	13.6
Non-MFA Products	212	1.4	5	0.9
Total industrial products	15583	100	588	100
Sensitive as % of total	59.7		85.4	
Non-sensitive as % of total	40.3		14.6	

Source: Calculated from Eurostat, System of GSP imports.

The EC's GSP scheme is continually under review. Marginal changes are regularly made, for example, increasing quotas and ceilings for industrial products, making minor additions to the list of agricultural products which can benefit, switching products between the sensitive and non-sensitive lists and altering (up or down) the tariff quotas faced by individual suppliers. Inspite of these improvements the GSP scheme remain highly complex and under utilised. For example, in the case of Pakistan more than 40% of GSP benefits remain under utilized. Alongwith factors mentioned above, other factors like the administrative complexity of the scheme, the complexity of the rules of origin, some supply constraints and the procedures necessary to establish GSP status are a further barriers in increasing the utilisation of the EC's GSP scheme. It implies that overcoming these problems, there is great room for Pakistan to increase the exports of manufactured items whose utilization has been low.

To sum up, the above discussion reveals that despite the complexity of the GSP scheme, Pakistan has been quite successful in the utilization of EC's GSP

scheme and has increased its utilization ratio. Pakistan's exporters are now reasonably familiar with the EC's GSP scheme mainly due to efforts undertaken by the EC under its Trade Promotion Programme (TPP) through conducting seminars and workshops in Pakistan from time to time. Nevertheless, the potential for an increase in exports covered under the GSP- on which tariffs are unlikely to be reintroduced in Pakistan's case- is considerable. In some potential manufactures, Pakistan has shown much inventiveness in spotting opportunities and to increase their exports which she was able to produce and sell cheaply and were covered under the GSP scheme by granting preferences. The list of such products is widening quite rapidly. There is a great deal of room for an increase of Pakistan's manufactures exports to the EC, if Pakistan remains flexible enough to shift to new products as opposed to focus on traditional exports. In this regard, more intentness is required towards increased efforts of export diversification and export upgrading and familiarisation with the EC's GSP scheme among Pakistani exporters.

4.2 GSP Trade Preferences vs MFN Tariff Reduction

The above discussion suggests that the value of EC's special and preferential arrangements to the recipient countries is limited in various ways. It is sometimes asked whether the developing countries would not be better advised to dispense with these preferences altogether with the benefits of the GSP and instead seek reductions in ordinary (MFN) tariffs on products of specific interest to them. The World Bank (1987) put this argument in the following way:

" It has been suggested that by accepting special and differential treatment the developing countries have struck a faustain bargain. In exchange for preferences, which brought them limited and risky bargains, they have given up a voice in reciprocal trade negotiations and left themselves open to attack by protectionists in the industrial countries, who accrue them of unfair trade. The most mature developing countries, at least, should ask themselves whether this bargain still makes sense" (World Development Report (WDR), p.167)

It is clearly evident from the examination of the structure and operation of EC's external trade policies that the EC has tried for different reasons to meet developing countries' demand for "special and differential treatment" what has been called "pyramid of privilege" - the hierarchy of its external trade relations. The worth of EC's GSP treatment for the developing countries in general, and Pakistan in particular, has already been considered in the previous sections. It was argued that the GSP preferences have had a positive if small impact on exports from these countries to the EC market. The GSP may not be as favourable as the Lome and other preferential agreements as regards both product coverage and size of preferential margin, but it did much to offset the disadvantages that a non-preferential country like Pakistan might otherwise face.

Similarly, The World Bank (1987) concluded that there is no doubt that as a result of limitations adopted by most industrial countries, the developing countries have gained little from the GSP. For example, in 1981 the United States imported $120.3 billion of goods from the developing countries. From GSP beneficiaries the total was $68.5 billion, and of this only a meagre $8.4 billion, or 12.3% actually entered duty free. A less effective picture appears if one examines the benefits of the EC's GSP to developing countries. For example, in 1986 and 1989 around 11.6% and 10.7% of EC's total imports from the developing countries were covered under its GSP scheme respectively. While 3.5% and 4.4% EC imports from these countries actually benefited for the GSP respectively in the same years as Table 4.6 indicates.

Table 4.6 EC'S GSP IMPORTS FROM GSP BENEFICIARIES

[Million ECUs]

	1986	1989
(I) Total extra-EC imports	334563	446716
(II) Imports covered by GSP	38886	47659
(III) Actually benefited	11528	19447
(II)/(I) %	11.6	10.7
(III)/(II) %	29.6	40.8
(III)/(I) %	3.5	4.4

Source:Calculated from Eurostat, GSP imports, concerned years.

Accordingly, Langhammer and Sapir (1987), in their comprehensive review of the US and EC schemes, concluded that "after more than a decade of orientation, there is not much evidence of the effectiveness of the GSP". Similarly, some studies of the GSP in the European Communities even show that imports from non-beneficiaries were growing at a faster rate than those from countries covered by the GSP (see, World Development Report, p.167).

In fact, due to the nature and application of preferences the contradictory elements of the GSP scheme are numerous. On the one hand, the scheme was created as a measure whose declared objectives were to help and promote the developing countries industrialization process but on the other, it has been blocked by antithetic needs of trade policies (e.g., the protection of the EC's competitive producers through safeguard clause and high levels of protectionism). With regard to the EC's GSP, Sideri (1989) identified some contradictory elements that emerge from the application of the EC's GSP scheme; the effects on trade expansion, in fact, are extremely limited mostly due to the numerous limitations of a protectionist nature. While the overall level has been reduced further in efficiency; furthermore, the coverage of products and the allocation of tariff quotas and ceilings has been directed principally at goods in which the beneficiary often does not have decisive comparative advantage.

In line with the above comments, this contradiction is clearly evident in the case of Pakistan when one compares the production structure and quota provisions. Table 4.7 reveals the fact that for most of Pakistan's major exports, the amount of GSP tariff quotas/ceilings have been meagre in relation to the country's total exports of these items to the EC market. Only in the case of two items carpets & rugs and men or boy's dressings where the country does not enjoy decisive comparative advantage preference limits have been very high. This seems to be true especially in the case of men or boy's dressings where Pakistan is relatively new entrants as opposed to Hong Kong, China, Macao, Singapore, etc.

The difficulty in evaluating the GSP is that there are different ways to measure its effects for developing countries. The above interpretation is of a static nature. In

the theory of customs union, static approach has its limitations. It is based in fact, on the traditional and decidedly restrictive hypothesis of the neoclassical structure of comparative advantage: free competition in transparent markets, perfectly substitutable products, equilibrium in the labour market, absence of added cost (transport, marketing, etc.) and finally, the complete absence of state intervention. This is fairly crude method as it assumes that the only benefit of the scheme is to provide a 'rent' (equal to the tariff concession) to the beneficiary countries and it makes no attempt to quantify whether the preferences have led to additional trade.

Table 4.7 EC'S GSP TARIFF QUOTAS AND TARIFF CEILINGS FOR PAKISTAN'S SELECTED ITEMS

[Volume=Tonnes]

Commodities	1988			1990		
	TQ/TC 1	Actual Export 2	1/2 (%)	TQ/TC 1	Actual Export 2	1/2 (%)
6302.21.00 Bed-Linen	181	8275	2.2	221	9712	2.3
5513.11.90 Woven Fabrics width>165 cm)	305	7418	4.1	600	9832	6.7
5513.11.30 Woven Fabrics	305	8592	3.6	600	11858	5.1
6208.91.10 Women or Girl's dressings	71	1155	6.2	107	2935	3.6
5701.10.99 Carpets	3274	2551	128.4	3500	2766	126.5
6203.42.35 Men or Boy's dressings	859	596	144.1	1667	894	186.5

Note: TQ= Tariff Quotas; TC= Tariff Ceilings.
Source: Compiled and calculated from Integrated Tariff of European Communities (TARIC).

A dynamic approach suggests, instead, that in the long term, preferences would offer incentives for the diversification of the export base, the substitution of production of primary goods with more finished goods accompanied by the reallocation of resources, an overall push towards development and industrialisation (Badgett, 1978) and a greater attraction for foreign direct investment (Kreinin, 1975; Yannopoulos, 1987).

As already mentioned, the world Bank (1987, p.167), for example, indicates that studies of the GSP in the European Community show that "imports from non-beneficiaries into the EC market were growing at a faster rate than imports from beneficiaries". On the contrary, Boormann, et al., (1981) concluded there are clear signs that the GSP has a trade-stimulating effects. Over the relatively short period 1973- 1976, they show that GSP trade increased disproportionately both by comparison with total third country imports and with general imports from the developing countries. Consequently, the beneficiary countries gained an increasing share of EC markets. On the other hand, Wolf (1987) concluded different conclusions that the dramatic growth of developing countries' manufactured exports after 1960 (at a volume growth rate of about 13% a year) was not due to preferences and did not need preferences.

Similarly, Karsenty and Laired (1987) examined the direct trade effects of 12 individual GSP schemes using an econometric model. They estimated that the developing countries' exports in 1983 were US $6536 million greater as a result of GSP preferences. In that year, the total developing countries' export benefiting from 12 GSP schemes amounted to US $280.6 billion. Whereas on the whole the total trade expansion was US $6.5 billion or of the order of 2.3%. Developing countries' exports benefiting from the EC's GSP amounted to US $96.7 billion, while trade expansion was estimated to be US $2.4 billion or 2.5%.

The results of Karsenty and Laird's study are of a similar magnitude to study conducted by MacPhee (1984). MacPhee estimated the benefits of EC, USA and Japan's GSP schemes at US $4 billion in 1980 and according to Karsenty these

benefits are US $5.5 billion for the same three schemes in 1983. Davenport (1986) concluded that the EC's GSP has made a significant contribution to the beneficiary countries but that this has been at the micro level than at the macro level. A more disaggregate approach reveals that these benefits are concentrated on a few countries. Over 50% of the EC's GSP benefits go to five top beneficiaries-China, India, Brazil, Thailand and Hong Kong (see Table 4.4).

The prominent question is, would the developing countries gain more from the GATT participation and instead seek reduction in ordinary MFN tariffs on products of specific interest to them? It is evident from the above discussion that although preference schemes yield positive benefits to beneficiary countries, it is not in itself an argument for holding on to them if some alternative strategy would yield even more benefits. In this regard, the World Bank's view is that the gains from trade liberalization for developing countries are substantial. Both theory and empirical evidence show that their fuller participation in world trade under the GATT process would increase their efficiency and growth and their overall benefits from trade would be even higher (WDR 1985, p.166).

In view of the above discussion, the developing countries are expected to benefit more from MFN tariff reductions than maintaining the GSP preferences in four important aspects. First, the trade flows of many products coming under the GSP provisions face volume limits which prevent the trade expansion incentives from operating. However, MFN tariff reductions on these products would generate trade creation incentive that would provide more favourable access to world markets for unlimited trade volumes. It seems that Pakistan's exports will benefit as its more than 80% exports to the EC market are considered sensitive and face quantitative restrictions.

Second, many important products of export interest to developing countries are not only currently excluded from the GSP preferences but these items face higher tariffs in the industrial countries. In the case of Pakistan, the relevant example is of basmati rice, the country's major export item which receive no preferences under the

EC's GSP scheme and face higher tariffs. For example, the import of rice (CCT heading No.ex 10.06) from the ACP countries and Portugal in 1987 were charged import levies ECU 292 and ECU 13 per tonne respectively. In contrast, rice coming under the same heading from third countries including Pakistan were charged ECU 457 per tonne [see, OJL, No.349 of 12.12.87]. The past experience shows that the developing countries' exports gained significantly less from tariff reductions in the GATT rounds than did exports from the industrial countries. This was mainly because relatively few of the MFN tariff cuts affected the types of products which developing countries traditionally exported. Table 4.8 points out that even after the Tokyo Round reductions, the average tariffs facing developing countries' exports remained higher than those facing the exports of industrial countries.

Table 4.8 EC'S APPLIED AVERAGE TARIFFS AND GSP TARIFFS

Products/ Group	Post-Tokyo Round	Applied Tariffs Average	Applied Tariffs GSP
Food	3.7	4.4	5.0
Agri. Goods	3.4	0.4	0.5
Raw materials	2.8	0.7	0.5
Fuel	0.1	0.3	0.2
Chemicals	8.4	3.4	4.1
Manufactured	8.1	4.6	6.4
Leather	10.2	2.1	2.8
Textiles	17.3	5.3	7.6
Footwear	19.9	7.3	9.3
Clothing	22.5	6.5	9.1

Source: Laird S and Yeats A. (1990).

On the other hand, the most important agricultural, fishery and textiles items export interest to developing countries are excluded from many GSP schemes. Trade in textile is excluded outright by the USA and Japan; the EC grants GSP tariff treatment only in those cases where the exporting beneficiary country abides by the VERs provided in the MFA. Thus even when textiles are included in the GSP, NTBs operate to limit trade expansion. It is true that many products would also be excluded from any MFN negotiations, especially textile and apparel products, footwear, and

petroleum. Nevertheless, we may anticipate that a general MFN negotiation round would result in tariff cuts on a broader range of products than are presently covered by the GSP schemes.

Third, GSP treatment is not available to all developing countries on an equal basis. For example, Taiwan is excluded from the EC's GSP scheme; Hong Kong faces special restrictions under the GSP scheme of Japan; most Mediterranean developing countries are excluded from the GSP schemes of the EC and the USA, and so on. In contrast, all countries which are signatories of the GATT would enjoy the full benefits of MFN tariff reduction. Pakistan has been benefiting from the EC's GSP since its inception 1971 and has not faced extra restrictions proviso within the GSP framework.

Fourth, the GSP treatment carries no longer-term guarantee. Because preferences are unilaterally granted to the developing countries, tariff and quota levels are not bound: they can be withdrawn or altered anytime. The uncertainty leads the larger exporters to retain exports for fear of triggering import restrictions in the industrial countries. On the contrary, tariff reduction would be bound in GATT, which means that the developed countries cannot unilaterally raise tariff levels without paying compensation to countries adversely affected. Due to these reasons developing countries including Pakistan are expected to gain more from MFN tariff reductions.

Karsenty and Laird (1987) have examined the various policy options concerning possible improvements to the GSP schemes. The study concludes that the full extension of the GSP without any limitation, shows the considerable potential for improvements, since imports by donors from preferential receivers would increase by $20.6 billion as a result of preference rate set at zero per cent. This full liberalization would provide an import increase (in the three major markets EC, the USA and Japan) from the beneficiaries of $18 billion- somewhat less than the $24 billion estimated by MacPhee (1984). Excluding textiles and clothing, the import increase would be in order of $10 billion, compared with MacPhee's estimation of $7 billion.

On the other hand, the estimated potential direct trade gains from the full MFN liberalization are around $17.8 billion. This compares with $20.6 billion under full extension of all the GSP schemes. The study also concluded that the most of products of interest to many developing countries including, clothing, footwear, textile fabrics, travel goods, fish, fresh & simply preserved, fruits fresh, dried and preserved, sugar and honey would benefit from the full MFN liberalization.

Thus, the first impression is that the developing countries gain more through maintaining GSP preferences than they would under MFN tariff liberalization. However, it is important to recall that what was said above comparative static analysis and takes no account of the long-term dynamic effects. In the context of dynamic effects, it is to be expected that under the MFN reduction a stimulus would be given to macro-economic growth in the developed countries as a result of two-way expansion of their trade. Since these countries constitutes the major markets for developing country exports, their higher growth rates in these countries would also be expected to provide an external dynamic stimulus to the trade of the developing countries. Under such a scenario it is most likely that the effects of MFN stimulation would be more than enough to close the gap compared with the option of full GSP extension so that the vast majority of developing countries would gain as much or more from the dynamic effects of MFN reductions.

The net direct trade effect for particular countries, however, will depend on the extent to which the negative effects from the loss of existing preferences are compensated by cutting MFN rates on products of export interest to the developing countries. Because of the different commodity structure of the export of individual countries, the size of the gains or losses could vary from country to country considerably.

If one is concerned about all developing countries, and in particular those most able to benefit from trade (as opposed to aid) policy, these countries would gain more from tariff reduction as opposed to maintaining the GSP preferences. This is because the GSP scheme to date provide a limited benefit to many of these relatively more

advanced developing countries. On the other hand, if one is concerned primarily with the poorer developing countries, the GSP has been an attractive commercial policy instrument for them. Generally, these countries are not affected by the volume limitations under GSP and they largely enjoy unrestricted duty-free access under their special preferential schemes. It seems that they would not benefit from any trade creation effect through tariff reduction. Trade diversion resulting from the erosion of their existing preferences margins would cause the least developing countries to lose from MFN tariff reductions. In the case of Pakistan, it seems that Pakistan would benefit more from MFN tariff reductions since most of Pakistan's major exports (see Table 4.3) are included in the list of products which would benefit from the MFN tariff reductions as suggested by Karsenty and Laired (1987).

Thus, the overall conclusion seems to be that if a straight swap of GSP preferences for MFN tariff reductions would be on offer, developing countries might well be advised to accept it. However, a cursory examination of the political economy of preferences suggests why such a deal is unlikely. Preferences can be regarded the principal instrument of foreign policy for the industrial countries and EC as well. They have an important policy symbolism in the context of the North-South dialogue. They enable them to claim an open-handed approach towards developing countries' exports at relatively little cost. In general, the developing countries, in so far as their views are reflected in UNCTAD documents, while welcoming the MFN tariff reductions, appear to wish to keep their preferential treatment within the GSP treatment, while endeavouring to offset the unavoidable erosion of preferences by obtaining substantial concessions from the industrial countries through improvements in the preferential schemes. However, it is the beneficiary developing country, at least, who should ask himself whether this bargain still makes sense.

4.3 Has the EC's special and preferential trade arrangements retarded EC's trade with developing countries?

The EC is a major economic grouping of twelve highly industrialised countries. Thus, it is not surprising that it represents a large share of international trade. If one includes the intra-EC trade (which is about the size of EC's external trade) then in 1990 the EC accounted for more than 40% of world exports and about the same percentage of world imports. Within the developing countries, consistent with the EC's trade regime, three main groups namely the ACP states, Mediterranean countries and Latin American and Asian developing countries are the major sources of extra-EC imports. Latin American and Asian countries' export to the EC market benefit from the provisions of the GSP preferences and a number of bilateral non-preferential trade agreements. On the other hand, ACP and Mediterranean countries enjoy an overall more favourable export status in the EC market as opposed to those benefiting from GSP preferences as examined earlier.

Some analysts argue that this discrimination nature of EC's external trade policy has been more talk than action. This section will concentrate on the examination of export performance of some developing countries comprising the GSP beneficiaries, the ACP and Mediterranean countries and draw conclusion whether these differential treatments have caused any trade diversion from less favourable GSP beneficiaries in the EC market.

The influence of EC's preferential trading policies can most readily be ascertained in this section. One would assume that the Lome Convention, in granting preferential tariff treatment and exemption from the MFA, would have to be beneficial to the ACP states. On the contrary, empirical evidence shows that there has actually been a decline in trade between ACP countries and the EC. Data also indicate that there has been cyclical movements as far as their export share of the EC market is concerned as is evident from Table 4.9. For example, the ACP share of EC imports from developing countries which was 16 per cent in 1980, after declining to 14% in 1982, rose to 18% in 1986, but then again fell

Table 4.9 DEVELOPMENT OF TRADE BETWEEN THE EC AND SELECTIVE DEVELOPING COUNTRIES

[% Share in EC's total imports from LDCs]

Countries	1980	1982	1984	1986	1988	1990
ACP States:	16.2	14.0	18.4	18.4	15.2	13.9
Nigeria	6.33	4.82	7.11	4.24	2.47	3.05
Ivory cost	1.24	1.12	1.40	2.07	1.38	1.17
Cameroon	0.59	0.68	1.28	1.23	0.95	0.96
Zaire	1.02	0.67	0.84	1.22	1.10	0.79
Gabon	0.74	0.61	0.66	0.72	0.94	0.76
Mauritius	0.25	0.24	0.27	0.46	0.57	0.53
Ghana	0.32	0.25	0.20	0.33	0.43	0.51
Liberia	0.38	0.32	0.40	0.51	0.58	0.49
Total	10.86	8.72	12.16	10.78	8.42	8.24
Mediterranean Basin:	18.2	23.2	26.1	26.3	25.9	29.6
Yugoslavia	1.69	1.93	2.87	4.54	5.05	5.34
Algeria	3.43	6.46	6.61	5.40	4.17	4.82
Turkey	0.81	1.21	1.95	3.20	3.73	4.13
Israel	1.39	1.31	1.64	2.32	2.47	2.41
Morocco	1.05	1.09	1.27	1.71	1.95	2.11
Egypt	1.85	1.96	2.72	1.70	1.41	1.60
Tunisia	1.07	0.92	0.90	1.30	1.31	1.56
Syria	0.75	0.63	0.73	0.43	0.36	0.86
Total	12.04	15.50	18.69	20.60	22.45	22.83
GSP Countries:	65.6	62.8	55.5	55.4	58.9	56.6
Brazil	3.70	4.55	6.29	6.85	8.00	6.39
South Korea	1.61	1.71	1.94	4.01	5.35	4.56
Hong Kong	2.84	2.85	3.41	4.92	5.42	4.11
Singapore	1.46	0.99	1.43	1.88	2.57	3.26
Thailand	0.98	1.22	1.29	2.02	2.54	2.85
India	1.42	1.91	1.95	2.22	2.80	3.16
Malaysia	1.48	1.29	1.91	2.02	3.01	2.51
Argentina	1.56	1.49	2.11	2.14	2.25	2.41
Mexico	1.55	3.05	3.39	2.07	2.11	2.05
Indonesia	0.99	0.88	1.09	1.52	1.83	1.99
Chile	1.10	0.99	1.01	1.42	1.88	1.82
Colombia	0.95	0.90	1.06	1.89	1.13	1.24
Pakistan	0.36	0.39	0.47	0.94	1.05	1.01
Philippines	0.67	0.72	0.89	1.04	1.14	0.87
Total	20.7	22.9	28.2	34.9	41.1	38.2

Source:Compiled and calculated from Eurostat, External Trade and Balance of Payments Statistical Yearbook, various issues.

to 14% in 1990. In contrast, countries participating in the Mediterranean Policy arrangements have seen significant improvement in their relative share of Community imports from developing countries. Over the last decade, these countries almost doubled their share in the EC market increasing from 16% in 1980 to 30% in 1990. Those countries not participating in either Community programme, have been the major source of EC imports from developing countries. They continue to account for the bulk (57% in 1990) of the EC's imports originating from the developing countries. Broadly speaking, they have not seen a significant change in their share of Community imports since the late 1970s.

Table 4.9 shows the development of trade between the EC and selective developing countries comprising from three major sources i.e., the Mediterranean, the ACP states and Asian and Latin American GSP beneficiaries. The countries included in our analysis accounted for more than 69% of EC imports from the developing countries in 1990, while their share was only 44% in 1980. The percentages relating to each of the individual countries refer to the share of EC imports from developing countries that emanate from countries within the group. Hence, for example, 23% of the EC's imports from developing countries in 1990 came from the Mediterranean countries included in our analysis, around 8% from the ACP states, and 38% from countries with no better access to the EC market than that provided by the EC under its GSP scheme. Of course, this does not apply that, for example, 8% of EC imports from the ACP states received Lome preferences. Because many of the exports of the ACP are of goods that have duty-free access to the EC market under the MFN. It would be possible, though laborious to calculate for each group the value of EC imports of products on which preferences exist. However, even this calculation would not show the share of EC imports that actually receive preference. Except in the case of GSP, the EC does not record the actual tariff rates that were applied by the customs authorities to import shipments, and so it is not possible to discover whether or not exporting countries actually benefited from the

preferences to which they are entitled on paper. It is clear from the GSP figures that they do not always do so, whether for reasons of misclassification by customs, incorrect form filling, exporter ignorance, or any other reasons. But even in the case of GSP statistics, figures are kept only for sensitive and non-sensitive products and according to a coding system that is not directly comparable with the Harmonised Nomenclature.

In such circumstances what we can do is to compare the export performance of developing countries which are the major EC trading partners. Comparing the overall performance of EC imports from developing countries in accordance with the EC trade regime during the 1980s, Table 4.9 reveals the fact that the pattern of tariff preferences it grants does not necessarily guarantee success in the export performance of the preferred recipients. Indeed, if tariff preferences were the only determinant of the recipient country's export performance, then one would expect recipient countries i.e., the ACP and Mediterranean countries to have a more successful performance in the EC market. The examination of the data presented in Table 4.9 transpires, however, that while the ACP exports enjoyed the most advantageous status in the EC market, they overall have exhibited a much poorer performance in the EC market. The share of almost all the ACP states included in our study declined or rose marginally or remained stable in the EC market during the 1980s. The overall share of ACP countries included in our analysis declined from 11% in 1980 to 8% in 1990.

In contrast to above experience, the Mediterranean countries exhibited better export performance than the ACP states. Among the Mediterranean countries included in our study Yugoslavia, Algeria, Turkey, Israel, and Morocco experienced significant increase in their market shares of EC imports from developing countries. Their share together rose from 8% in 1980 to 19% in 1990. On the other hand, the share of Tunisia and Syria increased marginally, wile Egypt's share of EC imports from developing countries decreased. It is worth mentioning that among the Mediterranean countries, the shares of Syria, Egypt and Tunisia remained highly unstable during the 1980s. As opposed to above experience, Asian and Latin

American countries that only benefited from the provisions of the EC's GSP scheme have experienced a significant increase in their market shares of EC imports from developing countries. Their market share rose from 20% in 1980 to 38% in 1990. It is important to note that not a single GSP beneficiary country included in our analysis faced decline in its market share in the EC market over the period under study. Once again this evidence seems to underline the fact that tariff preferences can not in themselves guarantee that a trade relationship will favour the recipient country, although it may be argued that it may moderate the asymmetry in favour of the recipient partner.

What then has been the net effect of the special and differential treatment for developing countries? Perhaps, in the face of rising protectionism, the very existence such treatments which promotes trade provides policy makers with a lever against future protectionist demands in the EC market. On the other hand, it is difficult to state categorically where they would be without special and differential treatment. If the special and differential treatment were in the form of tariff, it would have been simple to show that they had retarded trade, if any. But it is nearly impossible to estimate the combined effect of NTBs on the quantity or value of a country's imports. NTBs should, it seems, reduce the share of restricted imports in the restricted market. But in practice they proved to be porous. The GSP beneficiaries facing more NTBs succeeded in increasing the value of their exports by improving their quality, and hence value, or by switching from restrained categories of goods to ones not yet subject to NTBs. As a result, the share of GSP beneficiaries in the EC market, therefore, continue to increase. Of course, the share could grow still faster in the absence of NTBs.

While not conclusive, the above analysis suggests that the Community's discriminatory trade policy is not the only constraint on developing countries' exports. But the question is how far has this discrimination adversely affected their exports? The conclusion of our analysis seems to be that the ACP preferences are unlikely to have a major impact on the export of GSP beneficiaries because of supply constraints.

The Mediterranean countries, however, present a much stronger competitive challenge to GSP beneficiaries. It seems, however, that these countries have benefited more from the dynamic effects of trade preferences i.e., trade creation as opposed to trade diversion from the GSP beneficiary countries. But it is difficult to disentangle the role of trade preferences from other factors, including the fact the more successful exporters have been GSP beneficiaries which in theory are relatively disadvantaged in the EC's trade preference system. It has probably added some problems and diverted some trade away from the GSP beneficiaries towards the favourable ones. But there have been other problems too. The most frequently cited are supply problems associated with their industrial and trade policies.

4.4 Impact of the EC's trade Policy Regime on Manufactured Imports from Pakistan

It is generally believed that Pakistan is relatively disadvantaged in the EC's pyramid of privilege- the hierarchy of its trade preference system. At the apex of the pyramid of privilege are the ACP states and the Mashreq and Maghreb countries of the southern Mediterranean. Their preferential access to the EC market has been, in many cases, in the form of preferences over other third party suppliers, such as Pakistan. Further, agreements with these countries have also covered non-tariff barriers and have included investment and aid provisions. Hence, preferential agreements have to be interpreted as more than the provision of a few percentage points tariff reduction. For this reason, Pakistan and other developing countries have frequently called for the EC to accord them tariff treatment similar to that provided in the Lome Convention.

It is evident from the above discussion that overall the GSP beneficiaries exhibited better export performance in the EC market compared to the ACP and Mediterranean countries how enjoy better export status in the EC market. This section will concentrate on how Pakistan has fared in the EC market being at the bottom of pyramid of privilege enjoying the provisions of the GSP scheme. To this end, this

section will present an analysis of the performance of Pakistan's exports in the EC market during the 1980s, and the role of EC trade policy in causing adverse effect. Despite its narrow focus on Pakistan-EC trade, the analysis has broader implications both for Pakistan and for other developing country trade partners of the EC. Because Pakistan's experience has relevance as a case study illustrating the trade regime applying to EC imports from non-ACP developing countries.

Empirical evidence shows that in practice Pakistan has not been in such a disadvantageous position as seems to be from the EC's hierarchy of trade preference system. However, during the early 1980s Pakistan's manufactured exports to the EC market have been sluggish. Measured in current dollar, they were lower in 1982 and 1984 than had been in 1980. Similarly, EC's total imports from non-members were also lower between 1982 and 1984 as is evident from Table 4.10. Part of this explanation for declining the EC imports is the general phenomenon that has affected extra-EC imports from all sources: stagnation due to a combination of low European purchasing power and increasing protection in the EC. As a result extra-EC imports of manufactures decreased from US $177 billion in 1980 to US $154 billion in 1984. On the whole during the 1980-1985 period, extra-EC imports increased in constant dollar terms at an average annual rate of barley 0.5%, having grown by an average annual 7% in the 1973-1980 period (Sapir and Stevens, 1987).

Perhaps the most striking feature of Pakistan's manufactured exports to the EC is their concentration in a narrow product range which seems to be consonance with the country's overall composition of exports as examined in chapter 2. Table 4.10 bespeaks that manufactured goods classified chiefly by material SITC 6 basic manufactures accounts roughly 60% of the country's total exports. Most of the remaining trade is in SITC 5 chemicals. However, exports of SITC 7 machinery and transport equipment and SITC 8 miscellaneous manufactured articles play a negligible role. It is important to note that Pakistan's manufactured exports in value term rose significantly from Ecu 347 million to Ecu 1277 million showing an increase more than

Table 4.10 EC'S MANUFACTURED IMPORTS: 1980-1990

[Million ECUs]

Origin	1980	1982	1984	1986	1988	1990
Extra-EC	127453	153393	194603	209755	270273	320977
from LDC	20601	26487	30404	62083	52850	63057
Pakistan	249	326	385	551	889	1002
of which:						
SITC 5	58	71	86	224	335	394
% Share*	23.3	21.9	22.4	40.8	37.8	39.3
SITC 6	178	235	272	308	525	563
% Share*	71.8	72.2	70.7	55.9	59.0	56.2
SITC 7	2	5	7	5	10	19
% Share*	1.2	1.6	2.0	0.9	1.1	2.0
SITC 8	9	14	19	13	18	25
% Share*	3.8	4.4	4.9	2.4	2.1	2.5
Pakistan as % of:						
Extra-EC	0.20	0.21	0.20	0.26	0.33	0.31
LDC (%)	1.21	1.23	1.27	0.89	1.68	1.59
LDC/Ext.EC	16.16	17.27	15.62	29.60	19.55	19.65

* Percentage share in EC's total imports from Pakistan.
Source: Eurostat, External Trade Annual and Monthly Statistics.

268% between 1980 and 1990. Similar trends are visible while comparing Pakistan's exports according to SITC category-wise to the EC.

Perhaps the most blazing feature of Pakistan's exports is the significant diversification of its exports to the EC market. It also shows. It is clearly reflected in the increased share of SITC 7, more prominently SITC 5. The share of SITC 7 rose from 1.2% in 1980 to more than 2% in 1990, while the share of SITC 5 rose from 23% to 39% during the same period. Their increased share caused in pushing back SITC 6 in relative importance of country's manufactured exports to the EC market. As a result, the share of SITC 6 declined from 72% in 1980 to 56% in 1990. On the whole, the share of EC's manufactured imports from Pakistan in the country's total exports to EC rose from 74% in 1980 to 87% in 1990. Similar trends emerges when Pakistan's exports as proportion to extra-EC or EC imports from developing countries is examined. This evidence seems to underline the fact that during the 1980s, inspite

of increased protectionism in the EC, EC market remain enough open for Pakistan's manufactured exports.

On the other hand, a closer look at the country's export statistics at disaggregate level, however, reveals the seriousness of the problem of trade concentration. Three 2-digit SITC product categories make more than 50% of Pakistan's exports to the EC: 61 leather and leather manufactures, 65 textiles, and 84 clothing. Hence, there has been no significant diversification out of the traditional manufactured items that dominated Pakistan's basket of exports to the EC market. These trends also apply at a more disaggregated level.

Table 4.11 provides a detailed analysis of Pakistan's major 24 export items at 8-digit level to the EC market for recent years for which the data are available. Within this list, the analysis focused on manufactured goods which are regarded sensitive and are strictly regulated under bilateral agreement (VER) concluded between Pakistan and the EC within the framework of the MFA. These 24 commodities represent 64% of Pakistan's manufactured exports to the EC and over 44% of Pakistan's total exports to the EC market in 1990. EC imports from Pakistan has been analysed in terms of total extra-EC imports of these goods, EC imports from developing countries and EC imports from MFA countries.

Table 4.11 shows that unsurprisingly, Pakistan's share of EC's total imports, EC's imports from developing and MFA countries is most significant in, textiles, clothing and leather products. In the twenty four 8-digit commodity groups included in our analysis which Pakistan exported to the EC in 1990 it held an average 23% of total EC imports, 33% of EC imports from developing countries and 24% of EC imports from the MFA countries. In some commodities, the share is much higher e.g., 96% of EC imports from developing countries in woven synthetic fabrics, 77% in printed bed-linen of man-made fibres (MMF), 58% in toilet and kitchen linen of cotton, 55% in women's dressings of cotton and 48% in protective gloves. In other seven commodities Pakistan's share ranged between 30-43%, while in other nine commodities,

Table 4.11 EC'S MANUFACTURED IMPORTS FROM PAKISTAN: 1988-1990

['000' US $]

Product description		1988	1990	1988 Pakistani imports as % of Ext.EC imports	1988 Pakistani imports as % of EC ldc imports	1988 Pakistani imports as % of EC MFA imports	1990 Pakistani imports as % of Ext.EC imports	1990 Pakistani imports as % of EC ldc imports	1990 Pakistani imports as % of EC MFA imports
4203.10.00	Articles of leather	83441	151617	6.77	11.43	7.32	10 44	19.40	10.84
6302.21.00	printed bed-linen	49128	87676	34.77	57.24	36.74	27.78	43.37	29.84
5701.10.99	carpets & floor coverings	84604	73942	37.01	43.23	56.50	33.93	40.18	43.66
4106.20.00	Skin & leather Goat-alike	40733	52711	30.48	31.02	36.87	30.80	31.59	31.82
5513.11.30	woven fabrics (width<165cm)	30770	48150	32.42	34.44	41.33	40.48	43.90	43.71
5513.11.90	woven fabrics (width >165cm)	33478	39760	36.44	44.16	54.80	38.01	43.85	46.08
4104.31.30	Splits of Bovine leather	36633	36349	11.83	19.98	13.15	8.90	13.22	9.51
5205.12.00	Cotton Yarn (232.56 decitex)	12066	30569	5.48	16.89	6.17	10.40	22.97	11.54
6203.42.35	Gents dressings of cotton	7030	26868	1.44	1.94	2.22	4.23	6.27	6.59
6302.31.90	Bed-linen of cotton	22674	26424	17.83	39.21	22.10	15.05	29.46	16.52
5407.81.00	Woven synthetic fabrics	116	25797	7.72	26.56	9.46	90.32	96.22	93.39
6302.60.00	Toilet & kitchen linen	18075	25299	10.74	20.03	13.49	9.41	16.92	10.39
6109.10.00	Shirts & T-shirts, etc.	11171	23739	2.07	3.95	2.73	2.14	3.56	2.73
4203.29.10	Protective leather gloves	13528	21098	9.04	16.53	16.95	9.34	18.04	9.67
4104.39.10	Bovine leather	13873	19984	11.66	21.53	12.33	12.66	22.04	1.35
4104.31.19	Grains of Bovine leather	19514	19214	16.49	20.89	18.77	18.70	26.48	19.79
6208.91.10	Women's dressings of cotton	8060	18577	13.44	41.67	14.61	22.59	55.25	23.16
6302.91.90	Cotton toilet & kitchen linen	10467	15282	24.02	49.87	30.98	29.69	57.67	31.98
6108.31.90	Women's pajamas of cotton	6693	14094	7.21	17.71	9.91	8.81	23.43	9.49
6302.22.90	Printed bed-linen of MMF	2633	13090	16.99	47.22	19.09	48.00	77.18	52.00
4203.21.00	Sports gloves	9229	12663	36.02	41.48	42.93	42.56	47.76	45.57
5205.13.00	Cotton yarn(192.3 decitex)	2287	10937	2.15	3.70	2.40	7.15	10.90	7.60
5513.41.00	Printed polyester fabrics	7521	10665	22.89	28.54	24.07	27.21	35.11	33.76
6404.11.00	Sports fotwear	12209	10487	2.74	3.11	4.55	2.00	2.57	2.31

Source: Eurostat, External Trade Annual & Monthly Statistics.

the share in EC's manufactured imports vacillated between 11-27% in 1990.

