EXPORT BASKET OF PAKISTAN

HOW TO INCREASE EXPORT FOR CONTROLLING TRADE DEFICIT

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49th Common

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[1] 75 years Economic Survey of Pakistan

Available from https://www.finance.gov.pk/75_Years_Economic_Journey_of_Pakistan.pdf

[2] The Express Tribune. Trade deficit widens 32% in Dec [updated 08 January 2021]

Available from https://tribune.com.pk/story/2279112/trade-deficit-widens-32-in-dec

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INTRODUCTION

Britannica[3] defines balance of trade as "….the difference in value over a period of time between a country's imports and exports of goods and services, usually expressed in the unit of currency of a particular country The balance of trade is part of a larger economic unit, the balance of payments (the sum total of all economic transactions between one country and its trading partners around the world), which includes capital movements (money flowing to a country paying high interest rates of return), loan repayment, expenditures by tourists, freight and insurance charges, and other payments." Balance of payments includes all international receipt and payments either business to business, business to consumer as well as those executed by/for the government. In short, it reflects the state of a country's economy to the rest of the world.

If the exports of a country are greater than its imports, the country has a favorable balance of trade, or a trade surplus. On the other hand, if the exports are less than imports, an unfavorable balance of trade, or a trade deficit, exists. Here, import and export refer to both goods and services on both capital and current account. Asset transfers such as grant/sale of mining rights, trademarks, assets etc. comprise of capital account transactions while primary and secondary income payments constitute current account transactions. Capital account transactions are indicative of the country's finance portfolio in terms of foreign investments and FCY loans.

Primary income payments refer to payments made outside a country such as interest payments, dividends or remittances/ return/ profit paid to foreign investors or non-resident institutes. Secondary income moves between residents and non-residents and includes, amongst others, private/ individual remittances to other countries as well as government grants/ aid given outside the country. These current account transactions signify the resident's consumption patterns.

In simplistic terms, a trade deficit refers to a country buying more services and goods than it is selling. This may also indicate that the residents have sufficient resources to buy more goods and

[3] Britannica, T. Editors of Encyclopedia. "balance of trade." Encyclopedia Britannica [updated 25 September 2019] Available from https://www.britannica.com/topic/balance-of-trade.

services than what are being produced and exported, hence the need for imports to satisfy consumer demands. Generally it is assumed this would hurt the deficit running country's economic growth and job creation. However, to many economists, trade deficit is more about the imbalance between the country's investment rates and savings. When a country spends more on its imports it can make up for the shortfall for e.g. by borrowing money from international lenders or permitting foreign investments in its assets. If this borrowed money or investment is used wisely it can end up boosting the economy as what happened in the 1800s in the United States (U.S) where its utilization on railroads and other public infrastructure helped the U.S. develop economically.[4] However, a smaller/ developing country with a trade deficit might not be this lucky in obtaining Foreign Direct Investment (FDI) while foreign ownership of debt might also be risky. When trade deficit happened in East Asian countries such as Thailand and Indonesia in the 1990s, they attracted substantial foreign capital initially. However, with the advent of the Asian financial crisis, foreign investors quickly fled, leaving these countries to the mercy of global financial lenders/ markets.[5]

Trade deficit has perks as well as it ensures the availability of goods and services for the resident's consumption via adequate imports. On the flipside, however, are the pressures on the country's currency and external payments. As governments usually seek to encourage exports and consumption of locally manufactured goods, they usually alter policies to suit the same which may mean curbing importing or increasing duty on certain goods.

HOW VIETNAM AND BANGLADESH ENHANCED THEIR EXPORTS

Vietnam and Bangladesh can be taken into account as their economies had a comparative size to that of Pakistan some decades ago. Both these countries are examples of how a country can turn

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[4] Investopedia, Trade Deficit: Advantages and Disadvantages [updated 12 April 2022]

Available from https://www.investopedia.com/articles/investing/051515/pros-cons-trade-deficit.asp

[5] Investopedia, Asian Financial Crisis [updated 28 April 2021]

Available from https://www.investopedia.com/terms/a/asian-financial-crisis.asp around its export sector, and achieve balance of payment. Their enhanced exports translated into overall economic growth termed as “Export led growth”.

The textile & clothing industry offers an example of the shift of industries in Asia from one emerging country to another, as they progressively develop and thus lose their comparative cost advantage: from Japan to lower developed countries (Hong Kong, Korea, etc.) then to other Asian countries (Philippines, Thailand, Indonesia, etc.) and now to China, Bangladesh Vietnam, etc Vietnam is a late comer among Asian emerging countries, as its economic take off is very recent. Since the reforms implemented in the mid-1980s followed by the end of the US embargo, Vietnam’s growth rate has been among the highest worldwide: GDP has grown at the rate of around 7.5 percent *per* year and foreign trade has expanded at the rate of nearly 20 percent *per* year. At the national level, the proportion of the population living in poverty has been considerably reduced from 54 percent to 16 percent between 1993 and 2006.

Although financial liberalization has been slow and modest, Vietnam has received important foreign funding FDI has become a significant contributor to domestic investment (more than 10 percent of gross investment) and exports. FDI picked up with the completion of the WTO negotiation. Up to 2000, the oil and gas sectors were the principal recipients of FDI but from then on, light and heavy industries have received the lion’s share. Most of FDI has been conducted under the form of joint ventures with SOEs. This helped the State to orientate international integration as in China, and as it has been done before by other Asian countries, including Thailand.

Vietnam’s trade specialization using indicators of revealed comparative advantage. This specialization is consistent with a Hecksher-Ohlin model of trade, as Vietnam exports mainly labour-intensive goods and raw materials and imports intermediate and equipment goods. In spite of its rapid progress, Vietnam is still at the early stages of industrialization and international integration. Vietnam’s revealed comparative advantages rely on natural resources and labour-intensive goods. Vietnam’s specialization is very specific among Asian emerging countries, as it still mainly focuses on “horizontal” trade in which traded goods are produced from start to finish in one country. Its exports are based on its natural and labour resources while imports mostly consist of equipment and intermediate goods. The structure of revealed comparative advantages/disadvantages reflects this specialization pattern.

A big part of Bangladesh's success story comes from labor-intensive, export-oriented industrialization. It boasts the biggest manufacturing sector (as a share of GDP) in South Asia, and it continues to grow. In 2001, Bangladesh's merchandize exports amounted to $6.6 billion; in 2019, they were $47.2 billion, which more than doubles its share of world exports from 0.1 percent in 2001 to 0.25 percent in 2019.

But this success story derived from exports comes from an extreme concentration in garment manufacturing: The share of garments in Bangladesh's total exports increased from 75 percent in 2000 to more than 86 percent in 2019.

