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**Economic Cooperation between Pakistan and India:
Need, Problems, and Prospects**

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Visiting Fulbright Scholar

Program in Arms Control, Disarmament, and International Security

University of Illinois at Urbana-Champaign

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INTRODUCTION

Growing disequilibrium in the international trade and monetary system is causing unprecedented deficits in external payment positions and major currency fluctuations in the Third World. This situation also leads to deflationary and protectionist policies by industrialized countries. The emergence of assertive economic nationalism and the development of protectionist alliances in the North increase the Third World's sensitivities to an unjust world economic order. Ironically, the phrase "free trade" often obscures the effects of growing restrictions on trade imposed by the North that discriminate against the manufactures of Third World countries. This trend exposes the rigidity and lopsidedness of the contemporary international division of labor, which in theory and practice serves the interests of the strong in the global political economy. The North's reluctance to accept structural changes in the contemporary international order to accommodate the legitimate interests of the South creates and widens a gap in the equitable distribution of the benefits of interdependent economic linkages along the North-South dimension. Restricted flows of trade, finance, and technology from the North dictate the need for an alternative—comprehensive regional and bilateral economic cooperation among Third World countries.

With the formal launching of the South Asian Association for Regional Cooperation (SAARC) in 1985, there was a common perception among the weaker member states of the region that India would dominate SAARC and its goals of promotion of mutual trade and enhanced economic cooperation. This is not a far-fetched view, as "bargaining power" often brings an advantage for the powerful. In this context, Pakistan is in a relatively better bargaining position, as compared to the other SAARC member states, to interact with India. This can be beneficial for both major states of South Asia.

India and Pakistan are not only neighbors. They share a common historical past and socioeconomic affinities. Development of trade and other economic relations between them is natural and necessary to maintain historical continuity, peace, and stability—as well as fostering development—in South Asia. Expansion of these relations can help significantly in reducing regional tensions and mutual mistrust.

This paper explains and analyzes the need to overcome political and economic obstacles to foster increased mutual trade between India and Pakistan in the context of the global political economy. For this purpose, the time period selected runs from 1947 to 1990. With the uprising in India-controlled Kashmir in 1989 and allied issues since, there has been little significant change in trade relations between the states, although recent developments in the last decade and a half are an indication of hope for mutually beneficial cooperation. There are proposals to increase cooperation in the energy sector—principally a gas pipeline from Central Asia to India through Pakistan—but as of the writing of this paper the project was stalled. Thus, it is not addressed here.

The paper is divided into four parts. Part one deals with the need of developing countries like India and Pakistan for greater cooperation. Part two explains the issues hindering increased trade between them. The third part explains the historical and ongoing nature of economic interaction between India and Pakistan. The fourth part focuses on the prospects for better economic intercourse and presents some suggestions for the realization of full trade potential between these South Asian neighbors.

Proposals to institutionalize and strengthen economic cooperation between India and Pakistan must be based on four assumptions. First, the traditional search of India's neighbors, in general, and Pakistan, in particular, for extra-regional factors to balance a perceived Indian threat has resulted in economic linkages which constructed a "metropolitan" orientation for the Pakistani economy. Second, a "slapdash" breaking off of economic ties during the 1947 partition for political and security reasons not only undermined the possibility at the time for the establishment of a common market, but over the decades has institutionalized economic and industrial patterns which are resistant to the structural changes required for expanding and facilitating the process of bilateral cooperation. Third, equitable distribution of benefits from liberalization of trade and expansion of cooperation in areas of commercial and industrial activity will reduce the severity of hitherto unresolved political disputes to a manageable level. Finally, dialogue through a regional forum—South Asian Association for Regional Cooperation (SAARC)—and greater diplomatic and economic interaction can bring positive changes in the attitudes of policy-makers and foster a consensus on peaceful means of conflict resolution.

These are reasonable assumptions because economic pragmatism has the potential to curtail the disruptive influence of emotional factors on foreign policy. In a region where stereotypes, conflicting images, and the frequent perception of hostile motives play crucial roles in bilateral relations, attempts to foster economic cooperation are unlikely to remain unaffected by the dominant influence of political and security factors. It is always difficult to access the motivations of actors that drive foreign policy. Hence the standard methods of research used in social sciences, such as personal interviews, participant observation, and questionnaires, cannot be used for this type of study. Due to the limited scope of the paper, I have relied first and foremost on primary sources such as public documents, official government declarations, official records, reports, and statements of heads of state, prime ministers, foreign ministers and ministers for commerce and trade, as well as secondary sources, such as books and articles published in journals and newspapers.

Need for Cooperation

Peeling off the folds of history, one sees that the less developed countries of the world that suffered from colonial exploitation in the past were placed at an economic disadvantage when they gained formal independence, and that disadvantage continues to affect their present situation. Their economies were reconstructed as appendages to imperialism, frequently replicating the market distortions of colonialism. This hard fact is largely responsible for the continuing underdevelopment of the Third World. The post-war period witnessed a total collapse of the colonial system, as most former colonial countries achieved formal political independence. However, these newly independent nations often maintained their economic ties with the erstwhile imperialist countries and, as a result, they have yet to achieve real economic independence. Dependent economies in the Third World remain subject to external exploitation within the neo-colonial framework established by the advanced countries.¹ The present framework of international economic relations is biased in favor of advanced economies. Developing countries find the markets of developed countries frequently inaccessible, particularly for their manufactured goods. These goods face high tariff walls. As a consequence, their market share in the world market is shrinking. Due to limitations on value-added exports from these countries, their capacity to import is also falling. In other words, the developing countries are facing adverse terms of trade.

Given the unjust nature of the international economic system, the developing countries are pressing for thorough international trade reforms. The Group of 77 and non-aligned countries, in their summit meeting at Algeria (Sept. 1973), mooted the New International Economic Order (NIEO) at the United Nations Conference on Trade and Development (UNCTAD). This program of action is known as the “North-South Dialogue” and was formally adopted by the UN in a special session of its General Assembly in 1974. However, its implementation has been very limited, with results that are far from encouraging. Given the balance of international economic strength, there is little hope that partial reforms of international economic relations will significantly alter this situation.² In such circumstances, the less developed countries were left with no option except to develop mutual trade and build their collective strength to fight against unjust and uneven economic growth. Bilateral cooperation and mutual trade between less developed countries are the only ways to ensure the end of underdevelopment. These shared challenges demonstrate a need to develop mutual economic relations between India and Pakistan to work collectively against an unjust international economic order.

India and Pakistan share a common historical past. Development of economic relations between them is natural and necessary to maintain historical continuity and peace in the region.³ Expansion of relations between the two countries counteracts the mistrust engendered by more than half a century of considerable tension and occasional outright conflict. The first Indian prime minister, Jawaharlal Nehru, emphasized the need for cooperation between the two countries when he noted that these neighbors play an important role in Asia. By following a contrary policy where they oppose each other, then each neutralizes the other—considering that both now possess nuclear weapons, they even may be wiped from the face of earth.⁴ Pakistan’s first foreign minister, Zafarullah Khan, expressed similar views when he stated that the two countries—acting together—could play a decisive role in world affairs.⁵

Geographic and historical factors also dictate that the economies of the two countries should not be treated as mutually exclusive and separate.⁶ The realization of this necessity led to the signing of the first trade agreement between the two countries shortly after independence in May 1948, as well as a number of

¹ Jack Woddis, *Introduction to Neo-Colonialism* (New York: Harper & Row, 1976), 12.

² Sundra Sen, “New International Economic Order and Contemporary World Economic Scene,” *Economic and Political Weekly*, 1981 Annual.

³ Sucha Sing Gill and R. S. Ghuman, “Indo-Pak Trade: Prospects and Constraints,” in *Studies in Indo-Pak Relations*, ed. V.D. Chopra (New Delhi: Patriot Publishers, 1984), 187.

⁴ Ajay Saksina, *India and Pakistan, Their Foreign Policies* (Delhi: Anmol Publications, 1987), 185.

⁵ Zafarullah Khan, *Pakistan Foreign Policy Relations* (Karachi, 1951), 8.