The examination of data presented in Table 4.11 also reveals that there are only few commodities included in our analysis, in which Pakistan's share has been negligible. In fact, there are only two 8-digit commodities e.g., shirts and T-shirts, sports footwear whose share in the EC imports has been less than 5% in 1990. In addition to the two already mentioned items, exception is gents pajamas of cotton where Pakistan had 6% of EC imports from developing countries in 1990. A similar picture applies to most, but not all, items in relation to EC imports from the MFA countries.

More interesting than this static picture is the dynamic picture of changes between 1988 and 1990. As mentioned earlier a dynamic approach suggests that in the long term, preferences would offer incentive for the diversification of the export base, the substitution of product of primary goods with more finished goods and an overall push towards development and industrialisation. These trends are visible while examining the pattern of Pakistan's trade with the EC. It is reflected in the significant increase in the share of country's potential exports, most importantly, articles of leather, gent's dressings, woven synthetic fabrics, synthetic toilet and kitchen linen, grains of bovine leather, women's dressings of cotton, cotton toilet and kitchen linen, printed bed-linen of mane-made fibre and printed polyester fabrics as opposed to traditional exports carpets, cotton yarn, hides and skins, etc. These trends are comparable with trends of commodities benefiting from the GSP preferences in the EC market (Table 4.3).

It is important to point out that the most of aforementioned commodities are covered in the EC's GSP scheme and subsequently benefited from GSP preferences. However, GSP preferences given to potential exports were more generous than given to traditional exports. These trends are also visible at the aggregate level resulting an increase in the shares of SITC 5, SITC 7 and SITC 8, pushing back to SITC 6. As a result the share of formers rose from only 28% in 1980 to 43% in 1990, while the share of latter category declined from 72% to 56% during the same period. However,

it is difficult to conclude that this happened only due to GSP preferences. The pertinent question is to what extent GSP preferences have been responsible for stimulating the flow of such exports to the EC market? In this regard we may say that a country's economic structure and government policy are considered the most important factors assisting export diversification, though the GSP preferences had helped both as symbol of an underlying political and economic relationship and in some cases through the provisions of financial and technical assistance provide through bilateral agreement. If this finding can be generalised, then the GSP preferences and financial and technical assistance have helped Pakistan in proportion to its initial level of economic development.

Similarly, Table 4.11 sheds light on those commodities for which market shares have increased in relation to extra-EC imports, EC's imports from developing and from MFA countries. The immediate striking feature of this analysis is that there are many plus than minus signs. It indicates that in eighteen out of twenty four commodities in which Pakistan increased its market share in the EC's total imports from all sources. More or less similar picture emerges with respect to Pakistan's market share analysis when compared with the EC's imports from developing and MFA countries. As a result of this preponderance of positive over negative movements, Pakistan's share of the EC market for manufactured exports rose from 0.20% in 1980 to 0.33% in 1988. However, Pakistan's manufactured exports rose by 94% in 1988 as opposed to only 24% in 1990. As a result, despite of higher increase in most of major exports, Pakistan's share in the EC market fell slightly to 0.31% in 1990 as Table 4.10 indicates.

Despite this caveat, there are some interesting points to note from Table 4.11. There are two commodities woven fabrics and shirts, although increased shares in total EC imports are recorded, their share of EC imports from developing countries decreased. Another point of interest are the six commodities in which there was a difference in sign between the change in Pakistan's share of total imports and its share of EC imports from MFA countries. In all these exported commodities Pakistan's

share of total EC imports increased, but its share of EC imports from MFA countries fell. In other words, the EC turned increasingly towards other developing countries' sources of supply for imports of these goods, but Pakistan's market share remain generally low. There are three exceptions- where Pakistan's share of EC imports from MFA countries fell, even though its share of total EC imports and imports from developing countries increased - they are protective gloves, bovine leather and women's pajamas of cotton.

4.4.1 Comparative Export Performance of Pakistan in the EC, and Non-EC Markets

It is evident from the above discussion that exports from any country are dependent upon external factors and domestic policies and conditions. External factors determine the context in which domestic decisions are made and a nation's export potentials are exploited. Similarly, the world economy offers market opportunities for exports or presents barriers. The state of the global economy- its expansion and contraction- determines the general climate for exports. Internally, the key factors are the supply conditions that shape a nation's comparative advantage. In this way we may say that any change in a country's exports is at least partially attributable to changes in the world demand for its products. World demand is determined by the growth of foreign incomes, the elasticities of foreign demand for a country's exports, and changes in tastes. Changed supply and cost conditions in competing countries also affect a given country's export prospects. These factors are largely exogenous to an exporting country and as such it can exercise very little influence over it.

How does the picture of Pakistan's export performance of manufactured exports to the EC compare with that of Pakistan's exports to the world market? The answer is that there is a substantial similarity between movements in Pakistan's world and EC market shares, at least in the years between 1982 and 1990. Table 4.12 exhibits comparative statistics of Pakistan's export

Table 4.12 COMPARATIVE PERFORMANCE OF PAKISTAN'S EXPORTSIN THE EC, NON-EC AND WORLD MARKETS

[Million US $]

	1982	1988	1990	% Change 1982/90
Total Exports:				
World	1882355	2829098	3485000	85.2
Pakistan	2694	4661	6131	127.6
% share	0.14	0.16	0.18	
To EC	556	1426	1861	234.7
% share	20.64	30.59	30.34	
To Non-EC	2138	3235	4271	99.8
% share	79.36	69.41	69.66	
Textile and Clothing				
World	75217	183940	224300	198.2
Pakistan	1071	2719	3689	244.4
% share	1.42	1.48	1.64	
To EC	43	194	339	688.4
% share	4.01	7.13	9.19	
To Non-EC	1028	2525	3350	225.9
% share	95.99	92.87	90.81	
Leather & Leather Goods				
World	4115	8706	11112	170.1
Pakistan	104	265	317	204.8
% share	2.53	3.04	2.85	
To EC	51	189	251	392.2
% share	49.04	71.32	79.18	
To Non-EC	53	76	66	24.5
% share	50.96	28.68	20.82	
Carpets and Rugs				
World	857	1187	1338	56.1
Pakistan	136	224	232	70.6
% share	15.87	18.87	17.34	
To EC	39	85	74	89.7
% share	28.68	37.95	31.90	
To Non-EC	97	139	158	62.9
% share	71.32	62.05	68.10	

Source:Calculated obtaining data from Eurostat, UNCTAD Handbook of International Trade and Pakistan Economic Survey.

performance to the EC and world market in regards to the country's major exports over the period 1982 and 1990. Broadly speaking it indicates that overall as well as in all selected broad commodity groups, Pakistan export performance seems to be impressive as compared with that of world exports. Between 1982 and 1990 Pakistan's exports were increased by 128%, while world exports rose by 85% during the same period. The examination of data presented in Table 4.12 reveals the fact that an increase in Pakistan's exports to the EC market, overall and in the case of major commodity groups, is more pronounced as opposed to exports to the Non-EC market during the 1980s. On the whole, Pakistan's exports rose by 235% in the EC market, whereas in the Non-EC its exports rose by only 100% between 1982 and 1990. The examination of data presented in Table 4.12 reveals the fact that an increase of Pakistan's world market share from 0.14% in 1982 to 0.18% in 1990 was mainly attributed to its better export performance in the EC market.

During this period, Pakistan's average share in world exports was around 0.15%. Among the major commodity groups, textile and clothing which were 1.4% of world exports in 1982 increased to 1.6% in 1990. Carpets, carpeting and rugs also showed an improvement as the share of these products increased in world exports from 15.9% to 17.3% during the same period. The share of leather and leather manufactures increased marginally from 2.5% to 2.9% during the period under study.

It is apparent from statistics presented in Table 4.12 that in the case of textiles & clothing products, Non-EC market has been Pakistan's major market as opposed to EC market. However, during the 1980s, Pakistan achieved more success in the EC market than in the Non-EC market. As a result, Pakistan's share of EC imports rose from 4% in 1982 to 9.2% in 1990 showing a massive increase of 688%, while its share of Non-EC imports declined from 96% to 91% during the same years.

On the other hand, in leather and leather manufactures an opposite picture appears where the EC occupies a place of pride than the Non-EC market. Pakistan's exports of leather and leather manufactures performed better in the EC market increasing by 392% compared with just above 24.% to the Non-EC market. EC's

share of Pakistan's exports rose from 49% in 1982 to 79% in 1990 pushing back the share of Non-EC market from 51% to only 21% during the same period. Once again, the Non-EC appears to be a major market for Pakistan as far as the export of carpets, carpeting and rugs are concerned. Nevertheless, in this group, Pakistan's exports again performed better in the EC market than in the Non-EC. Pakistan's share in the EC market rose between 1982 and 1988 from 29% to 38%, but then fell to 32% in 1990. Exports to the world market show the same pattern. Between 1982 and 1988, Pakistan's share of the world exports rose from 15.9% to 18.9% and then fell to 17.3% during the same period. It would appear that among the factors explaining the slow growth of carpets and rugs is probably the result of supply constraints in Pakistan reflected in its loss of market share not only in the EC but also in the world market.

The above discussion indicates that Pakistan's exports performed better in the EC market than in the Non-EC market. However, the better performance in the EC was largely due to exports of textiles and clothing, leather and leather products and carpet and rugs: in all these categories Pakistan achieved more success in the EC market than in the non-EC market. The reflection of Pakistan's better export performance in the EC market can be felt at an aggregate level. Table 4.13 delineates different aspects of Pakistan's trade with the EC since 1975. Broadly speaking it reveals the fact that the evolution of trade between Pakistan and the EC has been much smoother and increasing progressively. It shows an encouraging trends and reveals the fact that Pakistan's position in the EC market has improved significantly as far as balance of trade, import covering ratio or market shares are concerned.

The overall conclusion seems to be that Pakistan's manufactured exports performed better in the EC market than in the Non-EC market and that satisfactory performance of Pakistan's manufactured exports in the world market was partly the consequence of Pakistan's better performance in the EC market. On the whole, Pakistan appeared to be bracing up ground not only in the EC but also in the world market as well over the period under study. Hence, it gives grounds to conclude that

Table 4.13 TREND IN PAKISTAN'S TRADE FLOWS WITH THE EC: 1975-1990
[SELECTIVE YEARS]

[Million ECUs]

	1975	1978	1980	1982	1984	1986	1988	1990
Exports to the EC	244	314	467	568	711	1017	1230	1461
Imports from the EC	431	661	939	1100	1578	1589	1606	1428
Balance of Trade	-187	-347	-472	-532	-867	-572	-376	33
Imports Cover Ratio	56.6	47.5	49.7	51.6	45.1	64.0	76.6	102.3
Pakistan's Exports as % of:								
Extra-EC Imports	0.18	0.18	0.18	0.17	0.18	0.30	0.32	0.32
Intra-EC Imports	0.19	0.17	0.17	0.17	0.17	0.22	0.23	0.22
Total EC Imports from LDCs	0.40	0.40	0.36	0.39	0.47	0.94	1.05	1.01

Source: Eurostat, External Trade statistical yearbook, various issues.

Pakistan's exports to the EC market were not severely affected by the discriminatory EC trade policy and by increased protectionism in the EC market and that the EC market remained more open for Pakistan's manufactured exports than to the Non-EC market. Pakistan's increased market share of EC imports lends support to this conclusion.

4.5 Concluding remarks

This chapter has examined the impact of EC's external trade policy regime on imports from developing countries in general and from Pakistan, in particular. The overall conclusion of our analysis is that the special and differential pattern of tariff preferences EC grants does not necessarily guarantee success in the export performance of the preferred recipients. The comparative export performance of developing countries consistent with the EC's trade regime showed that the most favourable i.e., the Mediterranean and ACP countries exhibited a much poorer performance in the EC market as compared to that of the less favourable i.e., GSP beneficiary countries.

Similarly, the export performance of Pakistan in the EC market shows encouraging trends. In comparison, Pakistan performed better in the EC market as opposed to many GSP, ACP and Mediterranean countries. An important conclusion to be drawn from Pakistan's better export performance and subsequent expansion of its exports to the EC market is that the EC's differential trade regime and increased neo-protectionism have not caused any serious threat to the expansion of Pakistan's exports to the EC market. The EC's GSP and financial and technical assistance provided under the CCA provisions emerged as policy instruments of resolving Pakistan's trade problems arising out of the neo-protectionism over the years.

The more encouraging than the static picture is the dynamic picture of Pakistan's export. This aspects of GSP preferences in the case of Pakistan's manufactured exports to the EC is visible which are reflected in the increased share of

country's potential exports as opposed to traditional ones. However, it is difficult to conclude that this export diversification was solely due to these preferences as it would be difficult to disentangle the effects of preferences from other factors such as country's economic structure and government policy which are considered to be the most important factors assisting export diversification.

In view of the role of the dynamic effects of trade preference we may conclude that the GSP preferences including financial and technical assistance have assisted Pakistan in achieving a degree of export diversification. In contrast, Pakistan's textile and clothing garment export to the EC market is strictly regulated by the MFA which is regarded the most prominent example of the use of bilateral arrangements to restrict the volume of exports by mutual consent. The attraction of a VER for developing countries is that they agree to VER because they benefit from scarcity premia (so-called quota premia) created by the import restraints. In this way, their lose in market share is compensated by greater profits on the sales they are allowed to make. Chapter 5 will concentrate on this issue and make an assessment of quota premia accrue to Pakistan for its textile and clothing exports to the EC market.

CHAPTER 5

AN ASSESSMENT OF QUOTA PREMIA AND THE EFFECTS OF MULTIFIBRE ARRANGEMENT (MFA) FOR PAKISTAN

Successful exports from developing countries are often greeted by industrial countries with an increased level of protection. Amongst the various means employed to achieve this result, voluntary export restraints (VERs) are probably the most important. A VER occurs when a government limits the exports of some goods from its territory to another country at a request of the government of that other country. The EC, like other developed countries relies heavily upon voluntary export restraints (VERs) legitimised under the MFA in regulating imports from developing countries. The effects of MFA for both the developed and developing countries are numerous. The exact economic effects of MFA are difficult to identify and quantify. However, this chapter intends to estimate the price raising effects of MFA for Pakistan by calculating the quota rents accruing for its clothing exports in the EC market.

To achieve the desired objectives, section 5.1 and 5.2 briefly summarise the short history and main objectives of the MFA and its economic effects for both the developed and developing countries. Section 5.3 shows, albiet theoretically, the significance of quota premia accruing to a restricted country due to VER. Section 5.4 gives details of the estimation of quota premia accruing to Pakistan for its clothing exports restricted under MFA by bilateral voluntary agreement to the EC market and reports the results. Abolishing or liberalising the MFA will have effects on the economies of both the developed and the developing countries. Such effects are considered in section 5.5 focusing on what the effects of MFA relaxation might be on prices, demand and supply both in the developed and developing countries using the extent of Pakistan's quota premia. Section 5.6 deals with different proposals forwarded for ending the MFA mainly with the object, if the MFA is to go, how should this best be done?. Section 5.7 focuses on the issue how far Pakistan has fared in the EC market in relation to its competitors consistent with the EC trade policy

regime under the MFA restrictions and how she is likely to perform in a scenario of world without the MFA. It should be kept in mind that in our analysis term MFA will be used so as to act like a single VER, restricting supply from certain countries and pushing up import prices. In other words, the restricted supplier, in our case Pakistan, represents all MFA restricted countries, the unrestricted supplier (the EC) represents the rest of the world (1).

5.1 The Multi-Fibre Arrangement: A Short History and Objectives

Protectionism in textiles and clothing is not a new phenomenon. Restrictions on multilateral basis date from 1961 and 1962. In 1961 a new textile and clothing regime "the Short Term Arrangement (STA)- was negotiated under the auspices of GATT, governing an important part of world trade in textiles and clothing. The STA was replaced in 1962 by the long Term Arrangement Regarding International Trade in Textile (LTA), which controlled cotton textile exports for the next ten years. The LTA remained in place until 1974, when the MFA took it place. The MFA was renewed in 1977 (MFA II), in 1982 (MFA III) for a period of four years and seven month and again in 1986 (MFA IV) for a period of five years (see, WDR, 1985, p136-137 and Mathews, 1991, pp.85-100).

The basic formal objectives of the MFA have remained unchanged throughout the period since 1974. They are to achieve the progressive liberalisation of world trade in textile products, while at the same time ensuring the orderly development of this trade, and the avoidance of disruptive effects in individual markets and on individual products. One of the principal stated aim of the arrangement is to encourage the growth of textile and clothing industries of developing countries. Developed countries imposing restrictions are required to pursue policies to encourage structural adjustment, i.e., to encourage textile and clothing firms which are not internationally competitive to move into viable lines of production.

The MFA was set up under the auspices of the GATT, and is an acknowledged and permitted 'derogation' from the ordinary rules of GATT. So the MFA is a legal agreement, negotiated and signed by participating countries, which allows for an exporting country and an importing country to reach a separate bilateral agreement (VER) to restrain the flow of textiles and clothing from the exporting country into the importing country. The two principal provisions of the MFA are Articles 3 and 4, which cover situations of actual and threatened market disruption. Where an importing country claims that market disruption is taking place, it is required under article 3 to consult the exporting country. The consultation may result in agreed bilateral measures. Where no agreement is reached, the importing country may impose unilateral restrictions, which it must report to the Textile Surveillance Body (TSB)- the supervisor of the MFA implementation. Article 4 of the MFA covers situations where there is a risk of market disruption. Only bilateral agreements are possible under this article, and it is under this provision that the normal bilateral agreements between importing and exporting countries are signed.

Market disruption is defined as occurring when there is serious damage, or the threat of serious damage, to the domestic industry. The damage must result from a sharp and substantial increase in imports from a particular source, at prices lower than those of comparable products, whether domestic or imported. The economic interests of exporting countries must be taken into account when establishing whether a situation of market disruption exists or not (for more detail see, Anson 1988, p.112).

Almost all developed countries, together with those developing countries which are substantial exporters of textiles and clothing, are member of the MFA. Most East European countries are members, and have bilateral agreements as exporting countries. This is also true of China. The original MFA I of 1974 had 42 participants, with the EC counting as one. The present number of participants is 43, covering 54 countries, with the EC signing as bloc. Bilateral agreements under article 4, imposing quantitative restrictions on imports into the developed countries, are the principal means of regulating trade between members. The developed countries

notably, the USA and the EC, negotiate bilateral agreements with the each of the developing countries. Japan and Switzerland, although members of the MFA, have not in general imposed any quantitative restrictions on textile imports.

An important feature of the MFA is that the exporting countries are responsible for the administration of the agreed quotas which establish limit on the quantity of goods (by weights, or by number of items, according to the product description) to be exported and for claiming the degrees of flexibility. They allocate the quotas among their own manufactures and traders, and issues export licences for the goods concerned. The bulk of the administration has been devolved onto the exporting countries. This is one of the aspects of the MFA that pleases developing countries. The administration burden imposes problems, but the system enables exporting countries to earn quota 'rents' as we shall see. On the other hand, importing countries monitor the agreed levels of imports, but intervene only when quotas are exceeded. (for further detail of the MFA see, for example, Keesing and Wolf (1980), Silberston (1984), GATT (1984), Sampson (1987), World Development Report (1985)), and Ram Khanna (1991).

5.1.1 The MFA and the EC

In consonance with the EC's trade policy regime, as examined in the previous chapter, three regimes apply to imports of textile products into the EC depending on the products and the country of origin. The MFA regime, the preferential regime for a number of Mediterranean and Lome signatories, the ACP states, and finally the autonomous EC regime on imports which applies to textile products not covered by the MFA regime or a preferential regime (for more detail see, Dartel van (1983).

The MFA protocols sets the ground rules, but contain no details as to quantities, etc. These are set out in the various bilateral agreements. Within the framework of the MFA the EC has negotiated under article 4 bilateral agreements with 21 developing countries- exclusive of China and Taiwan- and 6 East European

countries [2]. Thus the substance of the Arrangement lies in the bilateral (government to government) agreements signed under its auspices. The MFA itself merely sets out the terms and conditions which should be replaced by the signatory governments when negotiating volumes of trade in specific textiles and clothing products. The main characteristics of the bilateral agreements are as follows.

The agreements are applicable to the total range of the MFA products, which are divided into 114 categories and are grouped together into three groups. Group I contains the "very sensitive" products. The quotas at the EC level are further subdivided into 10 country quotas for each member states where the Benelux is considered to be one member state. The particular items covered differ from agreement to agreement, as do the quantitative limits on each category. The quantities in the agreements were based originally on existing patterns of trade, but the restraining country must allow some growth in imports of quota products under the bilateral agreements. Most of the EC's bilateral agreements under MFA IV fall into three categories. Export of Dominant suppliers (like Hong Kong, Korea, Macao and Taiwan.) were allowed only 1% growth on eight 'sensitive' product categories of Group I; most other countries were allowed to grow between 4 to 6% depending on product or country, and export of specially favoured countries was allowed up to 7% growth. Least developing countries are exempt from all restrictions (Mathews, 1991, p.96). Among flexibility provisions in the agreements are those for 'swing', 'carryover' and 'carry forward'. Swing is the freedom to exceed a particular quota by a maximum percentage, provided that there is a corresponding reduction in another quota. Carryover is the freedom to transfer a maximum percentage of a quota to the following year, and carry forward the freedom to draw on a percentage of next year's quota in the current year. Pakistan-EC bilateral agreement of textile and clothing products provides such provisions under Article 7 in the case of swing and carryover up to 7%, and 5% in the case of carry forward (see, OJL, No.255 of 11.12.1986).

The remaining categories are subject to the so-called "basket exit procedure". If exports from a given country reach a specified percentage of the total imports of the

product into the EC in the previous year, the EC can call for consultations so as to arrive at an agreed quota level; in the absence of agreement a quota may be imposed unilaterally. In addition to the quotas at Community level and the country quotas, the member states may, if approved by the Commission, apply Article 115 of the Treaty of Rome to restrain imports of the products under quota from third countries through other member states.

Finally, the "anti-surge procedure" can be applied so as to regulate the level of imports in previously under-utilized quotas for highly sensitive products in such a manner that share and substantial increase in imports are prevented. Summarizing, nearly all textile and clothing products imported into the EC from the MFA countries are subject to some restrictions: either by means of quotas or via the basket exit and anti-surge procedures as examined earlier.

In the case of the EC, imports of certain textile and clothing products from preferential suppliers are restrained through VERs, although the arrangements are less restrictive than under the EC's MFA bilateral agreements. Tariffs on imports of textiles and clothing from these countries have in general been abolished. Growth rates are more generous, as are provisions for swing, carry over and carry forward than for the MFA countries mentioned earlier. In practice, these restraints depend very much on the co-operation of the supplier country, and there have been many cases of imports exceeding the agreed limits. Among the preferential countries, Turkey is causing the greatest problems at present. Her textile and clothing industries have been expanding rapidly, and her exports have been growing very fast. Turkey is now one of the leading suppliers to the EC.

About 69 African, Caribbean and Pacific (ACP) countries have signed the Lome Convention with the EC. This guarantees free access to Community markets for their manufactures, subject to safeguards in certain instances. These arrangements have not much impact on imports of textiles and clothing into the EC, since most ACP countries have not been important exporters of these products. Mauritius has, however, caused problems for the EC in the past, and Caribbean countries may do so

in future. Their textile and clothing industries are now expanding rapidly, although they are geared particularly to production for the US market.

Empirical evidences suggest that inspite of a complex and formidable system of controls as the MFA, imports from these countries have grown rapidly not only to the USA, but the EC market as well. This suggest to conclude that the MFA still retained enough flexibility to permit some response to market forces. There is a general conclusion that the MFA has not so far been successful in preventing significant growth in market penetration by developing country textile and clothing exporters, although the growth would doubtless have been higher without these controls.

As for the MFA commitment to allow developing countries an increasing share of world trade, the evidence is generally positive. For example, over the periods of the MFAs, the exports of major 16 MFA suppliers into the OECD countries rose by 280% between 1973 and 1986 from US $26167 billion to $99298 billion, while their share rose from 21.1% to 32.6% during the same period [3]. Similarly, overall the share of developing countries' imports of textile and clothing into the developed countries rose from under 30% in 1973 to 40% in 1981 and further to 43.4% in 1986. The same trends are apparent from the examination of EC's textile and clothing import figures [4].

5.2 The Economic Effects of the MFA

There is no doubt that the MFA was devised and meant to protect the domestic textile and clothing industry in the industrial countries. Nevertheless. for those countries directly facing MFA interventions in the form of VERs there are several direct and indirect effects associated with the MFA instruments which have been widely discussed in economic literature (see, Anson, 1988, pp.126-142, Cable, 1987, pp. 619-646, Koekkoek and Mennes, 1986, pp.142-167, Hindley, 1987 and 1988, pp.689-706 and pp.268-289 respectively)

The MFA creates vested interests in the restrained exporting countries, and enables established producers to earn premia on account of quota limitations. Hamilton (1985) estimated that total rent income to Hong Kong amounted to 1% of its GDP in 1981-82, or 16% of the clothing industry's value added, while Wolf (1986) estimated quota premia equal to 5% of Hong Kong's GDP.

Another important effect derived from the above is that presence of substantial rents creates an incentive for those countries who benefit from quota rights to maintain the status quo and thereby use the instrument as a means of pre-empting competition from newly emerging producers. When arguments regarding 'certainty' of access are advanced this consideration should be born in mind. On the other hand, it also encourages the growth of exports to markets not restrained by quota.

'Upgrading' is a further by-product of the MFA which is well documented and quite well understood. Faced with quantitative restraints which apply to a complete category of products exporters have an incentive to specialize in higher value added products with higher margins. Insofar as this expedites the process of moving up-market for a given exporter it may be regarded as a beneficial by-product of this form of restraint. On the other hand, however, since the restraints by rising profitability may serve to maintain producers in particular activities longer than would otherwise be the case there is an associated efficiency loss.

It is also known that source specific interventions (VERs/MFA) influence market structure and firm's behaviour in the restrained market. This follows as a result of the fact that restrained suppliers administer the system and, in order to do so effectively they must cartelize (whether formally or informally). The usual price/output effects, the implications of which have been discussed above, can be expected to follow. In addition, however, a barrier to the entry of new firms is created in that a prerequisite to exporting to restrained markets is access to quota. If quota transfer rights are not tradeable/transferable, new entrants can effectively be excluded. If quota rights are transferable entry is possible. However, competition for quota

rights then means that at least some part of the rents is being absorbed in efficiency losses.

Similarly, an important effect of the MFA is that it encourages the establishment and growth of textile and clothing production in countries whose exports are not (yet) limited by quota, or whose quotas are currently under-utilised. Many of the minor exporters, especially the less competitive Latin American and East European exporters, lack militancy since they see MFA as providing a guaranteed market share in a field they would otherwise find difficult to enter. The necessary investment may be undertaken by indigenous entrepreneurs, or by entrepreneurs in restrained countries or through attracting foreign direct investment. In this essence we may say that the MFA stimulates towards investment and industrialisation.

One further effect which should be mentioned is the impetus given to trade deflection. Restricted access to some markets often serves merely to deflect exports to other markets. This phenomenon has been noted as being an especially prevalent feature of trade in clothing, (see Keesing and Wolf, 1980). From the standpoint of the exporting country this may raise the profitability of the introduction of additional restraints in other importing countries.

An additional consequence of the MFA is trade diversion from more to less restricted sources among developing country exporters. The OECD notes that "trade diversion effects have been wide spread in the past" (OECD, 1985, p.110). In the EC, substantial trade diversion occurred to some low cost non-MFA suppliers in the Mediterranean countries whose exports to the EC have consistently grown faster than those from countries with Multifibre Arrangements. Within these arrangements themselves, there has been considerable differentiation in treatment with trade diverting effects. There has also been a good deal of trade diversion in the form of "quota hopping". For example, the large-scale overseas investment by Hong Kong clothing industry has been partly motivated by the pursuit of low costs but also by a wish to evade quotas for example, in Macao in the mid 1960s, Mauritius in the early

1970s, Sri Lanka and Indonesia in the late 1970s, and more recently in the Maldives and, on much larger scale, China (Young and Hood, 1985).

From the point of view of the developed countries, the MFA has undoubtedly given their own textile and clothing industries some protection, but it has at the same time encouraged imports from other developed countries, and from low-wage countries with preferential access. Continuing pressure from low-wage countries, including those restrained by the MFA, has also encouraged outward processing, which allows developed countries to take advantage of relatively low wages in the clothing industries of nearby countries.

The effects of the MFA have clearly been numerous and varied, both as regards developing and developed countries. The pattern of world production and trade in textile and clothing must have been substantially different from what it would have been if there had been no MFA, although we cannot know exactly what the effects have been. Some of the changes that have taken place as a result of the MFA for example, the establishment of production in 'new' countries- will not now be reversed, even if the MFA were to be phased out, although here again we cannot predict what would happen (We will discuss this issue in section 5.7). But the increasingly all-embracing character of MFA controls, at least among developing countries, has now so narrowed the scope for further trade diversion among developing countries that its restrictive effects are more likely to be reflected in future in the growth of total developing countries exports.

5.3 Theoretical considerations: the Significance of Quota Premia

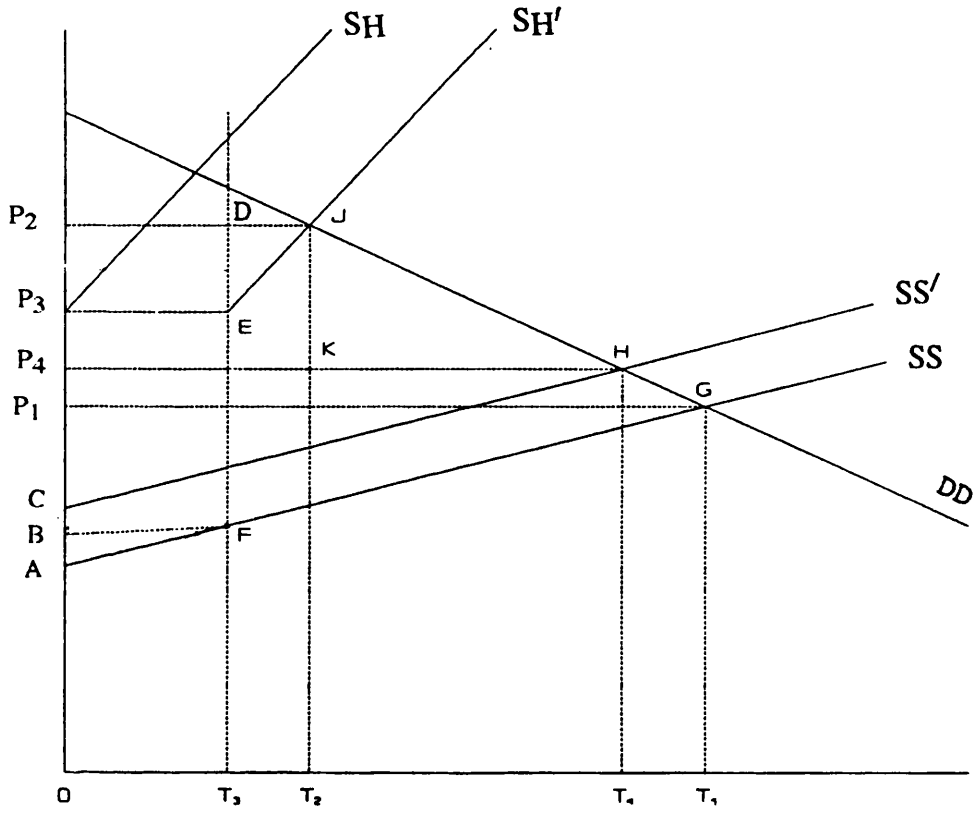
It is evident from above discussion that the imposition of quantitative restrictions than tariffs on imports into the developed countries and the EC as well, is the principal means of regulating trade in textile and clothing within the provisions of bilateral agreements (VERs) concluded within the framework of the MFA. At first sight, tariffs and quotas may appear to be quite dissimilar political tools for helping

comparative disadvantage producers. But every economics student knows that price and quantity are interrelated. So anticipate seeing that effects of a tariff and that of a quota are nearly the same: price up, imports down, comparative advantage production down, comparative disadvantage production up. Nevertheless, quota differs from tariff in one important respect, however. Because no import duty is collected, supplier countries benefit from the higher market price which prevails after the restrictions.

Quota is, however, a more effective barrier to trade than of a tariff. Under a quota, subsequent increase in domestic demand or decreases in domestic supply do not lead to large imports; whereas under a tariff they do. Thus an import quota, as compared to a tariff, is more certain, inflexible, and attractive to domestic special interests. Further, they are not highly overt and they offer compensation to both restricted and non-restricted exporters That's why VERs are considered attractive instruments of trade intervention to mercantilistically inclined policy makers than tariffs (for further detail see, Batchelder, 1981, Williamson 1991).

In order to know the effects of MFA restriction one has to assume that the MFA acts like a single VER, restricting supply from certain countries and pushing up import prices. In other words, the restricted supplier represents all MFA restricted countries, the unrestricted supplier represents the rest of the world as mentioned earlier. Figure 5.1 (taken from Silberston with modification) is a very simplified representation of what happens to the price levels in developed countries in the presence of quota restraints on imports. It shows that, in a free market, with tariffs, the price would settle at P_4. Given MFA constraints, however, the price settles at the higher level P_2. Developing countries exporters get only P_3, however, after deductions are made for tariffs, etc. in the importing countries. The vertical distance EF represents the quota rent for the marginal developing country exporter. The area $EFBP_3$ represents the total rent accruing to developing country suppliers, in our case Pakistan. Intra-marginal suppliers earn more rent per unit sold than marginal suppliers, depending on the slope of the supply curve. If one looks at the extreme case of a perfectly elastic (i.e. perfectly

FIGURE 5.1 SUPPLY AND DEMAND FOR CLOTHING BY THE EC UNDER VER



SS	Supply curve of developing countries and Pakistan (c.i.f. prices)
DD	Demand curve of EC consumers
S_H	Supply curve of EC industry
OT_3	Import quota into EC of developing countries and Pakistan
S_H'	Supply curve of the EC, displaced by import quota (OT_3)
P_1	Price of clothing in the EC, in the absence of quotas and tariffs
P_2	Price of clothing in the EC, given import quotas
DE	Tariff imposed by the EC
EF	Marginal quota rent obtained by developing countries and Pakistan
SS'	Supply curve of developing countries and Pakistan, plus tariff imposed by the EC
P_4	Price of clothing in the EC in the absence of quotas
$EFBP_3$	Total amount of quota rents obtained by developing countries and Pakistan

horizontal) supply curve, then all developing country suppliers would earn the same amount of rent per unit.

The usual practice, when quota premia are quoted, is to assume tacitly that the premium represents the distance EF. It is also tacitly assumed that the supply curve is horizontal, so that the quota premium EF is the surplus earned on all units exported. Similarly, area $EFBP_3$ represents the total amount of quota rents earned by the exporting country on account of his total quantities of exports (OT_3). It is an easy step from here to argue that if exporting countries' prices are higher by this amount than the supply price, i.e. than cost of production. If quotas were abolished, and a competitive market resulted, than no quota premium would arise, and price would be driven down to P_4 and the quantity imported will increase from T_3 to T_4 (tariff included). Hence, if we know export prices and quota premium, we can calculate how far prices are high due to quota rents and how far prices would fall if quotas were abolished.

This approach has many limitations. For example, it has been argued by Silberston (1984) that this is not the correct way to regard quota premia. In a completely free market for quota, quotas would be traded until the marginal profits from the use of quota were equalised throughout the market. On the assumption of reasonably elastic supply, these marginal profits would be close to the average level of profits. Where the market is restricted, however, so that only a proportion of quotas is traded, quota premia may fluctuate considerably as demand fluctuates. They reflect profits at the margin, for both sellers and buyers, but these marginal profits may differ considerably from average profits.

In Pakistan due to regulatory and business reasons the quota market is restricted. In Pakistan the system involves loss of quota in subsequent years if less than 95% of the quota is used. To retain quota, the quota holder must use at least 50% of the quota. He may transfer the other 50%, and will not subsequently lose future quota if total utilization is at least 95%. Usually, however, quota holders transfer much less than the permitted maximum. One reason for this may be that they want to

hold onto quota because they do not want to disrupt longstanding links with overseas customers. Moreover, even if they could charge prices which embody the high quota premia ruling in the market, they may hesitate to do so for fear of disturbing relations with their customers. Their export prices are, for this reason, likely to fluctuate less than the level of quota premia, and their average quota rents are likely to be less than quota premia when the latter are high.

When quota premia are paid, the price may even be higher than profits at the margin. An established quota holder may, for example, need extra quota to fulfil an order, and might be prepared to pay a good deal for this, in order not to let down his customer. The amount he pays may be greater than that represented by the distance EF, but it is still worth his while to pay this for the sake of the profits on the rest of the order. He would, however, have found it unprofitable to fulfil the order if he had had to buy all the quota he used at a price well above EF. Conversely, quota may be sold at low prices at times when orders are low. The incentive here is the need to get quotas utilised, in order not to lose them in future. The result will be that quota premia at such times may be well below the average level of profits being earned on exports.