Hence, the export led growth of Bangladesh and Vietnam, is driven by FDI, political stability, conducive government policies, specialization in some fields and comparative advantage in some items. Both of these countries have worked on enhancing their export that not only impart learning among its people but also improve living standard of the populace.

HOW TRADE DEFICIT/ SURPLUS EFFECTS THE ECONOMY

Trade surpluses do not necessarily mean strong economies. For e.g. Japan's economic growth is not reflective of its consistent trade surplus and that too spanning over decades.[6] Similar is the case with Germany which, despite a strong trade surplus, reflects an average economic growth.[7]

Likewise, foreign investors have shown more trust in the U.S. economy during its trade deficit stages than they have during surplus as the world has witnessed periods of strong economic growth

[6] Asia for Educators. Economy and Trade Fact Sheet, Basic points about Japan's economy and trading patterns Available from http://afe.easia.columbia.edu/japan/japanworkbook/economics/factshe.htm

[7] Brookings. Germany's trade surplus is a problem. [updated 03 April 2015] Available from https://www.brookings.edu/blog/ben-bernanke/2015/04/03/germanys-trade-surplus-is-a-problem/

during some heavy trade deficits, as consumers and businesses have also sourced more services and products internationally.[8]

Trade deficit results in outflow of a country's currency abroad. With the shrinking domestic money supply, some level of deflationary pressure is seen given the country's monetary policy, extent of the deficit as well as its demand for debt. The central bank of the country may increase the monetary supply to offset some of this decline while FDI may also ease the deflationary pressure.

HOW TO INCREASE EXPORT FOR CONTROLLING TRADE DEFICIT

Like most economies, Pakistan's economic growth is also dependent on its exports to stabilize its currency, finance imports, service debt and to overcome the consistent balance of payment deficit. All this whilst also being in line with market trends and quality, and be certified on internationally acceptable standards. While all or some selective measures can be put in place to increase exports, their success largely depends on how well thought out their selection is to suit the country's existing and proposed policies as none of the factors detailed below operate in isolation and their interdependency on one another has to be considered before their selection and implementation. A robust export led growth policy is needed to steer Pakistan's exports with rapid industrialization, high savings and investment rates as well as specialization in areas of competitive advantage. Further measures to increase Pakistan's exports so as to control the trade deficit are detailed below:

1. Recommendations under Strategic Trade Policy Framwork (STPF) 2020-2025

A. Competitiveness Enhancement:

Industries operating in the exportable sector usually face a dilemma of being subject to nationalist policies wherein production is incentivized for domestic markets rather than

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[8] VOA, Economy. US Trade Deficit Hits Record, Reflecting Strong Economic Growth. [08 February 2022] Available from https://www.voanews.com/a/us-trade-deficit-hits-record-reflecting-strong-economic-growt/6433235.html

the global markets. Such protectionist tendencies result in low value production hence a paradigm shift is needed to provide incentives to industries to move to production of high value products suitable for the competitive international market. A good example of this is the Man-Made Fiber to cotton ratio which stands at 70:30 globally whereas in Pakistan the same is 30:70 primarily due to lack of prioritization. Resultantly, even though the textile sector contributed 61% to the total exports in 2021-22[9] and even grew by 23% in FY21 (Rs.15.4 billion) compared to FY20 (Rs.12.526 billion)[10] it is still significantly behind the regional players in global textile export sector with China dominating with its cut throat technology and early adaptability. Import substitution policies have insulated the domestic industry from competition which in turn has led to low quality output and non-compliance to standards required for exports.

Source: Topline Securities

[11]

[9] Pkrevenue. Pakistan's textile exports hit record high at 19.33 billion in FY22.

Available from https://pkrevenue.com/pakistans-textile-exports-hit-record-high-at-19-33-bn-in-fy22/#:~:text=The%20textile%20exports%20contributed%20around,the%20fiscal%20year%202021%2F2022

[10] ProPakistani. Pakistan's Textile Exports Increased by 23% in FY21 [updated 23 July 2021]

Available from https://propakistani.pk/2021/07/23/pakistans-textile-exports-increased-by-23-in-fy21/

[11] South Asia Investor Review. Pakistan's Exports Surging At The Fastest Rate in South Asia [updated 31 October 2020]

B. Hence, in order to witness exponential enhancement in export, reforms are needed to address such issues promptly. Further, easing import restrictions may also positively impact our export's competitiveness. An example can be taken from anti-dumping duties which "….is a tariff imposed on imports manufactured in foreign countries that are priced below the fair market value of similar goods in the domestic market.'[12] Even though anti-dumping is a measure to rectify the situation arising out of the dumping of goods and its trade distortive effect, having an anti-dumping duty on products such as Polyester Staple Fiber would lead to a raw material price hike which will ultimately lead to uncompetitive exports. National Tariff Policy (NTP) 2019-24 has laid the basic foundation for rationalizing the tariff structure. Revisiting tariffs and rationalizing these will encourage competitiveness and openness.

C. Further, capacity of the authority enforcing compliance to international standards must be ensured for growth in exports.

B. Trade Related Investment

Export sector needs investment to boost. The investment can come from internal as well external sectors. Pakistan's economic growth during the last five years has been mainly domestic-market driven rather than export-led. Investment from abroad also called Foreign Direct Investment (FDI) is important to upgrade infrastructure and seek innovation and technology. Development in trade logistics, trade liberalization through World Trade Organization and regional trade agreements and emergence of Global Value Chains remained vital factors for this evolution. Ministry of Commerce has collaborated with Board of Investment (BOI) and Provincial Investment promotion agencies, to formulate a framework for integration of trade policy with investment policy to bring foreign investment to boost exports. :

Available from https://www.southasiainvestor.com/2020/10/pakistans-exports-surging-at-fastest.html

[12] Corporate Finance Institute. Anti-Dumping Duty [updated 6 May 2022]

Available from https://corporatefinanceinstitute.com/resources/knowledge/other/anti-dumping-duty/

C. Integration into Global Value Chain

Integration into the global value chain refers to participation in the value chain of high end products that fetches greater dividends. Participation in the global value chain can be enhanced by increasing the access to global value chains. Since the grant of GSP Plus concessions by EU to Pakistan in 2014, EU-Pak trade has improved markedly. The total volume of trade was USD $11.961 billion in 2013-14 which has progressively enhanced and stood at USD $14.506 billion in 2018-19, with a trade surplus of USD $1.814 billion. Furthermore, in order to better get integrated into the global value chain, diversification of exports is required. Pakistan's exports are concentrated in few products exported by few firms to few markets. Textiles sector accounts for around 61% of total exports of the country. The share of non-textiles in exports is less than 40%. Similarly, concentration of products in same sector is also inclined more towards low valueadded side