⁶ G.W. Choudhury, *Pakistan’s Relations with India, 1947–1966* (London: Pall Mall Press, 1968), 142.

subsequent trade agreements.⁷ Under an agreement signed on January 22, 1957, the two governments agreed to explore the possibilities of trade expansion on the basis of mutual advantage.⁸

Geographical proximity and economic complementarities are the obvious advantages and should have already brought India and Pakistan more closely together in commercial relations. Instead, political difficulties created artificial barriers to trade between them, which helps no one but the smugglers.⁹

The masses of Indo-Pakistan are suffering from a very serious economic situation. Their difficulties have been further multiplied by spiraling oil prices—leading to their dependency on the Gulf States—and the unwillingness of developed countries to offer fair terms of trade to developing countries. It is therefore not in their interest to put exclusive faith in the industrially advanced countries for trade and economic cooperation. Instead, they should try to expand trade among themselves. Experience has shown that reliance on traditional markets and resources alone will fail to sustain their developing economies.¹⁰ The common presence of an under-utilized labor force should not unduly discriminate against either country in terms of the benefits to be gained through mutual cooperation. India and Pakistan together form a market of formidable size, large enough for the exploitation of economies of scale without the concomitant ills of monopoly.

The primary difference in the level of economic development between Pakistan and India is the relative position of the industrial sector in both states. For example, consumer goods production accounts for a much larger proportion of total industrial output in India than it does in Pakistan. This difference reflects the nature of import substitution that occurred in the two countries since 1947. Pakistan has achieved a notable degree of import substitution in important consumer goods—such as textiles, sugar, edible oils, food products, cigarettes, footwear—and also in some intermediate goods, including paper and paper products, cement, and jute manufacturing. In India, besides the rapid growth of consumer goods industries, a considerable degree of import substitution has taken place in important basic intermediate goods—particularly steel, aluminum and chemicals—and producer goods, like machinery and machine tools, transport equipment, and heavy electrical equipment.¹¹

Thus, the economies of both countries are inward-oriented; neither country depends significantly on foreign trade. Indian capital goods account for about 25 percent of their total exports, raw material and intermediate goods of cotton, fertilizer, iron, etc., accounted for more than 50 percent of their total exports in that period. The important items of export from Pakistan are cotton, textiles, rice, leather goods, etc. Thus the industrial structure and pattern of foreign trade of these neighbors amply demonstrates the potential for a high degree of complementarity, which is an essential element of mutually beneficial regional economic cooperation.

Though the trade dependence of both countries on other countries appears to be small, they constantly face an adverse balance of trade. The trade gap is 60 and 77 percent, respectively, in the cases of India and Pakistan. Due to the massive flow of foreign resources in the form of loans and economic aid into both countries, they have compensated for such a large trade gap without seriously affecting their development programs. Improvements in the balance of trade—either through trade creation or trade diversion, achieved by fostering increased economic cooperation between the two countries—could be highly beneficial for both.

Pakistan faces tremendous problems of import substitution in capital and intermediate goods, which can only be achieved at a very high price. For India, the problem is to make fuller use of her existing capacity in capital and intermediate goods. Further expansion of capacity in these areas is fraught with both limited domestic demand and associated ills of monopoly without the benefits of greater economic cooperation.¹²

Both Pakistan and India are likely to lose by competing with one another in the world market. Collaboration between the two in non-trade fields may not boost foreign trade, but it can indirectly benefit various economic sectors in each. For example, such cooperation in the non-trade fields could include the mutual development of water and power resources, exchange of technical and academic expertise, etc. Thus,

⁷ Saksina, 187.

⁸ *The Statesman* (Peshawar), January 23, 1957.

⁹ Saksina, 197.

¹⁰ *Ibid.*, 200.

¹¹ *Ibid.*, 201.

¹² *Ibid.*, 203.

there are strong reasons for closer cooperation between the two countries.¹³ Both countries are at almost the same stage of economic growth in foreign trade and standards of living. A relatively higher rate of growth in Pakistan neutralizes its disadvantage of being a smaller partner. This ideal configuration of factors is essential for putting into place policies to advance economic cooperation's promise of substantial mutual benefit for both countries.

Economic cooperation between neighboring countries is a means of comparatively speedy economic development. The fusion of markets in neighboring countries through economic cooperation is certain to bring economic gains to both as it will introduce free trade while simultaneously providing the necessary protection against the onslaught from industries in other Third World countries.¹⁴

In the case of neighboring countries like India and Pakistan, this merger of internal markets is an important and potent tool of economic advancement. The most important advantage in such an arrangement is the expansion in the size of the joint internal market. The transformation of developing economies from agricultural to industrial is an essential requirement for sustained economic gains. Such a transformation is not possible unless there is sufficient demand generated for products from growth, either within the internal market or from the external market.¹⁵ In fact neither India nor Pakistan has sufficient demand from their individual markets or from markets abroad for much of their existing industrial base. The products produced by infant and inefficient industries cannot compete with the products of developed countries, undermining their ability to market to industrialized nations even if trade restrictions were not present. There is a need to expand internal markets through the development of economic relations between the two countries to enable their industries to take advantage of this growth, transforming agriculturally based economies into a growing industrial economic sector in order to alleviate the poverty of the masses.¹⁶

In the absence of effective economic cooperation, both countries are likely to pursue their own industrial development program, with each country developing redundant industrial units. In most cases, this will amount to a duplication of inefficient facilities and market structures. Due to the relatively poor quality of products typically produced in such protected markets, these producers are also unlikely to find markets in the industrialized world. Therefore, a need exists to determine areas of economic cooperation that foster industrial activities so there are efficient markets in each country. This would generate sustainable industrial activity and employment within both states.

It is time for the people of Pakistan to stop flagellating themselves over India's progress in diverse fields and look instead to the tremendous possibilities for mutually beneficial cooperation. Economic relations without strings are a prerequisite for global prosperity. Since the end of World War II, the trend has been to dismantle trade barriers and promote interdependence so that the economic lot of the people is improved. Trade should no longer be a tactic of economic imperialism; it has to be pursued on the basis of mutual advantage.¹⁷

¹³ Ibid.

¹⁴ R.L. Varshney and Raj Kumar, "SAARC: Need For Economic Cooperation," *Foreign Press Digest* (New Delhi), Vol. 38, No. 1 (January 1989).

¹⁵ Ibid., 3.

¹⁶ Ibid.

¹⁷ N.C. Menon, "Pakistan Need to Trade," *Hindustan Times* (Delhi), January 15, 1986.

PART TWO

Problems

Political

Since the partition of the sub-continent into India and Pakistan, the relationship between these neighbors has often been far from friendly.¹⁸ Both countries felt threatened by each other and continue to emphasize strengthening their armed forces. The gravest discord between any two members of the United Nations is found between India and Pakistan.¹⁹ The major causes of the conflict include differing ideologies,²⁰ negative images of each other, mistrust, and wide divergence in their foreign policy goals.²¹ Pakistani perceptions have been influenced by distrust of India—what it alleges are India's hegemonic regional and international ambitions, exacerbated by what Pakistan sees as an ambitious and aggressive regional foreign policy.²² This long history of acrimonious relations, armed conflict, and lack of accord on a number of regional and international issues creates a gulf of distrust between the two countries.²³ However, this troubling situation must be resolved to mutually benefit the populations of both nations.

The differing foreign policy concerns and alliances of the two countries are, in fact, both a product of and a contributor to the tensions. In line with India's troubling policy of opposing United Nations and other extra-regional involvement in South Asia, such perceptions of threat on the part of Pakistan are further motivated by India's historically close ties with the former Soviet Union—with Pakistan caught in between their two spheres of influence. Furthermore, India has strongly opposed Pakistan's close ties with the United States and the accompanying U.S. arms assistance to Pakistan. In the wake of the post-September 11 U.S. invasion of Afghanistan, for its part, India has feared further regional instability.²⁴ Thus, stable and secure borders, more than ever, are now a shared security interest.

India's strong alignment and security links with the former Soviet Union are motivated by a desire for the most sophisticated weapons from Russia's arms industry. India also seeks indigenous capability to develop and co-produce advanced weapon systems, adding to its capabilities as a fearsome war machine. Its ever-growing defense capability and assertive position on bilateral issues serve to magnify Pakistan's perception of the Indian threat.