There are various pieces of evidence to support the view that quota premia do not necessarily represents the average level of rents earned on exports. One is that there is often a marked change in the quota premium towards the end of the year: this occurs as exporters perceive that they will need some extra quota to fulfil their orders in the current, or alternatively that they have quota to spare. The second is that the proportion of quotas transferred in any year is often a low one, thus supporting the view that marginal quantities only are involved. The third is that quota premia (in the cases where they are included in the export prices) are sometimes high in relation to export prices, and thus would imply low or even negative costs of production if the premia really represented average levels of profits on exports.

Despite such criticism, virtually all commentators (Trela, I. and Whalley, J. 1988 and Silberston, 1984) take these premia to be equal to the surplus profit that can be earned on exports because of quota premium. Hence, if we know the quota

premium, and if we also know the export prices of goods traded under VER, we can calculate the extent and total amount of quota rents earned by an exporting country. Similarly, we would be able to know how far prices are high due to quota rents and how far prices would fall if quotas were abolished. Next section intends to measure the magnitude of quota premia for Pakistan in the EC market for its selective clothing items for 1987 and 1988 years for which the data were available [5].

5.4 Estimation of Pakistan's Quota Premia in the EC Market

Quota premia provides some idea of the rents at present earned by restrained exporters, and hence of the possible reductions in prices that might occur if these restraints were to be eliminated. Pakistan's system of quota allocation is not as much the open system as Hong Kong, Singapore, etc., but trade in quotas is officially permitted there. While there is no official record of the prices at which quota changes hands, the data used in this section are collected from firms exporting clothing articles to the EC member countries i.e., the United Kingdom and West Germany.

The MFA restrictions in the EC apply to some 114 product categories as mentioned earlier. Under the NIMEXE system these are classified into groups according to the degree of sensitivity of the items. For the purpose of calculating the extent of quota rent for Pakistan the most heavily restricted clothing garments comprising Group I forms the sample. This comprises 6109.10.00 T-shirts (Category 4), 6110.20.91 Sweaters (Category 5), 6104.62.10 woven trousers (Category 6), 6106.10.00 woven and knitted blouses (Category 7) and 6109.25.30 shirts (Category 8). These items, however, account for some around 25% of the country's all clothing exports to the EC, while Pakistan's more than 46% exports to the EC fall under the restrictions of the MFA (see Table 4.1).

As in all studies of this type a problem arises with respect to estimating the price raising effects of these quotas. A common response is to rely upon information provided indirectly by transactions in quotas i.e. quota premiums. Relying from quota premiums to ascertain an estimate of the price raising effect of MFA restrictions is not

without difficulty. For example, it has been observed that the value of quota premiums varies from one time of the year to another, and moreover there is a tendency for quota premiums to vary cyclically (Hamilton, 1984). Another objection to their use, raised by Silberston (1984) is that because only a proportion of the total quota is traded at any one time, quota premiums are biased in upward direction. The last point is not a serious objection, in part because the proportion of quota traded is not insubstantial, but, more importantly because in most markets arbitrage occurs at the margin and prices generated by such activity can, and are reasonably interpreted as providing signals regarding relative scarcities. The variability of quota premiums over the year and over the cycle is a more serious issue as we shall see in the case of Pakistan. In response to the former the figure used in the calculation below is an average of the premiums and export prices for clothing garments reported by firms exporting these items over the years 1987 and 1988. These limitations should be kept in mind when analysing results regarding quota premia for Pakistan.

The estimated results of Pakistan's quota premia in the EC market are reported in Table 5.1. It shows that quota premia, in relations to Pakistan's export prices was higher in 1988 (unweighted average 19.91%) than 1987 (unweighted average 18.88.%). This is also true for all categories, except category 7 blouses shirts, exported to the EC between 1987 and 1988. The higher level of quota premia indicates that the EC market for Pakistan's exports was more attractive in 1987 than 1988. However, taking weighted average provides contrast results which is higher (26.24%) in 1988 than (22.41%) in 1987. It should be treated with some cautions. The data reveals the fact that Pakistan's export quota by the EC was increased drastically by 12.5% in 1987. This phenomenon has played an important role in increasing export prices as well as quota premia in 1988. On the other hand, quota was increased only by 4.8% in 1988 [6]. As a result of higher demand for quota export prices and quota premia were increased in 1988. On the basis of above available information, we may conclude that Pakistan's export prices taking average for 1987 and

Table 5.1 PAKISTAN'S QUOTA PREMIA ON CLOTHING EXPORTS TO THE EC

Category	[Pakistani Rupees per garment] Export Prices		Quota Premia		Quota Premia as % of Export Prices	
	1987	1988	1987	1988	1987	1988
4 Tshirts, etc.	86.54	102.51	14.64	14.55	16.92	14.19
5 Sweaters, etc.	176.48	217.42	43.44	48.26	24.61	22.20
6 Woven Trousers	153.23	184.45	31.69	33.56	20.68	18.19
7 Blouses	115.63	144.04	22.07	20.48	19.08	14.22
8 Shirts	97.91	119.11	17.87	30.49	18.25	25.59
Average - unweighted					19.91	18.88
Average-weighted by trade value					22.41	26.24

Source: Export Promotion Bureau (also see, Note.5)

1988 were higher approximately by 20% (according to unweighted average) and by 24% (according to weighted average) due to MFA restrictions.

It should, however, be noted that all the items shown are of the sensitive categories falling within Group I which are subject to the most restrictive rates of growth. Using the second approach to calculate the tariff equivalent of the quotas in place or, in other words, to estimate the tariff level which would have the same (equivalent) restrictive effect. Crude approximations for a number of studies suggest that the protective effects of MFA quotas are at least as important as tariff protection and of course in addition to it (Cable, 1987). Accordingly these figures including tariff and quota premia together for Pakistan were on average 33% (according to unweighted average) and 37% (according to weighted average) in 1987 and 1988, (while 13% tariffs for clothing articles in the EC market are taken into account, TARIC, 1990). Thus the combined effect of the tariff and quota for Pakistan's clothing garments was to raise their prices in the EC market by between 33% to 37%. These figures are close to those estimated by other economists. For example, these figures are equal to 35% estimated by Koekkoek and Mennes (1988, p.205) and 34% by Greenway (1988, p.249) taking both tariff and MFA restriction together for the EC clothing industry.

The record of quota premia in Pakistan show that there are variations in these premia over time. Also at any time, there may be big differences between the levels of premia obtained, in different export markets, for any given category of clothing. The comparative export prices and quota premia figures for Pakistan's clothing garments both in the UK and West Germany for the same categories are shown in Tables 5.2 for the years 1987 and 1988. These results are also comparable with those reported earlier for the EC. It may be seen that the unweighted percentage of quota premia, in relation to Pakistan's export prices, is higher in 1987 than 1988, for both the UK and West Germany as was in the case of the EC. This seems to be true for all categories exported, except category 7 blouses. This category's export prices rose by 27% in the UK and by 22% in the West Germany, while quota

Table 5.2 PAKISTAN'S QUOTA PREMIA ON CLOTHING EXPORTS TO THE UK AND WEST GERMANY

	[Pak Rupees per garment] Export Prices		Quota Premia		Quota Premia as % of Export Prices	
Category	1987	1988	1987	1988	1987	1988
UNITED KINGDOM						
4 Tshirts, etc.	80.72	91.40	12.26	14.18	15.19	15.51
5 Sweaters, etc.	132.66	176.95	33.42	37.92	25.19	21.43
6 Woven Trousers	130.99	154.82	29.00	28.35	22.14	18.31
7 Blouses	113.50	144.12	19.02	18.38	16.75	12.75
8 Shirts	93.85	112.70	16.37	28.07	17.44	24.91
Average - unweighted					19.34	18.58
Average-weighted by trade value					24.35	29.49
WEST GERMANY						
4 Tshirts, etc.	92.37	113.63	17.02	18.90	18.43	16.63
5 Sweaters, etc.	220.30	257.88	53.45	58.60	24.26	22.72
6 Woven Trousers	175.46	214.08	34.38	38.76	19.59	18.11
7 Blouses	117.77	143.96	25.12	22.59	21.33	15.69
8 Shirts	101.98	125.53	19.36	32.90	18.98	26.21
Average - unweighted					20.52	19.87
Average-weighted by trade value					27.92	28.17

Source: Export Promotion Bureau (also see, Note.5)

premia experienced a decline by 3% in the UK and by 10% in the West Germany between 1987 and 1988. The most prominent feature which is visible is that both export prices and quota premia achieved higher growth rates in the UK rather than West Germany between 1987 and 1988.

The above analysis indicates that the average quota premia figures taken an average for 1987 and 1988 are relatively high in the West Germany (20.20% unweighted and 28.05% weighted) rather than the UK (18.96% unweighted and 26.92% weighted). It implies that for Pakistan the West Germany market has been more attractive than the UK. On the other hand the growth rates of export prices and quota premia reveals the contrasting facts. For example, between 1987 and 1988 export prices and quota premia in the UK market rose by 22% and 19%, while in the West German market they were increased by 21% and 22% respectively. The examination of each category also reveals the same facts, reflecting the buoyancy of the two markets in those years.

These differences in the level of quota premia seem likely to be related to differences in the profitability of exporting to the markets concerned. This may come about because similar clothing articles are exported to the UK and West German markets, with higher profits in the Germany, or because higher quality (or more fashionable) goods are exported to West Germany than the UK, with correspondingly higher absolute (and possibly proportional) profit margins. It is not easy to sort out which of these factors have been the more important, a comparison of quota premia with export prices only helps to throw some light on the question.

Keeping this in mind, it makes sense to suggest that Pakistan may have exported higher priced clothing garments to the West Germany than UK, and quota premia were correspondingly higher in the former market. There is a possibility that higher export prices to West Germany reflected higher profit margins rather than higher quality garments, but does not seem plausible in this case. Higher quota premia for Pakistan's exports in the West Germany market were, therefore, almost certainly linked to higher quality exports to that market than the UK. They certainly suggest

that differential profits- in the West Germany market at least- is an important part of the story.

In any event, the figures for the West Germany and UK are consistent. Nor do quota premia in these markets (overall or category-wise) tends to show wide fluctuations. It is important to note that all the figures are partial, since they do not reflect all the trading that takes place. In fact, the quota premia quoted here are for the premia reported by firms located in Lahore. They may differ from those prevailing in other big cities like Karachi, Quetta, etc., but in general they seem to follow the same trend. A more important point is that quota premia represent payments for traded quantities of quota only, and in practice the proportion of quotas traded not unconstrained. Quota premia may, therefore, reflect marginal rather than average quota rents. They are indeed likely to overstate the average level at times of high demand, and understate it when demand is low.

Knowing the total export value under the MFA and the extent of quota premia, we may calculate the total amount of quota rent earned by Pakistan in the EC market, representing by area $EFBP_3$ in Figure 5.1. Pakistan's total exports under the MFA were ECU 208 million in 1987 and ECU 225 million in 1988 as reported in Table 4.1. The estimated quota premia for Pakistan stood at 22.4% and 26.2% (weighted average) in the years 1987 and 1988 respectively (Table 5.1). Based on these figures, the estimated total amount of quota rent accruing to Pakistan in the EC market overall and EC member country-wise is reported in Table 5.3.

Table 5.3 manifests that the total amount of quota rent for Pakistan earned from the EC market amounted ECU 47 million in 1987 and ECU 59 million in 1988, corresponding to area $EFBP_3$ in Figure 5.1. This amount of quota rent is equal to 4.2% and 4.8% of Pakistan's total exports to the EC market in 1987 and 1988 respectively. As mentioned earlier that the EC negotiates quotas under the MFA as a bloc on behalf of member states

Table 5.3 ESTIMATED PAKISTAN'S QUOTA RENT IN THE EC AND EC MEMBER COUNTRY-WISE: 1987-1988

['000' ECU]

Country	1987	1988	Country	1987	1988
West Germany	11860	15060	Spain	3488	4422
United Kingdom	9767	12402	Denmark	1256	1595
France	7674	9745	Greece	698	886
Italy	6279	7973	Portugal	698	886
Benelux	4419	5611	Ireland	372	472
Total Estimated Quota Rent:				46511	59058
Quota rent as % of:					
MFA Exports:				22.4	26.2
Total Exports to EC :				4.2	4.8

Source: Derived from Tables 3.3; 4.2 and 5.1.

which is then distributed among the EC member countries according to a burden sharing formula given in Table 3.3. Applying the same formula, Table 5.3 reports the total amount of quota rent, earned by Pakistan from the EC on the whole and from the each EC member country for the years 1987 and 1988.

The examination of quota premia figures presented in Table 5.3 also bespeaks the relative importance of the EC's member countries' markets for Pakistan. It indicates that there exists rather high concentration of Pakistan's exports on the four EC member countries' markets i.e., West Germany, United Kingdom, France and Italy. Pakistan earned 76.5% of its total quota rent from these four EC member countries in 1987 and 1988 respectively. The West Germany and United Kingdom together accounted for 46.5% of the country's total amount of quota rents in the same years. In other words, aforementioned four EC member countries accounted for 76.5% of Pakistan's total exports, while West Germany and the United Kingdom together accounted for 46.5% of the country's total exports directed to the EC market.

The estimated quota rent figures for Pakistan in the EC market are highly comparable with that of other studies. For example, according to Greenway (1988), estimates of the rents accruing to Hong Kong clothing case to the UK amounted 13% of the value of exports of the restrained commodities. While Hamilton (1985) estimated that total rent income to Hong Kong amounted to 1% of the state's GDP in 1981-82, or 16% of the clothing industry's value added. On the other hand, Wolf (1986) suggested that about 5% of Hong Kong's GDP is accounted for by quota rents created by the MFA restrictions. These figures for India in the USA market estimated by Kumar Rajiv and Ram Khanna (1989) were equivalent to approximately 23% of the total export price. According to our estimates Pakistan's figure is slightly bigger than India which amounts equal to 25% on average taken as a whole for 1987 and 1988. In view of the limited nature of the quota auctions and non availability of data for full range of products for Pakistan and India as well make it difficult to conclude that these relatively high levels of quota rents accrue for Pakistan's exports restricted under the VER/MFA in the EC.

The above discussion makes it clear that developing countries including Pakistan agree to MFA restraints, partly because they fear even tougher unilateral restrictions if they do not and partly they may benefit from the scarcity premia created by the import restraints as we have seen above. Developing countries are thus partially compensated for the loss in market share by greater profits on the sale they are allowed to make. Abolishing or liberalising the MFA will have effects on the economies of both the developed and developing countries. Such effects will be discussed below.

5.5 Effects of MFA Liberalization

As examined earlier, the estimation of the effects of MFA relaxation are usually based on the height of quota premia accruing to an exporting country resulting from the MFA restraints. This argument has already been discussed, where it was

argued that quota premia cannot be taken to be an accurate guide to the average levels of quota rent being earned in Pakistan. It was also pointed out that quota premia in Pakistan vary from month to month, year to year and country to country, depending on the state of demand. Nevertheless, in the absence of precise information, it is assumed that, if the MFA were to be abolished and not replaced with other restrictions, export prices would fall by the extent of the quota premia. This section concentrates on the effects of the MFA relaxation, based on the height of Pakistan's quota premia accruing for its clothing exports in the EC market, for both the developed and developing countries

In Table 5.1 the weighted average of Pakistan's quota premia for selected categories of clothing exports to the EC (as percentage of f.o.b. price) was 22.41% in 1987, and 26.24% in 1988. The average out these two figures- to arrive at a rough 'average' quota premium- gives approximately 24%. If it is assumed that in the EC case the export price has to cover the quota premium, then eliminating the MFA restraints would imply an average fall in export price to the extent of Pakistan's quota premia i.e., 24%.

The figure 24% is almost certainly too high for Pakistan. Both 1987 and 1988 were years of strong demand, as the comparison of quota premia, as proportion of export prices in the years of 1987 and 1988 makes it clear. This is also reflected in the country's significant increase in quota limits for all categories consisting of group I comprising the most sensitive ones. In 1987 they were grown by more than 12.5% on average [6]. Quota premia in these circumstances- as was argued in section 5.4- were higher than the average quota rents being earned on export sales as a whole. In the absence of better information, it is perhaps reasonable to assume that the 1987-1988 quota premia may have been approximately doubled the average level of quota rents on clothing exports to the EC, taking one year with another. Then the average fall in f.o.b. prices, to eliminate such rents, would be 12% in the case of exports to the EC, rather than 24%.

If the Pakistan were the only exporting country concerned, one might

therefore conclude that the ending of the MFA, unaccompanied by other restrictions would lead to an approximately 12% average fall in c.i.f. prices for clothing into the EC market. However, it should be kept in mind that the scope for an average price fall greater than 12% might exist in the case of West Germany, as the figures in Table 5.2 suggest. But the UK is likely to be on the margin, as far as West Germany is concerned, leaving exporters some continued rents to be earned in the market of West Germany.

But Pakistan is not the only country concerned exporting clothing garments to the EC, as is obvious from the previous chapter. There are several other developing countries producing and marketing clothing garments of good quality at the low to medium end of the range, particularly, NIEs, India, China, Turkey, etc. In particular, China, India and Turkey are much more effective competitor and they are likely to be even more competitive in the long run than they are now than the NIEs. In comparison of supply prices of clothing, however, Pakistan stands to be an intermediate country as Table 5.4 manifests.

Table 5.4 AVERAGE SUPPLY PRICES OF QUOTA RESTRICTED TEXTILE AND CLOTHING: 1983-84

	[Relative to US supply Price=1.0]		
Exporting Country	Prices	Exporting Country	Prices
Hong Kong	0.68	Sri Lanka	0.55
Singapore	0.63	Hungary	0.55
Romania	0.60	Mauritius	0.52
Egypt	0.60	Indonesia	0.52
Thailand	0.60	Korea	0.49
Taiwan	0.60	Malaysia	0.47
China	0.55	Bangladesh	0.36
India	0.55	Turkey	0.31
Pakistan	0.55	Brazil	0.31

Source: Trela and Whalley (1989).

It can be seen from Table 5.4 that Pakistan's export supply prices relative to US prices, as reported by Trella and Whalley (1989) after adjusting differences in labour productivity and product quality, have been less than those of many NIEs i.e.

Hong Kong, Singapore and Taiwan, but are in the same range of China and that of India. The examination of the data presented in Table 5.4 provides enough ground to conclude that these countries would be effective competitors of Pakistan in future if MFA is abolished (This issue will be discussed in section 5.7). However, there are many other countries having supply prices less than Pakistan's as Table 5.4 indicates.

In a non-MFA world, therefore, Pakistan's costs may not well represent the lowest costs available to importers in the EC market. In terms of Figure 5.1, the question is, if SS' is the relevant supply curve in a non-MFA world which country would be at the margin, just able to supply profitable at the Price P_4? If this were Pakistan, then Mauritius and Indonesia would probably be intra-marginal suppliers, with lower supply prices. If other supplying countries, still left in the market, having higher supply prices than Pakistan, then he might be at the margin, leaving Pakistan an intra-marginal supplier. In that case a price of P_4 would represent a higher level of costs than that of Pakistan, and P_4 would represent a fall in price below P_3 (the present effective price level for MFA suppliers) of less than 12%. On the other hand, it is conceivable that if Pakistan would not be left in the market, so that a price of P_4 would represent a level of costs below that of Pakistan: in that case price would fall by more than 12% on average.

We cannot know in practice at what level P_4 would settle, in the absence of the MFA. Many changes would have to take place, over a period of some time, before the outcome could become clear. We will make here what is perhaps a not implausible assumption- that Pakistan in the long-run be on the margin. In that case, the assumed average fall in export prices and the consequent fall in import prices of 12% can still held to apply.

A question which has been much disputed is whether, if import prices in the EC and other developed countries as well were to fall by an appreciable amount, would this fall be passed on to consumer? It has been argued, for example, that the level of retail prices in a large country, with a substantial industry of its own, will be determined independently of imports. In this case, a fall in import prices will be

retained by importers, and by others in the supply chain, while not benefiting consumers. The rents formerly earned by the restrained countries would have been passed to importers rather than consumers. This itself is of course a benefit to residents of the importing country, although it would probably be generally felt that public interest would be better served if lower import prices were passed on to consumers, as well as giving benefit to importers, wholesalers and retailers.

But how convincing is the argument that consumers themselves will not benefit from the fall in export prices resulting an end of the MFA? An argument often used is that there are certain 'price points' in the retail trade, and that there are strong pressures for practical reasons for these price points to be maintained. This may be so, but prices generally have been rising for many years, and it has obviously been necessary for the general level of price points to be raised over time. It is difficult not to believe that, at times when prices are increased, some moderating influence would be exercised if import prices were falling in relation to prices of home suppliers. It can be expected that in the EC member countries whose clothing market in particular is dominated by a small number of retailers and mail order houses, due to competition between them, they are unlikely to retain high rents from lower priced imports without passing on some at least of these to consumers.

It has been argued (MacArthur, 1985) that the problem of what would happen to retail prices, in the absence of the MFA, is extremely complex. A fall in the prices of imported yarns and fabrics, for example, would help to reduce clothing prices putting pressure on margins in the clothing industry. A fall in the price of imported standardised clothing might not affect the price of fashionable clothing. Any serious attempt to estimate by how much retail prices might change as a result of removing MFA restraints, it has been said, would have a large margin of error- there is almost certainly no clear and reliable answer to it.

Such a view is undoubtedly correct. Yet it is also surely true that the ending of the MFA, given the conditions of supply in developing countries, is likely to lead to falls in both imported and retail prices. In view of our estimates it seems reasonable to

conclude, in all circumstances, that there might be a 12% fall in land prices from MFA suppliers based on the height of Pakistan's quota premia, and that this might reduce the price level of imported goods in the EC market by 6%. Thus, we may expect that at the retail level, MFA imports might fall in price by also 6%, so that a general fall of 6% in prices might occur, if the MFA were brought to an end.

Whether a similar fall in retail prices would occur in all the EC member countries is a question that is not easy to answer. A fall in landed prices is likely, but the fragmented and diversified structure of the retail trade in some of these countries preserves elements of local monopoly, and blunts the force of price competition. This might prevent price falls at the retail level as great as 6% in all the EC member countries. Nevertheless, a fall in import prices will encourage trade buyers to switch from domestic to imported purchases, and will thus put pressure on domestic textile and clothing manufactures. Further, to say that retail prices in the EC might fall on the average by 6% is not of course to deny that some prices, for specialised products, might not fall at all, or might fall very little. Fashion items, benefiting from quick response on account of relatively short supply chains, are likely to be of this type. On the other hand, there would certainly be occasions when imports came in at very low prices, severely affecting the market of domestic EC manufactures of the same type. It is possible that such imports, if sustained for some time, could make it impossible for the EC competing domestic production to survive at all.

The question of price cannot be separated from that of supply and demand. In the context of Figure 5.1 the elimination of the MFA would lead to a decrease in the foreign supply price from P_2 to P_4 (tariff included) as considered in section 5.3. On the other hand, the quantity imported will increase from T_3 to T_4. However, there are reasons to believe that, given the growth in textile and clothing industries of low-wage countries in recent years, the world supply of these commodities is likely to be highly responsive to price. Given free access, apart from tariffs, to the markets of the EC and other developed countries as well, there is little doubt that large additional exports from the restrained countries would be possible. Nor need the level of costs in

these countries be much above present levels. In time, real wages in low-wage countries would be expected to rise, as has happened in the NIEs and in other developing countries, but the gap between them and the developed countries will remain wide in the foreseeable future.

A shortage of raw materials could push up costs in developing countries, but this would presumably be a worldwide phenomenon, affecting the developing countries and developed countries alike. Also, in so far as supplies from developing countries displaced from developed countries, the net effect on demand might not be great. In any event, the supply of man-made fibres can be expanded without great difficulty in the long-run. The supply of raw cotton can also be expanded, although this may be at the expense of other agricultural production. The supply of wool, with its long gestation period, is the least elastic of all, but this is a fibre less likely than others to be used in large quantities by developing countries. In general, raw materials seem unlikely to be posing serious hurdles on long-run supply on the production and export of textile and clothing world-wide.

Various attempts have been made to estimate the magnitudes involved by stimulating the effects of complete tariff and non-tariff liberalisation on developing countries exports. In one estimate by IMF researchers, imports into the main OECD markets would rise by 82% for textiles and 93% for clothing given the assumption of infinitely elastic supply and if tariffs and quotas were both removed and not replaced by other restrictions (Kirmani, Molajoni, and Mayer, 1984). UNCTAD (1986) estimated that, on the same basis, developing countries' textiles and clothing exports would rise by 78% and 135% respectively. Trela and Whalley (1988) have even higher estimates. Their conclusion is that the effect would be to increase imports of textiles and clothing from developing countries into the USA, Canada and the EC, by 205%, 176%, and 224% respectively. They foresee big welfare gains for developing (and developed) countries, with the gains from improved access more than offsetting (except in the case of Hong Kong and Macao) the losses from rents being earned at present. The export gains for the MFA countries consist of additional exports to the

EC due to an increase in import demand (demand effect), plus additional exports to the EC because of substitution for EC imports from other suppliers, minus the rent losses. According to Koekkoek and Mennes (1986), the export gain accruing to developing countries would amount to US $1-2.5 billion for textiles and $1-2.7 billion for clothing, depending on the assumption regarding the tariff equivalent. Similarly, they concluded that in case the EC would abolish the MFA completely, the present employment in the MFA countries associated with exports of textiles and clothing to the EC, which equals about 1.25 million persons, would increase by some 20-45% due to increased exports to the EC.

All the estimates quoted above exaggerate the effect of ending of the MFA on developed countries, because they assume that all tariffs would go, and that developing countries will not open their markets. They are based also on higher figures for price reduction- derived from using high quota premia as a proxy for rents- than the height of Pakistan's quota premia of 12%. They show, however, that the supply from developing countries is likely to prove highly price-elastic in the long-run. It is worth mentioning that the consumers in the developed countries would be the greatest beneficiaries, enjoying a greatest degree of choice and cheaper prices. In the UK, for example, Silberston (1984) estimated, based on the height of Hong Kong quota premia, a fall in clothing prices ranging between 5% to 10% following the MFA's abolition. In view of our estimates, based on the height of Pakistan's quota premia accruing to its clothing exports in the EC market, a somewhat more than this fall ranging between 6% to 12% can be expected.

What would be the effects on demand, if the MFA were to be brought to an end, and some fall in price were to occur? The price elasticity of demand for clothing (as well as for other textile fibres) is not high. It is often taken to about -0.5 (Silberston, 1984). This implies that a fall in price of, say, 12% would increase the quantity demanded by half as much as this i.e. by 6%. A fall of 6% would increase the quantity demanded by 3%. In the new equilibrium situation the lower level of prices (caused by the changed supply conditions) and the increased level of demand

associated with this would persist, other things being equal. Thus giving a continuing benefit to consumers- a benefit which might be shared with those associated with the chain of distribution.

With the ending of the MFA, there would be in addition the effect of general changes in the structure of the economy at macroeconomic level over time which cannot be ignored. Behind the shelter of the MFA, developed countries have carried out a good deal of rationalisation and investment in textiles and clothing industries. At the same time, there have been technical developments, especially in spinning, weaving and knitting, which have contributed greatly to the increases in productivity that have taken place. Nodoubt that the efficiency of MFA suppliers has increased also. But these developments in the developed countries have reached the point where, especially in the textile industry, automatic processes have become so prevalent that in costs per unit of output they have become much more competitive than before. There have also been developments, using computers, by means of which changes in the design of woven and knitted cloth, and also variations of colour combinations, can be stimulated very quickly. It is now widely held, that, in the absence of subsidies and the like, high-wage countries are becoming increasingly competitive with low wage countries in many branches of spinning, weaving, and fully-fashioned knitting (Cable Vincent and Betsy Baker, 1983).

Keeping the competitiveness of the EC countries in mind it is impossible to assume that a fall in output and employment in textiles and clothing could occur in such a way as to have no offsetting effects on the economy as a whole. These effects would depend partly on the nature of the decline in textile and clothing, and partly on interactions in the economy and the shape of government policy. Silberston (1984), estimated that the macroeconomic effects of a fall of 10% in the import prices of textiles and clothing, and of 5% in home prices, would be to raise the Gross Domestic Product of UK by 1997 by 0.5%, and consumers' expenditures by 0.3%. The balance of payments would improve, since exports would rise more than imports. The overall effect on employment would be a net gain of 61,000, after taking into account the fall

in employment in textile and clothing. There is every reason to believe that such a process is likely to follow in the EC resulting from the end of the MFA.

5.6 Phasing out the MFA

The final objective of the MFA has been restated as a return to GATT rules. But no date has been fixed for the MFA's eventual abolition. The developed countries are only prepared to contemplate abolition of the MFA in exchange for a general liberalisation of world textile and clothing trade involving a better balance of rights and obligations and through the review of GATT rules and codes.

There is clearly much to be said, on general welfare grounds, for the MFA to be brought to an end, from the point of view of both developed and developing countries. It is true that many individual firms in countries subject to restraint, and many trade unions there, are not opposed to the MFA: they prefer the devil they know. But there governments want the freedom to produce and trade, and hence to develop, without distorting restrictions.

In the developed countries also, there seems to be a widespread feeling that it is time for the MFA to go. Some manufactures have long been preparing for it. Trade unions want to see a 'social clause' introduced into any agreement to the end of MFA, in order to improve labour conditions in the developing countries. In addition, the USA has proposed an investigation into the effects of social conditions on competitiveness, and this is now being undertaken. Clearly, there is much to be said for international pressure on low-wage countries to improve their working conditions, and for asking the International Labour Office to see what can be done in this direction. The whole process would necessarily take a long time, however, and could not reasonably be used as an excuse for delaying reform to the MFA.

The question is that if the MFA is to be ended, how should this best be done? In this regard, various proposals and suggestions have been made. One of the most prominent being the MFA quotas should be replaced by 'quota tariffs' put forward by Sampson (1987, pp.455-468). Under this scheme, the MFA as such would be brought

to an end. Importing countries would institute equivalent import quotas, on which the normal tariff would be charged, while very high duties would be levied on imports outside the quota. To begin with, the current bilateral export restraints would be converted to category-specific quotas, but this would be on a non-discriminatory basis. The importing country would then remove each year a set percentage of the quotas and place them in a global pool to be auctioned. Imports into this pool would be at MFN tariff rates. In the course of time only the global pool would be left. Liberalization would be brought about by a gradual reduction for out-of-quota tariffs, until they reached MFN levels, thus bringing import restrictions to an end. The key features of the scheme would be negotiable.

This proposal has much appeal. It moves in the direction of a transparent tariff regime. The auctioning of quotas would allocate them to whoever needed them most, and would also bring revenue for the government of the importing country. However, the scheme is open to a number of objections. Silberston, (1988) argued that it would be particularly objectionable from the developing countries point of view, since it takes away their rents, and substitutes a complicated new system for the widely accepted and understood MFA. It would also involve the 'unbinding' of bound tariffs, and create a potentially dangerous precedent. Other solutions on 'tariffication' lines have their attraction (Baghchi, 1989), but all have problems of the types discussed. Above all, tariffication proposals are subject to the major objection that they would involve a complicated and lengthy international negotiation, which might well take years to complete.

Other suggestions have been made for changes to the MFA, including one from Sir David Alliance, Chairman of Coats Viyella (1989), that the quotas should be given to manufactures in importing countries. This would no doubt help manufactures in these importing countries to plan their sourcing more efficiently, but it is open to the suspicion that quotas might be left unfilled, unless a mechanism were introduced to transfer unused quota. It would antagonise exporting countries, by taking their rents away from them. It would also involve complicated new negotiations.

By for the most obvious solution is to phase out the MFA by stages, over a period of time. The suggestion made by Raffaelli (1989), the Chairman of the Textile Surveillance Body of the MFA, have received widespread approval from exporting countries. His scheme was as follows:

First, terminate on, say, 1 January 1992, each of those restraints whose levels for 1991 represented lass than a (small) percentage of the consumption of each importing country for each product. This percentage should be gradually raised over time. The object would be to free the smaller suppliers from restraint first. Second, after, say, 1 January 1992, only new restraints justifiable under Article 3 (market disruption) should be introduced, and this only for exports taking a sizeable share of consumption in the importing country. The object would be to stop the abuse of Article 4, under which forced bilateral 'agreements' are reached.

Third, no agreement concluded under Article 4 before 1 January 1992 could be renewed or extended, once expired. This is a corollary of the previous step. Article 3 could be used in exceptional circumstances. Fourth, all agreements concluded under article 4 would automatically expire no latter than 31 December 1996. Fifth, from 1 January 1992, no growth rate could be less than 6% a year, or 4% initially in some cases and further growth rates should be increased by steps.

Sixth, a discontinuance after 1 January 1992 of all aggregate and group limits. Seventh, there must be effective surveillance. After a point, further restraints could be introduced only after the consent of the TSB.

On the other hand, Cable Vincent (1987) designed a phased out MFA approach and presented in a much simplified form highlighting those elements which relate to textile and clothing trade. According to his approach, the process of MFA liberalisation must begin with a 'standstill' agreement, to halt further imposition of protective measures. This would reinforce pressures on the MFA signatories not to increase the restrictiveness of quotas further. Phase I would then be designed to restore confidence in the GATT system, through quick resolution (say twelve month) of issues on which the debate is relatively advanced, which are not technically

difficult, or which the outline of common position is already discernible. It is possible to envisage such agreements in the following areas: disputes settlement, surveillance and transparency of all barriers and procedures, tropical products, treatment of least developed countries, and natural resource products. Issues like tariffs and rollback of trade barriers not consistent with the GATT should also be considered. Preparatory work could also be started on such issues as agriculture. But the key to this phase would be the settlement of 'safeguard' issues.

In phase II, negotiation would involve some of the more difficult issues focussing on reintegration of textile trade into the GATT, but including liberalisation of highest tariff items, infringement of intellectual property rights, barrier to agricultural trade, and anti-dumping, countervailing duties, and government procurement

The main purpose of Phase III would be to finalize (or at least make substantial progress in) treatment of the most difficult issues, such as trade-related aspects of investment, intellectual property rights and especially services, and to complete negotiations on those items which have been programmed to cover more than one phase- notably agricultural trade and rollback of barriers. In each case, however, developing country negotiators would have to decide how far to press for further liberalization if the price to be paid was a greater reluctance by industrial countries to negotiate a timetable for phase out of the MFA.

Whether the phasing out of the MFA should go until the year 2000 is a questionable matter. Raffaelli's scheme were designed to see most of the MFA restrictions eliminated by about 1997. However, some progress was made on bringing textile and clothing under the GAT rules. Quotas currently imposed under MFA IV would be notified to a new body to be called the Textile Monitoring Body. These quotas would then be removed in four stages beginning in 1992 under a new Textile Agreement. It was decided that in each stage a certain proportion of textile and clothing products would be removed from quota restraints while items that remained restrained at the end of each stage would be subject to increased quotas. On the other

hand, wide differences remained, however, over the length of the transitional period, the amount of trade which should be liberalised at each stage and over the rate of growth of the remaining quotas. Further, the EC continued to insist that some form of selective safeguard mechanism should be included.

Developing countries have proposed that the transitional period should be for six year, while the EC has pressed for a period of fifteen year. On the trade to be liberalised, two proposals have been made. The developing countries proposed that, on the expiry of the MFA, all quantitative restrictions should be removed on certain products, including textiles made of vegetable fibres, handloom fabrics and children's clothing. Restrictions on the remaining products should be progressively eliminated based on the 'degree of processing' approach, i.e. tops and yarns in Stage I, fibres in Stage II, made ups (e.g. carpets, ropes and canvases) in Stage III, and clothing in Stage IV. An alternative proposal is to retain each importing country to liberalise a specified percentage of its volume of imports at each stage, drawing the products to be integrated from all of the four groups at each stage.

The last, but not least important approach could be one which ensures that growth rates and quotas in bilateral agreements signed under further MFA are sufficiently high that they lose their restrictive effect. Given the fact that both exporting and importing countries now well familiarize with the working of MFA restraints, this option would not introduce any additional uncertainty, over that due to the greater competition for developed country textile and clothing industries which any liberalisation will entail. This option is attractive even if the MFA is phased out, VERs against individual textile and clothing exporters might still be applied. There is legal uncertainty as to whether VERs are, in fact, contrary to the GATT. While they are certainly not authorised by the GATT, most countries seem to take the view that they are not prohibited either. Thus phasing out the MFA would not necessarily mean that bilateral restraints would be ended, unless at the same time this issue were resolved in the negotiating group on safeguards.

What is clear from this discussion is that any scheme for phasing out or

relaxation of the MFA needs to be carefully worked out, and agreed between all the principal parties concerned. At this stage it is extremely difficult to anticipate the shape of any post-MFA agreement. The most plausible mechanism for liberalization would be one which incorporated rising quota increases and sweeping away of controls on the smaller and low-income suppliers. The difficulty facing those wanting an end to the MFA will be to find a transitional agreement which doesnot merely become another MFA; that is, a slightly more liberal version of present arrangements.

5.7 Export Efficiency of Pakistan as compared to its competitors in the EC Market

Having the picture of EC's trade policy regime in mind, we may analyse how does EC trade policies affect the access to market consistent with its trade regime and identify the role of EC's trade policy in causing adverse trends in this regard. It is generally argued that different channels of EC's trade policies affect the access to market by both the privileged and non-privileged developing countries in absolute as well as relative terms. It is the central theme of this section to analyse and provide empirical evidence how far has this discrimination adversely affected Pakistan's export performance in relation to its competitors in the EC market over the period 1988 and 1992?