D. Export Eco-System

Export eco-system comprises of entrepreneurs, established traders, export industries, policies framework for trade, border agencies, and trade associations. Facilitation needs to be done in all the associated areas from improvement of policy framework to upgrading the communication channels. Infrastructure also need to be improved. Given the geographic location of Pakistan, there exists a natural advantage and great potential for the country to be part of internationally flourishing transshipment industry. Pakistan's seaports can be put to maximum use with upgradation and institution of state-of-the-art loading and unloading transshipment facilities as intermediate ports. There are great prospects for the country by virtue of being strategically placed in one of the busiest sea routes between East Asia and Africa since the whole coastal belt has infrastructure limitations and shipping lines have a very small number of adequately equipped ports at their disposal for transshipment purposes. Transshipment operations are growing all around the world and countries are capitalizing on opportunities that are being offered by this mode of business

E. Institutional Strengthening

The Strategic Trade Policy Framework also details the structural changes needed to strengthen the institutions that would contribute towards enhancing exports. Firstly, Ministry of Commerce needs to have on its strength professionals and specialists of various sectors. The dire need of having sound professionals is impeding the smooth and efficient functioning of the ministry. Trade offices abroad also needs vigilant monitoring and evaluation. The officers need to be assigned KPIs and be evaluated on merit. There also is a need for a portal where all instructions related to trade will be place. It will not only facilitate the trader but also enhance transparency. The Directorate General Trade Organisations (DGTO) is the regulatory body of the Ministry of Commerce to register, regulate and monitor the functions of trade bodies. However, the organisation has faced multiple challenges in regulating trade bodies due to lack of available data. To streamline the data of registered members and administrative issues of the trade bodies, an online portal containing detailed data of all members of Associations and Chambers would be created for facilitation of the business community as well as transparency purposes. The trade bodies and their members would be able to check their data online and the record will be available for evaluation as well as improving administrative efficiencies of the DGTO's office. It would also facilitate an online registration and renewal mechanism for the various Trade Organizations and bodies. The government also needs to support national standard body to participate in international standard development activities of ISO, IEC, OIML, SMIIC and SARSO, to ensure the interest of national enterprises and their integration globally.

2. Investing in SMEs:

As per the estimates of Small & Medium Enterprise Development Authority (SMEDA), there are more than 5 million SMEs in Pakistan. These include startups, service providers and even manufacturing units, amongst others. SMEs contribute 40% of Pakistan's GDP and 25% in overall exports.[13] However, inconsistent policies and lack of empowerment is

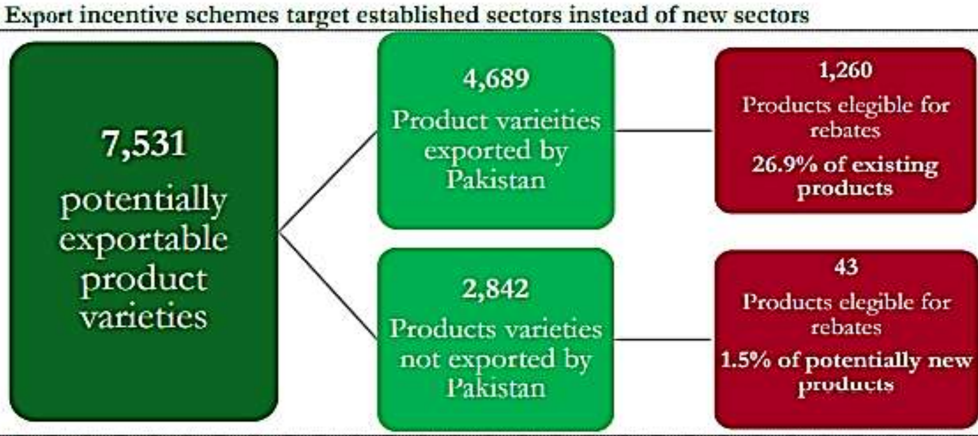
[13] State Bank of Pakistan.

inhibiting this sector to reach its true export potential. Easier access to finance, extensive and targeted skill development programs and Long-Term Financing schemes for purchasing/import of plant and machinery are just the tip of the ice berg with what can be done to promote this sector. Government encouraging SMEs by including them in their supply chain of public procurements can also be a reasonable starting point to unleash SME's potential especially in achieving social and economic benefits. Such well-designed policies stimulate technical development, increased trade margins and overall productivity, increased domestic tax revenue, would create jobs and ultimately result in economic growth.

3. Revamping Duty Drawback Schemes (Export Finance Scheme-EFS):

Duty drawback allows both importers and exporters to recover certain taxes, fees or duties paid on imported merchandise. This export incentive serves as a refund of certain duties collected on goods and is offered by many countries, including Pakistan. A careful analysis of these schemes reveals that eligibility to claim duty drawback is more likely for products that are typically exported by relatively larger firms, and for products that are well-established in Pakistan's export bundle. Only a handful of products that are not yet exported are eligible for rebate under the scheme.

Figure 3.24: Export incentive schemes target established sectors instead of new sectors



Source: World Bank staff calculations. Note: Exportable product varieties are defined following the classification of the Harmonized System at eight digits of disaggregation.

Available form https://www.sbp.org.pk/smefd/circulars/2022/C4-Annex-A.pdf

The current duty drawback schemes operational in Pakistan can be improved by the following:

i. In order to facilitate exporters, pre-payment of duties for exporting firms can be eliminated altogether to the extent of the drawback to ease their credit requirements.
ii. These schemes should also be made accessible to indirect exporters whose import inputs are used in production of exported final products.
iii. Utilization of home-grown produce should be encouraged by extending duty drawback for 5 years to exports using indigenous produced materials
iv. Scheme for gradual increase in duty drawback for garments etc. can be re-introduced
v. Make service exports eligible under the scheme

Yet, the incentives could make a difference precisely to the potentially new export products, as innovative firms venturing in new activities may need additional liquidity to overcome the costs of the innovation. The incentive schemes seem to be designed to preserve the current export structure and dynamism, rather than to transform it.

The new EFS scheme needs to be implemented in totality. Also all other schemes be replaced by the new one for standardization and simplicity for the exporters to avail.

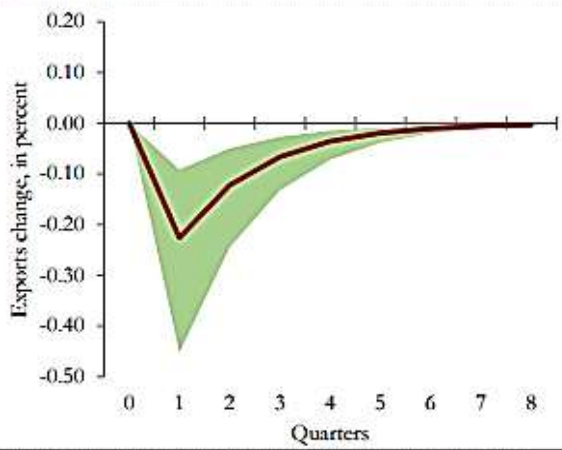
4. Political stability:

Lack of investment is one of the core reasons why Pakistan’s exports’ growth rate has been on a decline. This unfavorable investment environment stems from uncertainty. The volatility of Pakistan’s political environment as well as the disturbing law and order situation of the country have had an adverse impact on investments especially private ones. Stability in these areas would provide the county investments required to boost Pakistan’s exports.

