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No. 1

Commercial Policy of Pakistan

By

Mrs. N. Sarfraz



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## COMMERCIAL POLICY: INTRODUCTION

There is probably no country of note today which does not resort to various policy measures in order to control and regulate economic activity in different sectors of its economy. This is true both for the centrally planned as well as for the relatively free-market economies. The international trade sector is of special importance to governments, and thus comes under the purview of policy measures regulating the external economic relations of the country adopted to assist or hinder the export or import of goods and services. Commercial Policy has had a varied history; stress has been placed from time to time, over the last few centuries, on making trade highly restrictive or highly free, according to the prevalent modes of economic thinking. There is not a nation in the world today, however, which does not interfere — and restrict — the full development of its commerce with other countries by the use of one, or several, of the devices of modern trade restrictions: tariffs, prohibitions, quotas, foreign exchange control, agreements, subsidies, buy-at-home campaigns, and various uses of its customs administration. The effects of these policies, however, may not be restricted to the domestic economy of the country adopting them, neither may they be specific to the purpose for which a particular policy is adopted. Hence, it becomes imperative that careful consideration is accorded to the formation, implementation, and assessment of the final impact of such a policy.

Commercial policy has a special significance for an underdeveloped country such as Pakistan that is attempting to maximise the use of its available resources through planning. A significant part of the costs of development are in terms of foreign exchange, as it is necessary to import plant and equipment, raw-materials and other essential requirements of development from

the advanced industrial countries. The underdeveloped countries have to face a dual problem; they must earn enough foreign exchange to meet the costs of development planning, and must maintain equilibrium in their balance of payments. The problem is accentuated because, apart from the demand for imports originating from the development sector, the underdeveloped countries have low price and high income elasticities of demand for imports, while their exports to the outside world (with the exception of oil and some mineral resources) seem to face low price and income elasticities of world demand.

World-trade developed at a rapid rate after the Industrial revolution in the United Kingdom, which raised the import coefficient of that country greatly. Economic growth in the United States however, took place under more protection than was the case for Britain, and its own natural resources provided ample scope for its import coefficients to remain low. In the Twentieth Century, the Great Depression of the thirties revived the trend towards protection and bilateral trade. As a result, world trade suffered considerably, especially because it never moved back to the state of general multilateralism that prevailed before World War I. The Second World War encouraged the trend towards protectionism and away from multilateralism still further. Since the war, however, efforts have continuously been made to institute (at least) restricted multilateralism, through international charters as the International Trade Organisation (I.T.O.) and the General Agreement on Trade and Tariffs (GATT), through agreements among groups of countries, as the European Common Market (E.C.M.) and European Free Trade Area (EFTA), or through specific commodity agreements as the International Wheat Agreement. This trend has important implications for the underdeveloped countries attempting to industrialize and improve their economic condition. To the extent that some of these international organisations and agreements discriminate in favour of expanding

trade cooperation among the advanced industrial countries, they are, by implication, discriminating against the low-cost-manufactures of primary producing countries, made possible through the availability of cheap labour there. This tends to worsen the terms of trade between the two groups of countries, thus creating special policy problems for the underdeveloped countries.<sup>1</sup>

The present study undertakes an analysis of the commercial policy of Pakistan as formulated and practised during the period 1948-61, in the light of the general circumstances described above. The major aim of this study is to present the policies affecting the foreign trade of Pakistan, the objectives and instruments of policy adopted for its implementation, and finally, to attempt an assessment of the impact of these policies on the pattern, volume, and direction of Pakistan's foreign trade. The scope of the study is thus limited; parts of this policy which might have been induced by factors other than economic, or by fluctuations in Pakistan's foreign trade originating from the outside world are generally not included. With this basic assumption in mind, we proceed to outline the approach to be followed in the rest of this study.

Section I examines the objectives which may usually be kept in view by countries, while formulating policies regulating their external trade. These have been grouped under five headings for purpose of convenience of analysis.

Section 2 sets out in some detail the instruments of policy specially relevant for the purposes of this study, and generally applied to achieve given ends of policy.

Section 3 undertakes a broad review of the commercial policy of Pakistan since the Partition of the sub-continent. It briefly takes account of the changing pattern and direction of

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<sup>1</sup>/ Economic Commission for Asia and the Far East: Annual Survey of Asia and the Far East, for a number of years during the fifties.

trade of Pakistan first, and then proceeds to outline the various policy measures as adopted by Pakistan government to regularise and control its export and import trade, over the whole period.

Section 4 critically examines the success or failure in the achievement of the various policy objectives in Pakistan in the light of the facts as set out in Section 3. In the end, a few suggestions for a reorganisation of the commercial policy of Pakistan are outlined.