Tables 5.5 to 5.16 (placed in an appendix at the end of this chapter) summarise the results of export performance of Pakistan with regard to its competitors and different categories of countries, namely the GSP, GMP and Lome in relation to six selected items which figure prominently in Pakistan's exports to the EC market. To this end, six items of Pakistan's major exports identified by Harmonised Commodity Description and Coding System (HS) codes at the eight digit level are selected. The selection criteria used were the importance of the product in the country's exports to the EC market within the eight digit coding system in terms of value in 1991 and items regulated under the bilateral agreement concluded between Pakistan and the EC within the framework of MFA. These selected six items accounted for more than 16%

of Pakistan's total exports to the EC in 1991. The data used in this section is solely obtained from Eurostat published in the form of Microfiches.

The evolution of Pakistan's exports to the EC market clearly show upward trends in all selected items, both in terms of volume and value over the period under review. More importantly, the volume increase was accompanied by an improvement in unit values over the period under review. In comparison, Pakistan's export performance for selected items has been impressive in many aspects within the GSP countries and as opposed to the GMP and Lome countries. This indicates that EC's trade climate has become more favourable for Pakistan over the years, at least for selected items included in our analysis. However, one can observe from the data presented in Tables 5.5 to 5.16 that there exist a rather high percentage concentration in the extra-EC imports from Pakistan in terms of products. The share of the first selected five items in the extra-EC imports of the said items has ranged between 28-48%. The share of sixth selected item is relatively small 4%, while the volume and value are significantly high and represent an impressive improvement both in terms of volume and value over the years.

In the following paragraphs, Pakistan's export performance with regard to the six selected items in relation to its competitors and according to EC's trade regime will be discussed.

Item 6302.21.00 Printed Bed-Linen: The total value of EC's imports in this product was 398 million ECU in 1991 of which over 62% (248 million ECU) were accounted for by extra-EC imports. Table 5.5 indicates the relative importance of GSP, GMP and Lome countries in the extra-EC imports since 1988. It reveals that the trends for EC imports of bed linen show little change in terms of the distribution pattern between the GSP, GMP and Lome countries over the period under study. This is in fact what one would expect to find in this product group which is subject to the relatively stringent monitoring of imports as occurs under the auspices of the MFA.

When classified according to EC's trade regime, it is the GSP countries who dominate the EC market both in terms of value and volume as is evident from Tables

5.5 and 5.6 The GSP beneficiary countries have been providing more than half of total extra-EC imports of bed linen. However, the relative importance of these countries has declined since 1988 when they collectively accounted for 55% of extra-EC imports, a share which had fallen marginally to 54% by 1991. In contrast, countries participating in the Global Mediterranean Policy (GMP) have seen greatest fall in their relative share of exports of bed-linen to the EC market. Their share in extra-EC imports declined from 29% to 23% during the same period, while both the volume and value show steady increase. In contrast, the share of Lome countries in the EC market improved slightly from 1% in 1988 to 2% in 1991. However, imports of bed-lined from Lome countries remained an extremely small proportion of extra-EC imports mainly due to supply constraints as opposed to the GSP and GMP countries.

Table 5.6 evinces the movement of volume, unit values and unit value indices since 1988. From the evolution of the unit values of extra-EC imports of this item one may note that there exist a great difference in the unit values among the countries included in our study. This seems mainly due to difference in the quality of exported item by different countries. The data also indicates that the GSP and Lome countries experienced both an increase in the quantity exported and their unit value between 1988 to 1991 and the latter trend being even more pronounced than the first especially in the recent year. In contrast, the quantity exported by the GMP countries increased, while they experienced a decline in their unit value during the same period.

The changing pattern of growth rates highlights a number of interesting trends. Among the GSP countries in the export of bed-linen of cotton to the EC market Pakistan enjoyed a virtual monopoly in 1988 as is evident from Table 5.5. However, the importance of Pakistan as major supplier of bed-linen to the EC market has declined over the years. Its relative shares both in GSP countries and extra-EC imports has declined from 63% to 51% and 35% to 28% respectively between 1988 and 1991. On the other hand, India having the same terms of access as Pakistan, has been successful in increasing its relative shares from 17% to 24% in GSP countries

and 10% to 13% in extra-EC imports during the same period. This major change was contributed mainly by rapid growth of quantity exported increasing by 138% by volume term (183% by value) from India as opposed to Pakistan which rose only by 45% by volume term (and 66% by value term). Similarly, India also received higher prices for its exports of bed-linen than Pakistan which is clearly evident from Tables 5.6. Other GSP beneficiaries who have been successful in increasing their market shares marginally are Thailand, Indonesia, and Sri Lanka, while there has been no significant change in the relative shares of other GSP countries over the period under review.

It can be observed from Tables 5.5 and 5.6 that over the period under review, in spite of a fall in its market share, Pakistan still is a major supplier of bed-linen to EC accounting for more than half of the extra-EC imports originating from GSP countries and around one third of total EC imports originating from third countries. It may be important to note that a steady increase in volume, value and unit values of bed-lined exports has contributed to this better performance. The indices of Pakistan's export of bed-linen have been well above as opposed to Mediterranean countries. Among the Mediterranean countries, in spite of better terms of access as opposed to GSP countries in the EC market, Turkey faced the greatest fall in its market share. Its share in extra-EC imports fell from 23% in 1988 to 19% in 1991. It is also important to note that in spite of a large increase in the volume and value of Turkey's exports of bed-linen to the EC in 1991, its relative share in extra-EC imports remained more or less stable due to significant drop in its unit values. On the other hand, the evolution of data discloses that Pakistan's export performance has been much smoother and impressive compared with other countries included in our analysis, who enjoyed more favourable terms of access than Pakistan.

Item 5513.11.90 Woven Fabrics (width>165 cm): The value of total EC imports of woven fabrics (of a width >165 CM) stood at 187 million ECU in 1991. Of which 65% (121 million ECU) were originated from outside the EC, while the GSP countries contributed a lion's share of extra-EC imports of this item. Consistently with

the breakdown according to EC trade regime, Tables 5.7 and 5.8 indicate that the beneficiaries of GSP have been an important suppliers of woven fabrics to the EC market and also represent an improvement over the situation. Their relative share in extra-EC imports increased from 87% in 1988 to 92% in 1991. Not surprisingly, the GMP and Lome countries together accounted for a small proportion of extra-EC imports of woven fabrics over the years. In spite of better unit values, their share in the EC market has declined over the years. The general trend is for extra-EC imports of fabrics to increasingly be accounted for by the GSP countries. Growth rates conform this trend. It may be noted, however, that there was a dramatic increase in these growth rates when the growth rates achieved in 1991 are compared to the previous years, especially in the case of GSP and GMP countries as can be seen from the data presented in Table 5.7.

Among the GSP beneficiaries Pakistan appears to be a major supplier and enjoying a virtual monopoly in the export of woven fabrics to the EC market among the GSP countries over the years. The examination of data presented in Table 5.7 exhibits that Pakistan has improved its relative position certainly over the period under review. Its relative market share both in the EC market and GSP countries has increased significantly from 36% to 48% and 42% to 52% respectively. Within this group of countries India and China are to some extent Pakistan's competitors. However, their combined share in extra-EC imports and in the exports of GSP countries to the EC market has been less than half of those of Pakistan.

Table 5.8 displays trends of extra-EC imports of woven fabrics in terms of volume, unit values and unit value indices. From the evolution of unit values and unit value indices of EC imports of this item, one may observe that overall there exist little difference in unit values among countries over the years. However, there exist a slightly declining trend up to 1989, a sudden drop in 1990 and an improvement but smaller in 1991. It is also important to note that all countries experienced more or less the same situation as is concerned with the movement of unit values. It is clear from Table 5.8 that Pakistan has generally had a price advantage over other major

suppliers. The inferior quality of Pakistan's short stapled cotton must be considered in evaluating these differences.

In view of Pakistan's export performance of woven fabrics, it is important to note that in spite of a small amount of TQs of Pakistan given by the EC (630 tonnes in 1991, OJL, No.370 of 31.12.1992), Pakistan has been able to increase its exports far above these limits over the years. The value of this item increased by 107% from 28 million ECUs to 58 million ECUs between 1988 and 1991. The highest growth can be seen in the recent year as compared to the previous years. This increase seems to be a reflection of both an increase in quantities imported and its unit values, the former trend being even more evident than the second one. On the other hand, India was given TCs rather than TQs and better unit values, even so she has not been able to increase its market share, instead its market share declined sharply in the recent years. Similarly, all other GSP countries (except Indonesia whose share increased significantly) which enjoyed the similar terms of access as Pakistan, have experienced a fall in their market shares in the export of woven fabrics to the EC market between 1988 and 1991. In the same manner, the GMP countries, which enjoyed more favourable terms of access without any TQs, TCs and better unit values in the EC market than Pakistan, also experienced a declined in their relative shares in the EC market during the period under study.

Item 5701.10.99 Carpets and Floor Covering: In 1991 total value of EC imports of carpets was 170 million ECU of which over 95% (161 million ECU) were accounted by for imports from outside the EC. This compares with a total value imported in 1988 of 210 million ECU of which 92% were imported from outside the EC. Consequently imports of this product have declined in value terms from all sources and this fall is more pronounced in prices rather than quantity imported.

Examining the distribution pattern of suppliers within the EC's trade regime, Table 5.9 shows that in 1991 more than 93% of extra-EC or 88% of total EC imports of these products were originated in the GSP countries, with a value of 150 million ECU. Pakistan, India and Iran seem to be exclusive suppliers of carpets accounting

for 86% of extra-EC imports and 92% of GSP exports to the EC market in 1991. It can be observed from the data that within the GSP countries, Iran is lagging behind in the export of carpets and loosing its relative market share in the EC. Its relative share of carpet exports declined by a third from 21% in 1988 to 14% in 1991 in the extra-EC imports. Similarly, its share in the export of GSP beneficiary countries declined by just more than a third from 23% to 15% during the same period. In fact with the exception of an improvement in the share of India rising from 25% in 1988 to 37% in 1991 within the GSP countries, there has been virtually no improvement in the relative shares of other GSP countries. Whilst the GMP countries remained considerably small suppliers of carpets to the EC market accounting for 4-5% of extra-EC imports over the years.

Surprising results emerge when carpet imports are examined by growth rates achieved by different countries included in this study. Table 5.9 indicates the movement of growth rates since 1988. What is evident from this table is that there exists an increasing trend up to 1989 and a sudden dramatic drop in the following years. This trend is in line with the trend observed in total EC imports from all sources as mentioned earlier. In these years most of the GSP and GMP countries achieved negative growth rates irrespective to their trade preferences. For example, in 1990 only Morocco achieved positive growth rate, while all GSP and GMP countries experienced a fall in their exports in the EC market. This trend continued in 1991, although somewhat less dramatically. In 1991 India and Nepal achieved significant growth by 12% and 15% respectively as compared to previous year, while all other GSP and GMP countries faced a fall in their export of carpets to the EC market during the same period. Similarly, similar trends are visible when one examines the movement of unit values of carpet imports as Table 5.10 indicates.

Analysis of the growth rates recorded over the period under study in this product's values, quantities and prices on the one hand, and market shares on the other, shows change in relative importance of individual countries. It is important to note that all the GSP countries enjoyed the same status in the export of carpets to the

EC market. Their exports in the EC market were regulated by providing TCs rather than TQs (OJL, No.383 of 30.12.1989 and OJL, No.370 of 31.12.1991). Nevertheless, the emergence of India as significant supplier and to be a major competitor of Pakistan and Iran's lagging behind enjoying similar trade preferences in the export of carpets in the EC market can be considered an important event of time which is clearly evident from Table 5.9.

The general trends noted above are also visible when comparing Pakistan's exports performance in the EC market. Its share in the EC market declined slightly from 37% in 1988 to 35% in 1991. Similar picture emerges when Pakistan's export performance in terms of growth rates is examined. As a matter of fact, the overall picture has been impressive as opposed to many other GSP and GMP countries and a recovery in its relative share is visible in recent years. The EC's trade policy cannot provide a full explanation for this cyclical movement which appeared in extra-EC imports of carpets from different countries. Among the other factors recession prevailing in the EC countries and supply constraints in the supplier countries may be considered responsible for this slow down of EC imports of carpets from all sources.

Item 5513.11.30 Woven Fabrics (width =<165 cm): EC imported woven fabrics (of a width =<165 CM) worth 122 million ECU in 1991. This represented almost 63% (77 million ECU) of all EC imports originated from third countries. When classified according to EC's trade regime, there are the GSP countries who dominate in extra-EC imports of woven fabrics accounting for 94-95% coming from all sources. Neither the GMP countries nor the Lome countries have been important suppliers of this product to the EC. Table 5.11 shows the distribution pattern of suppliers exporting woven fabrics to the EC market over the period under study.

The overall trends for EC's imports of woven fabrics over the period under review show little change in terms of the distribution pattern. This is in fact what one would expect to find in this product group which is subject to the relatively stringent monitoring of imports and the imposition of controls, especially in the form of quotas and variations thereof, as occurs under the auspices of the MFA. The share of GSP

countries in extra-EC imports remained more or less stable between 94-95%. On the other hand, the GMP countries have slightly improved their relative position certainly since the beginning of the period. It is important to note that the GSP countries enjoyed better unit prices for their export of woven fabrics than GMP countries throughout the period under study. Table 5.12 summarises the relationship in changes in the unit values and the quantities imported by the EC from individual countries included in this analysis between 1988 and 1991.

The changing pattern of growth rates outlined in Table 5.11 highlights a number of interesting trends. From the examination of growth rates one can observe that there exists a declining trend over the period 1988-1991 as a whole. This trend seems to be in line with the trend observed in total EC imports originated from outside the EC (EC total import also declined from 171 million ECU in 1988 to 121 million ECU in 1991). As mentioned earlier, factors like recession in the EC countries and supply constraints in the exporting countries seem to be major contributor in this regard.

Table 5.11 also shows that within the GSP countries, Pakistan occupies a place of pride in the export of woven fabrics to the EC market accounting for 37% of extra-EC imports and around 40% of EC imports of woven fabrics imported from GSP countries in 1991. Inspite of stringent control on imports of this product as mentioned earlier, Pakistan has been successful in increasing its market share and exports both in terms of volume and value far beyond the quota limits (630 tonnes in 1991, see OJL No.383 of 31.12.1989 and OJL, No.370 of 31.12.1992) between 1988 and 1991. This increase seems to be a reflection of an increase in the quantities exported as opposed to an increase in its unit values. It is clear from the data presented in Table 5.12 that Pakistan has generally had a price advantage over other suppliers both including the GSP and GMP. However, the inferior quality of Pakistan's short stapled cotton must be considered in evaluating these differences. Within the similar trade treatment, India, Indonesia and Malaysia have also increased their relative shares, while the share of Thailand and Brazil remained more or less

stable during the same period. South Korea, Taiwan, Hong Kong and China, in contrast, experienced a fall in their shares of extra-EC imports over the period under review.

Item 6208.91.10 Women's Dressings of Cotton: The value of total EC imports of Women or Girls' Trousers and Dressings of Cotton stood at 116 million ECU in 1991. Of which around 67% (78 million ECUs) in 1991 were originated out side the EC. Table 5.13 divulges the trends of extra-EC imports of Women and Girls' trousers and Dressings of Cotton consistent with the EC's trade regime. It reveals the fact that the GSP and GMP countries, in contrast with the experience of previous items, are equally significant suppliers of cotton dressings for Women and Girls to the EC market both in terms of value and market shares.

The examination of market share of the GSP and GMP countries since 1988 presents surprising and contrasting results reflecting the changing pattern of growth rates. Table 5.13 betrays the trends of extra-EC imports consistent with its trade regime. It also highlights the performance of individual countries in terms of market shares and growth rates since 1988. It points out that over the years the GSP countries emerged as important suppliers of this product. They accounted for 42% of extra-EC imports in 1991. Their relative importance in the EC market increased significantly since 1988 when these countries accounted for only 33% of extra-EC imports of this item. Previously, the EC market was dominated by the GMP countries. The share of the GMP countries was as high as 65% in 1989, while the share of GSP countries in the extra-EC imports was only 30%. In spite of preferential trade treatment, the GMP countries appeared to be losing ground in the export of women and girls' dressings over the period under review. It seems that the provision of guaranteed shares in the form of tariff quotas or tariff ceilings under the MFA played an important role in this regard. As a result, the share of GSP beneficiary countries in the protected EC market rose dramatically.

Within the GSP countries, Pakistan has emerged an important supplier of dressings for Women and Girls over the yeas and presents an impressive increase in

its market share in the EC market in the export of said item. Its relative share in the import of this item increased from 13% in 1988 to 28% in extra-EC imports in 1991. Similarly, its share in total GSP exports increased from 40% to 67% during the same period. The export value of this item increased by 227% from only 6816 thousand ECU to 22264 thousand ECU between 1988 and 1991. The data presented in Table 5.14 indicates this increase is exclusively attributed to an increase in the quantities exported increasing by 299% between 1988 and 1991 rather than an increase in its unit values. On the whole, Pakistan's exports by volume term have been far above the limits of TCs (71 tonnes in 1988 and 112 tonnes in 1991, OJL, No.383 of 31.12.1989 and OJL, No.370 of 31.12.1992). It also seems that the provisions of TCs rather than TQs by the EC also contributed significantly in increasing its exported quantities to the EC market as TCs are administered liberally than TQs in the case of reimposition of customs duty as discussed in the previous chapter.

Among the GMP countries, Turkey seems to be Pakistan's major competitor and major supplier of Women and Girls' dressings to the EC market. In the same manner as in the case of overall GMP countries, Turkey, inspite of preferential terms of access appeared to be losing ground vis-a-vis Pakistan in the export of Deressing for Women and Girls in the EC market. Similarly, Pakistan's export performance in terms of growth and market share has been smooth and impressive as opposed to many GSP and GMP countries as indicated in Table 5.13. It is important to note that in retaining or expanding a share of world trade, a country must be able to compete effectively on the basis of price. It is evident from Table 5.14 that Pakistan generally had a price advantage over other suppliers. Pakistan's price competitiveness has also played an important in the expansion of Pakistan's market share in the EC market vis-a-vis its competitors.

Item 6203.42.35 Gents Dressings of Cotton: EC's total imports of Men's and Boys' Dressings of cotton from all sources were worth 987 million ECU in 1991. When compared to other above mentioned items, the relative importance of this items in the EC's total imports, originated from outside the EC, is rather less impressive.

This indicates that the EC member countries are equally significant producers and exporters of this item. For example, in 1991 about 52% (worth of 512 million ECU) of EC's total imports were originated from all sources out side the EC, while 48% from intra-EC sources.

In contrast to the experience of above item, in the export of this item three groups i.e., the GSP, GMP and Lome countries appeared to be suppliers consistent with the breakdown according to EC trade regime. Table 5.15 proclaims the status of these group of countries in the export of Men's and Boys' Dressings to the EC market since 1988. Similarly, as in the case of above item, the relative importance of GSP countries as suppliers for this product is low. They provided around 44% of extra-EC imports in 1991. Their relative importance as a supplier of this product represents a decline over the situation since 1988 when these GSP countries accounted for more than 47% of extra-EC imports. In contrast, the GMP countries experienced a rise in their market shares in extra-EC imports from 33% in 1988 to 36% in 1991. A similar rise in the relative importance of the Lome participants is also reflected in the data. Imports from Lome countries, however, over the period under review remained an extremely small proportion of extra-EC imports when compared to the 44% accounted for by countries participating in the EC's GSP scheme and participants of Mediterranean Agreements (GMP) who accounted for 36% of EC imports originated from all sources in 1991.

Within the GSP countries, the emergence of Pakistan as a significant supplier is visible from the data presented in Table 5.15. Although Pakistan's share in the extra-EC imports is relatively small than Hong Kong and China, but presents an increasing trend over the years. It is important to note that the provision of TCs rather than TQs and significant increase in TCs seem to be an important contributor factors in stimulating Pakistan's exports to the EC market (859 tonnes in 1988 and 1750 tonnes in 1991, see OJL, NO.383 of 31.12.1989 and OJL, No.370, of 31.12.1992). Previously, Hong Kong dominated the EC market providing more than half of total exports originated from GSP countries. The emergence of Pakistan and China over

the period under review as significant suppliers to EC market is an important event of time. With their emergence the share of Hong Kong in extra-EC imports declined sharply from 27% in 1988 to 17% in 1991. In contrast, the relative share of Pakistan and China increased steadily during the same period. Pakistan's share increased from only 1.44% in 1988 to 4.12% in 1991. In the similar manner, China's share rose from 3.20% to 4.12% during the same period. For the other GSP countries including Bangladesh, Malaysia and Thailand similar picture emerges who also have been successful in increasing their relative shares in the EC imports during this period. Except Bangladesh, all other countries were provided with TQs rather than TCs. Whilst, having similar trade preferences, Macao, Singapore and South Korea appeared to be losing ground in the export of Men and Boys' Dressings of cotton to the EC market. The trend for EC imports of Men and Boys' Dressings of cotton from the participants of GMP and Lome countries in terms of their market shares and distribution pattern shows little change over the period under study.

The examination of growth pattern of extra-EC imports provides some interesting results and confirms the changing pattern of market shares outlined above. Table 5.15 summarises the trend of growth for extra-EC imports of Men and Boys' Dressings according to its trade regime since 1988. What is evident from this table is that in the case of GSP countries there exists an increasing trend up to 1989, a slight drop in 1990 and a significant improvement in 1991. On the other hand, the GMP and the Lome countries experienced a significant increase in their exports up to 1990 and in 1991 they both faced a sudden drop in their growth rates in the EC market. From the examination of data presented in Tables 5.15 and 5.16 one may note that in spite of better terms of access as mentioned earlier and better unit values, the GMP and Lome countries experienced a severe fall in 1991 in their exports to the EC market. This was solely attributed to a drop in their export prices rather than the quantity exported.

To sum up, the above analysis points out that the pattern of tariff preferences the EC grants does not necessarily guarantee success in the export performance of the

preferred recipients. It transpires that the GSP beneficiary countries, that only benefited from the provisions of the EC's GSP scheme, exhibited strong export performance compared with the ACP and many Mediterranean countries whose exports enjoyed the most advantageous status in the EC market. Within the GSP beneficiary countries Pakistan's exports in the EC market fared well. Inspite of stringent controls imposed under the auspices of the MFA, Pakistan not only has been able to maintain the supply of its MFA exports but its relative market share of the EC market also rose significantly. It's share rose from only 1.9% in 1977 to 3.8% in 1986 and further to 4.7% in 1989 [7]. This evidence lends support to the view that the MFA restrictions have not posed any serious threat to the expansion of Pakistan's exports to the EC market. The observed export pattern points out that although overall Pakistan and many developing countries are in principle competing for similar products in the EC market, the further analysis undoubtedly shows up a greater degree of specialisation at a more disaggregated level indicating that their relative comparative advantage is increasingly residing in different products.

If one contemplates the eventual ending of the MFA, a question of considerable interest is how far different exporting countries, at present under MFA restriction, are likely to fare in a non-MFA world. In particular, how far are those countries, whose textile and clothing industries have been developed partly because of export restrictions on Hong Kong, Korea and Taiwan, likely to survive in such a world?

The answer is that if textile and clothing quotas were to be removed, there would be major disruptive implications between developing country exporters. Such is the degree of regulation at present that it is difficult to say which countries would benefit most from the increased opportunities, and which would experience a loss of market share. The main implications of the phasing out or relaxation of the MFA would be for garment trade, which is larger than textiles and more tightly restrained. The effects of phasing out or relaxation of the MFA on developing countries is difficult to predict; some say that smaller suppliers, whose emergence as clothing

exporters has been stimulated by MFA restrictions, would be able to grow with more confidence- without the disincentive of the risk of the basket extractor being applied to counter attempts to penetrate developed country markets. On the other hand, say others, that NIEs, whose marketing and distribution arrangements are more organised, would rapidly make use of the opportunity and squeeze out the less developed countries, thus preventing them from making any inroads. Further, supplier concentration seems inevitable without the allocation which the MFA provides, however, crudely or unjustifiably. When Norway moved to global quotas, for example, there was a strong shift in the short run to Hong Kong.

Quota rents sap the political will in some NIEs and developing countries. Moreover the existence and expectations of a continuation of quotas affect investment decisions. The quota premia which accrue to exporters because their exports have a scarcity value have been used for diversification and moving up market. This strategy could be seriously put in jeopardy in the event of a free for all with the consequent drop in price levels. The whole structure of world textile production has built up 30 years on the basis of investment and capacity adjustment in the expectation of yet another renegotiation of the MFA. Distortions are inbuilt and incorporate for a world without the MFA. This is no justification for perpetuation but underlines the importance of gradual phasing out or relaxation of the MFA.

Pakistan is a major low income developing country. Pakistan started exporting textile garments earlier than many other countries mentioned above. Pakistan has achieved considerable growth in exports of both textiles and clothing in the 1980s, mainly by improving its utilisation of quotas which is clearly evident from Tables 5.17 and 5.18. The examination of data presented in these tables reveals the fact that quotas are now beginning seriously to bite its textile and clothing exports. Pakistan's clothing manufacturers are upgrading their quality and, partly because of the production of

Table 5.17 AVERAGE QUOTA UTILIZATION RATES FOR MFA SUPPLIERS, IN PRODUCT GROUP I AND II

Country	1978	1983
Pakistan	89.2	102.9
Peru	31.6	102.9
Brazil	72.4	94.3
Hong Kong	101.0	89.8
Macao	90.3	87.1
South Korea	137.1	82.9
Sri Lanka	42.2	80.8
Indonesia	0.0	76.9
Thailand	83.2	68.4
Philippines	82.5	64.1
Singapore	81.1	57.6
Malaysia	84.5	53.5
India	71.2	50.1
Colombia	69.4	42.3
Mexico	22.5	24.8

Source: Koekkoek and Mennes (1986).

Table 5.18 PAKISTAN'S POSITION OF QUOTA UTILIZATION BY BROAD CATEGORIES (GROUP I)

[percentage]

Category	1987	1988	1989	1990
1 Cotton Yarn	99.8	116.1	116.8	113.5
2 Woven cotton fabrics	90.6	98.4	123.8	119.7
4 Shirts & T-shirts,etc.	85.3	97.9	94.3	132.6
5 Jerseys & pulovers,etc.	64.6	60.5	78.6	80.5
8 Men's woven shirts	81.4	90.5	84.1	97.8
9 Woven terry fabrics & toilet linen	106.9	105.5	132.0	128.6
Average:	88.1	94.8	104.9	112.1

Source:Compiled and calculated obtaining data from EC Commission.

garments with a higher import content than traditionally. They are also diversifying their export markets, attracting foreign investment and endeavouring all developments which are appropriate for a country like Pakistan. Quality has been poor in a number of sectors, while productivity is low, and there is shortage of skilled labour. Nevertheless, Pakistan is a low wage country without facing raw material shortages. There is little doubt that if it were free to follow its comparative advantage in textiles and clothing in an unrestricted world Pakistan's prospects would seem to be good. Similarly, Cable Vincent (1989) suggested that China, India and Pakistan are in much the same positions as far as their exports of textile and clothing are concerned. These three low wage countries represent together the strongest economic and political force for opening up the MFA systems.

5.8 Concluding remarks

The MFA has had distorting effects on both the developed and developing countries. Nevertheless, there is a general conclusion that the MFA has not so far been successful in preventing significant growth in market penetration by developing country textile and clothing exporters, although it could be argued that the growth would doubtless have been higher without these controls.

The argument of this chapter has been that, if all MFA were brought to an end, competition between developing countries to increase exports of textile and clothing to developed countries would become intense. Almost certainly, this would lead to a fall in export prices from these countries, and hence in import prices in the EC and developed countries as well. The extent of the fall in export prices has usually been linked by economists to quota premia accruing to developing countries resulting from the MFA restrictions.

The economic benefits for both the developed and developing countries resulting from the MFA's abolition would be considerable. It has been estimated that prices of textile and clothing in the EC would fall by 6% based on the height of quota premia accrue to Pakistan. If the MFA is to go, how best should it be phased out?

Various suggestions have been advanced in this regard. The most sensible course would seem to be a gradually to increase MFA growth rates and flexibility, so that within six to seven years most of the MFA will have withered away. The exact method by which this should be done needs careful thought, and must take account of adjustment problem in both developed and developing countries.

A comparison of Pakistan's export performance at disaggregated level in relation to its competitors indicates that despite stringent controls, the GSP beneficiary countries fared well in the EC market as opposed to the ACP and GMP countries who enjoyed more favourable status. Within the GSP beneficiary countries, Pakistan's export performance has been much smoother and impressive. This evidence proves that the MFA restrictions have not posed any serious threat to the expansion of Pakistan's exports to the EC market. This was mainly due to the emergence of the EC's GSP scheme as a potential policy instrument of resolving Pakistan's trade problems arising out of the MFA constraints. The commodity analysis reveals that Pakistan and many developing countries are thus principally competing for similar markets, although further analysis comparing Pakistan and developing countries undoubtedly showed up a greater degree of specialisation at a more disaggregated level indicating that their relative comparative advantages are increasingly residing in different products.

Notes to Chapter 5

1. In this chapter term MFA will be used so as to act like a single VER. This assumption seems to be reasonable. Many authors have assumed necessary for such type of analysis. See, for example, Wolf, 1983, pp.481-482, Koekkoek and Mennes,1986, pp.220.

2. The EC has MFA bilateral agreements with Argentina, Bangladesh (without quotas), Brazil, China, Colombia, Guatemala, Haiti, Hong Kong, India, Indonesia, South Korea, Macao, Malaysia, Mexico, Pakistan, Peru, Philippines, Singapore, Sri Lanka, Thailand, Uruguay (without quotas). The restrictions on Taiwan contain similar provisions to the MFA bilaterals. Those on Albania, the USSR, North Korea, Vietnam, Mongolia, and East Germany have a small number of quotas: goods otherwise are embargoed or liberalised (For detailed survey see, Anson, 1988, pp.125).

3. Sixteen major MFA suppliers with their shares in 1973 and 1986 respectively are: China 1.7 & 5.3, Taiwan 3.4 & 5.2, Hong Kong 6.5 & 7.6, South Korea 3.6 & 6.7, India 1.9 & 1.8, Pakistan 1.0 & 1.5, Mexico 0.8 & 0.6, Singapore 0.6 & 0.5, Brazil 0.4 & 0.7, Philippines 0.3 & 0.8, Thailand 0.3 & 0.9, Colombia 0.2 & 0.1, Argentina 0.2 & 0.1, Malaysia 0.1 & 0.6, Indonesia 0.0 & 0.6 and Peru 0.0 & 0.1. For further detail see, Anson (1988), p.129.

4. The share of developing countries exports of textiles in the EC market actually show a declining trend. Their share declined form 47.2% in 1973 to 45.6% in 1986. On the other hand, they experience a significant growth in their export of clothing. In clothing their share rose from 64.7% to 72.3% during the same period. For further detail see, Anson and Simpson, pp.175-200).

5. There are no officiall published data for Pakistan's quota premia.The data used for the analysis have been obtained from the Export Promotion Bureau and Ministry of Trade and Commerce compiled for internal use. The author is very grateful to Mr. M. A. Tariq the Labour Officer in providing him with the data.

6. In 1987 Pakistan's exports experienced a significant increase in its quota limits. The growth rates achieved category-wise were as follows. Figures in brackets are of 1986 and 1988: Category I 3%, (0.5% & 2.5%) Category II 7% (0.5% & 2.5%), Category IV 19% (4.0% & 5%), Category V 25% (5.0% & 6%), Category VIII 10.4% (2.0% & 3%) and Category IX 10.2 (5.0% & 6%). For further detail see, Official Journal of the European Communities, No.298 of 26.11.1979 and 245 of 05.09.1987.

7. The data were collected personally from the EC Commission during the author's visit to Brussels in April 1992.

APPENDIX TO CHAPTER 5

Table 5.5 Item 6302.21.00 Printed Bed-Linen of Cotton

(Value= 000 ECU)

Country	1988 Val	1988 GR %	1988 Share%*	1989 Val	1989 GR %	1989 Share%*	1990 Val	1990 GR %	1990 Share%*	1991 Val	1991 GR %	1991 Share%*
Category I:GSP												
Pakistan	41547	-	34.77	43069	3.7	32.91	49154	14.1	29.89	68850	40.1	27.78
India	11534	-	9.65	15290	32.6	11.68	22055	44.2	13.41	32592	47.8	13.15
Thailand	3649	-	3.05	5640	54.6	4.31	6953	23.3	4.23	12601	81.2	5.08
Brazil	4140	-	3.47	3932	-5.0	3.00	4821	22.6	2.93	6552	35.9	2.64
Indoneasia	1276	-	1.07	1122	-12.1	0.86	1571	40.0	0.96	4654	196.2	1.88
Sri Lanka	511	-	0.43	1251	144.8	0.96	2762	120.8	1.68	4640	68.0	1.87
China	1249	-	1.05	1295	3.7	0.99	1540	18.9	0.94	2029	31.8	0.82
Malaysia	64	-	0.05	817	1176.6	0.62	362	-55.7	0.22	1958	440.9	0.79
Hong Kong	1580	-	1.32	654	-58.6	0.50	664	1.5	0.40	594	-10.5	0.24
Total	65550	-	54.86	73070	11.5	55.84	89882	23.0	54.65	134470	49.6	54.26
Category II:GMP												
Turkey	27771	-	23.24	28411	2.3	21.71	31889	12.2	19.39	47325	48.4	19.10
Egypt	697	-	0.58	1580	126.7	1.21	2757	74.5	1.68	5447	97.6	2.20
Israel	4896	-	4.10	2727	-44.3	2.08	2253	-17.4	1.37	3283	45.7	1.32
Tunisia	705	-	0.59	750	6.4	0.57	535	-28.7	0.33	178	-66.7	0.07
Total	34069	-	28.51	33468	-1.8	25.58	37434	11.9	22.76	56233	50.2	22.69
Category II:LOME												
Mauritius	1125	-	0.94	1840	63.6	1.41	3150	71.2	1.92	4698	49.1	1.90
Zimbabwe	266	-	0.22	221	-16.9	0.17	247	11.8	0.15	178	-27.9	0.07
Total	1391	-	1.16	2061	48.2	1.58	3397	64.8	2.07	4876	43.5	1.97

Note: Val=Value and GR= Growth Rate. * Share % in Extra- EC Imports.
Source: Eurostat, External Trade.

Table 5.6 Item 6302.21.00 Printed Bed-Linen of Cotton

(Vol=Tonnes)

Country	1988			1989			1990			1991		
	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI
Category I:GSP												
Pakistan	8275	5.02	100	8538	5.04	100.47	9712	5.06	100.80	11965	5.75	114.61
India	2191	5.26	100	2743	5.57	105.89	3993	5.52	104.92	5225	6.24	118.49
Thailand	681	5.36	100	1065	5.30	98.83	1541	4.51	84.21	2581	4.88	91.12
Brazil	585	7.08	100	537	7.32	103.47	676	7.13	100.77	889	7.37	104.14
Indoneasia	177	7.21	100	137	8.19	113.60	224	7.01	97.29	751	6.20	85.96
Sri Lanka	106	4.82	100	272	4.60	95.41	617	4.48	92.86	958	4.84	100.47
China	172	7.26	100	173	7.49	103.08	177	8.70	119.82	183	11.09	152.69
Malaysia	9	7.11	100	132	6.19	87.04	84	4.31	60.60	397	4.93	69.36
Hong Kong	267	5.92	100	99	6.61	111.63	109	6.09	102.94	77	7.71	130.36
Total	12463	5.02	100	13696	5.34	106.26	17133	5.25	104.49	23026	5.84	116.31
Category II:GMP												
Turkey	3944	7.04	100	4504	6.31	89.58	4862	6.56	93.15	7307	6.48	91.98
Egypt	164	4.25	100	404	3.91	92.02	660	4.18	98.29	1143	4.77	112.13
Israel	583	8.40	100	272	10.03	119.38	203	11.10	132.16	304	10.80	128.60
Tunisia	84	8.39	100	75	10.00	119.15	57	9.39	111.83	16	11.13	132.55
Total	4775	7.13	100	5255	6.37	89.26	5782	6.47	90.74	8770	6.41	89.87
Category II:LOME												
Mauritius	199	5.65	100	346	5.32	94.07	532	5.92	104.74	721	6.52	115.26
Zimbabwe	92	2.89	100	70	3.16	109.19	50	4.94	170.86	33	5.39	186.56
Total	291	4.78	100	416	4.95	103.65	582	5.84	122.11	754	6.47	135.29

Note: Vol=Volume, UV=Unit Value and UVI=Unit Value Indices.
Source: Eurostat, External Trade.

Table 5.7 Item 5513.11.90 Woven Fabrics mixed with Cotton (width >165 CM).

