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Globalization and its Impact on Taxation Structure of Pakistan

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Abstract

Economic globalization has both negative and positive impact on the economy of Pakistan. In order to encourage free trade, tariffs were decreased under the framework of World Trade Organization (WTO) which had a negative impact on the tax structure of developing countries. For instance, in Pakistan, the decrease in tariff has been compensated with an increase in General Sales Tax (GST) and direct tax. Instead of compensating the decrease in tariff with GST and other taxes, Pakistan should improve its exports by enhancing the quality of its products, particularly textile. European Union has included Pakistan in the Generalized Scheme of Preferences Plus (GSP+), which may result in the betterment of the economy of Pakistan, good quality of products and increase in export and revenues.

Introduction

Economic globalization is growing economic integration of countries by an increase of cross-border transfer of goods, services, technologies and capital. According to Daniels & Van Hoose,[1] globalization is the increasing interconnection of peoples and societies and the interdependence of economies, government, and environment. Economic globalization is connected with neo-liberal policies which consist of decrease in tariffs, reduction or removal of restrictions on foreign investment, and the addition of services like banking and insurance in trade globally.[2] Economic globalization is a historical process which is outcome of human innovation and technological development. It is increasing integration of economies through transfer of commodities,

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1 J. P. Daniels & D.D. VanHoose, *Global Economic Issues and Policies*, 1st ed. (USA: Thomson- South Western, 2004), p.3.

2 Permanent Mission of Pakistan to the WTO, World Trade Organization, 2014. http://www.wto-pakistan.org/

services, capital, labor and technology globally.[3] Globalization is the process of interconnection of countries by trade, foreign investment, external assistance, and immigration of individuals and thoughts.[4] Shangquan[5] defined that economic globalization denotes the growing interdependence of world economies as a consequence of the increasing scale of cross-border trade of goods and services, flow of international capital and rapid spread of technologies. Market boundaries are mutually integrated and they are expanding continuously. It appears to be an irreversible trend as far as economic development is concerned – a whole new phenomenon in the beginning of the new millennium. According to Satyanarayana, Ramu, Reddy, Raghavulu & Mohana,[6] globalization denotes an economic process of integrating country‘s economy with the economy of the world through free enterprise and free trade. It propagates global capitalist development process as a way out for moving towards further heights in creating prosperity through which global poverty and inequality may be addressed efficiently.

According to the above mentioned definitions, economic globalization is a process of trade liberalization, elimination or reduction of trade barriers, reduction in tariff, deregulation and expansion of the global market place, transfer of capital, migration of labor, thoughts and technology across the borders.

World Trade Organization

The policies of World Trade Organization (WTO), IMF and World Bank have strengthened open economics across the borders. Negotiations laid the foundation of WTO and it makes all the decisions merely through

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3 Globalization: A Brief Overview, IMF 2008. https://www.imf.org/external/np/exr/ib/2008/053008.htm

4 *Beyond Economic Growth an Introduction to Sustainable Development*, 2nd ed. (Washington: World Bank, 2004). http://www.worldbank.org/depweb/english/beyond/global/ chapter12.html

World Health Organization (2014). http://www.who.int/trade/glossary/story043/en/

World Trade Organization (2014). What is the World Trade Organization, http://www.wto.org/english/thewto_e/whatis_e/tif_e/fact1_e.htm

5 G. Shangquan, *Economic Globalization: Trends, Risks and Risk Prevention*, 2000, http://www.un.org/en/development/desa/policy/cdp/cdp_background_papers/bp2000_1.pdf

6 G. Satyanarayana, M.R. Ramu, Y.K. Reddy, M.V. Raghavulu, & A.R. Mohana, ‘Globalisation and Socio-Economic Concept’, in G. Satyanarayana (eds.), *Globalisation and Development of Backward Areas*, 1st ed. (India: New Country Publications, 2007), pp.ix-xiii.

negotiations. Uruguay Round, the main part of the current work of WTO comes from 1986–94 negotiations. It also includes earlier negotiations under the General Agreement on Tariffs and Trade (GATT). Under Doha Development Agenda, which was launched in 2001; WTO is providing the platform for newer negotiations. Though WTO got its present form on 1st January 1995, nonetheless, the trading system that it is following is about half a century older. Since 1948, the GATT has been providing the rules.[7]

WTO advocates a freer and an anticipated trade. The objective of WTO is to end the crooked practices like quotas and subsidies in a segmented manner. However, the target of WTO is by no means resting at zero tariffs. The main agreements of WTO are GATT, General Agreements on Trade in Services (GATS), Agreements on Trade Related Aspects of Intellectual Property Rights (TRIPs), and Agreement on Agriculture (AoA), Textile and Clothing directly come under GATT.

