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THE DYNAMICS OF INDIA-PAKISTAN TRADE

A recent study by the Delhi-based research institute Indian Council for Research on International Economic Relations (ICRIER) shows that informal trade between India and Pakistan is almost twice the value of formal trade between the two countries. Informal trade is broadly defined as all trade between two countries that should be included in the national income statistics, according to conventional national income accounting, but is not. The study is based on survey conducted between September 2013 and March 2014 with 247 respondents across the cities of Ahmedabad, Amritsar, Chennai, Delhi, Hyderabad, Kolkata, Mumbai, Surat and Dubai. The persons approached for the survey included formal traders, informal traders and those belonging to the “knowledgeable persons” category, such as customs and port officials.

WHAT DRIVES INFORMAL TRADE?

Factors such as high tariffs, political tension, infrastructure impediments, ease of trading goods via third countries have generated a thriving industry for informal trade between the two South Asian giants. Nearly nine in 10 respondents said they found Pakistan’s negative list of 1,209 items as the most important factor pushing informal exports from India. Items on the negative list are those that are not allowed to be imported from India. More than one in every two items exported informally to Pakistan were on Pakistan’s negative list. Clearly, the restriction has fuelled indirect trade. 58% of the traders cited ease of sending goods via a third country as the second biggest important reason. This highlights weaknesses in infrastructure for formal trade, consequently leading to high transport costs. The third biggest reason was seen to be high tariffs. Compliance to the tariff liberalization plan of South Asian Free Trade Area (SAFTA) is expected

to bring down tariff rates. The agreement on SAFTA is a trade agreement to promote trade and economic growth in South Asia by reducing tariffs for intra-regional export. India also maintains a sensitive list of 614 items on which no tariff concessions are granted.

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WHICH COMMODITIES ARE TRADED?

Real jewellery, including gold, diamond and precious stones, accounted for the largest share of 23% of informal exports from India to Pakistan. About 30% of items on India's current sensitive list comprise of textiles, indicating that shift to formal trade can be expected once India relaxes its tariffs. While India's imports from Pakistan included items such as dry fruits and spices, informal exports from India included chemicals, tyres, alcohol and tobacco products, among several others. Informal exports from India to Pakistan in 2012-13 stood at \$3.9 billion, much higher than the just over \$2 billion worth of formal exports. Informal imports, on the other hand, from Pakistan valued \$0.7 billion, slightly more than formal imports of \$0.5 billion.

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HOW DOES INFORMAL TRADE TAKE PLACE?

Most of informal trade between the two countries were also found to be via a third country, in particular Dubai. About 68% of India's informal export to Pakistan was found to be routed via Dubai. 59% of informal import from Pakistan was accounted for by passengers travelling by bus or rail. 24% of informal import from Pakistan was via Line of Control trade routes, while 17% was via Dubai. The fact that Pakistan has refrained from according the Most Favoured Nation (MFN) title to India has also hindered barrier-free trade, say trade analysts. According to the World Trade Organisation, MFN means that every time a country lowers a trade barrier or opens up a market, it has to do so for the same goods or services from all its trading partners—whether rich or poor, weak or strong.

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FORMAL TRADE ROUTES ARE INEFFICIENT

The survey, which measured the efficiency of transport of goods via two routes—the Delhi Lahore route and the Delhi-Mumbai-Dubai Karachi-Lahore route—found that the latter route was 2.75 times more efficient in terms of transport per transaction cost incurred per container-kilometre. Higher transaction cost per-

tonne-perkilometre on the direct route is because of factors such as limited number of items that can be exported via road route, cumbersome customs checks at Attari/Wagah customs station, transaction costs in the form of bribes incurred in getting customs clearances, physical examination of goods and poor infrastructure, among others. While the total cost of shipping would still be lower in the formal channel, given the fact that the distance is one-tenth of the route via Dubai, predictability and comfort encourages traders to incur these high costs. The survey is not without biases, based on the knowledge of the respondents and owing to a possible bias in the sample selection. Also, unofficial capital transfers between the two countries have not been included. However, if appropriate measures are taken, a significant share of informal trade can be diverted to formal channels. Informal trade between India and Pakistan, though, is unlikely to be totally eliminated as ethnic networks between the two countries would continue to facilitate it at cheaper costs.

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