SECTION I

OBJECTIVE OF COMMERCIAL POLICY

For a fuller exposition of the aims and objectives of commercial policy, it is necessary, first, to outline the importance of foreign trade in an economy. International trade is traditionally known to be a "powerful engine of growth" in the sense that it widens the market and provides better opportunities of specialization and development.<sup>2/</sup> This viewpoint is based on the traditional theory of international trade, wherein the concepts of division of labour and extent of market are important. Theoretically, an exchange of goods and services on the basis of the comparative differences in production costs will result in some gains for the countries participating in such an exchange. With the classical assumptions of immobility of factors of production between countries and given natural resource the gains may be shared unevenly, depending on the play of reciprocal demand, the price elasticity of supply, and the relative flexibility of an economy to adapt itself to fluctuations in demand.

In spite of its advantages, however, international trade is not now a popular "engine of growth". The newly awakened nationalism, especially in the underdeveloped part of the world, does not respond favourably to a high dependence on external forces resulting from international trade. International trade bears on a limited sector of the economy, and in recent times the prosperity in this limited sector has not proved to be strong enough to pull the rest of the economy along with it (oil exports of a number of countries can be cited as the most obvious case

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<sup>3/</sup> Cairncross, A.K., "International Trade and Economic Development" Kyklos Volume XIII, Fasc: 4, 1960 and Economica, August 1961. Also see Nurkse, "International Trade and Economic Development" Wicksell lectures, 1959.

in point). The elements of instability and uncertainty in the foreign trade sector make its contribution to an economy uncertain and hence not to be relied upon. Notwithstanding these difficulties international trade today, more than ever, comprises an important part of an economy. Detailed analysis of national income or the net availability of goods in an open economy (as against a closed economy, which would consider only consumption, saving, investment and government sectors) is not complete unless its exports and imports have been taken into account. This is so because once the economy is opened to international trade, it is exposed to the influence of diverse elements originating outside the domestic economy. National income and its major components are closely linked, in different ways, with both exports and imports.<sup>3/</sup> A study of the various income and price changes originating in, and leading to, direct or indirect changes in international trade, though relevant, would be outside the scope of this study. However, the knowledge of these inter-relationships has, in a variety of circumstances over time, induced intervention in the free-flow of international trade, by the imposition of different taxes and other embargoes on the exports and imports of a country. Such intervention has come about for a variety of purposes, but some of these purposes are now recognized to be relatively valid arguments in favour of a regulation and control of the foreign trade transactions of a country.

Such controls and regulations may be applied to serve individual or group interests within a country or national interest or international interest. Where a regulation is framed to benefit any of the above given broad criteria, there may be

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<sup>3/</sup> Ruggles, R. and Ruggles, Nancy D., National Income accounts and income analysis, (New York: McGraw Hill Book Company inc. 1956) Chapter 5 and appendix specially pp. 79-80.

Meade, J.E., Balance of Payments (Oxford, 1951) Chapter 3, pp. 34-35.



no guarantees about the adverse effects and compensation of such effects for the injured party. These criteria, however, may not have an economic background. Policies in favour of individual or group interest may be framed to serve political or social ends. Internationally biased regulations (such as those agreed upon by contracting parties to the General Agreement on Trade and Tariffs) may be introduced to comply with the obligations of being a member of an international community, even though deviations from such a policy may be able to yield some gains to a single country or a group of countries. The case of nationally-biased policies is somewhat different. They may depend on the principle of the best exploitation and use of national resources, or such ultra-economic motives as national pride and defense. This is not to say, however, that policies based on such criteria are necessarily in conflict with economic motives. However, the task of achieving consistency in a world of conflicting criteria is made specially more difficult in situations where resources are limited and the desire of the people for economic development most urgent.

There may be no "analytical economic ideals"<sup>4/</sup> to be stated unequivocally because setting up of such ideals would mean preconceived value judgements as to the role that policy must play. For the purpose of convenience in analysis, however, we set forth the following broad categories of criteria which may usually be kept in view in the formulation of commercial policy, (specially) in an underdeveloped country.

1. Revenue purposes
2. Protection or resource allocation
3. Defense of the balance of payments
4. Stability of the domestic economy
5. Maximization of income from exports, and hence of the total national income
6. Economic development

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<sup>4/</sup> Haberler, G.Y. International Trade, p. 215.

1. Imposition of export or import duties with a view to collection of revenue for the government is a well-accepted end of commercial policy. It has a special significance for under-developed countries whose capacity to derive revenues from direct taxes (such as income and corporate profits taxes) is limited so that they must find alternative sources and import and export duties are among the easiest taxes to collect. Thus, dependence on customs duties as part of their revenue earnings is usually high in these countries.