Pakistan became the member of WTO in 1995. It is one of its founder members. Pakistan is following a strategy, which has its base on export-led-growth and it may prove fruitful for foreign trade. Pakistan is member of WTO to sustain current markets and to increase different markets for exportable goods and services. This may help bring tariff and non-tariff barriers lowered on a Most Favored Nation (MFN) basis. This liberty levels, in an effective way, the grounds for the suppliers at competitive level.[8]

Impact of trade liberalization on the economy of Pakistan

Economic globalization has a twofold impact on the world economy; both negative and positive. Globalization has made it easy to benefit from the technology of developed countries. It has also increased the work opportunities for laborers and has also enabled them to learn new skills. The developed countries too have access to the markets of developing and under-developed countries which has resulted in marring their economy. For instance, the cheaper price products of China have dumped the local industry of Pakistan. It has also led to an increase in the ratio of unemployment. The economy of developed countries is becoming stouter due to globalization. Due to the better quality of their products they are able to defeat the developing countries in international market. Their ratio of exports and revenue is also increasing. The developing countries are, however, unable to compete with these economic powers in the international market, so their export revenues are

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[7] Permanent Mission of Pakistan to the WTO, *op.cit*.

[8] *Ibid*.

constantly decreasing. Trade liberalization also changes the tax structure of developing countries such as Pakistan. According to Zaman,[9] the trade liberalization and tariff reforms have impacts on growth and employment. First, there has been a drastic fall in government revenue, although it has been compensated by a diversification of the structure of government revenue; second, there has been a rise in import payments due to cheaper products; third, the decrease in protection of industry has affected industrial employment and output, and fourth, there have been social costs, though these would be hard to quantify.

Trade liberalization & tariff: Pakistan was following import substitution policy with high tariff level and non-tariff barriers. This led domestic market to cut off from international market competition till 1970s. According to Khan,[10] during the early years of independence, foreign trade policy of Pakistan put emphasis on import substitution, although efforts were also made to stimulate exports. During 1950s, to deal with the balance of payment crisis, at the end of the Korean war-related product boom, quantitative restrictions on imports and other non-tariff barriers had been the primary policy instruments. In 1960s, a significant import liberalization policy was under taken for free list of imported items, automatic renewal of import license for industrial raw material and consumer goods. During 1970s, three most noteworthy measures of trade liberalization to reduce anti- exports bias were taken, such as devaluation, the elimination of the export bonus scheme, to end restrictive licensing in 1972.[11]

Reduction in tariff rates during late 1980s & 1990s: Since 1988, Pakistan has been following a comprehensive reform program with a strong emphasis on competitive trade, decrease in tariff walls and opening up of the domestic market. Tariffs were reduced substantially in the late 1980s and 1990s. Pakistan abolished most of its banned and quantitative restrictions. The tariff reduction program started in 1995.[12]

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9 A. Zaman, 'Economic Strategies and Policies in Pakistan, 1947-1997', in S. Mumtaz, J. Racine, & A.A. Ali (eds.), *Pakistan: The Contours of State and Society*, 1st ed. (New York: Oxford University Press, 2002), p.178.

10 A.H. Khan, 'The Experience of Trade Liberalization', *The Pakistan Development Review*, 37:4 (1998), pp.661-85.

11 *Ibid*.

12 M.A. Chaudry, 'Pakistan: WTO and Economic Reforms', in M.A. Chaudry, & E. Ahmed (eds.), *Globalization: WTO, Trade and Economic Liberalization in Pakistan*, 1st ed. (Lahore: Ferozsons, 2004), pp.23-41.