India's overall military capabilities and her quest for a superpower role in the region are strong factors influencing the defense and foreign policy orientations of Pakistan.²⁵ The geopolitics of the region places India in a commanding position, with a ring of weak and vulnerable states around it. The combined military resources of the other six nations in South Asia amount to only about fifty percent of the numerical strength of the Indian armed forces and thus cannot challenge its military might.²⁶

What is the real intention of India in adopting a posture of perpetual accumulation of military strength? This is the nagging question, which boggles the minds of many observers of the scene. Pakistan's reading of Indian motives is unequivocal in voicing concern about India's quest for hegemonic domination over South Asia. Unfortunately, Pakistan's problems with India run deep in history. The spill-over psychological effects of the communal blood bath of the pre-independence period; India's withholding of Pakistan's share of military stores and denial of cash balances to Pakistan at independence; disputes over sharing the waters of the Indus

¹⁸ S.S. Bindra, *Indo-Pak Relations: Tashkent to Simla Agreement* (New Delhi: Deep & Deep Publications, 1981), 11.

¹⁹ Choudhury, 3.

²⁰ Bindra, 11.

²¹ "SAARC at the Cross Roads: The Islamabad Summit and Beyond," *Spotlight on Regional Issues*, Vol. 8, No. 3 (March 1989), 10.

²² Agha Shahi, "Keynote Address at a Seminar on SAARC at Islamabad," *The Muslim* (Islamabad), February 18, 1986.

²³ Hasan Askari Rizvi, "Problems and Prospects of South Asian Regional Cooperation," *Regional Studies*, Vol. II, No. 2 (spring 1984), 20.

²⁴ "SAARC at the Cross Roads," 11.

²⁵ Leo E. Rose and Satish Kumar, "South Asia," in *Comparative Regional Systems: West and East Europe, North America, the Middle East and Developing Countries*, eds. Werner J. Feld and Gavin Boyd (New York: Pergamon Press, 1980), 236.

²⁶ Sushil Sharma, "Strains of Cooperation," *Pakistan & Gulf Economist* (October 27–November 2, 1990), 18.

Basin,²⁷ the secession to India of the three predominantly Muslim regions ruled by the three Hindu princes of Junagarh,²⁸ Hyderabad,²⁹ and Kashmir;³⁰ and three full-fledged wars—the last resulting in dismemberment of Pakistan—along with other issues such as Sir Creek, Siachen, the “Wullar Barrage,” and the recent demolition of Babri Masjid by Hindu fanatics have repeatedly perpetuated hostile images of India, undoubtedly impeding the normalization process. The threat from India is the central concern of Pakistan’s security policy, leading it to pursue a defense build-up disproportionate to its resources.

Of all the issues, the Kashmir dispute has proved to be the most intractable.³¹ “Plebiscite, partition, internationalization, political settlement, and all the text book solutions for a territorial dispute have been proposed for Kashmir and all have been fruitless.”³² This conflict remains the major obstacle to a peace settlement in the subcontinent.³³

Owing to mutual fears prompted by fear of hostile motives, India and Pakistan are trapped in a reactive regional arms race. India needs weapons to substantiate its claim as the “paramount” regional power. In line with their regional ambitions, Indian leaders raise objections to Pakistan’s security linkage with the United States and bitterly oppose its purchase of modern weapons. US security assistance to Pakistan, from the Indian point of view, upsets the natural balance of power in the region. Pakistan views Indian attempts to cast a veto on both the nature of its relations with major powers and on its defense procurement policy as the effectuation of an Indian variety of “Monroe Doctrine” in South Asia.³⁴ Pakistan’s nuclear program generates much heat in bilateral relations, which is destabilizing from the Indian point of view. Traditional rivalries, perceptions by many that the other is an enemy, and mistrust of each other’s intentions cast a long shadow over the prospects of tension-free Indo-Pak relations.³⁵

Two factors reinforce the fear complex. First, India’s pursuit of an assertive, dominant status in the region—through enhanced military capability and exclusive bilateralism—leads it to reject third party mediation. Since 1972, India has explicitly rejected all United Nations efforts to resolve disputes with her neighbors.³⁶ A second factor is the failure of Pakistan to evolve a meaningful dialogue that promotes a durable process of peaceful resolution of regional disputes.

The fundamental problem is suspicion and mistrust.³⁷ Some outstanding disputes have been solved, but the depth of this mistrust and prejudice vitiates prospects for an abiding “good neighbor” relationship. “Pakistan does feel,” says professor Quincy Wright, “that India has its eye out for re-annexation of Pakistan.”³⁸ This fear and mistrust is further engendered by statements from some Indian leaders; they continue to preach the illusory goal of a unified India—including Pakistan—up to the present day, sometimes in threatening language, sometimes in a more benign fashion. The ideal of a united India still seems to dominate a powerful sector of Indian opinion. “As late as 1963,” states Professor F.N. Trager, “Nehru regarded Pakistan as an area which should be reincorporated into an Indian dominated confederation.”³⁹ These major differences in the political and security perceptions of both countries, coupled with mistrust about each other’s intentions, affect the shape and scope of mutual cooperation between Pakistan and India.

²⁷ Mahtab Akbar Rashdi, *Indo-Pak Relations* (Jamshoro, Pakistan: Pakistan Study Centre, University of Sindh, 1988), 11.

²⁸ Choudhury, 6.

²⁹ Bindra, 23.

³⁰ Choudhury, 6-7.

³¹ Rashdi, 13.

³² G.W. Choudhury, *Pakistan’s Relations with India* (Meerut, India: Meenakshi Prakashan, 1971), 103.

³³ Rashdi, 17.

³⁴ Rasul B. Rais, “Mounting Threats to Stability,” *Pakistan Times* (Rawalpindi), October 27, 1983.

³⁵ Bhabani Sen Gupta, “SAARC Meet: Paradise Postponed,” *The Hindustan Times* (Delhi), November 18, 1986. See also Muhammad Ayoob, “The Primacy of Politics: South Asian Regional Cooperation in Comparative Perspective,” *Asian Survey*, Vol. 25, No. 4 (April 1985), 443, 457.

³⁶ K.R. Narayanan, “New Perspectives in Indian Foreign Policy,” *The Round Table*, October 1972, pp. 232–248. See also Balder Raj Nayer, “Treat India Seriously,” *Foreign Policy*, No. 18 (spring 1975), 133, 154.

³⁷ A.I. Akram, “India and Pakistan—A Glorious Future,” *Regional Studies*, No. 7 (July 1984), 4-5.

³⁸ A. Harrison, “Where to Make a Start?” *Hindustan Times* (New Delhi), April 29, 1983.

³⁹ F.N. Trager, “The United States and Pakistan: A Failure of Diplomacy,” *ORBIS*, Vol. 9, No. 3 (1965).

Economic

To analyze the economic problems restricting greater Indo-Pak cooperation, let us first examine them in the context of the global political economy. The principal form in which foreign capital comes into Pakistan is in the form of tied credits.⁴⁰ These credits are used to capture local markets for products from the metropolitan countries that manufacture industrial equipment. Metropolitan capital has a large stake in projects undertaken by the state itself. The metropolitan bourgeoisie—in the form of multinational corporations (MNCs)—exerts enormous economic and political power in Pakistan. Led by the advanced industrialized states, MNCs operate in Pakistan through enterprises wholly owned by them, as well as those that are owned in partnership with local private capital or public sector enterprises. Those Pakistanis associated with MNCs are the most powerful of the three dominant classes in Pakistan (the other two being landlords and the petty bourgeoisie).⁴¹ This metropolitan-associated bourgeoisie opposes entry of manufactured products from other developing Third World countries into Pakistan.⁴² The main opposition to the development of increased Indo-Pak trade within Pakistan comes from these powerful groups which are connected with western-based MNCs. India can supply many consumer goods to Pakistan at prices lower than such imports from Western countries.⁴³ Cheaper labor and lower freight cost make Indian products very competitive when they are allowed access to the Pakistani market.⁴⁴ Thus, Indian entry into Pakistan's market poses a serious threat to the interests of those associated with MNCs. The considerable influence that MNCs enjoy in Pakistan is one of the major constraints to the development of expanded Indo-Pak economic relations. These parallel foreign and domestic vested interests magnify the psychological threats of Indian domination over Pakistan and are thus instrumental in blocking the expansion of mutually beneficial economic relations between the two countries.