5. Exchange Rate:

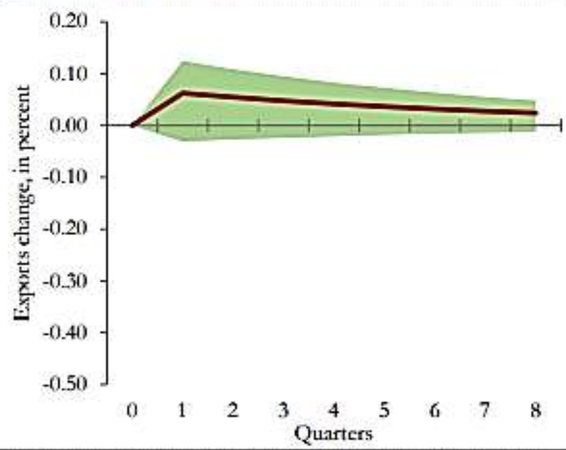
Exports can be encouraged by maintaining a fair exchange rate, neither over valued nor undervalued. Pakistan’s exports are highly sensitive to changes in the real effective exchange rate (REER): a 1% depreciation of REER results in a 0.5% increase in exports, provided everything else remains stable. However, exports' response to changes in REER happens at a much faster rate when REER appreciates (exports fall faster) than the increase in exports when REER depreciates.

Figure 3.25: Pakistan's export response to a 1 percent appreciation



Source: Brun et al. (2020). Note: the chart shows the quarterly adjustment in exports to a real effective exchange appreciation of one percent, along with the confidence interval for the change (shaded green area).

Figure 3.26: Pakistan's export response to a 1 percent depreciation



Source: Brun et al. (2020). Note: the chart shows the quarterly adjustment in exports to a real effective exchange depreciation of one percent, along with the confidence interval for the change (shaded green area).

This indicates supply side constraints. According to World Bank experts, "Setting aside the marked anti-export bias of the tariff policy, or incentives that do not favor growth or diversification, REER changes could play a role in the evolution of export competitiveness."[13]

6. Export incentive schemes:

Incentive schemes like DTRE and OES are too complicated so only about 10% exporters use it according to the World Bank, as opposed to 70% exporters in Bangladesh using export-related schemes.[13] The schemes are also not used due to the certifications, procedural and documentation requirements due to which smaller firms are not able to avail concessions included in these schemes. If incentives are to be offered they should be done so with simplified procedures. Further, the export incentive package needs to be strengthened by adding more items in its ambit and offering extensive incentives for exports to emerging markets. Rebates under the scheme should be sped by commercial banks with speedily reimbursement from State Bank of Pakistan.

7. Reducing red tape/ simplifying regulation:

Pakistan's export sector faces the dilemma of excessive red tape due to the obsolete and burdensome bureaucratic procedures. These not only affect new exporters trying to break into the global market but also existing exporters which are competing with world market forces despite being bound with outdated regulatory shackles. Long bureaucratic procedures negatively affect exports thus Government should seek to simplify regulations.

8. Easier access to finance:

Long-term and short-term credit's availability is crucial to all exporters especially SMEs which face stringent credit constraints compared to larger entities. As SMEs contribute 40% of Pakistan's GDP, improvements in this area are essential for favorable export growth and in ultimately tackling/ controlling trade deficit. Further, firms that do not have accumulated retained earnings find it difficult to quickly expand capacity and increase production. Therefore the need to provide easier access to SBP's long-term export finance schemes and away from reliance on external finance which may be cumbersome to obtain. Export financing should gradually be moved away from working capital and encouraged into capacity expansion through the Long-Term Financing Facility.

9. Financing schemes for closed export units:

A large number of businesses had to be shut down due to the recent wave of the global pandemic and resultant cash flow problems- a major chunk of these were SMEs. While the Government did intervene by introducing many schemes to provide relief from the aftershocks of Covid-19 on the economy, such as Debt Relief scheme, Temporary Economic Refinance Facility (TERF), Rozgar scheme[14], amongst others, there is still a gray area in the market for the exporters that still had to shut down. A discounted financing scheme for acquiring sick units which though are currently non-operational/ closed but can be made fully functional if acquired by larger business. With slight modification and

[14] State Bank of Pakistan

Available from https://www.sbp.org.pk/covid/index.html update, these units can be successfully integrated into businesses that have survived the pandemic lockdowns and can boost export capacity of existing firms.

10. Public-private partnership:

Presently export policy formation follows a top-down approach wherein policies are dictated from top-down. On the other hand, inclusion of market experts on trade within the policy formulation process via a public private partnership would be extremely beneficial in developing and implementing frameworks/policies and easier stakeholders' buy in case of reforms. Such policy mix would hence be bespoke on the basis of national/sub-national government as well as domestic players. Resultantly, the focus would be on the exports, prioritizing sectors based on worldwide demand, goods and services' diversity and implementation of easily comprehendible incentives and schemes. Further, trade mission with respect to services should be organized with the same fervor as is done with goods, to tap buyers in potential markets.

11. Analyzing the relationship between exports and domestic policies:

Understanding the interrelation between the export sector/institutes and policy is important. Domestic policies have both, direct as well as indirect effect on the export performance. Direct impact would involve the set of policy instruments which directly affect foreign trade while indirect affects would be the influence other policy measures have on the economic system such as fiscal policy, price controls, investment policies, exchange rate policies, etc. which may or may not stimulate export performance. If trade deficit is to be controlled via increased exports, all these policy measures cannot be considered in isolation as not only is the choice of policy material but also the constitutional and economic context and policy mix within which it is implemented.

Also, besides the traditional policy instruments, export growth can also be favored by improving the cooperation between the government and export/business actors. For e.g. an export consortia to facilitate SMEs to access the international markets might complement other government involvements.

12. Information Technology sector:

With agriculture and Textile dominating the export front, in order to increase exports Pakistan needs to focus on sectors that require minimum investments and infrastructure. Most suitable example of this is the IT sector and its ever rising global demand. A software house requires significantly less resources compared to a manufacturing entity. It is predicted that the global Software Engineering Market would develop at an 11.72% CAGR between 2016– 2022.[15] As manual processes are shifting to automated ones and as more workspaces become fluid due to pandemic, there is an ever increasing demand to automate industrial processes, introduce remote working and improve/ enhance existing design quality.