(Value= 000 ECU)

	1988			1989			1990			1991		
Country	Val	GR %	Share%*	Val	GR %	Share%*	Val	GR %	Share%*	Val	GR %	Share%*
Category I:GSP												
Pakistan	28312	-	36.44	26348	-6.9	34.45	31223	18.5	38.01	58154	86.3	47.94
India	6929	-	8.92	9170	32.3	11.99	12541	36.8	15.27	15651	24.8	12.90
China	7908	-	10.18	6946	-12.2	9.08	8958	29.0	10.91	12884	43.8	10.62
Taiwan**	14476	-	18.63	10626	-26.6	13.89	10099	-5.0	12.30	8800	-12.9	7.25
Indoneasia	1721	-	2.29	1493	-16.2	1.95	3342	123.8	4.07	8305	148.5	6.85
South Korea	3873	-	4.98	6203	60.2	8.11	5332	-14.0	6.49	4500	-15.6	3.71
Thailand	408	-	0.53	1393	241.4	1.82	2784	99.9	3.39	2460	-11.6	2.03
Brazil	1650	-	2.12	2006	21.6	2.62	679	-66.2	0.83	496	-27.0	0.41
Hong Kong	2401	-	3.09	1813	-24.5	2.37	531	-70.7	0.65	225	-57.6	0.19
Malaysia	54	-	0.07	67	24.1	0.09	167	149.3	0.20	171	2.4	0.14
Total	67792	-	87.25	66065	-2.5	86.39	75656	14.5	92.11	111646	47.6	92.03
Category II:GMP												
Egypt	59	-	0.08	128	116.9	0.17	809	532.0	0.98	2816	248.1	2.32
Turkey	1942	-	2.50	4157	114.1	5.44	55	-98.7	0.07	1018	1750.9	0.84
Morocco	133	-	0.17	-	-100.0	0.00	110	ERR	0.13	484	340.0	0.40
Israel	2392	-	3.08	1028	-57.0	1.34	624	-39.3	0.76	291	-53.4	0.24
Total	4526	-	5.83	5313	17.4	6.95	1598	-69.9	1.95	4609	188.4	3.80
Category III:LOME												
Zimbabwe	1398	-	1.80	694	-50.4	0.91	1139	64.1	1.39	1070	-6.1	0.88

Note:Val=Value and GR= Growth Rate. * Share % in Extra- EC Imports.** Not a GSP beneficiary.
Source: Eurostat, External Trade.

Table 5.8 Item 5513.11.90 Woven Fabrics mixed with Cotton (width >165 CM).

(Vol=Tonnes)

	1988			1989			1990			1991		
Country	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI
Category I:GSP												
Pakistan	7418	3.82	100	7009	3.76	98.49	9832	3.18	83.20	17880	3.25	85.22
India	1759	3.94	100	2414	3.80	96.43	3715	3.38	85.70	4614	3.39	86.11
China	2106	3.75	100	1834	3.79	100.86	2890	3.10	82.55	4044	3.19	84.85
Taiwan*	3247	4.46	100	2604	4.08	91.53	2712	3.72	83.53	2205	3.99	89.52
Indoneasia	422	4.22	100	404	3.70	87.56	940	3.56	84.24	2264	3.67	86.92
South Korea	841	4.61	100	1452	4.27	92.76	1313	4.06	88.18	1064	4.23	91.84
Thailand	100	4.08	100	349	3.99	97.83	737	3.78	92.59	670	3.67	89.99
Brazil	431	3.83	100	528	3.80	99.24	190	3.57	93.35	169	2.93	76.66
Hong Kong	536	4.48	100	449	4.04	90.14	132	4.02	89.80	56	4.02	89.69
Malaysia	11	4.91	100	11	6.09	124.07	29	5.76	117.31	31	5.52	112.37
Total	16871	4.02	100	17054	3.87	96.41	22490	3.36	83.72	32997	3.38	84.20
Category II:GMP												
Egypt	20	2.95	100	38	3.37	114.18	220	3.68	124.65	694	4.06	137.55
Turkey	524	3.71	100	1208	3.44	92.85	16	3.44	92.75	278	3.66	98.81
Morocco	27	4.93	100	-	-	-	24	4.58	93.05	121	4.00	81.20
Israel	495	4.83	100	211	4.87	100.82	152	4.11	84.95	57	5.11	105.65
Total	1066	4.25	100	1457	3.65	85.89	412	3.88	91.35	1150	4.01	94.40
Category III:LOME												
Zimbabwe	344	4.06	100	175	3.97	97.58	305	3.73	91.89	239	4.48	110.16

Note: Vol=Volume, UV=Unit Value and UVI=Unit Value Indices. * Not a GSP beneficiary.
Source: Eurostat, External Trade.

Table 5.9 Item 5701.10.99 Carpets (500 knotts/m).

(Value= 000 ECU)

	1988			1989			1990			1991		
Country	Val	GR %	Share%*	Val	GR %	Share%*	Val	GR %	Share%*	Val	GR %	Share%*
Category I:GSP												
Pakistan	71548	-	37.03	71055	-0.7	34.49	58065	-18.3	33.93	56763	-2.2	35.28
India	48631	-	25.17	55780	14.7	27.08	52386	-6.1	30.61	58735	12.1	36.50
Iran	41067	-	21.25	39503	-3.8	19.18	29205	-26.1	17.07	22790	-22.0	14.16
China	14573	-	7.54	18649	28.0	9.05	14665	-21.4	8.57	10504	-28.4	6.53
Nepal	407	-	0.21	916	125.1	0.44	868	-5.2	0.51	999	15.1	0.62
Total	176226	-	91.20	185903	5.5	90.24	155189	-16.5	90.68	149791	-3.5	93.09
Category II:GHP												
Turkey	5438	-	2.81	8622	58.6	4.19	7265	-15.7	4.25	5285	-27.3	3.28
Morocco	889	-	0.46	772	-13.2	0.37	1382	79.0	0.81	1159	-16.1	0.72
Tunisia	974	-	0.50	1011	3.8	0.49	870	-13.9	0.51	682	-21.6	0.42
Total	7301	-	3.78	10405	42.5	5.05	9517	-8.5	5.56	7126	-25.1	4.43

Note: Val=Value and GR= Growth Rate. * Share % in Extra- EC Imports.
Source: Eurostat, External Trade.

Table 5.10 Item 5701.10.99 Carpets (500 knotts/m).

(Vol=Tonnes)

Country	1988			1989			1990			1991		
	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI
Category I:GSP												
Pakistan	2551	28.05	100	2773	25.62	91.36	2766	20.99	74.85	2690	21.10	75.24
India	2443	19.91	100	2391	23.33	117.20	2498	20.97	105.35	3353	17.52	88.00
Iran	633	64.88	100	450	87.78	135.31	377	77.47	119.41	365	62.44	96.24
China	427	34.13	100	480	38.85	113.84	486	30.17	88.41	362	29.02	85.02
Nepal	27	15.07	100	50	18.32	121.53	48	18.08	119.96	8	124.88	828.41
Total	6081	28.98	100	6144	30.26	104.41	6175	25.13	86.72	6778	22.10	76.26
Category II:GMP												
Turkey	111	48.99	100	126	68.43	139.68	153	47.48	96.92	153	34.54	70.51
Morocco	118	7.53	100	108	7.15	94.88	209	6.61	87.77	167	6.94	92.12
Tunisia	13	74.92	100	13	77.77	103.80	11	79.09	105.56	4	170.50	227.57
Total	242	30.17	100	247	42.13	139.63	373	25.51	84.57	324	21.99	72.90

Note: Vol=Volume, UV=Unit Value and UVI=Unit Value Indices.
Source: Eurostat, External Trade.

Table 5.11 Item 5513.11.30 Woven Fabrics mixed with Cotton (width =<165 CM).

(Value= 000 ECU)

Country	1988 Val	1988 GR %	1988 Share%*	1989 Val	1989 GR %	1989 Share%*	1990 Val	1990 GR %	1990 Share%*	1991 Val	1991 GR %	1991 Share%*
Category I:GSP												
Pakistan	26022	-	32.42	20598	-20.8	28.45	33811	64.1	36.20	28462	-15.8	37.15
Thailand	12830	-	15.99	15188	18.4	20.98	12465	-17.9	13.34	12430	-0.3	16.23
Indoneasia	4221	-	5.26	5891	39.6	8.14	10921	85.4	11.69	10165	-6.9	13.27
Malaysia	2956	-	3.68	4613	56.1	6.37	5159	11.8	5.52	6704	29.9	8.75
India	2043	-	2.55	2188	7.1	3.02	6400	192.5	6.85	4801	-25.0	6.27
South Korea	13887	-	17.30	11706	-15.7	16.17	9257	-20.9	9.91	4688	-49.4	6.12
Taiwan**	10912	-	13.60	4745	-56.5	6.55	5970	25.8	6.39	2647	-55.7	3.46
China	1726	-	2.15	2923	69.4	4.04	4690	60.5	5.02	1329	-71.7	1.73
Brazil	771	-	0.96	446	-42.2	0.62	376	-15.7	0.40	681	81.1	0.89
Hong Kong	1055	-	1.31	374	-64.5	0.52	346	-7.5	0.37	608	75.7	0.79
Total	76423	-	95.22	68672	-10.1	94.85	89395	30.2	95.70	72239	-19.2	94.30
Cayegory II:GMP												
Egypt	60	-	0.07	99	65.0	0.14	225	127.3	0.24	920	308.9	1.20
Morocco	118	-	0.15	117	-0.8	0.16	179	53.0	0.19	112	-37.4	0.15
Israel	1055	-	1.31	374	-64.5	0.52	346	-7.5	0.37	332	-4.0	0.43
Turkey	112	-	0.14	120	7.1	0.17	144	20.0	0.15	61	-57.6	0.08
Total	1345	-	1.68	710	-47.2	0.98	894	25.9	0.96	1425	59.4	1.86

Note: Val=Value and GR= Growth Rate. * Share % in Extra- EC Imports.** Not a GSP beneficiary.
Source: Eurostat, External Trade.

Table 5.12 Item 5513.11.30 Woven Fabrics mixed with Cotton (width =<165 CM).

(Vol=Tonnes)

	1988			1989			1990			1991		
Country	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI
Category I:GSP												
Pakistan	8592	3.03	100	6653	3.10	102.23	11858	2.85	94.15	9912	2.87	94.81
Thailand	2781	4.61	100	3442	4.41	95.65	2986	4.17	90.49	3286	3.78	81.99
Indoneasia	968	4.36	100	1301	4.53	103.84	2600	4.20	96.33	2464	4.13	94.61
Malaysia	641	4.61	100	932	4.95	107.33	1016	5.08	110.11	1466	4.57	99.16
India	497	4.11	100	566	3.87	94.04	1675	3.82	92.95	1302	3.69	89.70
South Korea	2806	4.95	100	2474	4.73	95.61	2040	4.54	91.69	1177	3.98	80.48
Taiwan*	2284	4.78	100	976	4.86	101.76	1354	4.41	92.29	647	4.09	85.63
China	385	4.48	100	635	4.60	102.68	1103	4.25	94.85	323	4.11	91.78
Brazil	167	4.62	100	113	3.95	85.49	96	3.92	84.84	197	3.46	74.88
Hong Kong	226	4.67	100	87	4.30	92.09	73	4.74	101.53	150	4.05	47.41
Total	19347	3.95	100	17179	4.00	101.20	24801	3.60	91.25	20924	3.45	87.40
Cayegory II:GMP												
Egypt	20	3.00	100	26	3.81	126.92	67	3.36	111.94	255	3.61	120.26
Morocco	24	4.92	100	18	6.50	132.20	31	5.77	117.44	22	5.09	103.54
Israel	151	4.44	100	162	3.77	84.86	104	4.25	95.78	23	4.61	103.87
Turkey	23	4.87	100	16	7.50	154.02	27	5.33	109.52	16	3.81	78.29
Total	218	4.40	100	222	4.26	96.77	229	4.32	98.17	316	3.79	86.16

Note: Vol=Volume, UV=Unit Value and UVI=Unit Value Indices. * Not a GSP beneficiary.
Source: Eurostat, External Trade.

Table 5.13 Item 6208.91.10 Women or Girls' Dressing of Cotton.

(Value= 000 ECU)

	1988			1989			1990			1991		
Country	Val	GR %	Share%*	Val	GR %	Share%*	Val	GR %	Share%*	Val	GR %	Share%*
Category I:GSP												
Pakistan	6816	-	13.44	7652	12.3	13.66	14588	90.6	22.59	22264	52.6	28.49
Brazil	6126	-	12.08	5628	-8.1	10.04	5395	-4.1	8.36	5990	11.0	7.66
China	2733	-	5.39	2138	-21.8	3.82	1091	-49.0	1.69	2880	164.0	3.69
India	347	-	0.68	401	15.6	0.72	426	6.2	0.66	660	54.9	0.84
Hong Kong	572	-	1.13	521	-8.9	0.93	551	5.8	0.85	628	14.0	0.80
Sri Lanka	71	-	0.14	154	116.9	0.27	112	-27.3	0.17	486	333.9	0.62
Indoneasia	31	-	0.06	79	154.8	0.14	100	26.6	0.15	130	30.0	0.17
Thailand	70	-	0.14	61	-12.9	0.11	66	8.2	0.10	60	-9.1	0.08
Philipines	135	-	0.27	55	-59.3	0.10	83	50.9	0.13	35	-57.8	0.04
Total	16901	-	33.32	16689	-1.3	29.78	22412	34.3	34.71	33133	47.8	42.40
Category II:GMP												
Turkey	25093	-	49.47	27872	11.1	49.74	27967	0.3	43.32	32102	14.8	41.08
Egypt	261	-	0.51	382	46.4	0.68	971	154.2	1.50	626	-35.5	0.80
Morocco	195	-	0.38	230	17.9	0.41	376	63.5	0.58	377	0.3	0.48
Israel	233	-	0.46	7652	3184.1	13.66	71	-99.1	0.11	102	43.7	0.13
Total	25782	-	50.83	36136	40.2	64.49	29385	-18.7	45.51	33207	13.0	42.49

Note: Val=Value and GR= Growth Rate. * Share % in Extra- EC Imports.
Source: Eurostat, External Trade.

Table 5.14 Item 6208.91.10 Women or Girls' Dressing s of Cotton

(Vol=Tonnes)

Country	1988			1989			1990			1991		
	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI
Category I:GSP												
Pakistan	1155	5.90	100	1378	5.55	94.10	2935	4.97	84.22	4612	4.83	81.80
Brazil	506	12.11	100	449	12.53	103.53	433	12.46	102.91	469	12.77	105.49
China	393	6.95	100	291	7.35	105.65	163	6.69	96.25	245	11.76	169.04
India	29	11.97	100	31	12.94	108.11	44	9.68	80.91	43	15.35	128.28
Hong Kong	36	15.89	100	32	16.28	102.47	34	16.21	102.00	40	15.70	98.81
Sri Lanka	4	17.75	100	13	11.85	66.74	8	14.00	78.87	27	18.00	101.41
Indoneasia	3	10.33	100	6	13.17	127.42	13	7.69	74.44	10	13.00	125.81
Thailand	3	23.33	100	3	20.33	87.14	3	22.00	94.29	5	12.00	51.43
Philipines	4	33.75	100	1	55.00	162.96	2	41.50	122.96	1	35.00	103.70
Total	2133	7.92	100	2204	7.57	95.56	3635	6.17	77.81	5452	6.08	76.70
Category II:GMP												
Turkey	3125	8.03	100	3108	8.97	111.68	3036	9.21	114.72	3339	9.61	119.73
Egypt	43	6.07	100	54	7.07	116.55	132	7.36	121.19	83	7.54	124.26
Morocco	14	13.93	100	15	15.33	110.09	22	17.09	122.70	17	22.18	159.22
Israel	6	38.83	100	1378	5.55	14.30	3	23.67	60.94	4	25.50	65.67
Total	3188	8.09	100	4555	7.93	98.10	3193	9.20	113.80	3443	9.64	119.26

Note: Vol=Volume, UV=Unit Value and UVI=Unit Value Indices.
Source: Eurostat, External Trade.

Table 5.15 Item 6203.42.35 Men's or Boys' Dressings of Cotton.

(Value= 000 ECU)

	1988			1989			1990			1991		
Country	Val	GR %	Share%*	Val	GR %	Share%*	Val	GR %	Share%*	Val	GR %	Share%*
Category I:GSP												
Hong Kong	110815	-	26.76	98741	-10.9	21.86	85763	-13.1	17.18	85018	-0.9	16.59
China	13247	-	3.20	22181	67.4	4.91	35726	61.1	7.16	36174	1.3	7.06
Pakistan	5945	-	1.44	6759	13.7	1.50	9373	38.7	1.88	21099	125.1	4.12
Macao	18308	-	4.42	19992	9.2	4.43	18880	-5.6	3.78	17367	-8.0	3.39
Singapore	14622	-	3.53	14090	-3.6	3.12	10517	-25.4	2.11	13474	28.1	2.63
Malaysia	6090	-	1.47	7191	18.1	1.59	5991	-16.7	1.20	8549	42.7	1.67
South Korea	9199	-	2.22	8363	-9.1	1.85	6343	-24.2	1.27	8433	32.9	1.65
Bangladesh	1567	-	0.38	2975	89.9	0.66	4997	68.0	1.00	7732	54.7	1.51
Thailand	2576	-	0.62	5568	116.1	1.23	5758	3.4	1.15	6833	18.7	1.33
Philipines	4727	-	1.14	5732	21.3	1.27	5484	-4.3	1.10	6733	22.8	1.31
Sri Lanka	3057	-	0.74	3359	9.9	0.74	2765	-17.7	0.55	4519	63.4	0.88
Indoneasia	2253	-	0.54	5663	151.4	1.25	6084	7.4	1.22	4390	-27.8	0.86
India	3332	-	0.80	3009	-9.7	0.67	3457	14.9	0.69	3033	-12.3	0.59
Total	195738	-	47.27	203623	4.0	45.09	201138	-1.2	40.29	223354	11.0	43.59
Category II:GMP												
Tunisia	56946	-	13.75	62468	9.7	13.83	69890	11.9	14.00	70698	1.2	13.80
Morocco	45932	-	11.09	50025	8.9	11.08	69434	38.8	13.91	65699	-5.4	12.82
Turkey	30809	-	7.44	41639	35.2	9.22	44077	5.9	8.83	39280	-10.9	7.67
Egypt	1136	-	0.27	869	-23.5	0.19	2147	147.1	0.43	4172	94.3	0.81
Cyprus	3238	-	0.78	3443	6.3	0.76	3450	0.2	0.69	2919	-15.4	0.57
Total	138061	-	33.34	158444	14.8	35.08	188998	19.3	37.86	182768	-3.3	35.67
Category III:LOME												
Mauritius	6320	-	1.53	7829	23.9	1.73	8668	10.7	1.74	8000	-7.7	1.56
Zimbabwe	1478	-	0.36	2090	41.4	0.46	4131	97.7	0.83	3936	-4.7	0.77
Total	7798	-	1.88	9919	27.2	2.20	12799	29.0	2.56	11936	-6.7	2.33

Note: Val=Value and GR= Growth Rate. * Share % in Extra- EC Imports.
Source: Eurostat, External Trade.

Table 5.16 · Item 6203.42.35 Men's or Boys' Dressings of Cotton.

(Vol=Tonnes)

Country	1988			1989			1990			1991		
	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI
Category I:GSP												
Hong Kong	7637	14.51	100	6683	14.77	101.82	6251	13.72	94.55	6093	13.95	96.16
China	1404	9.44	100	2056	10.79	114.34	3217	11.11	117.70	3088	11.71	124.16
Pakistan	596	9.97	100	645	10.48	105.06	894	10.48	105.11	1857	11.36	113.91
Macao	1466	12.49	100	1528	13.08	104.77	1537	12.28	98.36	1293	13.43	107.55
Singapore	1048	13.95	100	993	14.19	101.70	782	13.45	96.39	973	13.85	99.25
Malaysia	455	13.38	100	510	14.10	105.34	435	13.77	102.90	624	13.70	102.36
South Korea	581	15.83	100	443	18.88	119.23	332	19.11	120.67	568	14.85	93.77
Bangladesh	127	12.34	100	268	11.10	89.97	445	11.23	91.01	771	10.03	81.28
Thailand	184	14.00	100	397	14.03	100.18	469	12.28	87.69	506	13.50	96.46
Philipines	431	10.97	100	467	12.27	111.91	514	10.67	97.28	641	10.50	95.77
Sri Lanka	277	11.04	100	282	11.91	107.93	244	11.33	102.68	411	11.00	99.63
Indoneasia	272	8.28	100	520	10.89	131.48	554	10.98	132.58	419	10.48	126.49
India	213	15.64	100	175	17.19	109.92	195	17.73	113.33	178	17.04	108.92
Total	14691	13.32	100	14967	13.60	102.11	15869	12.67	95.13	17422	12.82	96.22
Category II:GMP												
Tunsia	3202	17.78	100	3854	16.21	91.14	4179	16.72	94.04	4424	15.98	89.86
Morocco	3275	14.03	100	3782	13.23	94.31	5221	13.30	94.82	5328	12.33	87.92
Turkey	1776	17.35	100	2457	16.95	97.69	2416	18.24	105.17	2108	18.63	107.42
Egypt	109	10.42	100	74	11.74	112.68	179	11.99	115.09	317	13.16	126.28
Cyprus	195	16.61	100	194	17.75	106.88	221	15.61	94.01	213	13.70	82.53
Total	8557	16.13	100	10361	15.29	94.78	12216	15.47	95.89	12390	14.75	91.43
Category III:LOME												
Mauritius	363	17.41	100	432	18.12	104.09	450	19.26	110.64	505	15.84	90.99
Zimbabwe	117	12.63	100	239	8.74	69.22	400	10.33	81.75	409	9.62	76.18
Total	480	16.25	100	671	14.78	90.99	850	15.06	92.69	914	13.06	80.38

Note: Vol=Volume, UV=Unit Value and UVI=Unit Value Indices.
Source: Eurostat, External Trade.

CHAPTER 6

AN EMPIRICAL INVESTIGATION OF TRADE IMPLICATIONS OF THE EUROPEAN COMMUNITY'S SECOND ENLARGEMENT FOR PAKISTAN

With a share of some 40 percent of the world trade in 1990, the European Community is not only the biggest trading bloc of the world, it is also by far the largest trading partner of many developing countries including Pakistan. Almost one third of Pakistan's exports is to the EC countries which makes it, as a bloc, the most important trade partner to Pakistan.

The enlargement of the EC to include Greece, Portugal and Spain has, therefore, raised doubts about the future of Pakistan's exports to the EC market, especially textile and clothing, as these new members are significant producers and exporters of these articles and some other commodities which are exported by Pakistan.

The aim of this chapter is straightforward. It examines the possible implications of the EC's enlargement for Pakistan and investigates if the new members have posed a threat to Pakistan's exports to EC market. First and foremost one must examine the possible implications of the Enlargement for Member and non-member countries and draw an exact picture of the institutional links between Pakistan, the European Community and its new member countries both before and after the

Enlargement. This would allow further analysis to compare the two situations and predict the direct possible trade effects of the Enlargement for Pakistan derived from these changes in the institutional setting. This in turn would allow for a quantitative evaluation of trade implications for Pakistan's exports in the enlarged EC market. Accordingly, section 6.1 appraises the theoretical aspects of customs union and its possible trade implications for member and non-member countries, while section 6.2 examines pre and post-enlargement institutional arrangements and their possible effects on trade flows between the countries concerned. Sections 6.3 embarks on

empirical investigation of such implications for Pakistan in the enlarged EC and in the New EC Members as well. As a way of conclusion present and future prospects of Pakistan's trade flows with the enlarged EC are reviewed and evaluated in section 6.4.

6.1 Theoretical Considerations: Effects of Enlargement

For a long time it was simply taken for granted that the formation of a customs union would increase the welfare of its members. Free trade was seen as the optimum form of trade, so that any movement towards free trade would be a movement towards greater welfare. This belief was somewhat shaken when Viner (1950) argued that a customs union with its discriminatory tariff changes represents both a move towards free trade and a move towards potentially greater protectionism through the common external trade policy. This leads to two separate effects: 'trade creation' and 'trade diversion'. The former improves the international allocation of resources and increases welfare while the latter has the opposite effects. Whether the customs union, on balance, will increase or decrease welfare for its members, therefore, depends on the net effect of trade creation and trade diversion.

As a consequence of abolishing tariffs resulting from the formation or enlargement of customs union, the home expensive products are replaced by similar low cost products within the customs union. This is the case of trade creation- the positive trade and welfare effect of customs union formation. It consists of a production effect, in that production of a quantity of products switched from inefficient sources to more efficient sources within the customs union thereby saving resources. This change towards a more rational pattern of international specialisation improves the allocation of resources since products are produced within the customs union more efficiently. In addition, it will also have a positive welfare effect as a result of an increase in consumer surplus.

Trade diversion, on the other hand, occurs when the tariff changes that follow the creation of a customs union result in price changing in such a way as to lead

members to buy goods and services produced relatively less efficiently in partner countries in place of those produced more efficiently and cheaply in non-member countries. In this instance, the source of imports is shifted from a more efficient source outside the customs union to a less efficient one within the customs union. This would be the case of trade diversion- the negative trade and welfare effect of a customs union formation.

To the extent that a customs union frees trade within the bloc and causes a reduction of inefficient production within the union, there is a trade creation. To the extent that a customs union discriminates against non-members it has a trade diverting impact.

Trade diversion, which is considered to be a short-run static phenomenon, may be expected to take place under the following circumstances. In the case of a non-member country, whose export composition is such that a major part of it is produced in the union for duty-free intra-union trade, diversion in trade is likely to be pronounced, adversely affecting the non-member country's export earnings. Similarly, if the export composition of a non-member country is such that a greater proportion of it faces high tariff rates of the union, the magnitude of diversion is likely to be large. If the export composition of a non-member country does not conform to the above-mentioned pattern, then trade diversion is unlikely to be significant. Again, a non-member developing country may be made to face diversion if the union allows privilege access to products of other developing countries into its market by virtue of special trade arrangements. Thus, in the case of non-member country, whether a significant trade diversion has in fact taken place is an empirical question.

The theory of customs union pioneered by Viner argues that there is no general presumption about whether a customs union or free trade area increases or decreases the real income of member countries and the world. The outcome depends on the balance between trade creation and trade diversion. For a customs union to be beneficial to participants, trade creation effect must outweigh trade diversion effect,

so that on balance, following the formation or enlargement of a customs union, the suppliers are shifted from high-cost sources to low-cost sources.

Although mainstream static customs union theory gives us some important insights into the economic effects of a customs union, it should be treated with certain caution for various reasons. For instance, the assumptions on which the static analysis is based are clearly somewhat less than totally realistic. Factors such as monopoly power, scale economies, transport costs, information deficiencies, unemployment, adjustment costs, and non-tariff barriers are conveniently ignored.

Recently, the analysis of customs union effects has shifted away from those static effects to the dynamic effects. This area of customs union theory concentrates on the effects of a customs union referring to the long-term changes occurring in the economic structure of the countries participating in customs union, rather than on the once-and-for-all effects outlined above (Johnson 1957, Scitovsky 1958, Balassa 1963 and Cooper and Massell 1965). There is some debate among economists as to what exactly constitutes a true dynamic effect. However, the explanations of dynamic effects normally include expansion of production in many sectors, reduction in unit costs, creation of new and competitive industries, faster technological progress and also benefits from internal and external economies of scale. Under these conditions, the share of investment in GNP is permanently raised and a higher growth of the economy is attained. Accordingly, the main channels through which a scheme of economic integration leads to economic gains may be regarded as the specialisation of production according to comparative advantage, economies of scale arising from the potential utilisation of production units due to enlarged size of the integrated market, improvement in terms of trade resulting from a stronger bargaining position in the international market, enhanced economic efficiency brought about by intensified competition and changes in the rate of growth attributed to changes in both the quantity and quality of factors of production (Lipsy, 1975).

It is important to note that to measure the dynamic effects of a customs union is much more difficult and problematic than to measure the pure static effects. The

most direct consequences of the EC's recent enlargement for a non-member country can be indeed a loss of market share in the EC market, resulting from trade diversion.

On the other hand, the non-member countries may be benefited by potential benefits from the formation of a customs union, such as increased output and consumption within the union, which would increase the demand for imports into the union, although such benefits will take time to materialise. In the short run the static effect of customs union on non-members is expected to be of adverse nature. However, an appropriate change in the common external tariff could avoid this. Indeed, this external tariff could be adjusted in such a way that trade between the customs union and the non-member countries involves more or less the same collection and quantities of goods as before the formation of the union.

To sum up, the examination of customs union theory suggests that in a static framework, while trade creation is generally welfare improving, trade diversion need not necessarily reduce welfare. Occasionally, a customs union may generate 'external trade creation' resulting in an increase in imports from non-member countries. This occurs if non-member country's goods are complementary to goods whose internal demand is increased by the union. In this case, the non-member countries' exports are expected to increase as a consequence of the formation or enlargement of customs union, trade creation must by definition the outcome.

6.2 Institutional Changes and their Possible Effects on Trade with Pakistan

This section concentrates on the examination of EC's institutional links with its New Member States and Pakistan as well. It examines the pre and post enlargement links and their effects on Pakistan's trade flows with the EC and its New Member States.

6.2.1 The Pre-Enlargement Situation

EC-Pakistan institutional links were discussed in the previous chapters to some extent. However, in the context of our discussion, Pakistan's institutional links before the enlargement with EC-9 are summarised below. They consists of (a) a bilateral commercial cooperation agreement signed in 1976 between Pakistan and the EC-9 involving the concession by the two sides of most-favoured nation (i.e.. non-preferential trade agreement), (b) a series of bilateral agreements on textiles involving voluntary export restraints concluded within the framework of the MFA and (c) Pakistan benefits since 1971 from the EC's GSP treatment on those items covered by the scheme.

EC-Spanish institutional links before the enlargement were governed by the June 1970 preferential Agreement (OJL, No.182 of 16.08.1970). It provided (a) reduction of CET tariffs ranging between 25% to 60% varying from commodity to commodity on most industrial imports originating in Spain. It also provided partial tariff preferences on a number of Spanish agricultural exports (including food products) comprising a 30% to 50% reduction of the CET, but none at all on other agricultural products (comprising about 35% of Spanish agricultural exports). The signing of EC-Spanish Agreement on Textiles in 1978, allowed the EC to institute a surveillance system on Spanish exports of textile products, while in 1979, a system of administrative cooperation between the parties was introduced. A more restrictive agreement was in force regarding steel products (for more detail see, OJL, No.155 of 13.06.1978 and No.239 of 29.08.1978).

EC-Portugues institutional links were governed by the 1972 Agreement (OJL, No.301 of 31.12.1972). It provided free trade in industrial products and preferential tariff reduction on agricultural exports to the EC. The agreement was fully implemented insofar as Portugal's exports to the EC are concerned, although not in reverse direction. Full tariff liberalisation was linked to the outcome of negotiation for accession to the EC. Portugal's textile exports were regulated by EC-Portugues

Agreement on Textiles, following the EC-Spanish pattern as mentioned above (for more detail see, EC Commission, 1982).

EC-Greece pre-enlargement links were governed by the 1961 EC-Greece Association Agreement which provided for free trade in industrial products and partial tariff preferences on agricultural products. The agreement was fully implemented as far as Greece's industrial exports to the EC were concerned, with certain minor exceptions. Greece's textile exports to the EC before its entry were governed by EC-Greece Agreement on Textiles through the imposition of QRs (for further detail see, EC Commission, 1978).

6.2.2 The Post-Enlargement Situation

The post-enlargement situation of EC-Pakistan links are assumed to remain essentially the same, except for the following changes.

Greece, Portugal and Spain become a party to all the bilateral agreements concluded between the EC and Pakistan. It is important to note that soon after the enlargement, commercial cooperation agreement was replaced by a commercial, economic and development cooperation agreement signed in 1986 with the enlarged EC which covers wider aspects of economic relations than trade as discussed in chapter 3, section 3.4.

Further, Pakistan would receive benefit of GSP treatment in the three new member countries. For example, according to the Spanish Accession Treaty, Spain shall progressively apply the Generalised System of Preferences starting on March 1, 1986. Observe that the duties applied as from that date are identical to those applied on EC-originating imports. The preferential rates applied by the EC were assumed to take effect for most goods by January 1, 1996, with the important exception of fish products, for which the relevant date was January 1, 1993.

The post-enlargement status of all the EC's new members would change dramatically. There will be free trade in industrial and agricultural products between

the EC and its new members (to be fully implemented upon the expiry of transitional period). They will apply the CET and become a party to the Lome Convention, and to all individual agreements between the EC and Mediterranean countries. They will join the EC's scheme of tariff preferences on exports of developing countries, including that of Pakistan and adopt the EC's Common Agricultural Policy.

An obvious preliminary conclusion drawn from the above discussion is that the impact upon the economy of Pakistan of the entry of each of the three Mediterranean countries will differ because their pre-enlargement institutional links with the EC were by no means identical. Note that this is true independently of the other differentiating variables so frequently mentioned in the literature (such as their respective economic dimensions, the extent of their trade's overlap with third countries' imports, and so on).

Schematically, the most relevant changes from Pakistan's perspective are the following:

1. Spain will obtain free access to the EC for its agricultural exports, improving its status of preferred Mediterranean country, which entails very few tariff reduction in the pre-enlargement situation. The same is essentially true for Portugal, although not significantly so for Greece, whose agricultural exports were mostly exempted from tariff duties even before its accession. The EC will also obtain free access into Spanish, Greek and Portuguese agricultural markets.

2. The three new members will join the CAP upon accession to the EC, with all the advantages that this implies (e.g., export refunds, guaranteed prices, and so on) reaching them progressively after transitional periods. They will also have to respect after a while certain common disciplines (some production restraints, quality requirements, etc.) and apply the principle of Community preference and common agricultural prices.

3. The three new members must adopt the EC's CET. This invariably implies a reduction in tariff protection levels on non-EC member countries' industrial exports, although not so for some agricultural commodities.

4. The EC (nine member countries) will have to eliminate their highly restrictive limitation on "sensitive" products originating in Spain, Portugal and Greece, including textiles and clothing products. Further, Spain, Portugal and Greece, on the one hand and the EC on the other will increase their margins of preference on mutual industrial trade to 100%, thereby attaining a level of free trade in industrial goods. This may cause a trade diverting effects for Pakistan's exports overlapping with those of new members.

5. All Mediterranean and ACP countries will have free access without any limitations for their industrial exports into Spain, Portuguese and Greek markets. GSP beneficiary countries including Pakistan will also get tariff-free treatment in those markets but with limitations. The three new members must also adopt the EC's Textile agreements signed with several Asian and Latin American countries, including Pakistan within the framework of the MFA. Observe that the proportional tariff reduction for imports originating from these countries will be much larger than those from the EC or EFTA since the starting tariff applied by the new three members was already lower in the latter case.

6.2.3 Direct Possible Trade Effects of the EC's Enlargement for Pakistan

In view of the examination of customs union theory and institutional changes discussed in the previous sections, we may anticipate some possible direct effects of the EC's enlargement on Pakistan's trade flows with the enlarged EC. Two types of direct possible trade effects of the EC's enlargement for Pakistan are expected: 'trade creation' and 'trade diversion'. In brief, trade creation is the situation when the home expensive products are replaced by similar low-cost products within the customs union. On the other hand, trade diversion occurs when low-cost imported products from non-member country are replaced with the products produced less efficiently and more costly from the partner country. In this case, the source of imports is shifted from more efficient one outside the customs union to a less efficient one within the customs union. The most direct consequence of the EC's enlargement for Pakistan

may be indeed a reduction in its exports, resulting in a loss of its share of the EC's market.

Table 6.1 sums up the aforementioned changes and their possible direct trade effects for Pakistan. It discloses the general and sectoral effects which Pakistan may face due to the accession of Spain, Portugal and Greece into the EC. The expected effects are based on the assumption that the trade regime of the EC is such that it provides protection to the new members to the extent that the relevant cost differentials of production in the new member countries and Pakistan are covered. The examination of Table 6.1 bespeaks the following:

Table 6.1 GENERAL AND SECTORAL TRADE CREATION (TC) AND TRADE DIVERSION (TD) EFFECTS OF ENLARGEMENT AFFECTING PAKISTAN'S TRADE WITH THE EC

Changes in New Members' trade links with the EC	A Greece	B Portugal	C Spain
1) Free access to EC's agri. markets	---	TD	TD
2) Joining the CAP	TD	TD	TD
3) Adoption of the CET			
a) on industrial imports	TC	TC	TC
b) on agricultural imports	TD	TD	TD
4) a) Free access to EC's industrial market	TD	TD	TD
b) Free acceptance of EC's industrial goods	TC	TC	TC
5) Free or facilitated access to some Mediterranean markets	TD	TD	TD
6) Free acceptance of Mediterr. + ACP and LDC industrial imports	TC	TC	TC
7) Free or easier access of ACP+ Med. agricultural imports into Three's markets	TD	TD	TD

--indicates no effect as duties on Greece's agricultural exports were nil even before enlargement.

a) The trade diversion effects of the enlargement for Pakistan are likely to be severe for agricultural exports as these countries are significant producer and exporter of these commodities. The examination of Table 6.1 indicates that in the cases of trade diversion effects (lines 1, 2, 3b, 4a, 5, and 7) not only quantities exported by Pakistan will tend to drop but also prices charged must be lowered in relation to the pre-enlargement situation, whenever the domestic price in the EC drops as a result of the accession of New Members into the EC. The future looks awkward for products overlapping with Spain and Portugal's agricultural exports (like vegetable, fish products, citrus fruits, rice, etc), less so regarding Greece (e.g. tobacco), as duties on Greece's agricultural exports and most industrial products were nil even before the enlargement. The question of the effect of these changes upon world prices is all too frequently neglected, because of the assumption that neither the EC is an important consumer in world markets nor the New Members are key worl-wide suppliers. This is, however, not the case at least for several fruits and vegetable, and olive oil. For example, trade diversion in favour of Spain and Greece could reach proportional large enough to lower world prices. In such an eventuality, Pakistan would have to bear the impact of enlargement in her agricultural exports to the Middle East countries. It should be kept in mind that trade diversion is likely to be more than trade creation , i.e. if Pakistan's agricultural exports overlapping with the exports of Spain, Portugal and Greece are kept out of EC market.

b) The possible enlargement's effects for Pakistan noted in lines 3a, 4b and 6 are assumed to lead to trade creation. This situation will be favourable for Pakistan. This is so because Pakistan is assumed to be benefited by potential benefits from the EC's enlargement. The enlargement will generate 'external trade creation' resulting in an increase in manufactured and semi-manufactured imports from Pakistan. In this case, Pakistan's exports are expected to increase as a consequence of the EC's enlargement towards Southern Europe. The analysis of Table 6.1 shows that the overall negative effect apparently on Pakistan's industrial exports emerges more limited. Because by opening their markets fully to the EC and improving access for

other developed countries (EFTA) and due to the working of dynamic effects of customs union, the New Members and EC-9 as well will increase their demand for final goods, thus increasing demand for itermediary products from Pakistan. This of course will occur quite independently of the fact that direct industrial exports to the New Members are expected to undergo an overall increase at both the final and intermediary goods levels because of introduction of the GSP and adoption of "acquis communautaire" by the New Members.