Revenue tariffs are in the nature of taxes on (domestic or foreign) consumption and are imposed, in principle, without any other implicit effects such as protection, resource allocation, or income redistribution. Both the export duty, and the import duty may be shared, or completely borne by the importer or exporter, depending on the elasticities of supply and demand for each commodity.

A revenue tariff on imports would be justified only when there is no domestic production of the commodity in question (subject to the limitation that the commodity is not judged to be a "luxury" or "superfluous consumption" and the duty made prohibitive in which case its revenue yield would fall off consequent to the fall in imports), or if produced at home, the tariff is balanced by an excise tax on home production; or if a straight constant percentage ad valorem duty is imposed on all imports. Even in these cases, it is difficult to ensure against any elements of protection, however indirect; at most they may withhold from being discriminate and intentional.

2. Protection and resource allocation.

Tariffs have been used as an effective weapon for providing protection from foreign competition to indigenous, newly establishing industries. In fact, the well-known 'infant industry' argument is considered to be one of the chief justifications for interference with the free flow of international trade. This

justification emerges from the fact that whereas free trade is considered advantageous in the present, infant-industry protection ensures gains in future. This is an important criteria from the view point of underdeveloped countries, which have hardly any industry of note, or a few industries producing for the export market (apart from the small-scale, so-called cottage industry, which produces, perhaps, for a local market only). If some temporary interference with the freedom of imports may be expected to develop new industries, to bring hitherto unutilized or underutilized resources into productive use, and to effect a reasonably profitable reallocation of resources in a poor economy the experiment is certainly worthwhile, with "the possibility of ultimate gain for all countries".<sup>5/</sup> Of course, a provision for protection alone may not be able to achieve much unless it is implemented in collaboration with a broad-based, well-thought-out industrialization programme which takes care of such other matters as providing the capital-requirements involved. Re-allocation of resources follows automatically, for these countries usually start with the manufacture of some raw material abundantly produced in and previously exported by the country. Resources are in this way drawn away from export industries to import substitutes.

This reallocation raises other problems. Industrialization involves use of foreign exchange, for in the beginning, imports are the only source for securing capital goods. If the costs of financing the industrialization programme are to be met out of the current foreign exchange earnings of the country, increased absorption of the export product in the home industry, unless its production is raised simultaneously, poses considerable foreign exchange availability problems. The policy for protection must, then, take account of all these divergent questions — protection

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<sup>5/</sup> Nurkse, R., Problems of Capital Formation in Underdeveloped Countries (Oxford: 1953) Chapter V, p. 104.

for import substitutes or export manufactures or some combination of the two. This is to keep the balance of payments in equilibrium or even to improve it if with the use of previously unemployed resources, the net output of the protected industry turns out to be greater than the net loss in real income through a shrinking of earnings from raw exports, and the enhanced costs of the consumer in the intervening period. A protective policy thus, needs to take account, not of the short run gains from protection, but the longer range effects on income, savings and investment in a economy.

3. Defense of the balance of payments is another relevant criterion. Apart from tariffs for the sake of protection, other restrictive controls may be imposed on imports in view of a tight foreign exchange position. Some domestic spending can be diverted to home products or to forced savings, if the controlled imports are expensive consumer's goods without close substitutes in the home market. Underdeveloped countries suffer from pressures on the balance of payments due to continuously rising demand for capital goods, semi-manufactured raw materials, and other imports related to their development needs. Their high marginal propensity to import out of additional incomes limits their capacity to suppress consumers' import demands indefinitely; the high cost of managing these controls administratively makes such an operation expensive for government exchequers, and leakages in the control machinery become frequent. Pressures on the domestic price level emerge depending on the severity of these controls, the nature of the imports involved, and the price or income elasticity of demand for these imports in the domestic market. Thus, when a balancing of international payments of a country is one of the main considerations in the formulation of policy, budgeting and careful allocation of the current foreign exchange earnings may not be effective enough unless matched by action on the side of export promotion as well, because there is a limit beyond which imports may not fall,

specially in a developing country. The task of enhancing export earnings to meet a larger import-bill requires special efforts on the part of the underdeveloped countries which traditionally depend on a small number of primary commodities as their major foreign-exchange earners. Diversification of the pattern of exports deserves special consideration in this respect, as a large number of the primary commodity exports (because they operate under the difficulties of inelastic supply in the shortrun, fluctuating world demand and a number of other limiting factors suffer from the prospects of deteriorating terms of trade, and price-support schemes alone are ineffective. The balance of payments consideration thus, involves policy specification on a broad front.