"Pakistan's exports of information technology grew by 47.4 per cent to cross the $2 billion mark for the first time in the country's history (*for FY20-21*)…In absolute terms, the IT exports reached $2.12bn in 2020-21 as against $1.44bn in the preceding year…"[16] However, India's information technology and back-office sector will grow by 7.7% in fiscal 2020 to USD 191 billion, with exports touching USD 147 billion.[17] Hence, Pakistan has a lot more avenues to explore and grow its software export and IT solution industry, provided the limitations to its growth, as depicted below, are addressed.

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[15] Market Research Future. Software Engineering Market Estimated to Perceive Accrued Value with a Confounding CAGR; MRFR Unleashes Industry Insights Up To 2022 [updated May 2021]

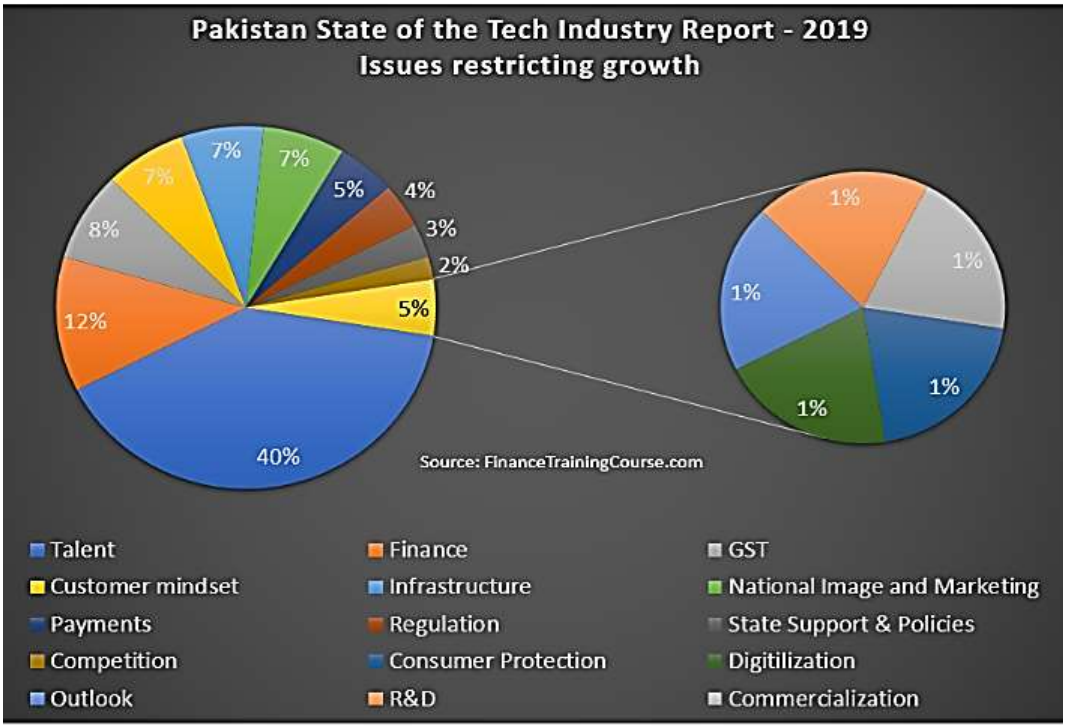
Available from https://www.marketresearchfuture.com/press-release/software-engineering-industry

[16] Invest Pakistan. IT exports cross record $2bn mark [updated 27 July 2021]

Available from https://invest.gov.pk/node/1493

[17] Business Standard. Nasscom sees IT industry revenues growing at 7.7% in FY20 at $191 billion [updated 13 February 2020]

Available from https://www.business-standard.com/article/companies/nasscom-sees-it-industry-revenues-growing-at-7-7-in-fy20-at-191-billion-120021201865_1.html



Pakistan Technology Industry Survey 2019 – Growing Pains [18]

Talent related issues are the primary challenge in meeting growth targets in this sector while access to finance remains the second. With minimal efforts and support, Pakistan's IT sector can expand exponentially. Trade Development Authority of Pakistan (TDAP) can play a major role in leveraging big data and artificial intelligence to facilitate exporters in the fast-paced online platforms.

13.Technology:

Outdated technology daunts the manufacturing sector. Due to poor enforcement of patents and trademarks, foreign countries are reluctant to share latest technology with Pakistan. Pakistan can sign Trade and Investment Framework Agreements globally to focus on areas such as artificial intelligence and e-commerce, furthering efficiency in the manufacturing

[18] Finance Training Course. Pakistan Technology Industry Survey 2019 [updated 28 November 2019] Available from https://financetrainingcourse.com/education/2019/11/pakistan-technology-industry-survey-2019/

sector. These agreements should also be made available to other sectors especially the SME sector to better place them in the global market.

14. Nurturing entrepreneurship:

Skilled unemployment (college graduates) in Pakistan is estimated to be around 20% according to UNDP National Human Development Report.[19] With the growing inflation and job layoffs/ business closures during Covid-19 lockdowns, unemployment levels are still high with the educated still being a significant chunk of the unemployed. If the same is made to continue, Pakistan would face severe difficulty in increasing its exports to control the trade deficit as economic returns required for economic growth would not be achieved.

Such educated population can be incentivized by prioritizing the ease of doing business not only within Pakistan but also outside Pakistan, i.e. exports. By doing so, a cycle of prosperity is triggered wherein not only do the educated get employed themselves but also create employment opportunities for others thus creating value for the economy and the society. Providing incentives for innovation results in entrepreneurship improving local/domestic goods and their productivity, making Pakistan a competitive player in the global market. However, to achieve the same, nurturing entrepreneurship would need an extensive focus.

15. Textile and Apparel parks:

Textile and apparel parks provide a one stop integrated solution for creation of world class infrastructure, welfare facilities, manufacturing support, etc. to prospective textile industries. Government may even provide grants to cover project costs while plug and play facilities are available for all investors (ready facilities in terms of building, water-power-sewage, etc. besides including in hand clearances required to start the industry). A proposal

[19] PIDE Blog. How to increase exports for Pakistan's sustainable economic growth? [updated 5 March 2021] Available from https://pide.org.pk/blog/how-to-increase-exports-for-pakistans-sustainable-economic-growth/

to establish one such park near Lahore is still in limbo with the Government not being able to capitalize on boosting exports, i.e. one major benefit of establishing such parks.[20] Hence, their fast track establishment is needed.