After introducing reforms in the 1990s, tariff has been simplified and cut down to a significant level. In FY 1987, the maximum tariff on import was 225 per cent which was lowered to 125 per cent in FY 1989, then to 80 per cent (excluding Iqra surcharge and import license fee) in FY1994.[13] In FY 1996, maximum rate of duty in the tariff was brought down from 70 per cent to 65 per cent.[14] In FY 1998, maximum tariff rate was reduced from 65 per cent to 45 per cent except for some imports like automobiles. The number of duty slabs were reduced from thirteen to five with rates of 10, 15, 25, 35 and 45 per cent. The tariff rate on plant and machinery was standardized and brought down to 10 per cent. Duties on primary raw material, secondary raw materials, intermediate goods and finished goods suitably cascaded between 10 and 45 per cent. Tariff rates on a wide range of smuggling prone items were brought down to 10 per cent and 25 per cent in order to curb smuggling. The tax base were broadened by introducing an across the broad minimum tariff rate of 10 per cent, except for imports of essential items. The tariff reform package was expected to simulate industrial production and investment.[15]

Reduction in tariffs from 1999 to 2013: President Pervez Musharraf introduced many reforms in tax system. He introduced policy reforms which included the generalization of laws, universal self-assessment, removal of exemptions, decreasing dependence on withholding taxes and an effective dispute resolution mechanism. To achieve positive results, he also undertook policy reforms dealing with administrative and organizational matters. The main tenacity of these reforms was to have a fully integrated tax management system.[16] In FY 2000, maximum tariff was reduced to 35 per cent with the exception of automobiles. Custom duties, non-zero slabs, were reduced initially from 13 to five in FY 1998 and further to four in FY 1999 (35, 25, 15 and 10 per cent). Tariff rates on smuggling-prone items were brought down to 10 per cent and 25 per cent. A minimum tariff of 10 per cent were imposed across-the-board exclusive of necessary items like wheat, fertilizers and life saving drugs.[17] President Pervez Musharraf also introduced tariff reforms like public announcement of tariff rationalization spread over 2001-04. Maximum tariff was reduced to 25 per cent in 2002-03 from 92 per cent

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13 *Pakistan Economic Survey 1993-94* (Islamabad: Ministry of Finance, Government of Pakistan).

14 *Pakistan Economic Survey 1995-96*, *ibid.*

15 *Pakistan Economic Survey 1997-98*, *ibid*.

16 *Pakistan Economic Survey 2007-08*, *ibid*.

17 *Pakistan Economic Survey 1999-2000, ibid*.

a decade ago, number of tariff slabs were brought down from 13 to 4 in the same period, reducing the use of excise duties in tariffs, endorsement of anti-dumping law consistent with WTO, import liberalization measures adopted for agricultural and petroleum products, restrictions on agricultural exports were removed and customs duty reduced on a number of smuggling prone items.[18] Maximum tariff on imports was raised once again to 35 per cent and reduced to 30 per cent in Financial Bill of 2012-13.[19]

In Pakistan, due to trade liberalization, maximum import tariff rates have been brought down from late 1980s to date. Main objectives of reduction in tariff rates were to make trade liberal, to reduce the prices of imported goods and to provide relief to general public.

Impact of tariff rates reduction on GST and direct taxes: With the ever increasing pursuit of a globalized economy, over the time, trade-related taxes are becoming less important as a revenue tool. Under the framework of GATT and WTO, Pakistan has gradually cut down its tariff and non-tariff barriers. The four main taxes in Pakistan include tariff, sales tax, excise duty and income tax. Tariff was the major source of revenue till 1980s.[20] In order to establish a free economy system, trade liberalization changed the tax structure of Pakistan. Since 1988, the decrease in tariff was compensated with an increase in General Sale Taxes (GST) and direct taxes. It is shown in Table.1 & Figure 1.

Table 1: Structure of Federal Tax Revenue

Years	Tax Rev as % of GDP	Direct Taxes (As % of Total Taxes)	Indirect Taxes (As % of Indirect Taxes)			
			Customs	Sales	Excise	Total
1990-91	11.0	18.0	54.9	17.6	27.5	82.0
1996-97	12.0	30.1	43.7	28.4	27.9	69.9
1997-98	11	35.0	39.1	28.3	32.6	65.0
1998-99	10.0	35.8	33.0	36.3	30.7	64.2
1999-00	9.1	32.5	26.4	49.9	23.7	67.5
2000-01	9.4	31.8	24.3	57.4	18.3	68.2
2001-02	9.2	35.3	18.3	63.7	18.0	64.7
2002-03	9.6	32.2	18.9	65.9	15.2	67.8

18 *Pakistan Economic Survey 2004-05, ibid*.