4. Stability of the domestic economy may be studied from two viewpoints - the price level and the level of employment; both are exposed to the effects of international trade in an open economy. The price level, as mentioned above, is affected through the general availability of imports in the domestic market,<sup>6/</sup> and this impact tends to be larger the larger is the share of imports in the total domestic market. The cumulative effect of a restrictive import policy shows up directly, by affecting prices of imports, and indirectly, by the readjustment of domestic resources under such a policy. Insofar as factors of production are attracted by the alternatives provided by such restrictions (of imports) or incentives (for export industries), the readjustment might tend to lead towards inflationary pressures in certain sectors.

The effects generated through the impact of trade on employment need consideration, too, especially when export-incomes are rising, which means the pressures of demand for imports would also be high. The commercial policy may be manipulated so as to lead

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<sup>6/</sup> Porter, R.C. 'Income Velocity' in the Pakistan Development Review, Vol: I No. 1 1961 p. 46, para-3.

to more savings and capital formation, but its success in this direction is debatable, so that it is difficult to define clearly the way in which a better level of employment could be achieved with the help of such a policy. There is nevertheless scope for supplementing other domestic policies of development with the commercial policy in such a manner that volatile fluctuations in the domestic economy are avoided and the risk of exposure to outside forces is minimised.

5. Maximization of income from exports is highly important from the point of view of revenue collection, balance of payments, and above all, national income. Exports may contribute more than half of the national income of a country, e.g. Venezuela and Malaya, but even where this percentage contribution is not very high, (Pakistan's export trade approximates some ten per cent of her national income) exports need consideration as they provide a basis for the volume of imports that may be permissible with given foreign exchange resources.<sup>2/</sup> National income is directly influenced as underdeveloped countries export mainly products of their soil, and ensuring a reasonable return to the cultivator is a huge task for the governments of these countries. Since these exports face fluctuating demand and price conditions in the world market, as mentioned earlier, some price stabilizing schemes at home are necessary. Regulation of supply of such exports, introduction of new exports, organizational changes in their marketing, provision of increased facilities and incentives, and diversification of the pattern of exports may be mentioned as some ways that the commercial policy of a country can adopt in order to maximise incomes from the export sector. Mere increase in the volume of traditional exports, under the present circumstances, may depress their prices, and hence incomes, rather than enhance these. The export sector cannot be disregarded, thus, and attention only to restriction or readjustment of imports may prove to be an erroneous policy. Exports may not contribute

the growth of an economy today as they did in the 19th century pattern of growth, but it is imperative that they do not lag behind the rest of the economy.

6. Economic development is a tricky subject, the how and why of it is still being unravelled, and one has to be cautious while dealing with this problem. Economists are today divided as to the role of international trade in economic development of a country, and examples can be cited both in favour and against its being the leading sector. All the growth in the 19th century (e.g. in England and Europe) was based on export economies, but development in Soviet Union has taken place virtually outside the world economy. How, then, can international transactions of a country be organized so as to contribute to its economic development? Perhaps one way may be to take care of the role of international trade in raising savings and contributing to capital formation in the economy. It may also be important to focus on institutional changes in the domestic economy, and to determine its absorptive capacity for the incoming foreign capital, (aid, grants, loans or private investment) as a supplement to domestic capital formation. That foreign trade is a vital source of supplies of capital equipment for development purposes in the short run may be accepted without much questioning. The fact emerges, then that the commercial policy of a developing country must be distinctly biased towards the achievement of the goals of development and growth.

The professed objectives of the commercial policy of Pakistan have been similar to these; to maximize the benefits from the foreign trade of the country. However, some additional considerations such as provision of sufficient consumer's goods to overcome shortages in the early period after partition, diversification of its trade among a larger group of countries to avoid dependence on a few, and discouraging concentration of this trade in a few hands in the home market have also been kept in view from time to

time. Attention has been paid to the extension and promotion of exports of the country, in view of the serious trade fluctuations experienced throughout 1948-60, to maximize government revenues, economic development, and stability of the economy. It is for later discussion, however, to evaluate the methods employed to achieve these goals of policy, and to assess the magnitude of success or failure in this respect.

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SECTION: 2

INSTRUMENTS OF COMMERCIAL POLICY

Regulation and restriction of the foreign trade of a country may take many forms, each of which is specially designed to attain a particular objective of policy. Given the foreign exchange resources, their budgeting and allocation among various items of import will, in general, determine the balance of payments position of a country. Various instruments of policy may be utilized, however, both to enhance the earnings and to meet various demands for foreign exchange through restrictions on imports. There might arise conflicts in the achievement of different objectives, but an ideal commercial policy would in general aim at resolving these conflicts so as to maximize benefits from foreign trade. The import schedule would thus be based on the availability of resources during a period and the relative essentiality of particular imports. The export policy, on the other hand would aim at securing an enlargement of these 'resources' so as to make possible the fulfilment of a wider area of demands in the import field. Here, we would consider the relative merits of some instruments of policy generally utilized to regulate the import and export trade of a country, and which are specially relevant for the purposes of the present study.