No.	Enabler	Description
1	Energy	• Fix electricity price at cents 7.5/kWh and RLNG price at USD 6.5/MMBTU for next 5 years • Long term uniform & internationally competitive energy prices across the country for exporting industry
2	Raw Material	• Vertical & Horizontal increase in production of cotton • Provide Polyester Staple Fiber without incidentals, duties & taxes
3	Liquidity	• Liquidate all textile Industry refunds of sale tax, income tax, policy & package initiatives • Provide ERF to all exports including yarn & greige fabric
4	Investments	• Investment in technology to upgrade existing machinery. *Prospective investors reluctant to make new investment decisions due to high cost of doing business* • Allow LTFF to indirect exports & enhance credit limit for investment under LTFF to PKR 3 billion per project • Industrial Credit allocation policy of SBP be reintroduced
		• Fast Track establishment of Integrated Textile & Apparel Parks enabling plug & play facilities for local and foreign investors • Special task force on revival of closed mills
5	Market	• Market Promotion measures for attracting international brands and retail chains of Europe & USA • Drawback of local taxes & levies to zero rate export (long term schemes)

Enables for Doubling Textile Exports[28]

16. Enhance demand for the exports (Demand side opportunity):

Expansion of exports for increased revenue also involves expansion into new markets which in turn requires a great deal of market research to target customers. A prerequisite of entering international markets is awareness so researching new territories is a must. For individual exporters this might not be feasible hence the Government needs to step in. TDAP should improve information collection and dissemination about foreign markets, product standards, other technical requirements for exporting such as logistics, customer service, order fulfilment, etc. However, even TDAP has limitations, being underfunded and having low technical capacity.

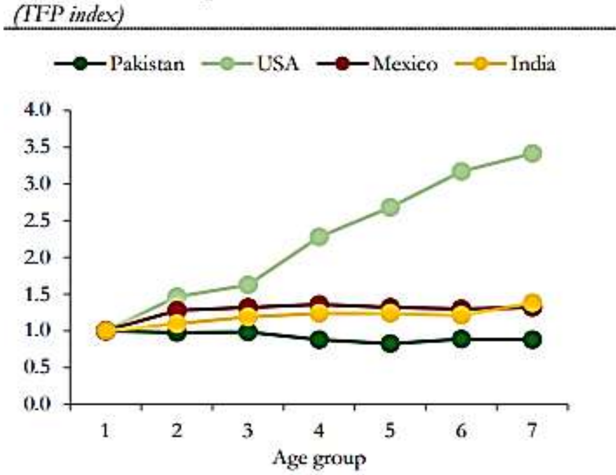
[20] Just Style. Pakistan apparel park plans hang in the balance [updated 16 April 2021] Available from https://www.just-style.com/news/pakistan-apparel-park-plans-hang-in-the-balance/

Every country has different dynamics and what works in one might not work in another, hence, research and provision of information is of utmost importance. Exporters particularly need to be aware of the different cultures, demographics, location, needs and interests of target customers, market growth rates, competitors, potential barriers to entry, forecasted demand, etc. Trainings may be provided at Government level to encourage exporters to overcome issues such as language barriers, business etiquettes and educate exporters regarding different regulations such as health and safety.

17. Increased Productivity:

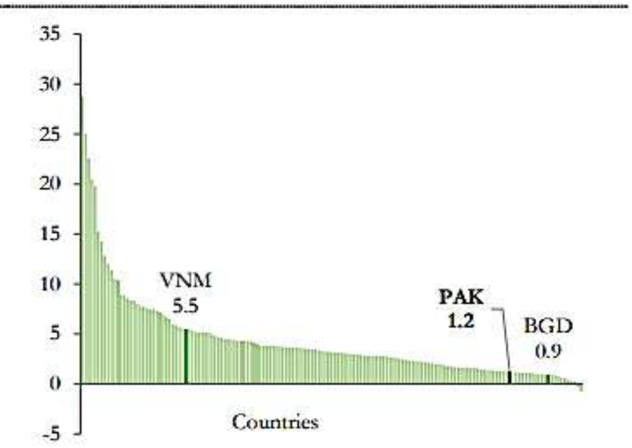
"Pakistani firms do not grow more productive with time, but rather the opposite: A 40-year-old firm is 87 percent as productive as a young firm of less than 10 years. Instead, in India or Mexico, the older firm is between 30 to 40 percent more productive than the younger one. In the United States, it is 341 percent more productive, on average."[13]

Figure 3.27: Firm's productivity over their lifecycle, Pakistan and comparators
(TFP index)



Source: Country Economic Memorandum – Country Scan. Mexico, India and USA data come from Hsieh and Klenow (2014), data for Pakistan comes from Lovo and Varela (2020).

Figure 3.28: Foreign direct investment
(Net inflows, in percent of GDP, average 2010-2020)



Source: World Development Indicators; World Bank staff calculations. Note: only countries with population over 1 million are included. Cyprus (77 percent of GDP) is excluded for scale reasons.

This is primarily due to:

1. Limited integration of Pakistan into the global marketplace.
2. Low FDI
3. Low/ limited presence of multinationals in the export sector

Resultantly, firms' capabilities are low as well as the same is directly associated with productivity. Hence, increasing productivity is a major step towards participating in global markets.

18. Value addition & diversification:

Currently, exporters in Pakistan face the dilemma of lacking value addition and innovation in their exports, as Trade-Related Aspects of Intellectual Property Rights (TRIPS) does not allow export of imitations. Value addition requires R&D and innovation which may be encouraged by not only enforcing intellectual property rights regime in letter and spirit but also TDAP interveining by providing trainings, conducting seminars or even establishing cartels for R&D according to sectors.

Further, Pakistan has failed to diversify its export base both in terms of products and markets. This is essential as diversification not only hedges against product or destination shocks but the ability to diversify inidcates a sector's competitiveness. As discussed earlier, textile and apparel account for almost 60 percent of Pakistan's exports. "… the number of product varieties (*as determined by HS code)* exported by Pakistan fell over the past decade, from an average of 3,167 in 2007–09, to an average of 2,894 in 2017–19.." hence "..Pakistan fell in the world ranking of product varieties exported, from the 38th percentile to the 45th percentile."[13]

In terms of number of markets reached, Pakistan fell from the "..22nd percentile in 2007–09 to the 29th percentile in 2017–19…. In 2019, Pakistan reached 8 percent of the pool of potential importers, up from the 7.4 percent observed a decade ago, and while it has made progress, it is still far from countries such as Vietnam, Malaysia, or Indonesia."[13]

Figure 3.10: Index of Export Market Penetration (IEMP) in selected countries 2009-2019

Source: World Integrated Trade Solution; World Bank staff calculations.