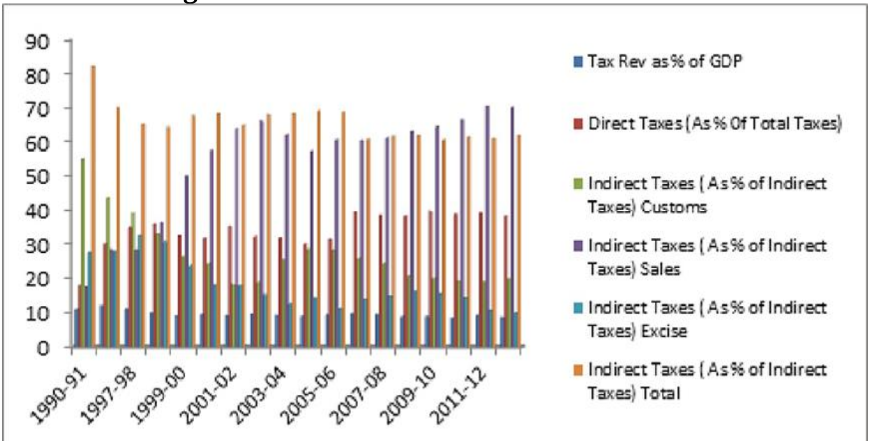
19 *Budget Speech 2012-13*, http://www.finance.gov.pk/budget/budget_Speech_12_13.pdf

20 A.R. Kamal, *Structural Adjustment and Poverty in Pakistan* (Islamabad: Pakistan Institute of Development Economics, 2003), pp.6-51.

2003-04	9.2	31.9	25.4	62.0	12.6	68.1
2004-05	8.9	30.1	28.5	57.2	14.3	68.9
2005-06	9.4	31.5	28.3	60.4	11.3	68.5
2006-07	9.7	39.4	25.8	60.3	13.9	60.6
2007-08	9.5	38.5	24.3	60.9	14.9	61.5
2008-09	8.8	38.2	20.7	62.9	16.4	61.8
2009-10	8.9	39.6	20.0	64.4	15.6	60.4
2010-11	8.5	38.7	19.3	66.3	14.4	61.3
2011-12	9.4	39.2	19.0	70.3	10.7	60.8
2012-13	8.7	38.2	19.9	70.0	10.1	61.8

Source: Pakistan Economic Survey 2007-08, p.65 & 2012-13, pp.60-61

Figure 1. Structure of Federal Tax Revenue

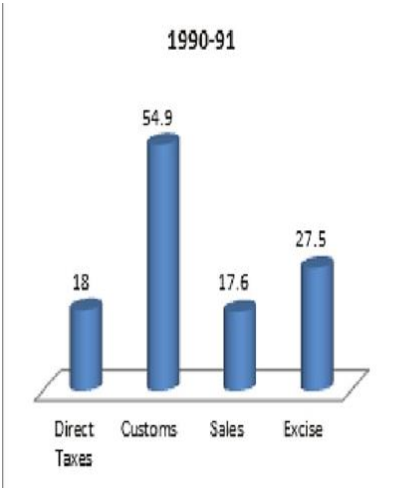


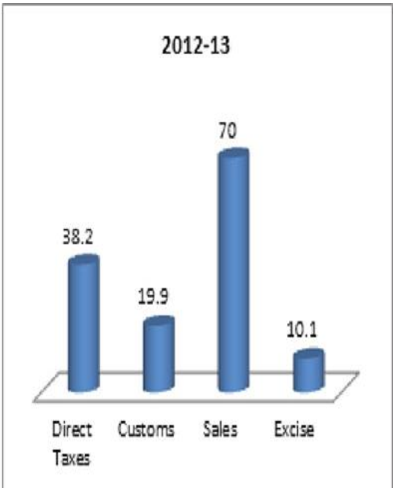
Source: see Table .1

According to Table and Figure 1, custom duty of the total indirect taxes accounted for 54.9 per cent in FY 1991, 24.3 per cent in 2007-08 and 19.9 per cent in 2012-13. Growth of import-related taxes declined to 3.0 per cent from 27.9 per cent in FY12. Decrease in the revenue due to custom duties has been adjusted by increase in GST and direct taxes. Sales tax, of the total indirect taxes, accounted for 17.6 per cent in FY 1991, 60.9 per cent in FY 2008 and 70 per cent in FY 2013. Direct taxes, of the total taxes, accounted for 18 per cent in FY 1991, 38.5 per cent in FY 2008 and 38.2 per cent in FY 2013.