External factors are also responsible for preventing Pakistan and its other SAARC partners from increasing their share in the volume of intra-regional trade.⁴⁵ These seven countries are all heavily dependent on the developed world for aid, technology, and assistance. This dependence on the industrialized countries and their institutions in turn determines the pattern and direction of much of the trade within the South Asian bloc. Moreover, the South Asian states are very poor in energy resources such as oil and gas. Hence they are forced to spend large portions of their scarce financial resources on the purchase of fuel from other parts of the world. This dependence on external fuel sources further limits their foreign trade options.

Continuing economic crisis in the global economy exacerbates the political crises in the Middle East, causing further deterioration in the economies of South Asian states, especially Pakistan and India. This increases their dependence on trade with the developed world. The Indian policy of non-alignment enabled that country to follow a relatively independent path of development.⁴⁶ As a result, India was able to maneuver between Washington and Moscow to create a somewhat independent economic base.⁴⁷ On the other hand, Pakistan tied its economy completely to that of the US bloc and lost the leverage of relations with Moscow in bargaining with the United States. Foreign indebtedness and huge energy bills also tied Pakistan's foreign trade and economy to that of the developed and oil exporting countries. Pakistan's major trade partners are industrialized countries, including Japan, followed by Middle Eastern countries. The same patterns prevail in respect to its imports.⁴⁸

Two other factors are responsible for hindering the expansion of Indo-Pakistan trade, in particular, and intra-regional trade in general. One is the lack of industrial complementarity and lack of competitiveness in the South Asian regional economies. The other is the geophysical and economic status of India vis-à-vis Pakistan and other smaller South Asian states.

⁴⁰ Hamza Alvi, "Character of State in Pakistan," in *Studies in Indo-Pak Relations*, ed. V.D. Chopra (New Delhi: Patriot Publishers, 1984), 197.

⁴¹ Alvi, 187–198.

⁴² *Ibid.*

⁴³ "Curbs on Indo-Pak Trade, MNCs Pressure," *Patriot* (New Delhi), July 29, 1978.

⁴⁴ *Ibid.*

⁴⁵ Gamini Corea, "Regional Cooperation in South Asia: Perspective and Progress," *South Asian Journal*, Vol. 1, No. 1 (July–September 1987).

⁴⁶ Chopra, 197.

⁴⁷ S.S. Gill, *Political Economy of Indo-Soviet Relations* (New Delhi: Rajesh, 1983), 151–156.

⁴⁸ *The Muslim* (Islamabad), August 26, 1988.

One example of this element of inefficient competitiveness is visible between India and Pakistan in the field of textiles. According to a Bangladeshi analyst, a “stumbling block in the full flowering of the process [of regional cooperation] is the self-perception of India as a colossus in the regional.”⁴⁹ Apart from India’s “self-perceptions,” India does overshadow Pakistan and other small states in the region by the sheer size of its market. Its population is three times more than the combined populations of all the other regional states. “It has virtually 100 percent of the total resources of the region in respect [to such strategic resources as] uranium, iron ore, bauxite, copper, gold, lead, manganese, silver, tungsten, zinc, asbestos, and diamond. It has more than 90 percent of the resources in coal, crude petroleum, chromium, magnetite, and salt.”⁵⁰ Moreover, India is at a far more advanced stage of economic development than most of the South Asian states, especially in the field of heavy industry. India has “attained high levels of sophistication in the development of certain industries and can produce the bulk of the capital equipment required for its own development and for export.”⁵¹

Bilateral economic relations between the two countries are currently minimal. Although the balance of what little bilateral trade exists continues to be in favor of Pakistan, it has neither been keen to expand such trade with India nor has it shown any great interest to include trade in the accepted areas of cooperation. This reluctance is based on Pakistani apprehensions that unregulated, increased economic exchanges with India could pose a threat to Pakistan’s industry, as they are seen as potentially working in favor of India’s more developed industrial infrastructure. Pakistan also fears that such regional cooperation could result in a gradual but growing one-sided economic dependence of Pakistan and the smaller SAARC nations on India, which could in turn lead to political dependency.⁵²

These economic disparities, especially in the relative levels of capital goods production between India and the rest of the South Asian region, raise “doubts about the role of ‘big brother’ [India] among the smaller nations of the region.”⁵³ Pakistan shares with the other regional states a fear that the removal of all trade barriers in the interests of regional cooperation could result in the smaller states becoming India’s dependent trade partners, selling their primary commodities in exchange for manufactured goods from India. This apprehension was expressed by a Nepalese analyst, who warned that his country should be watchful, because “in the name of regional cooperation, Nepal should not become the village of South Asia,” a mere supplier of primary commodities to the more industrialized countries.⁵⁴ The South Asian countries are not interested in promoting cooperation constructed so that it results in a one-sided dependence on India. “There is also a political aspect,” adds the Marga Institute survey on regional cooperation. “Economic dependence can result in political dependence and countries jealous of their independence cannot contemplate such relationships with equanimity.”⁵⁵

Moreover, the current state of direct communications between Pakistan and India is rather poor. Travel restrictions between these neighbors are much more severe than those applied to residents of other countries. It is difficult to find information on the production, consumption patterns, and trade channels of each country from sources within the other. This lack of communication between India and Pakistan is reflected in the broader issue of the inability of the respective national chambers of commerce to even identify broad groups of products that could be traded between the wider group of SAARC countries.⁵⁶

The domestic savings of Pakistan are insufficient to internally finance the investment required to realize an acceptable minimum growth rate of output in its gross national product (GNP). Similarly, Pakistan’s export earnings are quite inadequate to finance its growing import requirements. Accordingly, its reliance on foreign capital is rather significant, with the result that a substantial proportion—almost one half—of all imports is financed through foreign aid. Since such financing via foreign capital is usually tied to its source, a diversion of this trade to encourage increased regional cooperation will be difficult. While the limited resources of the South Asian countries pose a major constraint to trade diversion, the existence of idle capacities in a large number of industries holds promise for trade diversion.

⁴⁹ Mizanur-Rahman Shelley, “India and Regionalism in South Asia,” *The New Nation* (Dhaka), November 1, 1982.

⁵⁰ M.L. Qureshi, *Compatibility of South Asian Economies* (Lahore: Vanguard Books Ltd., 1984), 12.

⁵¹ Qureshi, 228.

⁵² “SAARC at the Cross Roads,” 17.

⁵³ Harrison, “Where to Make a Start?”

⁵⁴ P.P. Timilsina, “South Asian Economic Cooperation and Nepal,” *The Rising Nepal* (Kathmandu), September 12, 1980.

⁵⁵ Qureshi, 240.

⁵⁶ *The Muslim* (Islamabad), August 26, 1988.

PART THREE
Patterns of Economic Interaction

The complex economic relationships in the Indo-Pakistan subcontinent were not given any serious thought when the scheme for partition of British India into the independent states of Pakistan and India was being decided.⁵⁷ As a result, the interconnected economy of the former British Indian Empire was violently vivisected at independence for Pakistan and India in 1947.⁵⁸

Prior to independence, the economies of India and Pakistan were part of a deeply interlinked, unified economy. Partition dismembered the whole basis of the economy in the subcontinent.⁵⁹ The limited international trade that began between India and Pakistan was therefore a direct result of partition in 1947. Pakistan suffered badly, largely due to the preexisting uneven distribution of the industrial sector within the subcontinent economy. Major industries were concentrated in the areas that formed the Indian union. Pakistan retained only 16 out of 405 cotton mills; only 11 out of 153 sugar factories; and all the jute mills went to India. In short, India received 86 percent of the total industries and 90 percent of the total skilled workers.⁶⁰ The most productive coal, iron, and other mines fell into India's share of the subcontinent. This resulted in gloomy predictions about the economic viability of Pakistan, with many quarters predicting its early collapse as an independent state.