1. Tariffs and Customs Duties:

Tariffs and other customs duties are one important instrument of commercial policy aiming to control and regulate imports of individual commodities for various purposes. A uniform, ad valorem tariff, imposed on all imports, and unaccompanied by any quota restrictions on particular imports may serve only the purpose of collecting revenue for the government. This is rare in the present day world, however. Few tariffs, even when

imposed primarily for revenue purposes, may be expected to have no protective or income redistribution effects. The revenue yield as well as protective effect of specific tariffs may be fluctuating, unless they are imposed on some sliding scale system. Import taxes, thus, tend necessarily to protect domestic producers, (and not consumers) against outside competition.

Protection for infant industry (apart from improvement of the terms of trade<sup>8/</sup>) is a major argument considered valid for resorting to the imposition of tariffs. This automatically results in a reallocation of domestic resources too, favouring import-substituting, import competing or export-oriented industries. The choice of the industries protected is important here, for emphasis on any one of these will have a distinctly different impact on the national economy, the domestic price-structure and the balance of payments.

Tariffs for protection may temporarily interfere with the international welfare criteria in so far as the underdeveloped country would be establishing industries which were hitherto considered (perhaps) uneconomic for it to operate, and which would only be potentially economic for it. By disturbing the existing pattern of trade (presumably depending on the best comparative advantage principle, irrespective of the fact that such 'advantage' grew out of tradition, or an earlier start in the industrialization of one country) the underdeveloped country would thus be introducing elements of diseconomy, and in the short run the loss of welfare measured internationally may not be compensated fully. Some discrimination among groups within the country may also result through the employment of this instrument of policy, for the social costs of establishing a protected industry are generally high in the present. Thus, the choice of gains

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<sup>8/</sup> Considering the weak bargaining position of Pakistan in the world markets regarding almost all her exports, a study of tariffs for the improvement of the terms of trade is considered irrelevant here.

now and gains later, implicit in all programmes of development, would be evident in this sector, too.<sup>9/</sup>

When tariffs are employed for the purpose of correcting the balance of trade, they may be especially effective in case of commodities for which domestic demand has high price elasticity. They may also be used to utilize the price system to lower expenditures on certain undesirable imports, e.g. luxuries or current consumption and to encourage expenditure on others, e.g. machinery and equipment. This, however, may result in some inflationary pressure on money costs and prices,<sup>10/</sup> depending on the income elasticity of import demand for the former type of imports. However, though tariffs interfere with the free play of price system, they have the advantage of allowing the choice of buyers and sellers to be handled impersonally after the initial interference has been made.

Export duties, on the other hand, are levied principally for Government revenue purposes. However, these duties can be adjusted from time to time so that they move with the changes in export prices in the world market. This flexibility helps to safeguard the growers' interest by stabilizing internal prices of exportables and acts as an effective anti-inflationary measure in this sector of the economy.

## 2. Q u o t a s

Apart from influencing the price of an import, the quantity of an import may also be determined according to the dictates of the domestic elasticity of demand for an import (subject to the impact of the tariff) through such other quantitative restrictions

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<sup>9/</sup> The Galenson-Liebenstien argument about the programming of development expenditures and fixing of priorities to various types of expenditure, though open to criticism, is a case in point. See Galenson and Liebenstien, "Investment Criteria, Productivity and Economic Development", Quarterly Journal of Economics, August 1955.

<sup>10/</sup> Nurkse, R. Problems of Capital Formation in Underdeveloped Countries (Oxford, 1960), p. 112.

as imposition of quotas and specification of the source of imports. These restrictions tend to be discriminatory even when a quota is global, for if there is a time limit on fulfilling the quota, the importers are bound to favour the nearest source of supply. Often, however, fixation of import quotas is complementary with single country licenses which might be issued under bilateral agreements or other trade negotiations, so that import of a given quantity from one country may be agreed upon provided the other party takes some of the exports. This does not necessarily mean a barter arrangement; tentative upper limits for imports and exports may be fixed, subject to certain payments agreements, or tariff quotas may be introduced so that goods below a ceiling are subject to some concessionary rate of customs duty while imports exceeding that may be subjected to higher tariffs. Quotas have the advantage of lending a particular amount of certainty to a transaction, so that entry of imports of an essential nature in the domestic market is ensured, and their prices can be reasonably stabilized too. However, the scarcity value created by quota restrictions may go completely to the importer's pocket unless the government devises some way of taxing away part of this scarcity value from the importer, or such quota restrictions may be accompanied by domestic price or distribution controls, aiming at providing relief to the consumer of that particular import.