It is expected that Pakistan's exports which should benefit from the enlargement include not only industrial products getting easy access through the GSP, but also those which were previously not sold there at all because of high tariffs and preference for ACP and Mediterranean countries' exports. The alignment of New Member country's tariff toward the CET implies a reduction in protection levels, trade creation must be by definition the outcome. Further, Pakistan can divert exports, sold previously at world prices, to the New Members, where they will fetch a higher prices, dictated by the EC export supply prices (assumed to be in many instances over and above Japanese or US prices). But most importantly of all there may be a net export expansion, because the higher prices allow for some production at higher costs. In other words, for Pakistan, the enlargement implies the addition of three markets with a relatively higher GNP, to which it can export at privileged prices. The higher the difference is between average EC and world prices, the higher the expected impact. This is particularly true for sensitive products of interest to Pakistan where in general Pakistan's positive effects can be expected greater than negative effects.

To sum up, as things stand, there are nil tariffs on certain items which are of special interest to Pakistan. Certain trade liberalization measures also fall either under the MFA or the GSP, which these countries have fully adopted. Transitional period given to New Members for adjustment will also help in softening the effects of the enlargement. Furthermore, as Pakistan is not a major exporter of agricultural commodities to the EC, we may assume that the outcome of the effects of EC's enlargement for Pakistan would be trade creation rather than trade diversion. In the

next section we will investigate the effects of the EC's enlargement for Pakistan empirically.

6.3 Trade Flows of Pakistan with the Enlarged EC

In the light of the static and dynamic effects of a customs union discussed above we may suggest that other things being equal, the recent enlargement of the EC from nine to twelve is likely to have strengthened trade within the EC and to have weakened it with other countries outside the EC including Pakistan.

The EC is essentially a customs union, developing countries are likely to be most affected by the EC's recent enlargement. As a general rule, to the extent that their exports compete with those of the three new members i. e., Greece, Portugal and Spain, they will find themselves at a disadvantaged position with respect to their potential exports to the EC countries.

Viewed in this context, most probably Pakistan's agricultural and manufactured exports to the EC market are likely to be affected. All these three members are likely to pose problems for developing countries including Pakistan. But it is Spain that is likely to cause the greatest problems, both for the EC and for developing countries, particularly with regards to agricultural products. In the case of such products, one result of the enlargement inevitably will be a substantial increase in the EC's self-sufficiency. For example, it is expected that EC's self-sufficiency in different agricultural products will be increased in fresh and processed vegetables from 92% to 100%, in fresh and processed fruit from 78% to 95%, in potatoes from 98% to 100%, in tomatoes from 93% to 99%, in wine 108% to 112% and in olive oil from 85% to 100% (Stevens, 1981).

Consequently, countries exporting agricultural products to the EC, provided overlapping with the exports of those New EC member countries, will be seriously affected. The EC Commission has calculated that the countries most severely affected will be the Mediterranean basin i.e., Tunisia, Morocco, Cyprus, Egypt, Turkey and Israel. And products like olive oil and vegetable fats, fruits and

vegetables and wine comprised the list which were expected to be most likely to be affected. (Philip Mishalani, et. al, 1981 and Robert Taylor, 1980). It implies that other developing countries like Pakistan will be less affected. This conclusion seems to be valid as far as Pakistan is concerned mainly for three reasons. First, because Pakistan is relatively a small supplier of agricultural products to the EC market. Second, its major agricultural exports rice and tobacco are not directly competing with the products of the new members due to a variety difference. Third, Pakistan's minor agricultural exports to the EC market are adequately given trade concessions to the EC market under the EC's GSP scheme operative in favour of developing countries including Pakistan since 1971. As these new members will also adopt the EC's GSP scheme, it can be expected that Pakistan may find some outlets in the markets of new member countries for its agricultural products as mentioned in the previous section.

On the contrary, the impact of the enlargement on Pakistan's exports to the EC market in industrial products may be considered to be rather different. It is generally believed that Pakistan's industrial products competing with those of the new members will be most vulnerable. All these new members are the exporters of roughly the same textile and clothing products, notably cotton yarn and fabrics and some articles of clothing garments. Table 6.2 indicates the relative importance of textiles and clothing exports for Pakistan and New EC members as well.

Table 6.2 RELATIVE IMPORTANCE OF TEXTILE AND CLOTHING FOR PAKISTAN AND NEW EC MEMBERS
[Share Percentage in Total Exports]

Years	Pakistan	Greece	Portugal	Spain
1980	42.7	20.6	30.1	9.3
1981	45.6	24.4	30.5	9.4
1982	51.5	23.8	32.6	8.6
1983	55.5	25.0	32.3	9.0
1984	56.2	25.2	33.1	9.4
1985	52.3	26.1	35.5	9.3
1986	58.3	32.6	39.1	9.6
1987	66.5	35.7	40.8	9.5
1988	60.9	35.3	38.6	8.4
1989	64.6	29.1	36.6	7.5
1990	64.7	29.4	37.7	7.6

Source: UN- International Trade statistical Yearbooks.

The analysis of Table 6.2 clearly reveals the fact that in the export of textiles and clothing the New EC members, except Spain, are significant exporters of such items, while Pakistan being the most prominent one. From the date of accession, these three supplier of such industrial products of these New members would enter into the EC market without any restrictions as they have become an integral part of the EC and their export as part of intra-EC trade. This implies that these countries may increase their share of the EC market at the cost of other developing countries including Pakistan. On the other hand, as things stand at the present time, however, there are nil tariffs on certain items, which are of special interest to Pakistan. Certain trade liberalisation measures also fall either under the MFA or the GSP, which these countries have fully adopted. Further, transitional period given to these countries for adjustment will also help in softening the impact of the enlargement. Due to these arrangements, we may expect that Pakistan will not face any significant short-run diverting effect for its exports due to the inclusion of Greece, Portugal and Spain into the EC.

Since the establishment of diplomatic relations between Pakistan and the EC in 1962, their relationship has developed in a steady if unspectacular fashion. Nevertheless, trade has always been central to Pakistan-EC economic relations. Pakistan's trade relations with the EC were further strengthened with the accession of the United Kingdom into the EC in 1973. Since then the EC has been Pakistan's major market and principal supplier, accounting for about one third of the country's total trade. Pakistan runs a chronic trade deficit with the EC but this has recently improved considerably. Table 6.3 demonstrates the different aspects of Pakistan's trade flows with the enlarged EC between 1980 and 1990. It also reveals the fact that the total value of trade between Pakistan and the EC increased substantially over the period under study.

Table 6.3 TRADE FLOWS BETWEEN PAKISTAN AND THE ENLARGED EC

[Million US$]

Year	Exports	Imports	Balance of Trade	Exports as % of Imports	EC's share % in Pakistan's Total Exports	Imports
1980	612	1238	-626	49.4	20.7	22.9
1981	541	1166	-625	46.4	22.0	20.7
1982	530	1055	-525	50.2	19.7	19.7
1983	520	1163	-643	44.7	18.8	20.5
1984	524	1147	-623	45.7	21.0	19.6
1985	678	1218	-540	55.7	22.1	21.6
1986	997	1557	-560	64.0	27.0	28.9
1987	1268	1663	-395	76.2	28.5	26.0
1988	1451	1894	-443	76.6	31.1	26.9
1989	1597	1605	-8	99.5	32.2	23.1
1990	1861	1818	43	102.0	30.4	23.9

Source: Calculated obtaining data from PES and Eurostat.

It can be seen from Table 6.3 that imports from as well as exports to the EC as proportion of Pakistan's overall imports and exports, over the period concerned, have had increasing trends. Similar trends are apparent when EC's share in Pakistan's total trade both exports and imports are examined. Most importantly, this table indicates Pakistan's improved situation as far as balance of trade and import cover ratio are concerned. This became possible mainly due to the impressive growth of Pakistan's exports to the enlarged EC market, especially after the enlargement. For instance, before the enlargement between 1980 and 1985, Pakistan's exports on average were increased by 11% from ECU 612 million in 1980 to ECU 678 million in 1985, while imports from the EC were dropped by 2% from ECU 1238 million to ECU 1218 million during the same period. On the other hand, after the enlargement Pakistan's exports to the EC rose by 175%, while exports rose by 49% between 1985 and 1990. On the whole, the examination of data presented in Table 6.3 provides enough ground to conclude that Pakistan's trade with the EC did not suffer in any way following its enlargement towards Southern Europe. On the contrary Pakistan's trade with the enlarged EC appears to have gained momentum in the years following Greece, Portugal and Spain's entry into the EC. On the basis of above discussion we

may conclude that in the case of Pakistan, trade creation has been the greatest. As a result, the country experienced a net export expansion to the EC market following the enlargement.

This conclusion seems to be compatible with many studies which estimated the effects of the EC's enlargement. For example, the study conducted by Krugman (1988) reflecting the position of EFTA countries suggested that the overall unfavourable impact could outweigh the beneficial effects. Similarly, other studies (Truman 1969 and 1975; Williamson and Bottril 1971; Kreinin 1972, 1974, 1981; Aitkin 1973; Balassa 1975; Mayes 1978 and 1983) suggest that the EC customs union has significantly altered trade flows and has on the whole been trade creating. Trade creation has been greatest in manufacturing, and has outweighed the trade diversion that has occurred, particularly in agriculture.

In order to proceed with the analysis at a less aggregate level we have examined all items of Pakistan's major exports to EC identified by Harmonised Commodity Description and Coding System (HS) at eight digit level. All items of export to EC with a value of ECUs 10 million and above in 1991 are included. We have discussed items with the export values of ECUs 20 million and above in 1991 individually and the rest collectively. In total these items accounted for more than 36% of the country's total exports to the EC market in 1991. The analysis of these selected items would allow us to investigate the possible effects of EC's enlargement on Pakistan's exports at a less aggregate level. It may also throw some light on the long-term dynamic implications of EC's recent enlargement for Pakistan's exports. Tables 6.4 and 6.5 contain data pertaining to the selected items of Pakistan's principal exports to the EC market and the same for EC's new partners for the four years following the EC's recent enlargement, 1988 to 1991. In the following paragraphs comparative analysis of these selected items will be presented to some detail.

Item 4203.10.00 Articles of Apparel of Leather or Composition of Leather: It is not surprising that this item is the most prominent of Pakistan's export to EC in

Table 6.4 COMPARATIVE EXPORT PERFORMANCE OF PAKISTAN AND THE EC'S NEW MEMBERS IN THE EC MARKET [SELECTED ITEMS]

[Value=000 ECUs]

Country	1988			1989			1990			1991		
	Val	GR%	Share %	Val	GR%	Share %	Val	GR%	Share %	Val	GR%	Share %
Item 4203.10.00 Articles of Apparel of Leather or composition of Leather												
Pakistan	70564	-	5.3	85290	20.9	6.9	119062	39.6	8.5	135024	13.4	11.2
portugal	3179	-	0.2	2360	-25.8	0.2	2429	2.9	0.2	3744	54.1	0.3
Spain	1056	-	0.8	9606	809.7	0.8	9658	0.5	0.7	9332	-3.4	0.8
Greece	5026	-	0.4	3202	-36.3	0.3	1715	-46.4	0.1	1456	-15.1	0.1
Item 6302.21.00 Printed Bed-Linen of Cotton												
Pakistan	41547	-	18.2	43069	3.7	17.5	49154	14.1	16.6	68850	40.1	17.3
portugal	29860	-	13.1	33094	10.8	13.4	35249	6.5	11.9	34556	-2.0	8.7
Spain	1150	-	0.5	1787	55.4	0.7	3086	72.7	1.0	1959	-36.5	0.5
Greece	1549	-	0.7	1592	2.8	0.6	833	-47.7	0.3	343	-58.8	0.1
Item 5513.11.90 Woven Fabrics mixed with Cotton (width >165 CM)												
Pakistan	28312	-	22.4	26348	-6.9	22.0	31223	18.5	24.0	58154	86.3	32.7
portugal	3319	-	2.6	3094	-6.8	2.6	1610	-48.0	1.2	1053	-34.6	0.6
Spain	317	-	0.3	429	35.3	0.4	268	-37.5	0.2	242	-9.7	0.1
Greece	-	-	0.0	-	0.0	0.0	-	0.0	0.0	-	0.0	0.0
Item 1703.10.00 Can Molassess												
Pakistan	56505	-	25.5	57050	1.0	25.3	61411	7.6	27.1	47510	-22.6	21.7
portugal	400	-	0.2	55	-86.3	0.0	81	47.3	0.0	10	-87.7	0.0
Spain	-	-	0.0	-	0.0	0.0	7	0.0	0.0	28	300.0	0.0
Greece	-	-	0.0	-	0.0	0.0		0.0	0.0		0.0	0.0
Item 5201.00.90 Cotton (not carded or combed)												
Pakistan	152081	-	10.1	106332	-30.1	6.4	99981	-6.0	6.4	35959	-64.0	2.4
portugal	165	-	0.0	257	55.8	0.0	199	-22.6	0.0	437	119.6	0.0
Spain	24334	-	1.6	50063	105.7	3.0	21090	-57.9	1.3	25352	20.2	1.7
Greece	7591	-	0.5	55439	630.3	3.4	29670	-46.5	1.9	37352	25.9	2.5
Item 5513.11.30 Woven Fabrics mixed with cotton (width =<165 CM)												
Pakistan	26022	-	22.2	20598	-20.8	16.4	33811	64.1	20.8	28462	-15.8	23.3
portugal	333	-	0.3	349	4.8	0.3	659	88.8	0.4	103	-84.4	0.1
Spain	441	-	0.4	989	124.3	0.8	397	-59.9	0.2	165	-58.4	0.1
Greece	90	-	0.1	48	-46.7	0.0	-	-100.0	0.0	18	0.0	0.0

[Value=000 ECUs]

Country	1988			1989			1990			1991		
	Val	GR%	Share %	Val	GR%	Share %	Val	GR%	Share %	Val	GR%	Share %
Item 6208.91.10 Women or Girl's Dressings of Cotton												
Pakistan	6816	-	8.5	7652	12.3	8.7	14588	90.6	14.5	22264	52.6	19.2
portugal	5603	-	7.0	5179	-7.6	5.9	5948	14.8	5.9	8242	38.6	7.1
Spain	346	-	0.4	539	55.8	0.6	399	-26.0	0.4	621	55.6	0.5
Greece	1751	-	2.2	641	-63.4	0.7	144	-77.5	0.1	368	155.6	0.3
Item 6203.42.35 Men or Boys' Dressings of Cotton												
Pakistan	5945	-	0.8	6759	13.7	0.8	9373	38.7	1.0	21099	125.1	2.1
portugal	28534	-	3.7	37743	32.3	4.5	51675	36.9	5.4	58085	12.4	5.9
Spain	5571	-	0.7	6181	10.9	0.7	5622	-9.0	0.6	8015	42.6	0.8
Greece	7626	-	1.0	7272	-4.6	0.9	7480	2.9	0.8	6648	-11.1	0.7
Others Items												
Pakistan	62747	-	2.4	82058	30.8	2.6	132565	61.6	3.4	149386	12.7	3.4
Portugal	120509	-	4.6	182931	51.8	5.7	236845	29.5	6.1	273569	15.5	6.1
Spain	34934	-	1.3	40168	15.0	1.3	58236	45.0	1.5	55865	-4.1	1.3
Greece	253524	-	9.6	308336	21.6	9.7	331429	7.5	8.6	336162	1.4	7.5

Note: Val= Value and GR= Growth Rates. Share percentage in EC's total imports.
Source: Eurostat, External Trade (microfiches), concerned years.

Table 6.5 COMPARATIVE EXPORT PERFORMANCE OF PAKISTAN AND THE EC'S NEW MEMBERS IN THE EC MARKET [SELECTED ITEMS]

[Volume=Tonnes]

Country	1988			1989			1990			1991		
	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI
Item 4203.10.00 Articles of Apparel of Leather or composition of Leather												
Pakistan	1500	47.0	100	2136	39.9	85	3247	36.7	78	3960	34.1	72
portugal	53	60.0	100	65	36.3	61	35	59.4	116	41	91.3	152
Spain	77	137.9	100	70	137.2	100	99	97.6	71	75	124.4	90
Greece	64	78.5	100	38	84.3	107	22	78.0	99	11	132.4	169
Item 6302.21.00 Printed Bed-Linen of Cotton												
Pakistan	8275	5.0	100	8538	5.0	100	9712	5.1	101	11965	5.8	115
portugal	3729	8.0	100	4865	6.8	85	5013	7.0	88	4895	7.1	88
Spain	154	7.5	100	201	8.9	119	383	8.1	108	194	10.1	135
Greece	164	9.4	100	162	9.8	104	76	11.0	116	40	8.6	91
Item 5513.11.90 Woven Fabrics mixed with Cotton (width >165 CM)												
Pakistan	7418	3.8	100	7009	3.8	98	9832	3.2	83	17880	3.3	85
portugal	451	7.4	100	482	6.4	97	297	5.4	74	221	4.8	65
Spain	43	7.4	100	64	6.7	91	52	5.2	70	39	6.2	84
Greece	-	0.0	100	-	0.0	-	-	0.0	-	-	0.0	-
Item 1703.10.00 Can Molassess												
Pakistan	818979	0.1	100	823208	0.1	100	946257	0.1	94	666771	0.1	103
portugal	4446	0.1	100	575	0.1	106	825	0.1	109	275	0.0	40
Spain	-	0.0	100	-	0.0	0.0	94	0.1	0.0	271	0.1	-
Greece	-	0.0	100	-	0.0	0.0	-	0.0	0.0	-	0.0	-
Item 5201.00.90 Cotton (not carded or combed)												
Pakistan	126677	1.2	100	88480	1.2	100	77030	1.3	108	26719	1.3	112
portugal	88	1.9	100	154	1.7	89	38	5.2	279	249	1.8	94
Spain	18771	1.3	100	44626	1.1	87	14450	1.5	113	17959	1.4	109
Greece	6305	1.2	100	42716	1.3	108	21113	1.4	117	27954	1.3	111
Item 5513.11.30 Woven Fabrics mixed with Cotton (width =<165 CM)												
Pakistan	8592	3.0	100	6653	3.1	102	11858	2.9	94	9912	2.9	95
portugal	27	12.3	100	51	6.8	55	58	11.4	92	20	5.2	42
Spain	38	11.6	100	140	7.1	61	40	9.9	86	20	8.3	71
Greece	15	6.0	100	10	4.8	80	-	0.0	-	4	4.5	75

[Volume=Tonnes]

Country	1988			1989			1990			1991		
	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI
Item 6208.91.10 Women or Girls Dressings of Cotton												
Pakistan	1155	5.9	100	1378	5.6	94	2935	5.0	84	4612	4.8	82
portugal	495	11.3	100	488	10.6	94	552	10.8	95	762	10.8	96
Spain	14	24.7	100	26	20.7	84	20	20.0	81	25	24.8	101
Greece	96	18.2	100	43	14.9	82	11	13.1	72	20	18.4	101
Item 6203.42.35 Men or Boys' Dressings of Cotton												
Pakistan	596	10.0	100	645	10.5	105	894	10.5	105	1857	11.4	114
portugal	1204	23.7	100	1701	22.2	94	2339	22.1	93	2371	24.5	103
Spain	294	18.9	100	249	24.8	131	245	22.9	121	290	27.6	146
Greece	441	17.3	100	441	16.5	95	416	18.0	104	358	18.6	107

Note: Vol=Volume; UV= Unit Value and UVI= Unit Value Indices.
Source: Eurostat, External Trade (Microfiches), concerned year.

1991 since Pakistan is a major exporter of leather and leather goods (about 7% of Pakistan's total exports in 1987). Pakistan's performance in terms of capturing a higher share of the market is very impressive. With a growth of more than 90% over the period she managed to improve her share of the EC market from just above 5% in 1988 to more than 11% in 1991 (Table 6.4). This improvement was due to an increase of more than 160% in the volume of exports over the period, however, it was accompanied by a drop in the unit value index of nearly 30% (Table 6.5). The new members of EC have a relatively insignificant share of the EC market for this item and their position over the period has almost remained the same.

Item 6302.21.00 Printed Bed-Linen: Pakistan appears to be a very important supplier of Bed-Linen to the EC, although its share in the EC market declined slightly from 18% in 1988 to 17% in 1991. The EC's new members faced a much more significant fall in their market shares in the EC especially Portugal, the only significant competitor of Pakistan, with its market share declining from 13% in 1988 to less than 9% in 1991. Pakistan's better export performance over the period, as indicated by 66% growth in the value of its exports, has been mainly due to a substantial increase in the volume of exports showing a healthy rate of growth of nearly 45% which is very promising when it is considered next to an of 15% in unit value index over the period (Table 6.4). In the case of Portugal although the quantity exported was increased by 31% over the period while the drop in the unit value index resulted in a lower share of the market.

Item 5513.11.90 Woven Fabrics Mixed with Cotton (width >165 cm): Pakistan is a very important supplier of Woven Fabrics to the EC. Its exports accounted for 22% of EC's total imports in 1988 and almost one third of total EC imports of woven fabrics in 1991. As Pakistan is a major producer of raw cotton and cotton products, the substantial rise in the export of woven fabrics is not altogether surprising. Other factors like the provision of TQs/TCs and significant increase in their limits from year to year also played an important role in this regard. Among the three new EC members, no country seems to be competitor of Pakistan in the supply of woven fabrics to the EC market. Table 6.4 and Table 6.5 indicate that Pakistan's export performance has been much smoother compared with Portugal and

Spain in the EC market over the period under study. In the case of this item Pakistan enjoyed a staggering growth rate of 105% in the value of its exports over the period. This excellent performance was mainly the result of an increase in quantity exported, more than 140% over the period, rather than an increase in unit value index which dropped by 15%.

Item 1703.10.00 Canned Molasses: The new member states of EC do not seem to be in any competition with Pakistan in the case of this item. However, Pakistan appears to have lost a significant share of the EC market, perhaps to other developing countries. Table 6.4 indicates a substantial drop of nearly 23% in the value of her exports for 1991, though she enjoyed an upward trend over previous years. An overall drop of 16% in the value of imports of this item from Pakistan resulted in a drop in her market share from nearly 26% in 1988 to almost 22% in 1991. While the unit value index did not change significantly over the period the volume of imports from Pakistan did so in 1991 indicating a drop of nearly 19% over the period (Table 6.5). It seems that supply factors were responsible for the significant drop in the exports of this item in 1991.

Item 5201.00.90 Cotton (not carded or combed): Pakistan seems to have suffered a serious setback in the exports of this item to the EC market. It is interesting to notice that a drop of 30% in the value of her exports in 1989 was coupled with an increase of more than six folds in the exports of this item by Greece to the EC market. This resulted in an increase in market share for Greece from 0.5% in previous year to almost 3.4% in 1989. Spain's exports also show an impressive growth resulting in almost doubling of its market share to 3% during this year. Both countries have managed to push Pakistan's market share from 10% in 1988 down to just above 6% in 1989. There seems to be a case of trade diverting from Pakistan in the case of this item. In 1990, however, the values of exports by all countries appearing in Table 6.4 seem to have dropped significantly. Although there are signs of a slight drop in demand for imports - as indicated by the market share of Pakistan remaining constant despite a drop in its exports between 1989 and 1990 - it seems that other countries have taken a bigger share of the market mainly at the expense of Greece and Spain. In 1991 both Spain and Greece did recover some of their market shares while Pakistan suffered yet another significant set back probably as a result of other countries gaining a bigger share of

the EC market. Table 6.5 indicates that while the unit value index for Pakistan has not changed significantly the drop in exports has been mainly due to a dramatic fall in the volume of her exports.

Item 5513.11.30 Woven Fabrics Mixed with Cotton (width =<165 cm): Table 6.4 shows that Pakistan enjoys a very strong position in the export of woven fabrics to the EC. Although Pakistan's exports of this item seem to have been subjected to some fluctuations she has managed a growth rate of just above 9% in the value of exports and has slightly improved her market share over the period. In 1991 almost a quarter of the EC's total imports of this item was provided by Pakistan. As Table 6.5 shows the unit value for this item has dropped in the latter part of the period concerned, however, this was compensated, to some extent, by an increase of 15% in the volume of exports. None of the three new EC members appear to be competitor of Pakistan in the export of woven fabrics in the EC market over the period under review. This seems to underline the importance of supply conditions rather than trade preferences.

Item 6208.91.10 Women or Girls Dressings of Cotton: Pakistan provided more than 19% of EC's total imports of women or girls dressings in 1991. The value of EC imports of this item from Pakistan increased dramatically, by 227%, over the period increasing Pakistan's market share from around 8% in 1988 to more than 19% in 1991 (Table 6.4). Again an increase of three folds in quantities has been responsible for such a dramatic growth covering well for a modest drop in the unit value index (Table 6.5). Among the three new EC members, Portugal seems to be a significant competitor of Pakistan in the EC market. In contrast to Pakistan's performance, the market share of Portugal and Spain remained more or less stable, while Greece's share declined sharply over the period. This indicates that none of these countries have been able to match the degree of success enjoyed by Pakistan in the EC market.

Item 6203.42.35 Men or Boys Dressing of Cotton: In the case of this item although Pakistan's relative importance in the EC market is less impressive, she has enjoyed an impressive growth rate of more than 250% in the value of her exports coupled with more than two folds volume increase and an increase of 14% in the unit value index (Tables 6.4 and

6.5). Portugal has been the main Pakistan's competitor where the increase in market share for the former is very impressive. Despite this, it seems that changes in the conditions of entry into the EC market have not adversely affected Pakistan's exports to this market. In fact if anything the opposite seems to be the case. This is reflected in an overall increase of EC imports from all countries, except Greece whose share declined slightly, included in our study over the period under review. These figures also indicate that the demand conditions in the EC market resulting from EC's recent enlargement did not become unfavourable for Pakistan. This evidence seems to underlines the point that tariff preferences, though important, can not be held as the sole cause of determining a country's trade pattern.

Other Items: Ten items are included under this heading. They are items with export values between ECUs 10 to 20 million in 1991. A variety of different commodities such as cotton yarn, cotton dressings, leather articles, cotton and polyester fabrics appear in this group. Overall in the export of these items, Greece, Portugal and Spain compete with Pakistan. The demand for these products seems to have increased dramatically over the period and Pakistan and Portugal seem to have improved their shares of the market at the expense of Greece. Comparison of the figure for 1988 and 1991 reveals impressive growth rates of 138% for Pakistan, 127% for Portugal, 60% for Spain and 33% for Greece (Table 6.4).

In the case of some of these items Pakistan is a major supplier to the EC market, despite the relatively lower value of her exports of the commodity concerned. For example, in the case of woven synthetic fabrics Pakistan provides around 60% of total EC imports. Similarly, Pakistan's has been an important supplier of printed polyester fabrics, men or boys' singlets, protective gloves of leather and cotton pyjamas for women with the market shares of 26%, 22%, 8% and 7% in the EC total imports of these items. Detailed figures for these products are presented in Tables 6.A-I and 6.A-II (placed at the end of this chapter).

A feature of the statistics presented in Table 6.4 and 6.5 is that Portugal appears to be Pakistan's main competitor in some of the selected items while in the case of textile, clothing and leather products Pakistan occupies a place of pride in the EC market. As Pakistan is a

major producer of cotton, its substantial share and rise in its overall exports of textile and clothing in the EC market is not altogether surprising.

The evolution of Pakistan's export trade to the EC market clearly shows upward trends in almost all selected items, both in terms of volume, value and market share between 1988 and 1991. Such trends are even more pronounced when compared to intra-EC trade from its new members. It appears that during the period of study Pakistan's exports did not experience any large-scale diversion effect owing to EC's recent enlargement. On the contrary, there is enough evidence to suggest that the EC has not only maintained supplies from Pakistan in majority of items that constitute Pakistan's principal exports, but its imports from Pakistan increased substantially over the period concerned. The increase in the values of Pakistan's exports for the selected items were primarily due to substantial rises in the quantities imported. In many cases new EC member countries faced greatest fall in their market shares, while Pakistan's market share increased in the enlarged EC market over the period of study.

It seems that among the new EC members, no country seems to be competitor of Pakistan in the supply of many items. This is especially true in the case of items like articles of leather, can molasses, and fabrics, etc. In general it can be said that Pakistan's export performance in the EC market, in the case of her principal exports, has been much smoother than those of the EC's new three members. An important conclusion to be drawn is that changes in the conditions of entry into the EC market resulting from the EC's recent enlargement have not adversely affected Pakistan's principal exports.

It is important to note that Portugal, in particular, remained a competitor supplier to EC in some of the items of export interest to Pakistan. However, it seems that the continuity in Portugal's lead over Pakistan in most of these items remained absent. In fact, there appears only one item of Pakistan's export trade, namely cotton, in which the process of substitution has taken place. It is likely that this item has experienced strong competition from the African, Caribbean and Pacific and Mediterranean countries that have been granted preferential treatment by the EC.

With the exception of cotton it seems that while the EC new member countries managed to improve their share in the EC's total imports, they have posed no significant trade diversion threat on a continuous basis to Pakistan's prominent exports in the EC market in the years following their inclusion into the EC. It seems that EC demand factors were not generally unfavourable to Pakistan's exports resulting in Pakistan enjoying a growing share of the EC market. One of the most encouraging aspects of Pakistan's export performance has been the amount of diversification which has taken place over the years. Non-traditional export items have played a major role in improving the overall export performance of Pakistan in the EC market. Sharp rises in the exports of manufactured and semi-manufactured goods, which were given preferences under the EC's GSP scheme, have been primarily responsible for such improvements not only to the EC but also to the New Members as well.

The examination of aggregated trade statistics also reveal the fact that Pakistan has been successful in diverting its exports to the EC and its New Members as well to fetch the higher prices, dictated by the EC export supply prices. This seems to be in line with our analysis of section 6.2, where it was argued that pakistan's exports would benefit in the EC-9 and New Members as well getting easy access through the GSP. The introduction of the GSP scheme by the New Members would also stimulate export items not sold previously there at all because of high tariffs. The outcome of these changes were expected to lead trade creation favouring Pakistan. This is clearly evident from Tables 6.6 and 6.7. Table 6.7 reveals the fact that after the enlargement Pakistan's exports to the EC and its New Members as well increased rapidly as compared to non-EC market. For example, Pakistan's exports to the EC-9 rose by 146% before and by more than 251% after the enlargement. Similarly, its exports to the EC-12 were increased by 155% before and by 250% after the enlargement. On the other hand, Pakistan's exports to the non-EC market were increased by 53% between 1980-85 and by 156% between 1985-90. This evidence lends support to the conclusion that Pakistan's overall higher export achievements were mainly due to its better export performance in the EC market over the period under study. This is also reflected in Table 6.6. It shows that after the enlargement Pakistan's exports to the EC's New Members were accelerated. As a result, their share in the country's total exports to the EC rose significantly after the

Table 6.6 PRE AND POST ENLARGEMENT TRENDS IN PAKISTAN'S TRADE WITH THE EC AND ITS NEW EC MEMBERS

[Share percentage in Pakistan's total exports to the EC]

Year	EC-9	Greece	Portugal	Spain	EC-12
1980	94.6	1.3	0.7	3.4	100
1981	94.6	0.6	0.7	4.1	100
1982	94.6	0.8	0.5	4.0	100
1983	94.7	0.5	0.8	4.0	100
1984	93.2	1.0	1.4	4.3	100
1985	91.3	2.4	2.5	3.8	100
1986	90.9	1.4	3.1	4.6	100
1987	86.8	2.4	4.9	6.2	100
1988	87.0	1.1	4.6	7.3	100
1989	90.3	1.3	2.6	5.7	100
1990	91.5	1.2	2.0	5.4	100

Source: Compiled and calculated from PES 1992-93.

Table 6.7 VALUE AND GROWTH OF PAKISTAN'S EXPORTS TO THE EC AND NON-EC MARKETS PRE AND POST ENLARGEMENT

	[Value in Rs. Million]			% change over	
Country	1980	1985	1990	1980-85	1985-90
EC-9	4397	10813	37965	146.1	251.1
Greece	60	285	480	375.0	68.4
Portugal	34	303	810	791.2	167.3
Spain	158	446	2242	182.3	402.7
EC-12	4649	11847	41497	154.8	250.3
Non-EC	24631	37745	96783	53.2	156.4
Total Exports	29280	49592	138280	69.4	178.8

Source: Calculated from PES 1992-93.

enlargement. The greatest increase is seen in the shares of Spain and Portugal, while the share of Greece also rose but remained highly unstable.

It seems that, among others, the provision of financial as well as technical assistance provided by the EC and certain other arrangements such as the conclusion of bilateral cooperation agreements also gave stimulus to Pakistan's exports to the EC market. In fact, the EC's GSP can be regarded as a potential policy instrument for resolving Pakistan's trade problems arising out of Greece,Portugal and Spain's accession into the EC. Under the GSP scheme, Pakistan's exports including manufactures and semi-manufactures have benefited significantly and some made headway into the EC market. More importantly the openness of their markets after the enlargement through GSP and adoption of "acquis communautaire" by these countries, etc. provided opportunities for increased exports of interest to Pakistan. As a result, Pakistan gained a net export expansion resulting from the trade creation effects of the EC as a customs union.

So far as the long-run dynamic effects of the EC's recent enlargement are concerned the rising trend of Pakistan's exports to the EC and possibility of further improvement in trade and economic flows between Pakistan and the EC seem to lend support to the optimistic notions expressed by few of the customs union theorists. This school of thought suggests dynamic growth implications for a country joining a customs union as well as for the member countries which in turn may benefit the non-member countries. An expansion of the market improves production efficiency through economies of scale in production and distribution; it also contributes to healthy competition among business enterprises and improved market opportunities for investment and business. As a consequence, the possibility of a non- member country benefiting in the long-run from the member country's improved business exists. Although it is too soon to assess the long-term dynamic implications of the EC's recent enlargement for Pakistan, the recent unprecedented expansion may be regarded as evidence of the beginning of a favourable long-run phase in Pakistan-EC trade and economic flows in a revised organisational framework. The examination of

EC import trade data seems to be pointing at bright prospects for Pakistan's exports to the EC market in the future.

6.4 Concluding remarks

This chapter has examined Pakistan's trade relations with the EC in the context of latter's revised framework following Greece, Portugal and Spain's inclusion into its orbit. The main finding is that the beneficial impact of the enlargement has swamped the negligible negative impact of the EC's recent enlargement. Contrary to the belief that Pakistan-EC trade relations would receive a setback following the latter's enlargement, it seems that it has led to an improvement in Pakistan's overall exports to EC.

The detailed analysis of growth rates indicated that the EC's enlargement has led to an improvement in Pakistan's trade flows with the enlarged EC, owing primarily to the sharp rise in the export of manufactured and semi-manufactured goods which are covered under EC's GSP scheme. On the other hand, the commodity analysis revealed that Pakistan's non-traditional export items fared quite well in the EC market as opposed to traditional ones. Owing to the considerable diversification in the structure of production that occurred in Pakistan, the supplies of manufactured and semi-manufactured items aided the process of improvement in Pakistan's exports to the EC market. The EC's GSP scheme emerged as a potential policy instrument of resolving Pakistan's trade problems arising out of Greece, Portugal and Spain's entry into the EC. Most importantly, the commodity analysis at disaggregated level points out that their comparative advantage remain in different commodities, although at the aggregated level they seem to be competing with each other in the EC market.