The situation was further aggravated by the other disputes that emerged between the two countries, which continue to adversely affect their relations. Due to this political acrimony, trade and economic relations had a very slow start in 1947. Taking into consideration this slow pace of economic growth, the patterns of Indo-Pak economic interaction can be divided into three phases: from Independence to the Simla Agreement (1947–72); post-Simla to the first SAARC Summit (1972–85); and from the first SAARC Summit to 1990.

From Independence to the 1972 Simla Agreement

At the time of partition, a “Stand Still Agreement” was signed by the two countries, which permitted the free passage of goods between them.⁶¹ The result was the formation of a brief, de facto customs union between India and Pakistan.⁶² This came to an end in less than three months, when India refused to give Pakistan any share of the export duties collected on jute.⁶³

The Government of Pakistan offered to enter into arbitration on the jute dispute.⁶⁴ India, instead of agreeing to arbitration, declared Pakistan a foreign country for the express purpose of levying customs and excise duty. Meanwhile, the Stand Still Agreement came to an end on March 31, 1948. On April 1, 1948, India precipitated a crucial problem over the division of the Indus River waters, withholding its flow into the Sutlej Canal Project. However, in 1949 India signed another trade agreement with Pakistan, which allowed various categories of goods to cross the Pak-India borders without export licenses.⁶⁵

Further improvement in Indo-Pakistan trade and economic relations might have been positive, except for the British government's decision to devalue the pound sterling. India devalued its currency in 1948. However, Pakistan did not follow suit, a decision that was received with indignation by India. In retaliation, the Reserve Bank of India stopped quoting any rate for the sale or purchase of Pakistani currency. The ensuing economic war of attrition made the 1949 trade agreement a dead letter.

⁵⁷ Choudhury (1968), 141.

⁵⁸ Douglas Brown, “India and Pakistan: A More Harmonious Phase,” *Daily Telegraph* (London), August 15, 1949.

⁵⁹ Sucha Sing Gill and R.S. Ghuman, “Indo-Pak Trade: Prospects and Constraints,” in *Studies in Indo-Pak Relations*, ed. V.D. Chopra (New Delhi: Patriot Publishers, 1984), 189.

⁶⁰ Naeema Sultan Begum, “Indo-Pakistan Trade Relations,” *Pakistan Horizon* (Karachi), September 1950.

⁶¹ Alvi, 189.

⁶² Choudhury, 143.

⁶³ Government of India, *White Paper on Indo-Pakistan Trade Relations* (New Delhi, 1950), 3-4.

⁶⁴ *Dawn*, November 16, 1947.

⁶⁵ Choudhury, 144.

Inter-dominion trade came to a dead stop in September 1949—at the time, 60 percent of Pakistan’s total foreign trade was with India, while 30 percent of India’s trade was with Pakistan.⁶⁶ In the “battle of rupees,” both parties lost. More than a hundred cotton and jute mills in India closed down. India used coercive methods, including a protest to the International Monetary Fund (IMF) disputing recognition of a higher value for Pakistani rupees, but Pakistan stood firm against India’s economic pressures. Eventually, both states realized that the interdependence of their economies required some minimum level of cooperation.

Following diplomatic negotiations, a meeting between the two prime ministers to discuss the issue occurred in April 1950. Afterward, Indo-Pak economic relations entered into a complementary phase. Solving the trade deadlock, Pakistan and India signed a trade agreement on April 21, 1950, with both parties welcoming it as the first step towards reviving mutual trade.⁶⁷ Though there were certain criticisms of it, generally the promise of cooperative trade relations was welcomed.⁶⁸ However, the ongoing dispute over exchange rates remained the main obstacle to full resumption of trade. This dispute was subsequently referred to the IMF. While the IMF’s decision was pending, negotiations were reopened at India’s request. A new trade agreement was signed on February 25, 1951, ending seventeen months of deadlock through India’s acceptance of the par value of the Pakistani rupee.⁶⁹

Despite these initial difficulties, trade and economic relations persisted between the two countries until the 1965 war, which led to severe trading restrictions.⁷⁰ During 1966–67, absolutely no trade occurred due to a trade embargo imposed by both parties. The situation was little better throughout the period from 1968–70. This trade embargo between the belligerents provided opportunity for others to replace cross-border trade by entering the Pakistani and Indian markets.⁷¹ During this period, inter-state smuggling continued, with Indian goods routed to Pakistan via third countries at much higher prices than the export income of these goods to India. This smuggler’s paradise was another indicator that there was nonetheless a need to cooperate for mutual benefit. During 1970–71, Pakistan also imported goods worth Rs. 4 million (approximately \$67,000 at today’s exchange rate of \$1 for 60 Pakistani rupees) from India, as a gesture of goodwill to seek resolution of prisoner of war (POW) repatriations after the dismemberment of Pakistan.

From the Simla Agreement to the First SAARC Summit

The Simla Agreement of 1972 constitutes an enduring basis for the normalization of relations between Pakistan and India.⁷² Indo-Pakistan trade and economic relations, severed in 1965, were re-established by it in 1974. In pursuance to Article 3 of the Simla Agreement, a trade protocol was signed in November 1974, lifting the embargo on trade between the two countries. Full working relations resumed in January 1975 with an agreement signed at Islamabad. Both countries agreed to most favored nation (MFN) treatment of each other.⁷³ The agreement envisaged inter-governmental trade. Later in 1976, trade was also extended to the private sector on both sides.

Mutual trade worth Rs. 230 million (\$3.8 million) in the year 1975–76 was a good beginning, but the trade dwindled to a mere Rs. 90 million (\$1.5 million) in the next year.⁷⁴ During 1977–78, trade rebounded to a level of 650 million rupees (\$10.8 million), due to activity in the private sector. Private trade was allowed for just two years from July 1976 to July 1978, after which it was again banned. Accordingly, the trade dropped in 1978–79. This decline was followed by an upward trend in 1979–80 as a result of efforts by both governments to revive mutually beneficial trade. During this period, a marked increase in the unit value of imports and exports from both countries occurred, but due to inflationary pressures, the total value of mutual trade actually fell. This was further confirmed by a general decline in their share of each other’s imports and exports. Pakistan’s share of

⁶⁶ *Christian Science Monitor*, October 20, 1950.

⁶⁷ *The Times of India*, April 22, 1950.

⁶⁸ *The Times of India*, April 27, 1950.

⁶⁹ Choudhury, 154.

⁷⁰ Chopra, 217.

⁷¹ Chopra, 189. See also *Pakistan & Gulf Economist*, Vol. 18, No. 18 (May 6, 1978), 5.

⁷² *Pakistan & Gulf Economist*, Vol. 21, No. 46 (November 14, 1981), 26.

⁷³ Chopra, 190.

⁷⁴ All figures given in the paper have been taken from data published in the yearly publications of the Government of Pakistan’s Federal Bureau of Statistics. See <http://statpak.gov.pk/depts/fbs/publications/publications.html>.

India's imports averaged 4.52 percent in 1951–56, but declined to an average of 0.20 percent during 1975–76 to 1979–80. In exports from India, Pakistan's share has followed a downward trend from 4.58 percent to a matching weak performance of 0.20 percent during the same period. The same trend can be observed in India's share of Pakistani trade. India's share of Pakistan imports stood at 4.05 percent in 1960–61, declining to 2.25 percent during 1961–62, then to 0.05 percent during 1975–80. India was the destination of 15.83 percent of Pakistan's exports in 1960–61 and 6.81 percent overall during 1961–66, but this declined to only 0.1 percent during 1975–80. These figures indicate that both countries were drifting apart, instead of coming closer together on trade.

The balance of trade remained highly favorable to Pakistan, as shown in Appendix I. Except during five years—1957–58, 1960–61, 1964–65, 1976–77 and 1978–79—in which the balance of trade was favorable to India, the balance of trade has typically favored Pakistan. In five out of seven years from 1975 to 1983, Pakistan maintained a trade surplus with India.⁷⁵ This fact in itself should be a major motivating factor for the benefits of Pakistan's enhancing its trade and economic relations with India.⁷⁶

In October 1982, Pakistan allowed private firms to import forty specific categories of items from India under the supervision of the Trading Corporation of Pakistan (TCP), a government entity assigned the task of opening letters of credit with Indian exporters.⁷⁷ A list of the items is given as Appendix II.