Comparison of FY 1990 and FY 2013 tax structure has been given in the Figures 2 & 3.

Figures 2 & 3: Comparison between the Tax Structure of Financial Year 1990-1991 & Financial Year 2012-2013





Source: see Table .1

This rising trend in GST has increased the burden on general public. It is necessary for Pakistan to decrease sales tax and to enhance its revenue by promoting textile industry and trade with neighbors.

An overview of the textile industry

Textiles carry utmost significance in the sector of manufacturing. In Pakistan, it enjoys the longest chain of production. It has vital power for the addition of value throughout the process of its manufacturing. All the levels of processing, from cotton to the manufacturing of garments, inclusive of ginning, spinning and all, are done at home. Forty per cent of the labor force is employed by this industry; it provides twenty-five per cent of industrial value-added, and livelihood to ten million plus farming families. This industry utilizes banking credit to an amount of about forty per cent and provides eight per cent of GDP to our manufacturing sector. If we ignore the disturbances caused by seasons and cycles, we can say that textiles ensure about sixty per cent of our national exports. We are fourth largest manufacturers of textiles and we consume third part of cotton globally; we also hold a comparative advantage, largely pre-empted by the exports of a comparatively low value. It is shown in the twelve ranks of the total exports of the world.[21]

[21] *Textile Policy 2009-14* (Islamabad: Ministry of Textile Industry, Government of Pakistan), p.1.

Textile exports indicated a sign of progress as it is increased by 5.9 per cent in FY13, in contrast to a decline of 10.6 per cent in FY12. The improvement was mainly due to the rise in quantum of cotton yarn, bed-wares, towels, readymade garments and hosiery. This improvement largely emanated from higher demand of cotton yarn and fabrics from China, duty free access of 75 items to the EU, and some improvement in exports to the US. Demand for cotton yarn and fabrics from China and Hong Kong remained heavy, for in those countries there was an increase in labor wages and government policy of minimum support price to cotton growers kept increasing which increased the cost of yarn production. Pakistan can benefit from this trend as it has plenty of cheap labor and a large cotton production base. Moreover, the declaration of duty waivers on 75 products by the EU in 15 November 2012 provided some impetus to value-added textile exports, which can further increase with the status of GSP Plus.[22]

Advantages of GSP Plus status to the economy of Pakistan

The international trade committee of the EU Parliament approved GSP Plus status for Pakistan on 5 November 2013, effective from January 2014. Due to this status, about 20 per cent of Pakistani exports can go into EU market at zero duty and 70 per cent at preferential rates. Pakistan mainly exports textile products to European countries, with the status of GSP Plus, these exports, which are currently subject to more than 10 per cent tariffs, will benefit. At present, Pakistan's textile export to EU is about US$ 4 billion, which is 1.6 per cent of EU's total eligible imports for GSP Plus. Pakistan can potentially increase its share now to 2 per cent and this status would support Pakistan to export more than US$1 billion worth of products to the international markets. In order to exploit this opportunity, textile industry has to increase both its production and quality.[23]

Pakistan's inclusion in the EU GSP Plus scheme offers enormous benefits in terms of increase in exports. It is estimated that only the textile industry would earn profits of more than Rs. 1 trillion per year. Increase in exports would resultantly facilitate economic growth and benefit the generation of millions of additional jobs in the country. The leading beneficiary of the GSP Plus scheme would be in the textiles and garments sector. Trade analysts have estimated an overall growth of almost 15 per cent in the two sectors by the year 2014-15 and adding approximately US $ 1.5 billion to the total exports of Pakistan. Similarly other sectors like leather and leather articles, footwear, plastics, ethanol,

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22 *Annual Report 2012-13*, State Bank of Pakistan, Karachi.

23 *Ibid*.