Quota restrictions in the export sector may be applied only in the case of goods declared essential for the economy or in short supply, where restriction of the export volume is considered desirable. Thus, ceilings for exports may be fixed when and where exports are permitted. Also the quantity of a particular export commodity to a given country may be fixed when commitments under barter or bilateral agreements are to be fulfilled.

### 3. Exchange Control

Exchange control is an important instrument of policy practiced by almost all countries of the world today. Exchange control usually means a regulation of the purchase and sale of the earnings of foreign currency by the residents of a country by a central authority such as the central bank. An important facet of exchange control is the adjustment of the exchange value of a currency in terms of other foreign currencies. Exchange control is an selective measure of policy which can help in discriminating among import items or among different sources of import.<sup>11/</sup> Also, it may discriminate among groups within the country, (e.g. exporters and importers) if the exporters must surrender their foreign exchange earnings at the official rate of exchange when this rate is artificially high (i.e. the currency is overvalued). In the absence of domestic price controls on imports, then, the importers' gains would be disproportionately higher if foreign exchange is made available to them at the official rate of exchange.

The basic reason for the establishment and maintenance of modern exchange control systems has been the protection of the balance of payments.<sup>12/</sup> An exchange control system, apart from imposing various types of direct restrictions on private foreign exchange dealings and limiting capital outflows, may operate also through special standstill and payments agreements, or indirectly through the imposition of selective credit controls.

### 4. L i c e n s i n g

A common form of restriction on imports is the prohibition of all imports except under licensing. It is useful when due to limited foreign exchange resources, control over the total quantity (or value) as well as the composition of imports is desirable. Thus, the possession of an import license enables the

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<sup>11/</sup> United Nations. Department of Economic Affairs,  
Governmental Policies Concerning Unemployment, Inflation and  
Balance of Payments, 1951-52, (New York, 1952) p. 66.

holder to purchase the appropriate means of payment from the exchange control authorities. This means that the granting of import licenses is to be closely coordinated with exchange policy. Similarly, licensing may be used for the enforcement of quotas. Restrictions on the volume and direction of trade through quotas necessitates issuance of licenses to enable importers to bring specified volume of the restricted commodity from specific countries or groups of countries. Implementation of quotas through licensing would thus ensure the source of an import, and determine the existence and extent of any intentional or unintentional discrimination, e.g. licenses may be issued under a global quota, open to all countries, divided among countries, for a specific group or currency area, or to be operative under a bilateral agreement.

Such administratively effective control over the composition of imports as well as payments for imports may achieve the objectives of a development oriented reallocation of resources and stabilization of the balance of payments. Thus licensing may be used to shift resources from the import of consumption to import of capital goods and industrial raw-materials for economic development, and to allocate exchange for the import of special types of equipment with a view to protection, import substitution or export promotion (when such imports are utilized mainly as inputs by an export-biased industry). The total volume of imports or of particular imports, (e.g. luxury items) may be restricted through licensing in order to correct a disequilibrium in the balance of payments.

A relatively liberal form of licensing is the open General License (O.G.L.) where general permission may be granted to any person or firm to import or export without restriction, any goods specified against currency areas placed on the open General License. This generally means that the mere placing of a commodity on an O.G.L. provides authority to anyone to open a letter of credit and draw the required amount of f.

exchange without having to present any identification such as an import license. Naturally, this system operates only in times of easy foreign exchange availability.

Export licensing, on the other hand, serves the purpose of conserving essential requirements for domestic purposes, strategic or otherwise. Also, it can be utilized as one means to provide stability in prices of the domestic export sector, e.g. restrict export supplies of a product facing a decline in its price.

#### 5. Bilateral Trade Agreements

Apart from the unilateral methods used by individual countries for the regulation of imports and exports, as elaborated in the previous discussion, countries may resort to bilateral methods for procurement of supplies or disposal of exports in the most advantageous manner possible. The history of bilateral trade agreements originates in the balance of payments difficulties accompanying and following the Great Depression of the thirties. The severe contraction of the volume of goods internationally traded and fall in primary export prices that ensued necessitated a movement towards bilateral methods of exchange of goods and settlement of payments within restricted areas. The device has proved useful in easing postwar problems of reconstruction and development by facilitating the process of trade for countries facing difficulties in their international trade sector. Mostly, such agreements incorporate commitments on the part of the contracting parties to issue licenses or authorise the use of foreign exchange for imports from each other of fixed values or quantities. Thus, an effort is made to increase trade with one another by extending special concessions to each other.