In March 1983, the Indo-Pak joint commission was established with the objective of promoting mutual beneficial cooperation between the two countries in economics, trade, industry, and other fields. The first meeting was held in Islamabad in January 1984 and the participants identified items for mutual trade.

From the First SAARC Summit to 1990

The South Asian Association for Regional Cooperation (SAARC) was organized in 1985. The now-familiar priority areas of promoting the welfare of South Asian populations, economic growth, social progress, and cultural development, as well as strengthening self-reliance amongst SAARC members, were not specified at that time. However, it was soon realized that acceleration of economic growth and raising standards of living were simply not possible without improved economic cooperation.⁷⁸ Accordingly, the 1987 SAARC summit explored the possibilities for increased economic cooperation among its members. Trade between Pakistan and India, the two major members in SAARC, became a priority area for cooperation in the hope that it would give immediate and tangible results. However, activity in this field since has so far not been encouraging. The volume of Pakistan's bilateral trade with India remained the same in the early years of SAARC (1986–87) compared to the mid-1970s.⁷⁹

Organized trade between India and Pakistan remains at a much lower level than its potential volume. It is mostly incidental and restricted. When there are spot shortages in certain consumer goods, Pakistan uses the Indian market to meet these sporadic shortfalls in supply. Pakistan imported potatoes, onion, and pulses from India during shortages. Regular imports from India include some minor items like betel leaves and spices. On the other hand India's imports from Pakistan are highly selective and restricted to a few traditional goods.

Pakistan's trade with India accounts, on average, for only 15 percent of its overall regional trade. India pursues very restrictive trade policies. Most products that Pakistan can export to India are effectively blocked by high tariffs, quotas, and even outright bans. Imports from India to Pakistan for public sector use are restricted. However, the private sector is allowed to import a select list of 322 products from India.

Commodity composition of exports to India presents quite a distressing picture, as demonstrated by Table 1 on the next page.

⁷⁵ Taranath Bhat, "India and Pakistan: See-Saw Economic Relations," in *Studies in Indo-Pak Relations*, ed. V.D. Chopra (New Delhi: Patriot Publishers, 1984), 218–229.

⁷⁶ Anjum Ibrahim, *Pakistan Times* (Rawalpindi), December 7, 1985.

⁷⁷ "FICCI Delegation to Pakistan," *FICCI Report* (New Delhi), 1983.

⁷⁸ "SAARC at the Cross Roads."

⁷⁹ M.I. Lashkar, *Pakistan & Gulf Economist*, January 7–13, 1989.

Table 1: Economic Classification of Pakistani Exports to India

(Percentages)

Year	Primary	Semi-Manufactured	Manufactured
1978	01.4	98.6	00.0
1979	11.3	88.7	00.0
1980	02.8	97.2	00.0
1981	00.5	99.4	00.1
1982	30.8	69.2	00.0
1983	20.0	80.0	00.0
1984	24.9	74.1	01.0
1985	13.0	86.9	00.1
1986	59.3	40.3	00.4
1987	49.9	42.7	07.4
1988	70.7	22.1	07.2
Average	24.4	74.2	01.4

Source: Annual Report, Ministry of Commerce and Industry, Government of Pakistan, from 1978–88.

Not a single exported item presents a consistent trend over the eleven-year period. For example, residual fuel oil and naphtha accounted for more than 90 percent of Pakistan's exports to India in the early 1980s. This category completely disappeared from the list of exports after 1984. Similarly, pig iron exports accounted for one half of total exports to India in the 1982–84 period, but it does not even appear in the list of exported products in other years. It seems that Pakistan's trade with India is guided by temporary exportable surpluses or is used to counter temporary shortages. A sharply declining trend in the exports of manufactured goods and a rising trend in the share of primary goods in Pakistan's exports to India are quite evident from the above table. Increases in the share of primary goods, through largely due to an absolute decline in the export of manufactured goods, may also be attributed to increases in the exports of raw dates and raw cotton. Exports of cotton yarn have also registered a sharp increase.

Pakistan's imports from India show a very sharp fall in the period from 1978 to 1983, followed by a gradual increase in the subsequent period, as discussed above. Pakistan's main imports from India include tea, vegetables, and iron ore. They also include a number of manufactured products, showing a relatively more stable pattern than exhibited by Pakistan's exports to India. More than half the imports from India on average, and more than three-fourths in 1988, consist of raw materials. The imports of raw materials have increased rather sharply, but the import of both manufactured consumer and capital goods shows a declining trend.

This analysis of the various stages of Indo-Pakistan economic relations shows that there is a large scope to expand mutually beneficial trade relations between the countries. Due to certain political and economic constraints, the potential has not been fully realized in the past.

PART FOUR

Prospects

The economic compatibility of Pakistan and India is dependent on the scope for economic cooperation available to them. A cursory examination of the economies of both countries reveals that there are great prospects for economic cooperation between these neighbors, although the actual level of cooperation at present is limited.

Both countries face a common problem in exporting their products to the industrialized countries due to the import restrictions they face.⁸⁰ Both need greater leverage to bargain with multinational corporations for technology transfers. This is also true in negotiations with international monetary agencies to achieve a desirable international economic order.

India and Pakistan also have a comparative cost advantage in trade with each other over countries outside the region. These advantages include lower transport costs due to their geographic proximity, on-the-spot customs inspection facilities, easier time schedules, better understanding of each other's market mechanism, and easier settlement of payments.⁸¹ There exists great potential for establishing common shipping and insurance services. In view of rising energy prices, transport costs are likely to rise, so the "transport cost advantage" of intra-regional trade is likely to increase in the future.⁸² This further substantiates the potential payoff for economic cooperation.

Pakistan and India share common problems of high rates of population growth, ascending poverty curves, and rural under-development. In academic areas that address these issues of underdevelopment, both can benefit through greater technical cooperation, bilateral exchanges, and shared facilities for scientific and technical research. Since they share so much in common, it is appropriate to share research resources for the benefit of both.

Joint ventures remain important vehicles to promote the industrialization process, especially in developing countries. These may take the form of technical collaboration, incorporating firms in the host country through proprietorship with MNCs (who bring both equity capital as well as expertise) and indigenous investors, and pooling the resources of various countries. Such pooled investments make it possible to set-up industrial plants that can efficiently and profitably serve regional markets.

India is a relatively industrialized country compared to Pakistan. In trade and commerce, the Indians are famous for their skills, adroitness, and craft. Pakistan's trading classes, on the other hand, have a mixed reputation of supplying products different from samples previously exhibited and under-invoicing/over-invoicing, both to cheat the client and their own government.⁸³ Competition in an open regional market should serve to eliminate such anti-competitive practices.

The consumer, for all her patriotism, shows little sympathy for traders who sell goods at exorbitant prices. There is a need for Pakistan to seriously review its protectionist policies to arrive at a balanced and sound approach to the country's future international trade position. Trade with India has certain inherent advantages, i.e. the potential for easy communication, lower transport costs, and financial institutions to facilitate trade, in addition to its potential for the generation of political goodwill through the free flow of trade. Establishment of economic ties on a reasonable basis will lead to confidence building, creating mutual trust to overcome a past undermined by suspicions and embittered by three wars.

Pakistani industry is highly protected and the prices of its goods are non-competitive. For example, Pakistani textiles are better than Indian ones, but their entry into the Indian market is unlikely because of their non-competitive prices. On the other hand, Pakistan is currently importing some Indian goods via Singapore, Dubai, and other third parties—at excessive prices.⁸⁴ These include such goods as: high-speed diesel engines, tires, electronic items, video films, etc. This demonstrates an existing need to open the Pakistani market to competitive goods.

⁸⁰ Qureshi, 9.

⁸¹ S. K. Singh, Indian Ambassador to Pakistan (interview with reporter), *Dawn* (Karachi), February 17, 1986.

⁸² Qureshi, 11.

⁸³ Bashir Ahmed, "Indo-Pak Trade Prospects," *Pakistan Times*, February 8, 1986.