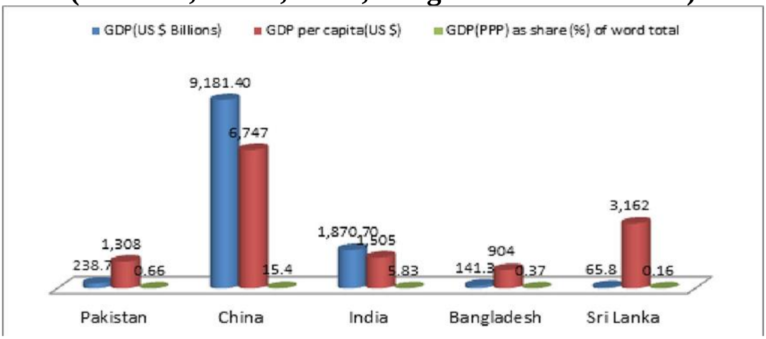
fresh and processed fruits etc. also have the potential to take advantage of the duty free access and to record healthy growth levels.[24] The possible advantages of GSP Plus are:

- Pakistan may enhance its exports in EU.
- Development of textile industry may due to increased demand of textile products.
- Rise in job opportunities for the general public.
- Increased revenue for the exchequer.
- Pakistan may invite FDI from China and other countries in the textile sector which would ensure potential for rapid export expansion.

Threats & challenges for Pakistan trade

Pakistan has to face several challenges: China is an emerging global economic power. The economic position of China and India is strong in the South Asian region. Althought, both the countries have large population, yet their GDP, GDP per capita and GDP PPP as share percentage of world total is greater than Pakistan, Bangladesh and Sri Lanka which is presented in Figure 4.

Figures 4: Key Indicators Comparison - 2013
(Pakistan, China, India, Bangladesh & Sri Lanka)



Source: The Global Competitiveness Report 2014–2015, Geneva, World Economic Forum

China continues to be the leading exporter of textiles and clothing. In 2012, EU accounting 38 per cent and the United States 20 per cent of world imports remained as the major markets for clothing.[25] According to Ahmed, Hamid & Mahmud,[26] Pakistan's share of world exports has remained almost stagnant

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[24] *Dawn*, 12 December 2013. http://www.dawn.com/news/1072051

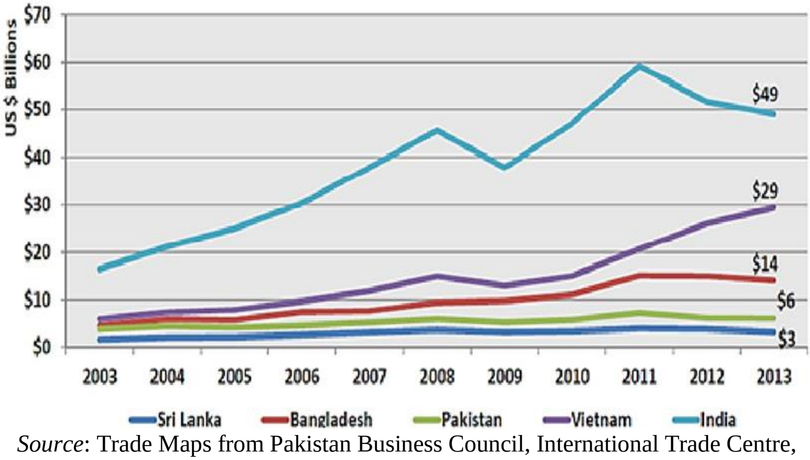
[25] *Pakistan Economic Survey 2013-14, op.cit.*

[26] H. Ahmed, N. Hamid & M. Mahmud, 'Exports: Lessons from the Past and the Way Forward', in R. Amjad & S. Burki Javed (eds.), *Pakistan Moving*

over the past three decades. South Asian neighbors of Pakistan and other East Asian countries have shown a remarkable increase in export shares. Malaysia and Thailand entered their rapid export growth phase in the 1980s and 1990s, while Bangladesh and India started it in 1990s, which continues to date. Since 1980, India has managed to increase its export share almost fourfold and Bangladesh by more than three times. As a result, Pakistan's exports which, in 1980s, were more than a third of India's and almost four times that of Bangladesh, are now less than one tenth of India's and almost equal to Bangladesh. The latter has achieved this tremendous growth through exports in the garments sector, and today the worth of the exports of Bangladesh is over 14$ billion, which is almost four times the value of Pakistan's garment exports. Pakistan's textile exports have to compete with Sri Lanka and Bangladesh and they already have duty free access to European markets.

The exports of Pakistan to EU have been outstripped by the competitors that mostly started their exports from a base which was comparable to the Pakistani base. The comparison of their exports is detailed in the Figure 5.