Thus, the overall conclusion drawn from the analysis of trade flows between Pakistan and the EC is that the enlargement of EC has had no adverse effects on Pakistan's trade flows with the enlarged EC. The examination of available empirical evidence did not indicate any large-scale diversionary impact. In view of the fact that only a few years have elapsed, it is too soon to asses the long-term dynamic

implication of EC's enlargement for Pakistan's exports. Nonetheless, in the light of the manner in which the non-traditional items of Pakistan's exports to the EC market have performed over the period under study, it may be safe to predict bright prospects for the expansion of Pakistan's exports to the EC market in future. Nevertheless, the challenge for both Pakistan and the EC will be to identify means and ways in which the EC could provide positive assistance to Pakistan in diversifying its export base, alleviating the supply constraints, and assisting Pakistan to adjust to demand shocks which may be caused by the possible future enlargement.

APPENDIX TO CHAPTER 6

Table 6.A.1

COMPARATIVE EXPORT PERFORMANCE OF PAKISTAN AND THE EC'S NEW MEMBERS IN THE EC MARKET [OTHER ITEMS]

[Value=000 ECUs]

Country	1988			1989			1990			1991		
	Val	GR%	Share %	Val	GR%	Share %	Val	GR%	Share %	Val	GR%	Share %
Item 5205.12.00 Cotton yarn measuring <174.29 Decitex but >=232.56 Decitex												
Pakistan	10424	-	2.4	10204	-2.1	2.6	24001	135.2	5.2	18469	-23.0	4.5
portugal	3213	-	0.7	3530	9.9	0.9	4258	20.6	0.9	5565	30.7	1.4
Spain	16760	-	3.9	18668	11.4	4.8	28536	52.9	6.2	19940	-30.1	4.9
Greece	27407	-	6.3	31867	16.3	8.2	28049	-12.0	6.1	24120	-14.0	5.9
Item 6109.10.00 T-Shirts, singlets and other vests of cotton (Knitted or crocheted)												
Pakistan	9447	-	0.9	12585	33.2	0.9	18642	48.1	1.0	16922	-9.2	0.7
portugal	90321	-	9.1	145657	61.3	10.2	197524	35.6	10.6	231251	17.1	10.1
Spain	7022	-	0.7	6336	-9.8	0.4	7822	23.5	0.4	9646	23.3	0.4
Greece	162515	-	16.3	218840	34.7	15.3	248143	13.4	13.3	259311	4.5	11.4
Item 4203.29.10 Protective Gloves of Leather or composition of Leather												
Pakistan	11440	-	7.9	12109	5.8	6.8	16568	36.8	8.3	16579	0.1	8.2
portugal	12	-	0.0	41	241.7	0.0	62	51.2	0.0	447	621.0	0.2
Spain	1126	-	0.8	1356	20.4	0.8	1638	20.8	0.8	4543	177.4	2.3
Greece	-	-	0.0	-	0.0	0.0	-	0.0	0.0	-	0.0	0.0
Item 6108.31.90 Women or Girls' Pajamas of Cotton (Knitted or crocheted)												
Pakistan	5660	-	4.9	7163	26.6	5.3	11068	54.5	6.4	16439	48.5	7.4
portugal	10410	-	9.0	10979	5.5	8.2	9800	-10.7	5.7	11196	14.2	5.0
Spain	336	-	0.3	268	-20.2	0.2	250	-6.7	0.1	279	11.6	0.1
Greece	2960	-	2.6	3910	32.1	2.9	4990	27.6	2.9	4076	-18.3	1.8
Item 6207.91.00 Men or Boys' cotton singlets and other vests												
Pakistan	2268	-	5.7	5097	124.7	10.7	7691	50.9	16.1	14077	83.0	25.9
portugal	4156	-	10.4	6425	54.6	13.5	7868	22.5	16.5	7874	0.1	14.5
Spain	142	-	0.4	210	47.9	0.4	397	89.0	0.8	182	-54.2	0.3
Greece	2178	-	5.5	50	-97.7	0.1	904	1708.0	1.9	330	-63.5	0.6
Item 5513.41.00 Printed Polyester Fabrics, containing width =<170 G/M2												
Pakistan	4360	-	7.9	7576	73.8	11.6	7590	0.2	12.5	13963	84.0	21.9
portugal	1142	-	2.1	710	-37.8	1.1	314	-55.8	0.5	95	-69.7	0.1
Spain	773	-	1.4	1411	82.5	2.2	1753	24.2	2.9	2727	55.6	4.3
Greece	-	-	0.0	-	0.0	0.0	-	0.0	0.0	-	0.0	0.0

[Value=000 ECUs]

Country	1988			1989			1990			1991		
	Val	GR%	Share %	Val	GR%	Share %	Val	GR%	Share %	Val	GR%	Share %
Item 5407.81.00 Woven Synthetic Fabrics, weighing <85% synthetic mixed with cotton												
Pakistan	98	-	1.0	8284	8373.5	50.8	20258	110.2	69.7	11647	-42.5	58.8
portugal	77	-	0.8	66	-14.3	0.4	35	-47.0	0.1	24	-31.4	0.1
Spain	615	-	6.1	540	-12.2	3.0	1639	203.5	5.6	1431	-12.7	7.2
Greece	-	-	0.0	-	0.0	0.0	-	0.0	0.0	-	0.0	0.0
Item 6404.11.00 Sports Footwear												
Pakistan	10325	-	2.2	8143	-21.1	1.5	6545	-19.6	1.2	11417	74.4	1.7
portugal	2318	-	0.5	2612	12.7	0.5	1745	-33.2	0.3	1508	-13.7	0.2
Spain	4715	-	1.0	6486	37.6	1.2	12193	88.0	2.1	14810	22.3	2.2
Greece	58	-	0.0	38	-35.6	0.0	154	305.3	0.0	93	-39.6	0.0
Item 5202.99.00 Cotton waste												
Pakistan	3409	-	4.5	2978	-12.6	3.1	6574	120.8	5.3	10500	59.7	8.5
portugal	1886	-	1.5	1206	10.0	1.2	554	-54.1	0.4	497	-10.3	0.4
Spain	492	-	0.7	1212	146.3	1.2	896	-26.1	0.7	932	4.0	0.8
Greece	9205	-	12.2	11387	23.7	11.7	12480	0.0	10.1	12571	0.7	10.2
Item 6107.21.00 Men or Boys' Nightshirts and Pajamas of cotton												
Pakistan	3289	-	3.1	4885	51.6	3.8	5039	1.1	3.7	10288	104.2	5.5
Portugal	7501	-	7.0	11464	52.8	8.8	14273	24.5	10.4	14477	1.4	7.7
Spain	275	-	0.3	240	-12.7	0.2	348	45.0	0.3	237	-31.9	0.1
Greece	5151	-	4.8	6630	28.7	5.1	7263	9.5	5.3	8674	19.4	4.6

Note:Val=Value and GR= Growth Rate. Share percentage in the EEC's total imports.
Source: Eurostat, External Trade (microfiches), concerned years.

Table 6.A.II

COMPARATIVE EXPORT PERFORMANCE OF PAKISTAN AND THE EC'S NEW MEMBERS IN THE EC MARKET [OTHER ITEMS]

[Volume= Tonnes]

Country	1988			1989			1990			1991		
	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI
Item 5205.12.00 Cotton Yarn measuring <174.29 Decitex but >= 232.56 Decitex												
Pakistan	4265	2.4	100	4409	2.3	95	10556	2.3	93	7441	2.5	102
portugal	887	3.6	100	1225	2.9	80	1360	3.1	86	1824	3.1	84
Spain	6443	2.6	100	7719	2.4	93	11412	2.5	96	7929	2.5	97
Greece	9043	3.0	100	11238	2.8	94	8681	3.2	107	7699	3.1	103
Item 6109.10.00 T-Shirts, singlets and other vests of cotton (Knitted or crocheted)												
Pakistan	1313	7.2	100	1677	7.5	104	2594	7.2	100	2244	7.5	105
portugal	4527	20.0	100	7316	19.9	100	9302	21.2	106	10341	22.4	112
Spain	275	25.5	100	237	26.7	105	306	25.6	100	439	22.0	86
Greece	8907	18.2	100	11801	18.5	102	12428	20.0	109	12493	20.8	114
Item 4203.29.10 Protective Gloves of Leather or composition of Leather												
Pakistan	1412	8.1	100	1523	8.0	98	1951	8.5	105	1902	8.7	108
portugal	1	12.0	100	1	41.0	342	5	12.4	103	26	17.2	143
Spain	37	30.4	100	39	34.8	114	47	34.9	115	48	94.6	311
Greece	-	0.0	100	-	0.0	-	-	0.0	-	-	0.0	-
Item 6108.31.90 Women or Girls' Pajamas of Cotton (Knitted or crocheted)												
Pakistan	821	6.9	100	1005	7.1	103	1742	6.4	92	2324	7.1	103
portugal	757	13.8	100	748	14.7	107	624	15.7	114	718	15.6	113
Spain	13	25.8	100	12	22.3	86	10	25.0	97	11	25.4	98
Greece	154	19.2	100	201	19.5	101	231	21.6	112	215	19.0	99
Item 6207.91.00 Men or Boys' cotton singlets and other vests												
Pakistan	430	5.3	100	928	5.5	104	1604	4.8	91	3015	4.7	89
portugal	436	9.5	100	661	9.7	102	816	9.6	101	708	11.1	117
Spain	6	23.7	100	14	15.0	63	34	11.7	49	16	11.4	48
Greece	191	11.4	100	9	5.6	49	45	20.1	176	13	25.4	223
Item 5513.41.00 Printed Polyester Fabrics, containing width =<170 G/M2												
Pakistan	916	4.8	100	1448	5.2	110	1682	4.5	95	3015	4.6	97
portugal	128	8.9	100	95	7.5	84	37	8.5	95	9	10.6	118
Spain	66	11.7	100	118	12.0	102	130	13.5	115	273	10.0	85
Greece	-	0.0	100	-	0.0	0	-	0.0	0	-	0.0	-

[Volume= Tonnes]

Country	1988			1989			1990			1991		
	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI	Vol	UV	UVI
Item 5407.81.00 Woven synthetic Fabrics, weighing <85% synthetic mixed with cotton												
Pakistan	25	3.9	100	2827	3.3	84	8207	2.5	63	4576	2.5	65
portugal	12	6.4	100	7	9.4	147	9	3.9	61	6	4.0	62
Spain	92	6.7	100	79	6.8	102	221	7.4	111	210	6.8	102
Greece	-	0.0	100	-	0.0	0.0	-	0.0	-	-	0.0	-
Item 6404.11.00 Sports Footwear												
Pakistan	3252	3.2	100	2146	3.8	120	1890	3.5	109	3067	3.7	118
portugal	165	14.0	100	242	10.8	77	162	10.8	77	138	10.9	78
Spain	453	10.4	100	599	10.8	104	1168	10.4	100	1430	10.4	100
Greece	6	9.8	100	2	19.0	193	14	11.0	112	7	13.3	135
Item 5202.99.00 Cotton waste												
Pakistan	4524	0.8	100	3819	0.8	100	7694	0.9	113	12951	0.3	100
portugal	2396	0.5	100	2451	0.5	100	1136	0.5	107	919	0.6	120
Spain	707	0.7	100	2029	0.6	86	1432	0.6	90	1461	0.6	90
Greece	14709	0.6	100	18076	0.6	101	14502	0.9	138	15270	0.8	133
Item 6107.21.00 Men or Boys' Nightshirts and Pajamas of cotton												
Pakistan	510	6.4	100	728	6.8	106	802	6.3	97	1456	7.1	110
Portugal	564	13.3	100	737	15.6	117	845	16.9	127	822	17.6	132
Spain	13	21.2	100	10	24.0	113	14	24.9	118	9	26.3	124
Greece	352	14.6	100	433	15.3	105	464	15.7	107	536	16.2	111

Note: Vol=Volume; UV= Unit Value and UVI= Unit Value Indices.
Source: Eurostat, External Trade (Microfiches), concerned year.

CHAPTER 7

AN EMPIRICAL INVESTIGATION OF MOTIVATING FACTORS OF FOREIGN DIRECT INVESTMENT IN PAKISTAN

Foreign direct investment (FDI) is considered an important vehicle for development, and Pakistan, like most developing countries, has been keen to attract more of it. The virtues supposedly associated with FDI are many: it can helps new jobs which is important in developing countries where unemployment is often a seemingly intractable problem; foreign investment can serve as a useful medium to help raise the technological levels and the management skills of the host country; FDI can make a positive contribution to the balance of payments of the host country because export-oriented investments can help earn much needed foreign exchange while investments for import substitution purposes can help save what little foreign exchange reserves there are in most developing countries including Pakistan. It is not the purpose of this chapter to present all of the arguments in favour of or against foreign direct investments. The point to be made is that most developing countries are convinced that FDI is good and every effort is made to attract it as much as possible. Pakistan is no exception.

In view of Pakistan's economic situation, in order to enhance the pace of industrialisation, export diversification and upgrading, its imperative for Pakistan to rely more on FDI as compared to portfolio transfers. Because FDI is considered a choice which is often preferable to classical forms of lending and which makes technological transfer easier. The purpose of this chapter is to explore the ways and means by which Pakistan can become an attractive site for such investment in relation to its competitors in general and from the EC, in particular.

7.1 Objectives and Plan of the Study

The EC is a net exporter of direct investment capital: investment it makes in other countries is regularly higher than investment it receives from the rest of the world. Similarly, the EC has been Pakistan's major trading as well as aid and investment partner. With the signing of Commercial, Economic and Development Cooperation Agreement (CEDCA) in 1986 with the enlarged EC, which includes in its orbits almost all sectors of the economy, the prospects of increased economic relations including trade, aid and investment are obvious. It, therefore, seems the appropriate moment to be identifying and analysing the factors which are likely to motivate the inflow of foreign direct investment from the EC to Pakistan.

To this end a case study was conducted to explore, what special interest foreign investor might have in mind while creating a subsidiary abroad. The case study was confined to EC firms which have invested and received promotional privileges in Pakistan. A questionnaire was sent to firms belonging to four EC Member Countries i.e., the UK, the FRG, Italy and France which proved to be the county's major partners in the trade, aid and investment sphere and whose names and addresses were available [1]. The main purpose of the questionnaire (which is placed in the appendix at the end of the chapter) was to find the importance of the various factors that have motivated EC investors to come to Pakistan, as well as to identify and rank factors that are of concern to EC investors in Pakistan. It is hoped that the results of the case study, though based only on limited primary data related to promoted EC firms, will provide some insight into the nature of EC investment in Pakistan. However, this chapter starts with the examination of the role that foreign capital assistance has played in the economic development of Pakistan.

7.2 Capital Inflows and Economic Development in Pakistan

It is obvious from the previous analysis that Pakistan has since its inception relied heavily on foreign capital assistance and the EC countries both at the multilateral and bilateral levels have been its major source of such resources. Foreign capital assistance in its various forms (for example, project aid, commodity aid, food aid, BOP support, etc.) has played a key role in the economic development of Pakistan. Not only it has supplied resources which could not be mobilised easily in an economy with low per capita income and savings, more efficiently, it put at the disposal of Pakistan scarce foreign exchange without which basic investment and consumption could not have been satisfied. It is interesting to explore whether foreign capital assistance played a positive role in the economic development of Pakistan or caused greater indebtness over the years.

From the capital importing country's point of view the use of external resources should facilitate a push of national GDP growth rates in such a way as to permit future debt servicing out of additional income generated through the productive employment of external resources. The determination of an adequate debt burden based on this consideration can be regarded as some kind of an economy-wide investment problem under uncertainty. As such, the success of foreign lending is open to changes in the factors which determine the efficiency of the development programme. Emphasizing this investment aspect of international lending allows us to distinguish between two major problem areas.

First, changes in the international environment pose a permanent threat (and a chance) to the actual performance of the economy. This is the case, for example, when the international economy suffers from an extended period of depression., so that export prospects become cloudy and terms of trade (eventually) deteriorate. These kinds of macro disturbances, however, are very often accompanied or even caused by external shocks which might change relative prices in the long run.

Secondly, there may be an inadequate use of capital inflows in the importing country itself, so that the rate of return on capital falls short of plannings. This threat to future debt servicing capacity appears to be especially pronounced in countries which suffer from internal economic and political instability and which persistently sustain a highly distorted incentive system.

Another form of the inadequate use of external credit takes place, if it is used to raise the national consumption level instead of adding to productive ventures. When capital inflows are used to substitute for national savings (in the case of saving constraint) or imports of consumer goods are increased (in the case of foreign exchange constraint), no additional income is likely to be generated and future debt servicing has to be financed out to be unchanged GDP. As regards the debt servicing capacity, credit financing of current expenditure and misallocation of inevitable funds appear to be almost equivalent. In both cases the return on total capital inflows will be negatively effected and servicing of debt out of increased GDP becomes doubtful.

Evaluating a country's debt position and establishing its capacity to absorb and repay debt is a complex process. The changes in the external debt situation of a country have long term implications for its capacity to service its present debts and to contract new ones. In economic literature several key indicators (ratios) are used to measure this. In measuring Pakistan's debt burden and debt burden capacity nine indicators (ratios) are used: (i) external debt outstanding to GNP; (ii) external debt outstanding to exports; (iii) debt-service payments to exports (also referred to as debt-service ratio); (iv) debt-service payments to foreign exchange earnings (FEE); (v) debt-service payments to gross national payment (GNP); (vi) international reserves to debt outstanding; (vii) international reserves to imports; (viii) interest payments to GNP; and (ix) interest payments on external debt to exports (also referred as to interest-service ratio).

The results of Pakistan's debt burden and debt-service capacity measurements are reported in Table 7.1. It seems nacessary to analyse major trends and the importance of these ratios here. The debt-service ratio

Table 7.1 SELECTED EXTERNAL DEBT RATIOS OF PAKISTAN

(US $ million)

Year	Total External Debt	Ext. Debt % of		Debt-Servicing % of			Reserves as % of		Int. Payments % of	
		GNP	Exports	Exports	FEE	GNP	Ext.Debt	Imports	GNP	Exports
1970	3425	32.2	815.5	43.3	-	1.7	8.4	37.9	0.8	19.3
1971	3766	32.7	637.2	20.6	-	1.3	5.3	31.2	0.4	8.6
1972	4022	62.0	492.3	23.6	18.1	3.0	7.1	35.8	1.3	10.5
1973	4427	49.4	431.5	19.2	14.2	2.2	10.5	34.0	0.9	7.7
1974	4796	42.3	461.6	23.9	16.3	2.2	8.4	19.1	0.9	10.0
1975	5755	42.7	506.2	21.9	13.7	1.8	8.4	23.5	0.8	9.5
1976	6341	40.4	555.7	27.3	15.3	2.0	9.7	26.4	0.9	11.9
1977	7189	37.8	548.4	24.9	11.2	1.7	6.0	15.3	0.9	12.4
1978	7792	36.8	555.7	25.6	12.0	2.1	13.0	27.5	1.0	11.9
1979	8658	34.0	366.1	24.7	11.9	2.3	10.4	19.1	0.9	9.9
1980	8765	28.9	296.3	20.4	10.6	2.0	18.1	37.3	0.8	8.2
1981	8799	27.0	357.1	19.9	8.8	1.5	21.2	33.2	0.6	8.2
1982	9312	29.3	345.7	23.5	9.6	2.0	15.7	27.3	0.8	9.1
1983	9469	27.7	342.1	26.3	10.9	2.1	24.1	48.5	0.8	9.9
1984	9732	28.3	390.6	31.6	12.9	2.3	22.6	42.1	0.8	10.0
1985	11108	30.5	361.8	29.5	13.4	2.6	10.7	21.1	0.8	9.9
1986	12023	32.0	326.2	29.9	15.5	2.8	13.6	30.4	1.0	9.3
1987	12913	31.7	289.8	25.1	14.7	2.3	13.8	27.9	1.0	9.6
1988	14190	34.2	304.4	24.1	14.3	2.7	19.3	18.9	1.1	9.4
1989	15094	36.2	302.6	24.9	14.4	3.0	18.1	17.7	1.2	9.9
1990	15853	33.9	258.5	21.5	14.0	2.8	19.2	19.1	1.1	8.7

Source: Computed from Economic Survey of Pakistan, various issues.

is the proportion of foreign exchange earnings from merchandise exports which is used to meet debt-service payments. A debt-service ratio of less than 10% is considered desirable; a ratio of 20% is regarded as the upper limit. However, several countries with a ratio of over 20% have been able to avoid rescheduling their debts in the past, while others with ratios of far less than 20% have had to resort to rescheduling. The debt-service ratio is therefore not an acute prediction of existing or potential liquidity problems. Nevertheless, it is widely used when making judgement about a country's immediate creditworthiness. The debt-service ratio as well as debt-service ratio to FEE of Pakistan has declined markedly over the last two decades reflecting the good export performance and adequate inflow of worker remittances from abroad.

The ratio of debt-service payments to GNP takes into account the productive capacity of the whole economy and is a useful indicator because of its long-term implications for a country's debt-servicing capacity. The implication is that if a country's GNP is growing much faster than the growth in the national debt, it may not pose any serious problems. With this in mind the debt-service problem seems not to be very serious in the case of Pakistan. Inspite of increased capital inflow mainly from commercial borrowing on high interest rates, Pakistan has been successful in reducing or at least stabilizing around 2-3% its ratio of debt-service to GNP reflecting the better performance of the economy over the last two decades.

The interest-service ratio is perhaps a better indicator of a country's debt servicing capacity than the debt-service ratio, for as long as lenders have confidence in the economy, they will be prepared to roll over the principal. The interest-service ratio shows the proportion of export earnings that should be committed for the payment of interest. For Pakistan, during the 1970s, the ratio showed an upward trend as a result of increased interest rates and larger volumes of commercial borrowing. However, during the 1980s, the ratio remained fairly constant around 8-9%. Similarly, interest ratio to GNP also remained more or less constant over the last two

decades. As mentioned above, was possible because of the better performance and better management of the economy.

International reserves act as a buffer against fluctuations in foreign exchange earnings. A country with a high ratio of international reserves to debt outstanding or a high ratio of international reserves to imports would be in a far better position to service its debt. Both these ratios for Pakistan had an upward trend until 1984 followed by a sharp decline in subsequent years.

The ratio of debt outstanding to exports is a basic measure of the level of indebtness. This ratio is commonly regarded as an important measure of the risk incurred by lenders. A debtor country is likely to face a high risk of running up arrears when its ratio of debt to exports exceeds the level of 200% (William Cline, 1985). While this general rule should be kept in mind, the concessional nature of most of the debt in low-income countries including Pakistan should be taken into account in evaluating their high ratios. This ratio declined markedly for Pakistan during the last two decades reflecting an appreciation in the long-term debt-servicing capacity of Pakistan.

The ratio of debt outstanding to GNP provides an indicator of a country's debt-servicing capacity in the long term. The implication of this ratio is that if debt increases faster than GNP over a long period, the debt burden will become heavy. This ratio for Pakistan rose significantly in the first half of the 1970 mainly due to the poor performance of the economy. Nevertheless, with the better performance and management of the economy during the 1980s, this ratio declined markedly.

To sum up, the nine indicators together show that the debt-servicing capacity of Pakistan has improved markedly over the last two decades. This indicates that over the years Pakistan utilised successfully the borrowed resources in productive activities. Consequently, the economy achieved higher growth rates during the last two decades. Pakistan's GDP in constant term grow by 4.9% in the 1970s and by 6.5% in the 1980s (PES, 1992/93, p.2). On the basis of ratios measured above, it can be concluded that the debt problem seems not to be very serious in the case of

Pakistan. Factors like the better performance of all the sectors of the economy, productive utilisation of borrowed resources, better management of the economy and above all, the political stability which the country enjoyed, especially during the 1980s, have all supported improved economic situation of the country. Nevertheless, for further progress it is important for Pakistan which has borrowed and intends to further borrow (because its increased exports of goods and services are hardly likely to be sufficient to meet the higher demand for imported capital and technology) from different sources to adopt policies that should attract more FDI as opposed to foreign capital assistance or portfolio transfers.

7.3 FDI Inflows in Pakistan

Trends and Sectoral Distribution: Pakistan has been the second largest recipient of FDI among the South Asian countries. It is important to note that the more positive policy stance adopted by Pakistan over the last decade has led to a marked jumped in inflows of FDI in Pakistan. FDI in Pakistan increased by 321% from only US $21.9 million in 1980 to $92.2 million in 1988. In the 1980s, the average annual inflows of FDI (excluding reinvested earnings() were around US $42 million for Pakistan, around 50 million for India, around $41 million for Sri Lanka and around $2 million for Bangladesh. If FDI is taken in relation to total gross domestic investments, Sri Lanka led the way with 2.1%, followed by Pakistan (1.4%), Bangladesh (0.4%) and India (0.2%) (calculated from World Investment Report, 1992).

These figures are very low in comparison with many economies of East Asia, where FDI inflows of $2-4 billion per annum were not uncommon, and where its contribution to domestic capital formation ranged from 2.2% in the People's Republic of China to 15.2% in Malaysia; 14.4% in Indonesia; and 25.5% in Singapore. The Republic of Korea was an exception at 1.4%, but its combination of nationalistic policies combined with the support of giant domestic private conglomerates was very

unusual. As the technologically most advanced and dynamic of the East Asian NIE, its experience has important lessons for countries like Pakistan which will be discussed later.

It is likely that in the past Pakistan had policies that were perceived as relatively unwelcoming to FDI in comparison to neighbours in Southeast Asia. Despite the adoption of liberal economic policies in the last two decades, Pakistan still has restrictions on activities were FDI would be welcome; this has deterred investments in the simpler labour-intensive industries where local firms are strong (but where foreign investors could add to growth and exports). Some bureaucratic obstacles remain formidable and can serve as an instrument to favour domestic firms, forcing foreign firms to seek alliance with powerful local groups. Labour legislation makes firing of employees (and the exit of firms more generally) difficult. Incentives are not transparently administered.

The sectoral composition of FDI reflects a country's relative stage of industrial development and the impact of past policies. Thus, FDI in Pakistan is moderately concentrated in manufacturing (around 60%), with 40% in services, reflecting the role of Middle East investments in property, hotels and finance. Although, Pakistan started to implement more liberal economic policies in the past two decades, the pace and extent of liberalization has been rather slow. These reforms still lag behind those undertaken in many developing countries, and Pakistan continues to present a poor image to potential foreign investors. Pakistan has a substantial advanced industrial sector and has insisted that foreign investors be directed into high-technology and export oriented activities. Pakistan also has an enormous supply of low-wage, low-skill manpower which could be used to attract foreign investments into garment and other simple assembly activities. Pakistan's export processing zones have not been very successful in terms of creating jobs and exports by East Asian standards. Its labour intensive exports (which have grown impressively in garments and leather products) have been mainly in the hands of local firms. This may have had beneficial effects on domestic enterprise development and

the creation of local linkages, but it may have also retarded the upgrading of Pakistan's garment exports and greater specialization vis-a-vis East Asian exporters.

Pakistan is well endowed with cheap and unskilled labour. It has potentially large market and has enjoyed steady , but not spectacular, rates of growth. It also has substantial advanced industrial capabilities to support a highly diversified and competitive industrial structure. This means that Pakistan can attract a vast variety of foreign investments in manufacturing and sophisticated services if she provides the right incentive climate and infrastructure.

To conclude this section, therefore, there are a number of reasons why we find Pakistan has failed, despite the size of its population and potential for industrial growth, to attract significant amounts of FDI in the past. Some of the constraints are being eased, particularly by reform of the inward bias of the trade regime and the discrimination against foreign ownership. It seems that if Pakistan persists with policy reform, she will clearly increase her attractiveness to international investors. If she is able to mount an efficient industrial strategy, her long term pulling power will be even greater. Nevertheless, the results, in terms of attracting a sustained flow of foreign investments, will vary with the pace of policy implementation. However, we can anticipate that Pakistan may be able to attain substantially higher levels of FDI because she has the substantial industrial base to support efficient operations in a range of simple to complex industries. In the long term, however, Pakistan will need to boost its human capital and improve its labour market, physical and technological infrastructure, and administrative capabilities.

7.4 Determinants of FDI

Dunning (1981) has constructed an eclectic approach which explains why foreign direct investment takes place. According to this theory, there are three sets of determinants of FDI, each relating to an advantage of direct investment over alternative modes of serving the firms customers at home and abroad. The first

necessary condition for FDI is that foreign firms must possess certain assets which its competitors either do not possess or which they have but not in the same degree or on the same patterns. These assets or ownership-specific advantages include technology, marketing, management, access to inputs and markets. The ownership advantage is necessary to outweigh the disadvantage of being foreign.

The second requirement for foreign direct investment is that the enterprise must find a location outside their own country which is attractive enough for the exploitation and internalization of their ownership-specific advantages. The locational advantage may derive from a fundamental comparative advantage, such as an abundance of high-quality, low-wage labour, from relatively low transportation costs, or from policy-determined costs arising from trade restrictions, labour legislation, pollution controls and direct incentives to or restrictions on direct investment.

Finally, even when there is an ownership advantage and a locational advantage there must be an internalization advantage that the enterprises must find it worthwhile to exploit these advantages themselves (i.e., internalize them) rather than to sell them or sell the right to use them to foreign firms. Should all these three conditions be fulfilled, the enterprise will engage in foreign investment abroad. Exporting will be the decision if the location condition is not fulfilled, and portfolio resource transfer (agreements, licensing, etc.) will be the route if only the first condition is fulfilled. Table 7.2 proclaims the conditions determining these choices.

In view of Pakistan's need to enhance the pace of economic development, export upgrading and diversification, it is, therefore, desirable to increase the volume of such flows to the country. This necessitates a clear understanding of the various factors which determine FDI. Above discussion suggests that inflows of FDI are determined by a complex set of economic, political and social factors and that investors look beyond the array of investment incentives (in particular fiscal incentives) offered. Performance requirements and various restrictions and regulations act as disincentives to foreign direct investment and often

Table 7.2 CONDITIONS DETERMINING THE FORM OF FDI

Route of Serving Market	Advantages			
	Form	Ownership	Internalisation	Locational
	FDI	Yes	Yes	Yes
	Exports	Yes	Yes	No
	PRT*	Yes	No	No

* Portfolio Resource Transfer

serve to offset the positive effects of investment incentives. What should be determined in evaluating the policy impact of foreign direct investment is the net incentive effect, taking into account all policies which directly affect business risk, profitability and ability to repatriate capital and investment returns.

7.5 Motivating Factors of FDI in Pakistan: Survey Results

The major sources of Pakistan's foreign direct investment have been the United States, Switzerland, Japan and Member States of the European Community. Among the foreign investing countries in Pakistan, Member States of the EC as a group is currently the largest single source of foreign direct investment in Pakistan. FDI from the EC Member countries encompasses all sectors of the economy including agriculture, industry, energy, infrastructural development, etc. According to Pakistan Investment Guide 1991, in total there were 140 foreign firms engaged in different sectors of the economy. Out of which around 50% firms belong to Member States of the EC. The share of the USA was 22% (31 firms), Switzerland 7% (10 firms) and Japan 6%. The country-wise breakdown of EC firms and their share in

Pakistan was as follow: the UK 27% (37 firms), the Federal Republic of Germany 14% (19 firms), Italy 2% (3 firms), France 1.4% (2 firms), Denmark 1.4% (2 firms), Holland 2.8% (4 firms) and Spain 1.4% (2 firms) [2].

As mentioned earlier, a questionnaire was sent to firms belonging to the four EC Member States i. e., the UK, FRG, France and Italy. Included in this sample in total were forty-five firms, ranging in size from large to medium, producing garments and electronic, metal, and textile products. In this regard 25 firms from the United Kingdom, 15 firms from the FRG, 2 firms from France and 3 firms from Italy whose names and addresses were available have been included in the case study (see appendix). The questionnaire was divided into three parts. The first part dealt with the factors that motivated EC investors to come to Pakistan; the second part concerned with the factors in Pakistan that are of concerns to EC investors; the last part concentrated on the reasons EC investors entered into joint ventures with Pakistani firms.

Only 12 firms (27%) of the consulted firms replied positively in response to our questionnaire. It is important to note that there have been observable differences in the response pattern among the firms belonging to four EC Member States. Around 7 firms (58% of total responded firms) from the United Kingdom and 5 firms (42% of total responded firms) from the FRG responded positively (see appendix). Most of the UK firms regretted or returned the questionnaire unfilled indicating their difficulties in managing these types of questionnaires due to the shortage of manpower. For example, one firm responded "We find that, due to the increasing number of questionnaires being received at our Head Office, our small staff would spend a disproportionate amount of their time completing them. We therefore regret we are unable to accede to your request".

It would be worth mentioning that firms from France and Italy neither responded positively nor negatively. Nevertheless, with this limitation in mind the analyses of the results are considered useful in that they can at least shed some light on EC firm's attitudes towards investing in Pakistan.

7.5.1 Motives for Investment

The question of why multinational enterprises own and control operations abroad has been analysed by a number of authors by using a transaction cost approach. Similarly, the question of why production is undertaken in different countries has been treated as a question of minimizing what could be termed, in broad sense, production costs (see, Buckley and Casson, 1976, Vernon, 1976, Rugman, 1981, and Teece, 1986). In both cases the explanation offered by the theory basically has to do with cost minimisation.

A list of twelve motivating factors were presented to the firms for indicating the most appropriate degree of importance motivating them to invest abroad. This list of factors included many of the concepts contained in the current theories of foreign investment and some a priori reasons for FDI. The factors listed were not mutually exclusive and included motives of a firm investing abroad and characteristics of host country. The results of the survey are presented in Table 7.3.

Because of the possibility of a large volume of business, market size of the host country and cost differentials have a positive impact on the inflow of FDI. This type of behaviour can be observed in our study too. Table 7.3 points out that two groups of factors are regarded as significant motivations for FDI. The first group is concerned with factor supply and factor prices. The pursuit of lower cost structure, especially land cost and cheap labour, seem to be the most important factors. The second group of factors concerns the assurance of a sustained growth of demand in the domestic market. It is because FDI represents the commitment to resources to operations in unfamiliar environments and thus higher risks, firms tend to invest in countries with large market size for compensation. Other empirical studies also do reveal a positive relationship between market size and FDI (see, Agarwall, 1980, Davidson, 1980 and Nigh, 1985).

Table 7.3 MAJOR FACTORS MOTIVATING EC INVESTORS

Motivating Factors	Degree of Importance in Percentage			
	VI	IMP	FI	NI
1. To open up new markets by directly investing Overseas.	25	50		25
2. To get better access to large and expanding markets for the products manufactured.	67	17	16	
3. To obtain higher rates of profits overseas.	8	33	50	8
4. To get better access to raw material source.		42	8	50
5. To gain benefit from cheap labour and land cost (as compared to the cost in EC).	50	42	8	
6. To enjoy favourable policies in favour of foreign firms.	50	33	17	
7. To circumvent trade barriers and/ or import restrictions.	17	25	58	
8. To facilitate the export of products to another country.		42	33	25
9. To avoid governments' environmental control in Europe.			25	75
10. To avoid unfavourable conditions for expansion in Europe.			8	92
11. To match rival's investment in Pakistan.			17	83
12. Other motives (Please specify and tick as appropriate).				

Note: VI= Very Important; IMP= Important; FI= Fairly Important and NI= Not Important.

It is worthnoting that most EC investments in Pakistan are oriented toward production for local markets and investment for the purpose of opening up new markets is an equal important consideration. This is mainly because by temperament, Pakistan's population (120 million in 1993) with more than 3% annual growth rate) is consumption oriented. In particular, the demand for supply of electric energy is increasing at a phenomenal rate of 10 to 12% per annum. Hence, the foreign investor is assured of a sizeable market looking for the good things in life. The geographic location of the country confers additional advantages in export. In close proximity on the Western side Iran and Middle East offer ready markets for export. Overland route to Iran is already shaping into an invaluable link. In the North the traditional silk route offers land access to Southern China. Afghanistan heavily relies on trade from Pakistan.

It is also evident from the analysis of data that favourable policies and the provision of incentives to foreign investors do have positive effects in attracting investors to Pakistan. These "pulling" factors seem to be more important compared to the "pushing" ones like environmental control regulation or unfavourable conditions for expansion in Europe or match rival's investment in general and the EC in particular. Similarly, circumvention of tariffs and import restrictions are not the reasons why the EC firms invest in Pakistan. Nevertheless, the profit motive (as listed in item 3) is not necessarily independent of the other factors; most respondent were candid enough to rank its importance. On the basis of above discussion, it can be concluded that the exploitation of ownership-specific advantages are generally of secondary importance in the firms' decision to go abroad; the location or "pull" factors are of primary importance.

7.5.2 Criteria for Selecting a Host Country

Economic theory predicts that a firm investing in production facilities will choose the location that minimize total costs, given the distribution of demand in local (national) markets. Labour cost differentials, transportation costs, the existing of tariff and non-tariff barriers, as well as government policy (e.g., taxes affecting the investment climate in a given host country) are generally held to be important determinants of location choice. This basic framework has been extended by several authors. Aliber (1970) takes into account the size of foreign markets as well as the "costs of doing business abroad" and Harish (1976) includes the costs of controlling foreign operations. Such costs are likely to be less in familiar markets, that is, markets that are culturally similar to the home country or markets with which company has previous experience.

To understand the importance of location factors in attracting FDI from the EC, we were asked the firms to check the most appropriate factors and give the degree of importance in regard to selecting a host country. Because it is of interest and importance to understand how firms make decision on the selection of host country. Of course, from the criteria ranked by the firms, we also obtain information on the motives for investment. The results are summarised in Table 7.4. It is important to note that reported results in Table 7.4, therefore, also serve to cross-check and supplement those reported earlier in Table 7.3.