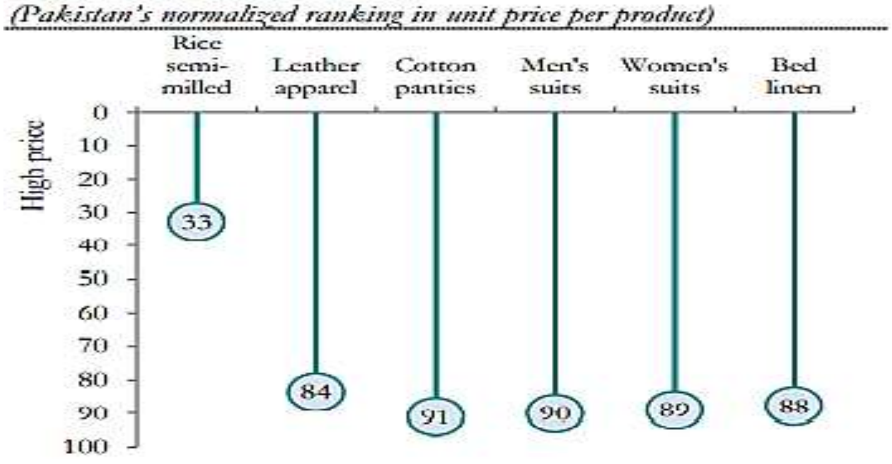
These have limited the exporting firms' ability to achieve economies of scale and have kept exporting firms at a small scale.

19.Competitive pricing:

If we look closely at our largest export sector, i.e. textile and apparel, it is noted that the prices our exporters fetch are far lower that of the competitors. This may be indicative of exporters specializing in low quality standard items. For the rice segment, however, Pakistan ranks 33rd in terms of the price fetched.[13] This price competitiveness can be greatly improved by branding, complying with international standards, certifications, etc.

Figure 3.11: Quality ladders

(Pakistan's normalized ranking in unit price per product)



Source: World Integrated Trade Solution; World Bank staff calculations.

Note: based on average prices of exports to the EU. For each product line, only countries with exports over USD100,000 were considered. A value of 1 implies that Pakistan is fetching the highest unit price for that product, a value of 100 the lowest. HS codes of the products shown (from left to right): 100630, 420310, 611592, 620342, 620462, 630232.

Further, pricing is not just about understanding exchange rate differences, as transportation costs, packaging, agent's commission, cost of financing, etc would vary with each new market. Therefore it is essential that prices are kept under check so as to market them into the new territory. For the purpose Government may offer consultancy facilities especially to new exporters to determine competitive prices for the exports offered.

20. Curtailing export subsidies:

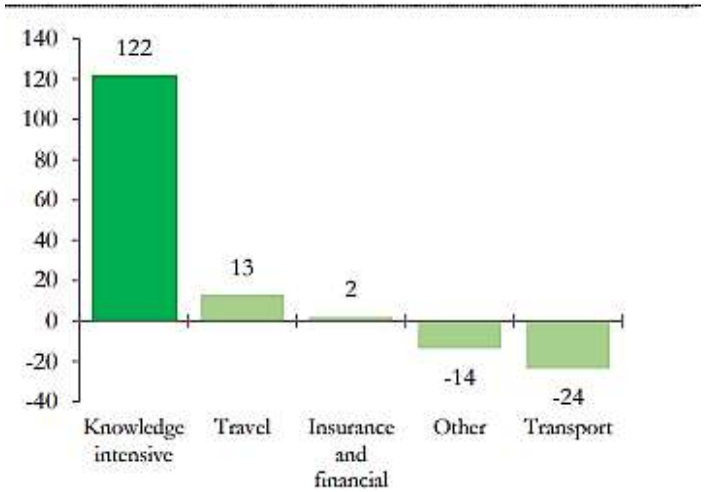
"Government subsidies help an industry by paying for part of the cost of the production of a good or service by offering tax credits or reimbursements or by paying for part of the cost a consumer would pay to purchase a good or service."[21] Subsidies cost the national exchequer valuable money as part of the costs are being covered by the Government. Hence, export subsidies, where given, must be clearly linked with the performance of the exporter and should automatically stand withdrawn once thresholds are crossed. This, however, involves a lot of transparency and technological advancements with respect to developing systems and regulations/ frameworks to fully automate transactions. Such systems also need to balance being clear, simple and concise so as to encourage exporters especially new exporters whilst also improving the overall efficacy. National Tariff Policy (NTP) 2019-24 has laid out the basics of implementing time-bound subsidies to the industry.

21. Focus on the service sector:

Existing trade policies focus extensively on goods with the service sector being ignored. As trade becomes digitized, export of services is becoming more important than ever. During the past decade, knowledge-intensive sectors have grown rapidly within the service sector while the sector itself has largely remained stagnant due to the contraction of transport and other services exports.

[21] Investopedia. How Do Government Subsidies Help an Industry? [updated 10 May 2022] Available from https://www.investopedia.com/ask/answers/060215/how-do-government-subsidies-help-industry.asp#:~:text=Government%20subsidies%20help%20an%20industry%20by%20paying%20for%20part%20of,purchase%20a%20good%20or%20service.

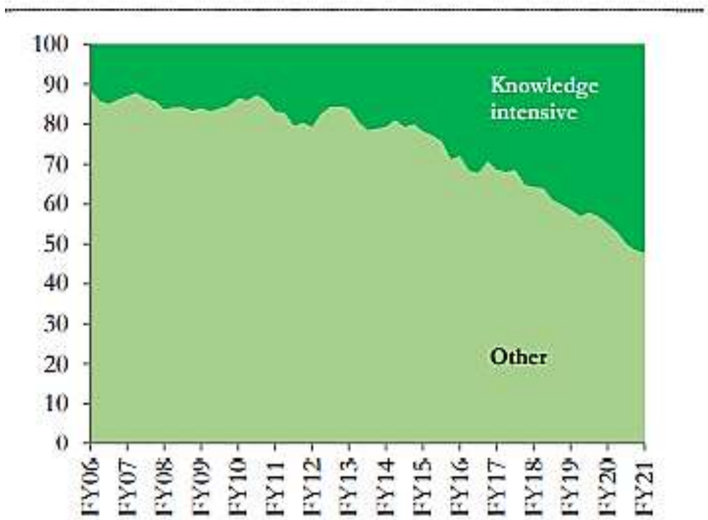
Figure 3.12: Contributions to growth of services exports, FY06-FY21



Source: State Bank of Pakistan; World Bank staff calculations.

Pakistani freelancers and SMEs embraced the global trend of internationalizing business services-this was further fueled by remote working due to the pandemic. "The share of knowledge-intensive services exports in total services exports grew from 10 percent in 2010 to 50 percent in 2020."[13]

Figure 3.13: Composition of service exports, FY06-FY21
(In percent)



Source: State Bank of Pakistan; World Bank staff calculations.