6. State Trading

Governments resort to state trading as another protective device used for the benefit of special industries, or for the procurement of goods of which government is a big user. It may also be used as a measure of introducing discrimination in trade in emergencies like war. An example would be war-time Britain, which was importing almost sixty per cent of its requirements of food products and other materials on state trading basis. Since State trading tends to eliminate the commercial importer as one link in the chain of market mechanism, it may not be viewed very sympathetically by advocates of a free market economy. It is necessary, however, under some conditions, to ignore individual gains.

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A review of the Commercial Policy of Pakistan has to take account of the economic conditions prevailing during the formative years of the nation's existence. Specially to be noted are the effects of the Partition of British India in 1947, when Pakistan came into being. This geographical division of what was previously, under the British rule, one political and economic unit, greatly influenced the pattern of the economies of the two newly emerging nations.

Industrial development in pre-partition India was rather lop-sided, with concentration of industry in certain areas only. The areas now comprising Pakistan were predominantly agricultural and industrially backward. Thus, the problems facing Pakistan from the very beginning were manifold; it had to look after the marketing of its primary commodities, and to build up an industrial base for the development of the economy almost from its very foundations. Adding to its difficulties was the complete dislocation and disruption of its economic life because of the events that followed Partition. One major effect of considerable interest from our point of view was the fact that Partition, by dividing regions which had functioned for long on a complementary basis, changed what formerly was inter-regional into international trade. This meant that the raw materials of Pakistan origin and the manufactures of Indian industries no longer enjoyed the same privileges in each other's market as previously. Pakistan had to establish new trade contacts with the outside world for the import of essential commodities like cloth, coal, iron and steel, in order to replenish its stocks, depleted greatly both during World War II and by the disruption of normal trade channels by Partition soon after the end of the War.

#### I

#### Pattern of Economy since Partition

The pattern of the foreign trade of Pakistan was determined by its resource endowment. As mentioned earlier, Pakistan inherited valuable raw material resources at the time of Partition, and its export earnings depended largely on two cash-crops, cotton and jute. Since it had little industry of note, it had to depend on imports for almost all its requirements of manufactures as well as some other commodities vital for nation-building activities, and for the purpose of economic development. India had been a natural market for its

disturbance of friendly relations with that country immediately after Partition, it was essential to look for other markets both for its exports and imports. Another important reason underlying the policy of diversification was the necessity to earn foreign exchange, especially from hard-currency areas, in order to import machinery and other equipment essential for the development of the country and to satisfy other broader objectives of the national economic policy. Export earnings had to be locked after particularly because they constituted a considerable part of the national income and of government revenues, approximating on an average, nearly 60 per cent of total revenue during the first few years after Partition.

#### Pattern of Trade

The pattern of Pakistan's foreign trade was similar to that of other relatively underdeveloped countries. The export earnings of Pakistan depend precariously on the performance of a few agricultural commodities, notable among which are jute and cotton. These two raw materials provided nearly 86 per cent of its total export earnings in the earlier years upto 1952-53, while tea, tobacco, raw wool and hides and skins accounted for the rest.<sup>13/</sup> Imports consisted mainly of manufactured goods providing for consumption, development and defence, - textile manufactures alone accounting for about 30 per cent. This pattern has changed considerably in recent years (since 1953 onwards) however, with the establishment of cotton and jute textile manufacturing as well as a number of other industries in the country, so that the export of manufactures has risen from about 2 per cent in 1948-49 to nearly 30 per cent in 1960-61, while imports of consumer's manufactures have given way to machinery and equipment and industrial raw material. The accompanying Tables 1-A, 1-B, 2-A and 2-B will throw light on the changing pattern of foreign trade of Pakistan during these years.

#### Direction of Trade

Pakistan's trade connections were limited to a very few countries at the time of Partition. In fact, Pakistan had trade contacts of note with only four

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<sup>13/</sup> Government of Pakistan: Ministry of Economic Affairs: Report of the Economic Appraisal Enquiry Committee, (Karachi, 1953) p. 8, para 13.