Figure 5: Total EU Imports from India, Bangladesh, Pakistan, Sri Lanka & Vietnam EU-27 Imports



Source: Trade Maps from Pakistan Business Council, International Trade Centre, Selected Trade and Manufacturing Data for Pakistan, 2014, p.49.

GSP Plus status will be awarded for a period of 10 years with assessment by EU after every two years of compliance status. Therefore, it will be significant for Pakistan to carry on observing 27 conventions that

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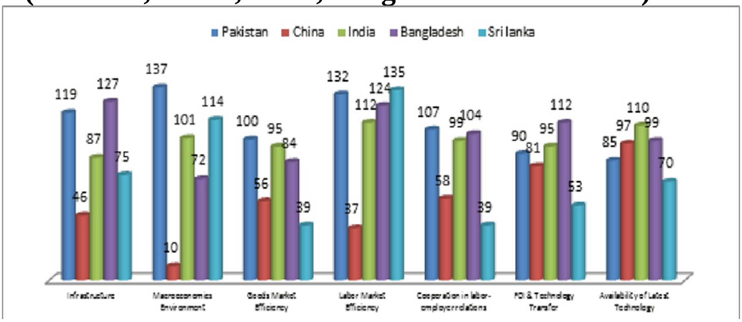
The Economy Forward. 1st ed. (Lahore: Lahore School of Economics, 2013), pp.167-93.

requires effective coordination among federal and provincial governments. At industry level effective implementation of relevant labor, environmental laws and human rights are essential. In 2010, Sri Lanka had lost its GSP status due to EU reservations which were associated to governance and human rights. It resulted in the closing of hundreds of garment factories and rendering of thousands of workers jobless. Moreover, ongoing energy crisis and law and order situation may prevent industrial sector from investing and thus enjoying full benefits of GSP Plus. If both these issues are not addressed urgently, Pakistan would not be able to exploit the potential.[27]

Improving the business environment for trade

A country's investment climate is an important factor for international incorporation. According to the World Economic Forum (2014), Pakistan ranks 137th on macroeconomic stability, which is below China and other South Asian countries like India, Bangladesh and Sri Lanka. Pakistan ranks 119th on quality of infrastructure, which is better than that of Bangladesh but worse than that of China, India and Sri Lanka. In order to develop industrial sector and trade, Pakistan must improve macroeconomic environment and infrastructure. Pakistan also lags behind in good market efficiency and cooperation in labor-employer relations. Its labor market efficiency is better than that of Sri Lanka. Pakistan's FDI and technology transfer is better than that of Bangladesh and Sri Lanka. In availability of latest technology, it just lags behind Sri Lanka. (See Figure 6)

Figure 6: The Global Competitiveness Index (Pakistan, China, India, Bangladesh & Sri Lanka)



Source: see Fig.4

To attract FDI, enhance exports and expand human capital, it is essential to promote other complementary policies like improvement in the functioning of labor markets, governance, availability of skilled and

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27 *Annual Report 2012-13*, State Bank of Pakistan, Karachi.

technical work force and reliable and well-functioning infrastructure facilities like power, gas etc.

The strategies of the countries of East Asia are a model to be followed by Pakistan. The investment of these countries was mainly made in the infrastructure of physical form. They had a target to improve their facilities at port level, in the systems of transportation and in making sure that the industries get appropriate supply of energy. The examples of countries like Korea, Japan, Singapore, and Taiwan are worth mentioning. As far as incentives are concerned, they have provided them in the form of the availability of credit at a cheap level, a break in the payment of taxes, and incentives in the form of income tax and the like. In these countries, the availability of imports at a duty free point for export industries, the growth of new markets for the export of goods, macroeconomic environment and the export-related policies were worth ensuing. They supported aggressive policies for industries of an equal value to increase domestic capacities for manufacturing so that a wide range of goods of intermediate level may be produced. These policies had a focus on both the human and physical capital formation. In these countries only those standards were adopted which were based on higher quality control and they were appreciated to follow the international standards for this could attract direct foreign investment. This ensured high rate of growth for these countries. It itself ensures a true spirit to devise the policies at various levels.[28]

Trade with neighbouring countries (China & India)

Pakistan can also generate revenue by developing trade with neighbouring countries like China and India. China, as a neighbour and an old ally, offers Pakistan enormous opporunities. Pakistan's economic interdependence with China has grown rapidly in the last decade. There is an opporunity for Pakistan, which has a large textile sector, sports goods, surgical instruments, and light engineering. The strategy of Pakistan to attract investment from China in import–substituting industry has been a failure in the past. Pakistan may only attract investment for assembly plants.