⁸⁴ Raunaq Singh (interview with reporter), *Pakistan & Gulf Economist*, February 18–24, 1989.

Similarly, there are a number of goods that India can profitably obtain from Pakistan. For example, the textile trade of the two countries at the global level is governed by multi-fiber arrangements (MFAs). In their textile exports, both countries encounter similar quota restrictions. The record shows that both frequently failed to fulfill their individual allotted quotas for exports to the European Economic Community, the United States, and other major markets. As textile exporters, both countries should cooperate with each other and ask for cooperatively managed, interchangeable quotas in the international market. This has been proposed at the Asian Textile Council, which operates under the Confederation of Asian Chamber of Commerce and Industry (CACCI), which represents the textile exporting countries of Asia as a whole. The trend in textile trade negotiations indicates that such an arrangement can be beneficially developed between India and Pakistan.

Other areas for cooperation are joint tenders for the supply of products to the Middle East and joint ventures with less developed countries. Areas which show substantial promise for such cooperative ventures include automobile spares, components, and accessories; glass manufacturing; machine tools and compressors; electrical and electronic goods; farm equipment such as power tillers, seed drillers, harvesting machines; and miscellaneous items in the engineering sector. Pakistan and India can also pool their technologies, manpower, and expertise to execute service sector projects like consultancy services, civil construction work, and other turnkey projects.

Industrial joint ventures can be undertaken to manufacture products. Identified as in demand within SAARC and by less developed countries. Products of such joint ventures should be made free of all tariff and non-tariff barriers, to aid in import substitution as well as developmental export promotion. Such projects will increase the supply of products that are in short supply in the market, bringing benefits to consumers.⁸⁵ Industrial cooperation through regional ventures as well as intra-regional transfer of appropriate technology is essential to increase markets and production capacity.

Industry in Pakistan that is internationally competitive is now mature enough to withstand Indian competition. If the period of trade protection isolation of Pakistan's local industry is further extended, the country's industrialists will not be able to learn from competition. South Korea learned to compete with its superior neighbor, Japan, and its industry profited—not by eschewing free trade—but through the instruments of competitive pricing, fixing of exchange rates, and technology transfers.⁸⁶ Better trade prospects enable Pakistan's industry to exercise its viability in competition with India.

India's per capita food consumption is much lower than Pakistan's and its grain surpluses are based on a starvation level diet. Pakistan now has agricultural surpluses. Thus, Pakistan can help fill the Indian food gap by entering into a free-trade relationship with India.⁸⁷

India offers an enormous market for Pakistani products. Even a small share of such a market will bring considerable benefits to Pakistan's industry and more generally to its economy. From the Indian point of view, the gap that exists between the levels of industrialization of the two countries provides India with an opportunity to market many products that Pakistan now imports from far off countries at high prices.⁸⁸

Another possible area of mutually beneficial trade, as suggested by the Indian writer Ali Jawad Zaidi, is to allow free trade in materials related to literacy—books, journals, periodicals, and newspapers. The lack of opportunities for intellectual intercourse is a significant factor in maintaining barriers between the two countries. India is a substantial potential market for Urdu books from Pakistan. Even books published in English can find a sizable readership in India. India publishes 20,000 new titles every year, as against 500 by Pakistan. Indian books are cheap. Thus the possibility of the balance of the publishing trade remaining in India's favor can be taken care of by fixing a ceiling for import and export. Even a partial opening of the market introduces an element of competition that will benefit Pakistan's writers and publishers.⁸⁹

⁸⁵ Govind Ram Agrawal, "Some Avenues for South Asian Economic Cooperation," *South Asia Journal* (New Delhi), January 1, 1987.

⁸⁶ Shahid Javed Burki, *The Nation* (Lahore), July 13, 1987.

⁸⁷ Ibid.

⁸⁸ *Dawn* (Karachi), November 20, 1985.

⁸⁹ *Dawn* (Karachi), October 20, 1987.

PART FIVE

Suggestions for Realizing Full Trade Potential

Production of goods that are competitive in quality with those in world markets, better marketing, and identification of existing and projected production capacities in the region with regard to those products for which SAARC countries rely on foreign imports would considerably enhance intra-regional trade prospects. Such a trade diversion does not necessarily involve a movement towards less efficient production. Nevertheless, dynamic advantages from trade expansion can only be realized if tariffs are lowered and other barriers are removed, especially on products in which almost every South Asian country has sufficient production capacity. It should include industries that have overcome initial cost disadvantages, while discouraging unproductive investments intended solely to serve internal markets. This trade expansion must be viewed as a force which compels both states to reduce the severity of unresolved issues to a manageable level and brings about a commitment by policy-makers to resolve such remaining issues amicably.

Some steps that are required for an expansion of trade are enumerated below:

- 1) Improvements in communications. Trade enhancement among SAARC countries is dependent on better communication facilities. In order to improve the information flows between businessmen and industrialists of all South Asian states, the following measures are suggested.
 - a) Easing of visa restrictions. SAARC countries should consider abolition of visa restrictions. However, if it is not politically feasible to remove visa restrictions in all cases, those dealing in international trade could be issued special passports to automatically entitle them to visa and other exemptions from formalities such as police reporting, etc.
 - b) Trade festivals and exhibitions. While SAARC countries do participate in industrial exhibitions organized by other regional configurations, it would be more useful if specific industrial exhibitions focusing on the SAARC countries as a group were organized. A SAARC *mela*, or trade fair, with effective participation from all the countries of South Asia should be held every year to introduce goods produced in SAARC countries and encourage regional cooperation through networking.
 - c) Liberalized system of foreign exchange. SAARC countries should consider limited convertibility of their currencies for intra-regional trade. Pending such convertibility of the currencies, these countries should provide mechanisms to facilitate foreign exchange for industrialists making business-related trips to other SAARC countries.
 - d) Regional trade information centers. Each country should set up an information center to collect and disseminate information on potential imports and exports within the SAARC region. Similarly, embassies should play a more active role in disseminating information about the markets in the region.
 - e) SAARC Chamber of Commerce. Businesses involved in regional trade should be encouraged to form a SAARC Chamber of Commerce to promote policies to facilitate their growth.
 - f) Transport and telecommunication facilities. At present postal, telex, telefax, and telephone facilities among SAARC countries are rather limited and reflect the persistence of colonial and global communication priorities, instead of strong regional networks. Improvements in regional interconnections are necessary to facilitate expanded trade.
- 2) Liberalization of trade regimes. At present, tariff and non-tariff barriers on imports into almost all SAARC countries are quite stringent. Trade restrictions are even more severe on products that could be traded amongst SAARC countries. It would, therefore, be useful if the South Asian countries liberalize their trade regimes, with a first step being to lower duties on products that have trade potential within SAARC. It would lower such tariffs below the average level of import duties for non-SAARC products; all non-tariff barriers on intra-regional trade should be removed. Liberalizing trade policies by encouraging competition ensures efficient production.
- 3) Easing resource constraints. A primary reason for the current limited trade among SAARC countries has been a lack of resources to finance imports. The diversion of existing trade from the developed countries to benefit the development of South Asian countries is possible if the exporting countries provide long-term financing for such transactions. This will not only enhance trade, but it also reduces production costs. For

example, Pakistan's long-term loan to Bangladesh has been instrumental in raising Pakistan's exports of engineering goods to Bangladesh.

- 4) Generation of complementary export surpluses. Exportable surpluses of trade goods needed for interchange between South Asian nations can be generated by re-orienting industrial production structures to complement each other. Surveys are necessary to identify these markets and to determine the appropriateness of industrial investments with reference to comparative advantage, reorienting the growth of regional industry by referencing it to the needs of the SAARC common market.
- 5) Transit facilities. In order to ensure trade among South Asian countries on an equitable basis, it is important to foster the fundamental comparative advantages brought about by their close proximity. At present, unnecessarily high costs of transportation, imports, and exports for Nepal distort her comparative advantage. Nepal needs to be provided transit facilities in accordance with international practices.