The results again suggest that land and labour costs and favourable government policies regarding foreign investment are very important considerations for making FDI. Of course, it is of no surprise that political stability is a prerequisite. This is reflected by the importance accorded to political stability (item 1), and, to some extent, to steady growth of GNP (item 8) and specified government policies on foreign investment (item 3). This uneasiness about Pakistan did not come as a surprise against a backdrop of frequent coups and change in political governments over the years. Table 7.4

Table 7.4 FACTORS IN PAKISTAN OF CONCERN TO EC INVESTORS

Motivating Factors	Degree of Importance in Percentage			
	VI	IMP	FI	NI
1. Political stability in the host country.	67	17	17	
2. Generally good labour relations.	17	75	8	
3. Well specified government policies on foreign investment.	67	25	8	
4. Availability of low cost land and labour.	83	17		
5. Availability of specific types of raw materials, material components and semi-manufactures.	25	33	25	17
6. Favourable attitude of the general public toward foreign investment.	42	42	16	
7. Favourable geographical location.	25	17	58	
8. Steady growth of national income of the host country.	17	58	25	
9. Adequacy of infrastructural facilities.	33	42	25	
10. Favourable balance of payments conditions and stable external value of the national currency.	25	42	33	
11. Availability of local financial capital.	8	33	58	
12. Availability of skilled labour.	50	42	8	

cont'd overleaf

Table 7.4 FACTORS IN PAKISTAN OF CONCERN TO EC INVESTORS – continued

Motivating Factors	Degree of Importance in Percentage			
	VI	IMP	FI	NI
13. To gain profits from size and potential of the host country's market for the products manufactured.	25	67	8	
14. Provision of investment incentives by the host country:				
14.1 Income tax exemption.	8	67	25	
14.2 Tariff protection.	50	42	8	
14.3 Exemption or reduction of duties on imported materials.	42	50	8	
14.4 Favourable conditions for foreign exchange remittances.	75	25		
15. Efficient government supportive services to foreign investors.	42	33	25	
16. Availability of auxiliary industries and ancillary services in the host country.		33	67	
17. Existence of knowledgeable local investment partners.	8	50	42	
18. Others (Please specify and rank degree of importance).				

Note: VI= Very Important; IMP= Important; FI= Fairly Important and NI= Not Important.

confirms the findings given in Table 7.3 that factor cost and factor availability are the important location factors. The factors of production concerned are labour and land. The cost and availability of capital have seldom if ever been problems to EC investors.

Furthermore, it is also evident from the above mentioned table that good infrastructure, government efficiency, tax concession, and absence of foreign exchange control should be of some importance in the selection of host country. It can be derived from results that most of EC firms seem to set up subsidiaries in Pakistan for cost reduction and capturing the host country's market. This is reflected by the importance accorded to potential and size of the host country's market for the products manufactured (item 13) and availability of low cost land and labour (item 4). The availability of component and semi-manufactures is given a relatively low importance. While in selecting a host country, good labour relations, good attitude of general public and well specified government policies toward foreign investment were given a great importance.

The results of Table 7.4 again are supportive to the earlier conclusion that the "pulling" factors of a growing market in Pakistan and investment incentives offered by the government are important in the selection of a host country for investment. The existence of knowledgeable local partners is another factor of concern indicated by the respondent. It is so because the decision to undertake a FDI in a particular country is the outcome of a decision process where projected revenues and costs are evaluated. Increased knowledge of a foreign country reduces both the cost and the uncertainty of operating in a foreign market, and should increase the probability of an investment being made in the country (Buckley and Casson, 1981). It is also interesting to note that the investors appear not too concerned with the availability of auxiliary industries and ancillary services. This may be due to the fact that most of the EC Firms operate on a self-sufficiency basis-either providing those services themselves or requiring little support from such services.

Similarly, geographic proximity of the home country and the host country, representing a lower cost of managing foreign subsidiaries, should have a positive impact on the inflow of FDI to the host county. The closer geographically two countries are, the higher the possibility of them sharing similar culture. Thus, geographic proximity not only implies lower monitoring and communication costs for subsidiaries in foreign countries, it also implies fewer difficulties in managing foreign subsidiaries caused by unfamiliar foreign culture. One concept that has similar implications to geographic proximity is psychic distance. Psychic distance is defined as factors that prevent or disturb the flows of information between firms and markets. Examples of such factors in the international context are difference between the home and the host country in language, culture, political systems, level of education, level of industrial development, etc. It has been shown that psychic distance has a significant impact on the time order of establishing foreign operations in new host countries. Empirical findings on the impact of geographic proximity on FDI also suggest a positive relationship (Davidson and McFetridge, 1985 and Rugman, et al, 1985).

It is clear from the above discussion that business and family connections, and language and cultural affinity, is another set of motives for selecting host country which were not included in our questionnaire due to simplification purpose. Conventionally, it is believed that these factors are important in explaining the direction of EC bilateral investment in Pakistan. The pattern of EC bilateral investment examined in chapter 3, especially the UK investment in Pakistan, seems to have a great influence of these factors. However, the examination of EC's pattern of bilateral and multilateral investment in Pakistan seem to suggest a decreasing importance of geographic proximity on foreign direct investment over time. The increased bilateral and multilateral investment from the EC in Pakistan seem to be supportive of this view.

7.5.3 Motives concerning Joint-Ventures

In the above discussion, it seems that we have placed very heavy emphasis on the location factors in pulling EC's FDI in Pakistan. However, as the local firms in the host country enjoy all the location advantages and in addition have the advantage of familiarity with the local situation, EC firms must possess some advantages over the local firms for them to be competitive. There is no question about the competitiveness of EC's firms with local firms, but to compete with other firms from the USA and Japan, there might be some difficulties. Undoubtedly, the EC firms operating in Pakistan are possessing better management and marketing skills than the local firms. In addition, they possess, depending on circumstances, more advanced and more appropriate technology with a much longer experience in production as opposed to the local firms.

The picture that we have obtained is therefore that the EC firms are initially attracted by location factors, but FDI is not made until they find that they have some ownership specific advantages over the local firms. Of the various ownership-specific advantages, superior and appropriate technology, overall experience and better management and marketing skills are the major advantages. It is easy to see that proprietary assets in the form of longer experience and better management and marketing skills can be exploited much more easily and more profitably through internalization rather than by selling them or selling the right to use them. The EC firms when making FDI are perhaps strongly motivated by the desire to reduce costs of production; they accordingly gave higher degree of importance to the location motives.

The last part of questionnaire shed lights on motives responsible for increased EC investment in Pakistan in the spheres of joint-ventures. The main purpose of this was to find out some reasons and suggest some ways for further increase of EC's investment in the form of joint-ventures in Pakistan which is supposed to be more useful bringing better experience, marketing and management skills and enhancing

the technological level of local firms. Table 7.5 evinces the survey results concerning the motives for the EC investors to enter into joint-ventures with local firms in Pakistan. Nonetheless, results also serve to cross-check and supplement those reported earlier. The Pakistani partners acquaintance with local labour market, local market conditions and practices seem to be important motivating factors for EC investors to enter into joint-ventures with Pakistani partners as opposed to obtaining local finance. It seems so because firm-specific advantages and resources have a positive correlation with a firm's FDI activities. FDI usually requires a large investment in obtaining information, and setting up foreign operations. Investing firms, facing these cost advantage, have to compete with local firms. Therefore, large firms seem to be more capable of absorbing the cost and risks involved, and to possess more advantages to offset the disadvantageous position. Thus, size represents a major advantage as well as resources for a firm to go abroad. Other many empirical studies also confirm this relationship (Buckley, Peter and Mark Casson, 1976, Buckley and Pearce, 1979 and Lipsey, et al, 1983).

Another important reason for entering into joint-ventures seems to be to gain acceptance by the Pakistani public and government. The government, of course, through the Bureau of Investment, can, but rarely does, exercise its authority to require foreign investors to take on Pakistani Partners. The need to obtain additional local capital from local source and to use outstanding machinery do not appear to be important factors sought after by EC investors when entering into joint-ventures with the local firms. It indicates the fact that, of course, the EC firms have better technology and strong financial conditions as opposed to local firms. In line with the findings of Cohen (1975) on foreign firms in East and Southeast Asia, diversification of risks is an important consideration in the decision for EC firms to go abroad in general and in Pakistan, in particular.

To sum up, generally the most important factors that may influence investment decisions include the recipient country's development strategy, its market philosophy,

Table 7.5 REASONS FOR THE EC INVESTORS TO ENTER INTO JOINT-VENTURES WITH PAKISTAN

Motivating Factors	Degree of Importance in Percentage			
	VI	IMP	FI	NI
1. To increase the sales of capital goods or other intermediate inputs to Pakistani market.	20	50	20	10
2. To enjoy special incentives provided by Pakistan to foreign and domestic investment.	20	70	10	
3. To obtain local finance.	10	20	50	20
4. To reduce risk.	30	40	30	
5. To benefit from your Pakistani partner's acquaintance with:				
(a) the local labour market.	30	50	10	10
(b) the local market conditions and practices.	60	30	10	
(c) local governmental services.	20	60	20	
(d) local financial sources.	10	30	50	10
(e) local sources of material supply.		50	40	10
6. To gain better public acceptance by the Pakistani people and the government.	30	50	20	
7. To make use of outstanding machinery used in partner's firm.		20	30	50
8. To match the investment of competitor in Pakistan.		30	40	30
9. Others (Please specify and rank degree of importance)				
10. Any other comments. (Please use the back of this page if necessary).				

Note: VI= Very Important; IMP= Important; FI= Fairly Important and NI= Not Important.

the size and potential growth of its domestic market, the provision of fiscal incentives and the country's natural resource endowment. In practice, the relative importance of these factors has been shown to vary from country to country and over time. Despite the substantial incentives offered to potential investors, countries with small domestic markets and limited natural resources in Africa and Caribbean have been unable to attract significant inflows of direct investment. On the other hand, the faster growing NICs in Southeast Asia have been able to attract FDI on the basis of their export-oriented development policies without significant incentives. Most FDI in manufacturing has been to serve protected host-country markets. Without protection, the foreign company may have preferred to export than to invest in the developing countries.

The past experience shows that countries which have adopted more outward-oriented development policies have encountered fewer problems with direct investment. With such policies, production for either domestic or export markets is made equally attractive. The result is that investments which have taken place reflect the country's comparative advantage. This in turn, has reduced the need to offer incentives that distore factor proportions or to impose restrictions in the outflow of profits as these countries have been able to adjust to change in the international economic environment.

It is unclear as to whether the provision of incentives matter much in raising the overall level of FDI in developing countries including Pakistan. Various studies (for example, Reuber, et al, 1976 and Guisinger and Associates, 1985) have suggested that those incentives are not of great importance in decision-making about investment. In one study, only 13 per cent of respondents ranked host-country incentives among the top three factors affecting investment decisions in developing countries in 1983. In a recent study, however, incentives were found to be of importance in two-thirds of investment decisions. In our study too the provision of these incentives proves to be of secondary nature. However, the provision of such incentives has been important in the sense that in their absence, either the investment

would not have been made, or made in a different country. It reveals that incentives appear to matter less in affecting the aggregate flow of FDI but more its allocation among countries. For example, if a firm has decided to invest abroad, the choice of location takes both incentives and performance requirements into account. Similarly, if a particular country eliminates all incentives, it might lose some new investments to its neighbours who do not. Perhaps most important is that once changes are introduced into the overall environment towards the private sector and FDI, in particular, through increased host country regulations and intervention, no specific incentives can encourage foreign investment. Thus, the contribution of FDI to the development process depends significantly on the policy framework within which the investment takes place.

7.6 Benefits and Costs of FDI: Lessons for Pakistan

The development impact of foreign investment on host country has always aroused great controversy, but this controversy has subsided greatly in recent years. As noted earlier, a number of factors have led developing countries to change their earlier trade, industrialization and investment strategies. Prominent among these is the realization that FDI does not have many of the costs previously associated with it and that many developing countries have managed to industrialize successfully with FDI. It will be noted that open door policies to FDI are neither necessary nor sufficient to ensure industrial (or any other form of) development. However, in the right circumstances FDI does offer many benefits, and alternatives may not be equally open to country like Pakistan.

The contribution that FDI can make are well known. Apart from finance, which is increasingly am important consideration to countries like Pakistan with mounting debt burdens, FDI can bring in new technology and provide continuous access to changes in technology. Moreover, it can import new managerial and marketing skills; stimulate domestic consumption, provide entry into export markets and helps lower protective barriers in the home countries of MNCs; and help local

suppliers improve their quality and competitiveness. More generally, in a world of growing technological progress and rising costs of keeping up with such progress, alliances with MNCs may be an essential requirement for Pakistan to participate in sophisticated technologies.

It is important to note at the start that the benefits of FDI, like those of any other investment, depend crucially on broader economic framework in which investments are made. When the incentive structure is distorted and competition stifled by widespread, uneconomic regulations, FDI can be inefficient. The benefits of FDI can be maximized only in a relatively free and market-oriented environment where private economic decisions do not diverge greatly from the social good. This does not, however, mean laissez faire, completely free market without intervention.

The experience of East Asian NIEs illustrate clearly the benefits of export orientation combined with high levels of government intervention. The Republic of Korea, in particular, intervened heavily in almost every aspect of industrial activity. It protected infant industries, promoted large private groups, subsidized and directed credit for selected activities, targeted exports, pushed the growth of research and development, and invested heavily in the educational and institutional support needed for industrial growth and competitiveness. It also restricted foreign entry, confining it to activities where local enterprise were unable to gain access to, or keep up with, the advanced technologies involved (Alice Amsden, 1990). This enabled it to develop the indigenous industrial sector more vigorously as it diversified into complex industries, forcing it to invest massively in technological effort to compete internationally. The outcome was perhaps the most compressed and rapid experience of industrial development witnessed in modern times.

The lessons of Korean experience for Pakistan are mixed. The pattern of interventions in Pakistan in trade and industry have been different from those in the Republic of Korea. Inward orientation and controls on economic activities in Pakistan were directed at other objectives than efficiencies and led to technological lags and stagnation. Established local industries did not make a significant mark in world

markets or keep up with technological frontiers. Internal competition was unduly restricted, as was the inflow of foreign technologies. Protected Pakistani enterprises are now enough "mature" and need the stimulus of foreign competition and access to foreign technologies to become efficient and competittive. Past restrictions on foreign entry may have outlived their usefulness as an aid to local "infant" enterprises.

There is clearly a need for further liberalization in Pakistan to remove the more inefficient of past interventions and make industries more export oriented. In this context, a liberalization of FDI regulations can be very useful input into the more general liberalization of trade and domestic competition. However, this is not the only lesson of East Asia NIEs. The other is that the process of liberalization, including that on FDI, has to be controlled and integrated with a set of efficient interventions.

In this context, the experience of Republic of Korea suggests strongly that indigenous technological effort is imperative for industrial dynamism, and reliance on FDI must not substitute for local research and development (R&D). Foreign technology, in whatever form, should only be an input into a continuous local process of absorption and upgrading. Passive dependence on foreign technology can transfer the results of innovation done elsewhere, but it cannot provide a domestic base of technological capabilities that long-term growth and diversification requires.

Of all the models of technology transfer, FDI carries the largest risk of creating such dependence. MNCs are the world's leading generators of new technology, but their innovative activities remain centralized in the developed countries. There are sound economic reasons for this from the MNC perspective. There are large economies of scale in conducting innovative R&D, so that it is costly for MNCs to set up research activities in host countries. R&D requires advanced skills that most developing countries lack and also need interaction with other innovators, research institutions, universities and technology infrastructure institutions, all of which also tend to be weak in many developing countries. FDI then becomes a very efficient means of transferring the results of innovation rather than the innovative process itself.

This may not matter for developing countries with relatively small industrial bases and weak capabilities. It does matter for Pakistan that have a base of innovative capabilities and can fruitfully add to it. The entry of foreign investors then has to be controlled and directed to promote the development of local innovative capabilities. FDI should be encouraged when it feeds into local innovation and should be restricted when it threatens to substitute for local innovation. Where possible, foreign investors should be stimulated to undertake local adaptive and innovative effort. Local enterprises should be encouraged to enter into joint ventures with technological leaders as well as investing in their independent R&D. Both local and foreign firms should be encouraged to utilize the large science and technology infrastructure, with its extensive research and development facilities and its pool of qualified manpower. Where necessary, the government must step in to assist indigenous innovation and to coordinate the technological efforts of local firms.

The second lesson of the Republic of Korea is that the liberalization process in general should be gradual and controlled. The process of exposing industries to international competition has different implications for three different categories of industries. The first category includes mature industries where the relative simple technology have been mastered and are already competitive in world markets. These industries should be exposed to world markets immediately and given all the facilities needed to export.

The second includes those that are intrinsically unviable: these "white elephants" should be allowed to close down as soon as possible and resources shifted from them with as little social disruption as possible. The third category is more complex. It includes enterprises that have complex technologies and are not currently competitive, but are potentially so if given time and support to "re-learn" new skills and technologies. These probably comprise a large part of the industrial sector in Pakistan, with substantial manufacturing activity. They can only be exposed to direct import competition gradually, with selective assistance to upgrade their capabilities: in other words, selective interventions have to be retained. The retention of

instruments of intervention has to be extended to introduction of new industries that have difficult and expensive learning periods (the infant industries of future). Each of these temporarily protected industries, however, has to be persuaded and induced to enter export markets as quickly as possible to offset the disincentive of effects of protection: this is perhaps one of the most important lessons of the industrialization of the Republic of Korea for Pakistan.

The conclusion of this discussion is that FDI does offer substantial benefits to Pakistan if combined with a gradual and well-conceived plan of economic liberalization and domestic capability development. In the last analysis, "market friendly" interventions remain necessary for industrial development, and selective interventions should be retained in the move to greater reliance on FDI. Investment promotion programmes should reinforce the bottom-up approach. Incentives should be addressed to industrialised countries' firms as well as to those of developing countries. On the other hand, programmes for improving the performance of joint ventures should be undertaken by joint institutions, with host country partners playing a decisive role. However, Pakistan has traditionally been the country where government interventions have done the most economic harm in the past, and the time is now ripe for a massive dismantling of controls and regulations. In a future ideal policy regime, only a very few instruments of intervention should be retained and they should be used very sparingly. The EC, being the group of most industrialised countries, can play an important role in enhancing the pace of Pakistan's economic development through increased development cooperation. The challenge for both Pakistan and the EC is to find ways in which the EC could provide positive assistance in the form of investment in future.

7.7 Concluding Comments

This chapter has attempted to provide a better understanding of motives for attracting foreign direct investment in Pakistan in general and from the EC, in

particular. It has also appraised the role of foreign direct investment and foreign capital assistance in the economy of Pakistan. The study revealed that they have contributed significantly to the economic growth and efficiency of Pakistan over the years. There are indications that foreign direct investment has contributed more than official flows or foreign capital assistance, supporting the view that in addition to financing capital formation, it has also facilitated the transfer of technology, technical know-how, marketing and managerial skills.

The analysis of various factors motivating foreign direct investment pointed out that the exploitation of ownership-specific advantages are generally of secondary importance in the firms' decision to invest abroad; the locational or "pulling" factors are of primary importance. The "pulling" factors such as growing domestic market and availability of cheep and skilled labour and the provision of various incentives seem to be more effective in attractive foreign investment compared to the "pushing" factors like environment control regulations or unfavourable conditions for expansion in the EC Member States. However, an important prediction indicated by the case study is the existence of a stable political and economic environment accompanied by outward-looking development strategies and realistic financial and exchange rate policies.

The study suggests that Pakistan's foreign investment policy must gradually be evolved toward a much greater degree of flexibility, in order to attract more of it and to adopt a rapidly changing international environment. Naturally, a key objective of Pakistan's investment strategy must be the rapid increase of manufactured exports, in order to relieve the country's foreign exchange constraint. In order to achieve such a goal, foreign investment in the country must contribute to the development of a highly efficient productive structure, fully able to compete in international markets and to lower the domestic price level through greater competition. Evidently, the task of transforming the structure of industrial output to make Pakistan's exports more competitive in foreign markets opens ample possibilities for different type of cooperation with modern firms located in the EC member countries.

Notes to Chapter 7

1. Names of EC's Promoted Firms were obtained from Pakistan Investment Guide 1991, while address were obtained from Kompass, various issues, available in the Mitchell Library, Glasgow, the United Kingdom.

2. The share of these countries in Pakistan's total investment has been calculated by the author obtaining data from Pakistan Investment Guide 1991, Ministry of Industries, Islamabad, pp. 125-129.

APPENDIX TO CHAPTER 7

The attached questionnaire was sent to the firms included in our study. The main purpose of the questionnaire was to find out the importance of various factors that have motivated EC investors to come to Pakistan, as well as to identify and rank factors that could be of concern to EC investors in Pakistan. It was divided into four parts. The purpose of part I was to obtain general information about the firm concerned. Part II dealt with the factors that have motivated EC investors to come to Pakistan. Part III coped with the factors that could be of concerns to EC investors in Pakistan. Finally, Part IV was concentrated on the identification of reasons why EC investors entered into joint ventures with Pakistani firms. List of consulted EC firms in Pakistan is also attached herewith.

Questionnaire

PART I GENERAL INFORMATION.

1. Name of Firm.

2. Year of Establishment in Pakistan.

3. Major Products.

PART II MAJOR FACTORS MOTIVATING EC INVESTORS. Please tick [ ] the most appropriate column.

Motivating Factors	Degree of Importance: Very important	Important	Fairly important	Not important
1. To open up new markets by directly investing Overseas.	.....	.....	.....	.....
2. To get better access to large and expanding markets for the products manufactured.	.....	.....	.....	.....
3. To obtain higher rates of profits overseas.	.....	.....	.....	.....
4. To get better access to raw material source.	.....	.....	.....	.....
5. To gain benefit from cheap labour and land cost (as compared to the cost in EC).	.....	.....	.....	.....
6. To enjoy favourable policies in favour of foreign firms.	.....	.....	.....	.....
7. To circumvent trade barriers and/ or import restrictions.	.....	.....	.....	.....
8. To facilitate the export of products to another country.	.....	.....	.....	.....
9. To avoid governments' environmental control in Europe.	.....	.....	.....	.....
10. To avoid unfavourable conditions for expansion in Europe.				
11. To match rival's investment in Pakistan.	.....	.....	.....	.....
12. Other motives (Please specify and tick as appropriate).	.....	.....	.....	.....

PART III FACTORS IN PAKISTAN OF CONCERN TO EC INVESTORS.

Motivating Factors	Degree of Importance			
	Very important	Important	Fairly important	Not important
1. Political stability in the host country.	.....	.....	.....	.....
2. Generally good labour relations.	.....	.....	.....	.....
3. Well specified government policies on foreign investment.	.....	.....	.....	.....
4. Availability of low cost land and labour.	.....	.....	.....	.....
5. Availability of specific types of raw materials, material components and semi-manufactures.	.....	.....	.....	.....
6. Favourable attitude of the general public toward foreign investment.	.....	.....	.....	.....
7. Favourable geographical location.	.....	.....	.....	.....
8. Steady growth of national income of the host country.	.....	.....	.....	.....
9. Adequacy of infrastructural facilities.	.....	.....	.....	.....
10. Favourable balance of payments conditions and stable external value of the national currency.	.....	.....	.....	.....
11. Availability of local financial capital.	.....	.....	.....	.....
12. Availability of skilled labour.	.....	.....	.....	.....
13. To gain profits from size and potential of the host country's market for the products manufactured.	.....	.....	.....	.....

Motivating Factors	Degree of Importance			
	Very important	Important	Fairly important	Not important
14. Provision of investment incentives by the host country:	.....	.....	.....	.....
14.1 Income tax exemption.	.....	.....	.....	.....
14.2 Tariff protection.	.....	.....	.....	.....
14.3 Exemption or reduction of duties on imported materials.	.....	.....	.....	.....
14.4 Favourable conditions for foreign exchange remittances.	.....	.....	.....	.....
15. Efficient government supportive services to foreign investors	.....	.....	.....	.....
16. Availability of auxiliary industries and ancillary services in the host country.	.....	.....	.....	.....
17. Existence of knowledgeable local investment partners.	.....	.....	.....	.....
18. Others (Please specify and rank degree of importance).	.....	.....	.....	.....

PART IV REASONS FOR THE EC INVESTORS TO ENTER INTO JOINT-VENTURES WITH PAKISTAN.

1. To increase the sales of capital goods or other intermediate inputs to Pakistani market.	.....	.....	.....	.....
2. To enjoy special incentives provided by Pakistan to foreign and domestic investment.	.....	.....	.....	.....
3. To obtain local finance.	.....	.....	.....	.....
4. To reduce risk.	.....	.....	.....	.....

Motivating Factors	Degree of Importance			
	Very important	Important	Fairly important	Not important
5. To benefit from your Pakistani partner's acquaintance with:	.....	.....	.....	.....
(a) the local labour market.	.....	.....	.....	.....
(b) the local market conditions and practices.	.....	.....	.....	.....
(c) local governmental services.	.....	.....	.....	.....
(d) local financial sources.	.....	.....	.....	.....
(e) local sources of material supply.	.....	.....	.....	.....
6. To gain better public acceptance by the Pakistani people and the government.	.....	.....	.....	.....
7. To make use of outstanding machinery used in partner's firm.	.....	.....	.....	.....
8. To match the investment of competitor in Pakistan.	.....	.....	.....	.....
9. Others (Please specify and rank degree of importance)				
10. Any other comments. (Please use the back of this page if necessary).				

LIST OF CONSULTED EC FIRMS IN PAKISTAN

UNITED KINGDOM

1. Unilever Ltd, London, UK.
2. Brooke Bond Leibig Ltd, London.
3. British American Tobacco Co.Ltd.
4. J.B. Coats Glasgow, Ltd.
5. Johnson & Nicholson Group Ltd, London,UK.
6* ICI, Ltd, London, Uk.
7. W. Woodward Ltd, London, UK.
8. Glaxo Group Ltd, UK
9* Smith & Nephew Associated Companies Ltd, Uk.
10. Recket & Colman Ltd, UK.
11. Gulf Oil (Great Britain), London, UK.
12* Shell Petroleum CO. Ltd, UK.
13. Burmah Oil Co. Ltd, UK.
14. British Insulated Callenders Cables Ltd. UK.
15. Brush Engineering Co. Ltd. UK.
16* The English Electric Co. Ltd. UK.
17. W Canning Co. Ltd. UK.
18. EMI Ltd. UK.
19. Filtrona Group of UK.
20. Wellcome Foundation Ltd. UK.
21* Fisons Public Ltd. Co. Uk.
22. I & J Newbery International Sports Ltd. UK.
23* Gray of Cambridge Ltd. UK.
24. Boots Co. Ltd. Notingham, UK.
25* Morgantic Limited, UK.

FEDERAL REPUBLIC OF GERMANY

1. BASF-Aktienge-Selleshaft. Germany
2* Hoechest A.G. Frankfurt, Germany.
3. A. E. G.Akteinge sellschat, Germany.
4* Siemens A. G. Munich, Germany.
5. Countinho Caro & Co. Keramag Wessel-Werk, Germany.
6. Seelecinann Bauman G.M.B.H., Germany.
7* Gebrauder Martin, 7200 Tuttlingen, West Germany.
8* Shering Aktienge Sell Schaft, Berlin, Germany.
9. Agrob. Anlogenban G.M.B.H., Germany.
10. VDO, Adolf, Schindling A.G., Frankfurt, Germany.
11. Kirauf Engineering GUMBTT, Germany.
12. Rolf Bernhard Rode Brigite, Frankfurt, Germany.
13. Klein, Schanzline and Becker AG, Germany.
14* Bayer Handles, Germany.
15. Fuhrameister C. Hamburg, Germany

FRANCE

1. F.F.T.S. Spemobi, Paris-Rue-Baron, France.
2. Prepac Villijunif, France.

ITALY

1. Archfar Laboratories, Italy.
2. Fiat Tractors S.P.A., Italy.
3. Elko Organization, Italy.

* Firms responded positively.

CHAPTER 8

SUMMARY AND CONCLUSIONS

This study was devoted to the examination of the trade and economic relations of Pakistan with the European Community in the context of the latter's special and preferential trade and development policy regime. The EC's economic relations with developing countries broadly consists of the usual combination of trade concessions and aid which are granted to certain groups of developing countries. Most of its development cooperation policy is conducted at the national level. The vast majority of aid and investment, for example, is dispensed by EC member countries through bilateral agreements with the recipients. In the field of trade, the EC of course plays a much more important role. At present the intervention that does occur at the EC level is conducted through a number of channels, principally the Generalised System of Preferences (GSP), the so-called Global Mediterranean Policy (GMP), the Lome Conventions and non-preferential agreements with certain countries in Asia and Latin America.

The evolution of Pakistan's trade and economic relations with the EC started formally with the establishment of diplomatic relations in 1962. An important watershed in their relations was reached after Britain's accession into the EC in 1973. Britain's accession to the EC and its enlargement from six to nine served to reinforce the development of economic relations with the developing countries including Pakistan which had special relations with Britain. Although the focus of Pakistan-EC relations has been on trade, the scope of their economic relations has been enlarged progressively over the years.

At present, the EC is by far the country's single largest trading partner and principal supplier of capital goods and leading donor of foreign capital assistance. Their economic relations now extend beyond purely commercial or sectoral interests to take in various forms of development cooperation i.e. industrial, scientific, technological, etc. Three events, the introduction of EC's GSP, the inclusion of UK

into the EC and the conclusion of commercial cooperation agreement seem to be credible for the increased relationship between Pakistan and the EC. However, the commercial cooperation agreement signed in 1976 can be regarded as the keystone of these relations which provided Pakistan and the EC with a favourable legal basis for expanding their cooperation in the fields other than trade. This expanding relationship is reflected in the new Commercial, Economic and Development Cooperation Agreement, signed in 1986. In the preamble to this agreement the two sides call for closer cooperation across the whole range of commercial and economic endeavour. Cooperation in the field of trade was reinforced and extended to take in economic and development cooperation. In this context, the EC and Pakistan undertook to encourage industrial cooperation and the transfer of technology between their economic operators and to promote scientific and technological cooperation. Provision was also made for development cooperation, with the EC undertaking to intensify its support for Pakistan's development programme.

Examined in this context, major findings of the present study and statement of conclusions can be summarised as follows:

a) The evidence from the examination of EC's external trade and development cooperation regime lends support to the view that the EC's trade as well as development cooperation policies are regionalised, discriminatory in their nature and complicated in their operation. The very complexity of the trade regime governing access to EC market can be seen as a form of trade barriers in itself. This is also reflected in the complex and discriminatory network of EC's external trade relations with non-member countries what has been called a 'pyramid of privilege'- the hierarchy of its trade preference system.

b) What is concerned with the impact of EC's special and preferential trade treatment, the examination of EC's import performance from various developing countries consistent with its trade regime indicates that the pattern of tariff preferences EC grants does not necessarily guarantee success in the export performance of the preferred recipients. Indeed, if tariff preferences were the only

determinant of the recipient country's export performance in the market of the donor country, then one would expect recipient countries to have a more successful performance in this market. Empirical evidence transpired that while the ACP countries enjoyed the most advantageous status in the EC market, they have overall exhibited a much poorer performance in the EC market compared to the Mediterranean countries. Nevertheless, the most successful countries regarding export performance in the EC market have been the Asian and Latin American countries that only benefited from the provisions of the EC's GSP. In comparison, Pakistan's export performance in the EC market has been impressive compared with many GSP beneficiaries and beneficiaries of the GMP and Lome Convention. In the light of this evidence we may conclude that the EC's trade regime, though based on regionalism, has not obliterated the access of Pakistan's exports to its markets. The increased curve of Pakistan's exports and their increasing share of the EC market seem to be supportive of this conclusion.

c) The examination of the effects of MFA restrictions regarding Pakistan's textile and clothing exports reveals the fact that the country earns a significant amount (around 5% of its total exports) of quota premia from the EC market. Thus, Pakistan's losses are partially compensated for the loss of market share by greater profits on the sales she is allowed to make. This study also appraised the argument that if the MFA were brought to an end, one of the effects would be to bring about much greater competition in world markets. This would almost certainly lead to falls in import prices equal to the extent of quota premia accruing to an exporting country. It has been estimated that prices of textile and clothing in the EC would fall between 6-12% based on the height of quota premia accruing to Pakistan from the EC market.

In the case of the EC, there are preferential arrangements, outside the MFA, for Mediterranean and ACP countries. The comparative analysis of Pakistan's export performance in regard to its competitors in the EC market indicated that despite stringent controls and being at the bottom of EC's 'pyramid of privilege', the GSP beneficiary countries fared well in the EC market as opposed to the ACP and GMP

countries who enjoyed more favourable status in the EC market than the former ones. Within the GSP countries, Pakistan's export performance has been much smoother and impressive. Once again this evidence seems to underline the fact that tariff preferences can not in themselves guarantee that a trade relationship will favour the recipient country, although it may be argued that it may moderate the asymmetry in favour of the donor. The evidence of Pakistan's better export performance revealed that the MFA restrictions have not posed any serious threat to the expansion of Pakistan's exports to the EC market. This was mainly due to the emergence of the EC's GSP scheme as a potential policy instrument for resolving Pakistan's trade problems arising out of the MFA constraints. The commodity analysis reflected that Pakistan and many developing countries are thus principally competing for similar markets, although further analysis undoubtedly showed up a greater degree of specialisation at a more disaggregated level indicating that their relative comparative advantages are increasingly residing in different products.

d) Turning to the impact of the EC's second enlargement for Pakistan's exports, the analysis indicated that the beneficial impact of the enlargement has swamped any negative impact of the EC's enlargement. The detailed analysis of growth rates indicated that the EC's enlargement has led to an improvement in Pakistan's trade flows with the enlarged EC. Overall the country experienced a net export expansion in the EC market after the enlargement. This became possible owing primarily to the sharp rise in the export of manufactured and semi-manufactured goods which were granted preferences under the EC's GSP scheme. The EC's GSP scheme emerged as a potential policy instrument for banishing Pakistan's trade problems arising out of Greece, Portugal and Spain's entry into the EC. Under the EC's GSP scheme, Pakistan's manufactured and semi-manufactured exports benefited significantly and some made headway into the EC market. Most importantly, the commodity analysis at disaggregated level pointed out that their comparative advantage remain in different commodities, although at the aggregated level they seem to be competing with Pakistan in the EC market.

Thus, the overall conclusion is that contrary to the belief that Pakistan's trade and economic relations would receive a setback following the EC's second enlargement, it has led to an improvement in Pakistan's overall export flows to the EC market. Empirical evidence did not indicate any large-scale diversionary impact. In the light of the manner in which the Pakistan's exports have fared in the EC market over the period under study, it may be safe to predict bright prospects for the expansion of Pakistan's exports to the EC market in future.

e) The evolution of trade statistics showed that the composition and pattern of Pakistan's foreign trade with the EC has historically shown a great resemblance to those of other developing countries; exports of primary commodities have traditionally accounted for the bulk of its exports. Exports of manufactured items have tended to be made up of traditional, simpler types of manufactures. As a result, there exists the structural imbalance in Pakistan's foreign trade- high propensity to import and relatively low price elasticity of supply of exports together with an exceedingly low capacity to increase export production significantly. This structural imbalance has resulted in considerable deficits in its overall trade and current accounts and forced the country to rely heavily on foreign capital assistance to bridge the resource gap.

The study revealed that in order to enhance the pace of industrialization and to avoid any debt and debt servicing problem, it is imperative for Pakistan to rely more on FDI as opposed to portfolio transfers both as a source of foreign capital and improved technology. FDI has contributed significantly to the economic growth and efficiency of Pakistan, while the EC member countries have been the major source of FDI in Pakistan. There are indications that it has contributed more than official flows or foreign aid, supporting the view that in addition to financing capital formation, it has also facilitated the transfer of technology, technical know-how, marketing and managerial skills. In view of Pakistan's need for further industrialization, export diversification and upgrading and more importantly to be competitive in the world market, it is crucial for Pakistan to attract such flows. An important prediction

indicated by the case study is the existence of a stable political and economic environment accompanied by outward-looking development strategies and realistic financial and exchange rate policies. It suggest that it is crucial for Pakistan to review critically incentive scheme for foreign investors and the regulations imposed on the performance of foreign direct investment. It is, however, noteworthy that specific incentives and regulations governing FDI have had less effect on how much investment a country receives than has its general economic and political climate, and its financial and exchange rate policies.

Finally, the analysis contained in this study is timely as the EC is in a state of flux and its relationship with the developing countries is being altered by internal and external changes. Factors like trade liberalisation within the GATT round, the completion of Single European Market (SEM), the reform of Common Agricultural Policy (CAP) and developments of Eastern Europe are bound to influence the pattern of EC's trade and economic relations with developing countries including Pakistan. Pakistan, like many developing countries, fear the erosion of traditional preferences, diversion of investment, tougher competition on world markets and a reduction of EC source towards its own relatively poorer regions at the expense of official development assistance. It seems that the success of Pakistan-EC economic relations in future will depend largely on how well Pakistan restructures its economy in line with the changing international environment in general and EC in particular. However, these areas are required to be explored by further research.

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