If Pakistan could control the movements of Islamic militants which cross over into China, a tremendous boost to economic activity may be made possible through transit trade, which in itself may make China invest into the northern regions of Pakistan and generate

[28] J. Page, 'The East Asian Miracle: Four Lessons for Development Policy', *NBER Macroeconomics Annual*, 1994, pp.9, 219-69, Retrieved from http://www.nber.org/chapters/c11011.pdf

opporunities for the export of the products of Pakistan to western China.[29]

Trade is the main factor in bilateral relationship between Pakistan and India. At the time of partition of the subcontinent in 1947, more than 70 per cent trade of Pakistan was with India and 63 per cent of exports of India were to Pakistan. However, trading relationship, did not last long. It plummeted, subsequent to the first armed conflict in 1948-1949. By 1951, trade, as whole, was in favor of Pakistan. Pakistan exported, from India goods worth US $113 million and imported goods worth only US $ 0.08 million. Until the war of 1965, the balance of trade remained in favor of Pakistan, except for a couple of years. After the war, trade remained suspended for a decade. It started again in 1975, after the signing of bilateral trade agreement between the two countries. Nonetheless, it continued for a short period of three years. Thus, the only time the two countries traded, based on the formal agreement, ended in 1978. During these three years, though with a small volume, the trade remained in favor of India. For the next twelve years, until 1990, volume of trade doubled to US $ 160 million and it remained in favor of Pakistan. The terms of trade shifted in favor of India during 1993-1994 and it remained so to-date.[30]

Under the obligations of the World Trade Organization, the Pakistan cabinet on 2 November 2011 approved a proposal, granting India the status of most favored nation. According to a State Bank report, many investors remain uncertain about the recent drive for trade liberalization with India, and are unwilling to take any strong position. Moreover, certain business groups are anxious that they may be drived out of the market by Indian products, especially those who are enjoying a near-captive market[31] This trade may endanger both agriculture and industry, especially the small scale industries. This may make the problem of unemployment worse. Indian economy is on the path of development while Pakistan is facing many political and

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[29] N. Hamid, & S. Hayat, 'The Opportunities and Pitfalls of Pakistan's Trade with China and Other Neighbors', in R. Amjad, & S. Javed Burki (eds.), *Pakistan Moving The Economy Forward*, 1st ed. (Lahore: Lahore School of Economics, 2013), pp.395-416.

[30] *MFN Status and Trade between Pakistan and India*, Government of Pakistan, Pakistan Institute of Legislative Development & Transparency 2012, http://www.pildat.org/publications/publication/FP/TradeRelationsbetweenPakistanAndIndia_IndianPerspective_Jan2012.pdf

[31] *Annual Report 2012-13*, State Bank of Pakistan, Karachi.

economic problems. To compete with India, Pakistan needs to improve economic climate and standard of its products.

Conclusion

Economic globalization has a subterranean impact on the economy of Pakistan. Maximum tariff rates have been brought down from late 1980s to date. Reduction in federal revenue has been compensated with an increase in GST, which increases the tax burden on general public. The prerequisite for relieving the poor is to cut down GST. Pakistan should improve its revenue by developing textile and clothing industry and by enhancing its imports. It is important to promote textile industry and to improve its quality to enjoy benefits from GSP+. In order to attract foreign investment and to expand exports, Pakistan also needs to improve macroeconomic environment and infrastructure. The policy of ensuring sound development is very much important for it may help facilitate private domestic investment and it may also strengthen human capital. To promote textile industry and to expand foreign trade, Pakistan should:

- Develop macro-economic stability to improve investment climate, investor confidence, industrial products and exports.
- Solve energy crisis to remove this great obstacle in the development of industrial sector.
- Introduce latest technology for industrial development.
- Stimulate the improvement of infrastructure facilities.
- Take measures to improve quality of the textile and clothing sector.
- Strengthen the integrity of the financial system, making capital markets far more accessible to investors.
- Upgrade the system of education in Pakistan, improve the skills of our future generation, and enhance our labor force.
- Enforce relevant labor rights and environmental laws at the industry level.
- Advance bilateral trade with China and other neighbouring countries.
- Invite FDI in the manufacturing sector.