CONCLUSION

An analysis of the historical context of trade and economic interaction between the India and Pakistan makes it clear that great opportunity exists for an expansion of mutually beneficial economic relations between these two neighbors. This potential has not been exploited in the past due to various political and economic constraints. As a result, both have paid a heavy opportunity cost in economic terms. These nations share a long border and have fairly well-developed railway, road, and sea links. Their geographical proximity and contiguity, with well-established transport connections, definitely can cut transportation costs through increased mutual trade with each other, as compared to equivalent trade outside the region. In fact, geographical proximity and economic complementarity are natural compulsions, which should bring Pakistan and India closer, insofar as commercial relations are concerned. Putting an end to the illogical barriers artificially created by vested interests in both countries is the next step in achieving mutually beneficial economic growth. Due to their previous, often hostile political relationship, economic issues remain subservient to political objectives. Huge amounts of their scarce resources are spent on armaments. This unproductive expenditure can be cut drastically by enhancing mutual cooperation in economic, cultural, and political fields.

APPENDIX I

Indo-Pakistan Trade: From 1948–49 to 1990–91

(Values in Indian rupees in crores, with US dollars in millions calculated at \$1=45 Indian rupees)

Year	Exports to Pakistan	Imports from Pakistan	Balance of Trade	Total Trade
1948–49	76.68 (\$15.26 m)	107.38 (\$23.86 m)	-30.70 (\$6.8 m)	184.60 (\$41.02 m)
1949–50	43.30 (\$9.62 m)	44.05 (\$9.79 m)	-0.75 (\$0.17 m)	87.35 (\$19.41 m)
1950–51	30.60 (\$6.80 m)	43.87 (\$9.75 m)	-13.27 (\$2.95 m)	74.47 (\$16.56 m)
1951–52	45.25 (\$10.05 m)	87.50 (\$19.44 m)	-42.25 (\$9.39 m)	132.75 (\$29.50 m)
1952–53	30.90 (\$6.87 m)	21.88 (\$4.86 m)	+9.02 (\$2.01 m)	52.78 (\$11.73 m)
1953–54	8.01 (\$1.78 m)	19.28 (\$4.28 m)	-11.27 (\$2.51 m)	27.29 (\$6.06 m)
1954–55	9.75 (\$2.17 m)	19.38 (\$4.31 m)	-9.63 (\$2.14 m)	27.13 (\$6.03 m)
1955–56	8.30 (\$1.84 m)	27.11 (\$6.02 m)	-18.81 (\$4.18 m)	35.41 (\$7.87 m)
1956–57	7.92 (\$1.76 m)	15.76 (\$3.50 m)	-7.84 (\$1.74 m)	23.68 (\$5.26 m)
1957	6.68 (\$1.48 m)	13.42 (\$2.98 m)	-6.74 (\$1.50 m)	20.10 (\$4.47 m)
1958	7.32 (\$1.63 m)	6.31 (\$1.40 m)	+1.01 (\$0.22 m)	13.63 (\$3.03 m)
1959–60	7.21 (\$1.60 m)	8.59 (\$1.91 m)	-1.38 (\$0.31 m)	15.80 (\$3.51 m)
1960–61	9.51 (\$2.11 m)	14.01 (\$3.11 m)	-4.50 (\$1.00 m)	23.52 (\$5.23 m)
1961–62	9.45 (\$2.10 m)	13.86 (\$3.08 m)	-4.41 (\$0.98 m)	23.31 (\$5.18 m)
1962–63	9.40 (\$2.09 m)	16.67 (\$3.71 m)	-7.27 (\$1.62 m)	26.07 (\$5.79 m)
1963–64	7.17 (\$1.59 m)	9.36 (\$2.08 m)	-2.19 (\$0.49 m)	16.53 (\$3.67 m)
1964–65	9.78 (\$2.17 m)	15.75 (\$3.50 m)	-5.98 (\$1.33 m)	25.53 (\$5.67 m)
1965–66	4.88 (\$1.08 m)	5.65 (\$1.26 m)	-0.77 (\$0.17 m)	10.53 (\$2.34 m)
1966–75	Negligible	Negligible	Negligible	Negligible
1975–76	0.76 (\$0.17 m)	22.12 (\$4.92 m)	-21.34 (\$4.72 m)	22.90 (\$5.09 m)
1976–77	9.00 (\$2.00 m)	1.72 (\$0.38 m)	+7.28 (\$7.28 m)	10.72 (\$2.38m)
1977–78	13.32 (\$2.96m)	23.91 (\$5.31m)	-10.59 (\$2.35m)	37.25 (\$8.28m)
1978–79	19.45 (\$4.32m)	12.80 (\$2.85m)	+6.65 (\$1.48m)	32.25 (\$7.17m)
1979–80	8.50 (\$1.89m)	24.68 (\$5.49m)	-16.18 (\$3.60m)	33.18 (\$7.37m)
1980–81	1.02 (\$0.23m)	75.39 (\$16.75m)	-74.37 (\$16.53m)	76.41 (\$16.98m)
1981–82	4.95 (\$1.10m)	54.70 (\$12.16m)	-49.75 (\$11.06m)	59.65 (\$13.26m)
1982–83	6.50 (\$1.44m)	32.28 (\$7.17m)	-25.78 (\$5.73m)	38.78 (\$8.62m)
1983–84	11.77 (\$2.62m)	27.79 (\$6.16m)	-16.02 (\$3.56m)	39.56 (\$8.79m)
1984–85	12.91 (\$2.87m)	15.75 (\$3.50m)	-2.84 (\$0.63m)	28.66 (\$6.37m)
1985–86	14.64 (\$3.25m)	26.59 (\$5.91m)	-11.95 (\$2.66m)	41.23 (\$9.17m)
1986–87	14.95 (\$3.32m)	27.50 (\$6.11m)	-12.55 (\$2.79m)	42.45 (\$9.43m)
1987–88	20.12 (\$4.47m)	30.59 (\$6.80m)	-10.77 (\$2.39m)	50.71 (\$11.27m)
1988–89	35.02 (\$7.78m)	72.17 (\$16.04m)	-36.15 (\$8.03m)	108.18 (\$24.04m)
1989–90	51.39 (\$11.42m)	53.79 (\$11.95m)	-2.40 (\$0.53m)	105.18 (\$23.37m)
1990–91	73.60 (\$16.36m)	84.49 (\$18.76m)	-10.88 (\$2.42m)	168.09 (\$37.35m)

Source: Government of India, Director General of Commercial Intelligence and Statistics, Calcutta, 1996.

APPENDIX II

List of Items for Private Sector Imports from India through Trading Corporation of Pakistan

- | S. No. | Description of Items |
|--------|--|
| 1. | Tea |
| 2. | Wood and timber |
| 3. | Betel leaves |
| 4. | Betel nuts |
| 5. | Ginger |
| 6. | Tamarind |
| 7. | Seeds-vegetables, fruits and flowers |
| 8. | Vegetable plants for dyeing |
| 9. | Cutch and gambier |
| 10. | Essential oils |
| 11. | Books (technical, professional and religious only) |
| 12. | Spices excluding chilies, turmeric and cumin seeds |
| 13. | Steel strips for manufacture of razor blades |
| 14. | Viscose, fiber and yarn |
| 15. | Ferro-alloys |
| 16. | Calculators, calculating machines |
| 17. | Ball bearings (permissible size only) |
| 18. | Lifts and escalators |
| 19. | Cane planter |
| 20. | Cutter binder |
| 21. | Potato/onion diggers |
| 22. | Rice sprout transplanters |
| 23. | Rotary cutters |
| 24. | Rotavaters |
| 25. | Spinner broadcasters |
| 26. | Drilling rigs |
| 27. | Postal franking machines |
| 28. | Carbon electrodes |
| 29. | Compressor units for air conditioning parts |
| 30. | Compressors for domestic refrigerators |
| 31. | Fire engines |
| 32. | Microscopes and other laboratory instruments |
| 33. | Felt for paper mills |
| 34. | Phthalic (Raw materials for synthetic resin) |
| 35. | Citric acid |
| 36. | Lactic acid |
| 37. | Saccharine |
| 38. | Aluminum powder and paste |
| 39. | Cash registers incorporating calculator devices |
| 40. | Duplicating machines |