A special cell in Ministry of Commerce to cater specifically to this sector and its issues would provide the much needed boost.

22.Lowering import duties:

Domestic firms face lower transport costs in domestic markets than globally and are well versed with the local market. They have a natural tendency to sell locally rather than aiming to export. High import duties imply the local market gets insulated against imported goods which become expensive. Hence, the profits of selling domestically become artificially large. The Government's too encourages local selling and even though Pakistani market is large, the global market is 318 times larger. Such import duties incentivize export substitution instead.

The NTP is a positive development in this area as it recognizes tariffs as trade facilitators rather than revenue collectors. It has sought to rationalize tariffs gradually whilst institutionalizing tariff policy decisions.

23.Preferential Trade Agreements (PTAs):

PTAs are tools used by countries to seek market access and ensure deeper market penetration and global integration. They may include synchronization of border and custom procedures, quality standards, investment integration, lower trade tariffs, etc. While the number of PTAs worldwide has gone up from 50 (1990s) to 300 (2019, Pakistan is only signatory to 4 whereas the average worldwide is 13 PTAs per country. Amongst those 4, Pakistan had truly benefitted from The China–Pakistan Free Trade Agreement (CPFTA), while the South Asia Free Trade Agreement (SAFTA) is only partially implemented.[22] Without PTAs, Pakistan only has limited access to foreign markets, hence, the opportunities created by them must be fully exploited.

[22] World Bank. 2021a. "Pakistan's Export Potential: Some Estimates and Implications", Policy Note. World Bank. Islamabad.

24. Other factors that may enhance exports for controlling the trade deficit are:

i. Like with all businesses, timing is very important in increasing exports. In some places, what is being exported may be ahead of time while in others it could be outdated.

ii. New markets need to be developed and explored especially in Central Asia, Turkey and Iran.

25. Policy Recommendations

The World Bank report on Pakistan Development update- Reviving Exports summarized the above into the following policy recommendations. [13]

	Policy Recommendation	Timeframe	Responsible Agencies
Anti-export bias of tariff policy	Design and implement a long-term tariff rationalization strategy. Gradually reduce import duties and tariff cascading. Identify potentially affected sectors and implement time-bound support to displaced workers.	Long run	Ministry of Commerce (MOC), National Tariff board (NTB)
	Phase out regulatory and additional customs duties.	Long run	MOC, NTB
	Digitize and automate duty remission schemes for exporters, with trust-based systems and risk-based audits, and time-bound approval processes.	Short/long run	Federal Board of Revenue (FBR)
	Equip the NTB to make evidence-based policy decisions, building capacity in the National Tariff Commission; strengthen the link between academia and the Government.	Long run	MOC, NTB, NTC
Market access	Negotiate market access with high export potential markets and equip trade negotiators with necessary skills and resources.	Short run	MOC, Private Sector
	Establish foot-and-mouth disease-free zones in partnership with the private sector, to secure beef exports to the fast-growing Chinese market through the China–Pakistan FTA.	Short run	Ministry of National Food Security and Research, MOC, Provincial Govt., Private Sector
	Support exporters to increase destination reach by leveraging market access provided by China-Pakistan FTA and the Generalized System of Preferences.	Short run	MOC, Private Sector, Trade Development Authority Pakistan (TDAP)
FDI promotion	Amend the Investment Act to harmonize it with the Investment Policy of 2013.	Short run	Board of Investment (BOI)
	Simplify processes for registration of paid-up capital in SBP, and profit repatriation of multinationals.	Short run	State Bank of Pakistan (SBP)
	Professionalize the investment promotion agencies and coordinate it with export promotion agencies.	Short/long run	BOI, TDAP

Export subsidies (drawbacks)	Increase eligibility of duty drawback schemes, including services exports; reduce average rate and dispersion; consider the growth of exports as the basis for the subsidy rate rather than the level of exports.	Short run	MOC
	Condition 100 percent of the incentive on export growth, relative to the previous period, automatically making new exporters eligible.	Short run	MOC
	If differential rates are to be applied, consider the following to target products for higher rates: i) new export products, (ii) new exporters, (iii) more sophisticated products, and (iv) products that are not water intensive.	Short run	MOC
	Evaluate the impact of DDT and DLTL.	Long run	MOC
Export Credit	Reallocate resources into the LTFF, away from the EFS.	Short run	SBP
	Reconsider extent of subsidy in LTFF and EFS based on a cost–benefit analysis.	Long run	SBP
Export promotion	Harmonize export intelligence and consolidate it under one agency; consolidate trade portals and keep them under the	Short run	Pakistan Software Export Board (PSEB), TDAP, FBR
& facilitation	National Single Window, complying with the WTO Trade Facilitation Agreement.		
	Digitalize market intelligence provision support by relying on available international platforms.	Short run	TDAP, PSEB
	Re-consider financial support to firms to participate in trade fairs and exhibitions by evaluating its impact. Focus support on new exporters in the interim.	Short run/long run	MOC, TDAP
	Increase transparency in the use of the Export Development Fund, monitor and evaluate associated expenses.	Short/long run	MOC
	Reduce restrictions to foreign currency outflows. Increase the USD400,000 outflow limit beyond which approvals are required to incentivize firms to register export proceeds in Pakistan.	Short run	SBP
	Allow firms to maintain (greater portions of) export proceeds in foreign currency accounts.	Short run	SBP
	Enhance the e-commerce framework, with focus on regulatory changes to personal data protection.	Short/long run	MOC, Ministry of Information Technologies and Telecommunications
	Consider double taxation agreements to reduce the tax burden on exports of modern services.	Long run	MOF, FBR, MOC
Skills	Collaborate and agree on a curricular update with professional and technical advice.	Long run	Higher Education Commission (HEC), Private Sector, Universities
	Recognize credits from internationally quality-accredited online courses (e.g., focusing on the IT sector, coding courses from Coursera and EdX).	Short run	Higher Education Commission
	Support upgrading of firms' capabilities, focused on new exporters and evaluate its impact.	Long run	Small and Medium Enterprises Development Agency

Source: World Bank Staff elaboration

CONCLUSION

It can therefore be concluded that a boost in exports for controlling Pakistan's trade deficit requires an export policy whose success depends on its clearly defined goals, objectives and priorities. In particular, the environment should be made conducive for:

- Encouraging potential exporters by providing the necessary infrastructure, regulation, fiscal policies, access to finance, etc.
- Fostering synergies between public and private stakeholders including policymakers, local producers and exporters
- Providing easier access to credit
- Providing bespoke and targeted assistance supplemented by constant evaluation.
- Stimulating institutional development
- Building Pakistan's image in the foreign market (via advocacy, information provision, advertising, etc.)
- Technological development in industries and other sectors
- Nurturing innovation
- Improving productivity.

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