CHANGING PATTERN OF FOREIGN TRADE OF PAKISTAN PRINCIPAL EXPORTS  
(Private Account)

Commodities	(Rs. in millions)												
	1948-49	1949-50	1950-51	1951-52	1952-53	1953-54	1954-55	1955-56*	1956-57	1957-58	1958-59	1959-60	1960-61
Total:	949.2	1186.7	254.1	2006.8	1462.2	1256.4	1169.3	1777.8	1607.6	1421.6	1307.2	1791.0	1782.1
Raw Jute	--	525.8	1098.4	996.0	566.4	556.4	598.2	828.7	705.8	853.5	654.8	729.1	848.1
Jute manufactures & Yarn	--	--	--	--	--	3.6	23.1	105.7	91.0	90.8	155.2	227.1	313.8
Raw cotton	364.8	397.6	987.5	777.5	694.0	497.4	302.6	462.1	352.4	214.0	192.1	188.8	137.6
Cotton yarn & manufactures	--	--	--	--	--	--	1.3	35.7	92.6	33.4	53.8	231.4	118.2
Wool	31.0	35.1	79.8	31.2	57.8	46.9	50.0	68.3	98.6	66.7	65.3	75.4	70.9
Hides	28.3	13.2	40.2	13.8	16.8	15.0	28.0 <sup>a/</sup>	10.9	11.5	5.0	10.6	15.3	8.7
Skins	20.2	16.4	24.8	19.2	19.8	22.2		27.7	32.3	28.0	39.7	67.6	44.5
Tea	42.4	45.6	29.0	42.0	30.8	31.8	55.8	34.3	51.4	19.3	27.9	35.5	1.1

Source: Central Statistical Bulletin and Report on Currency and Finance (1960-61)

\* Devaluation of Pakistan Rupee took place in August 1955.

<sup>a/</sup> Break up not available, total is for both hides and skins.

Table I - B

Changing Pattern of Foreign Trade of Pakistan Percentage share of principal Exports in total Export Trade.

Commodities	1948-49	1949-50	1950-51	1951-52	1952-53	1953-54	1954-55	1955-56	1956-57	1957-58	1958-59	1959-60	1960-61
Raw Jute	68.0	44.3	43.1	49.9	38.8	43.5	49.0	46.5	43.9	60.1	50.0	40.7	47.6
Jute manufactures and Yarn	---	---	---	---	---	0.3	1.8	5.9	5.7	6.3	11.9	12.7	17.6
Raw Cotton	21.0	23.5	38.7	39.4	47.1	39.6	24.7	25.9	21.9	15.1	14.7	10.2	7.7
Cotton Yarn and manufactures	---	---	---	---	---	---	0.1	2.0	5.8	2.3	4.1	12.9	6.6
Wool	2.0	2.9	3.1	1.5	4.0	3.7	4.0	3.8	6.1	4.7	5.0	4.2	4.0
Hides and Skins	2.0	3.5	2.5	1.6	2.5	3.0	2.3	2.1	2.7	2.1	3.8	4.6	2.9
Tea	2.0	3.8	1.1	2.1	2.1	2.5	4.5	1.9	3.2	1.3	3.1	2.0	---
Rest	5.0	12.0	11.5	5.5	5.5	7.4	13.6	11.9	10.7	8.1	8.4	12.4	13.6

Based on Table I-A

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2A  
CHANGING PATTERN OF FOREIGN TRADE OF PAKISTAN

PRINCIPAL IMPORTS (Private Account)

Rs. in millions

Commodities	1948-49	1949-50	1950-51	1951-52	1952-53	1953-54	1954-55	1955-56	1956-57	1957-58	1958-59	1959-60	1960-61
Total	1258.1	1132.0	1430.3	1962.8	936.2	735.1	922.1	989.8	1019.4	939.7	839.7	1682.0	2120.8
Chemicals, Drugs & Medicines	47.2	39.9	43.5	64.0	42.4	45.2	48.4	75.4	80.8	93.6	76.4	141.3	157.4
Machinery & mill work	66.8	82.1	111.9	175.3	136.8	166.0	318.5	182.0	268.6	304.7	324.9	551.1	485.8
Metals & Ores	42.3	57.4	70.2	183.2	82.8	76.9	80.2	131.8	197.0	278.0	220.0	257.6	484.4
Mineral oils	27.2	35.3	62.9	97.7	89.1	94.6	108.2	114.2	102.4	81.6	99.9	238.2	263.3
Cotton Twist & Yarn	148.6	156.2	205.5	257.7	56.7	64.2	28.0	15.1	8.9	7.0	1.5	8.7	21.9
Cotton piece goods	353.4	213.3	330.5	368.6	89.2	3.2	36.8	63.4	11.2	1.7	1.1	4.2	2.4
Vehicles	58.1	58.0	65.5	93.0	41.9	27.0	44.6	58.5	91.2	139.6	98.8	152.8	254.5

Source: Report on Currency and Finance, 1953-54, 57-58, 60-61 (based on C.S.C. data)

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CHANGING PATTERN OF FOREIGN TRADE OF PAKISTAN

PERCENTAGE SHARE OF PRINCIPAL IMPORTS IN TOTAL IMPORT TRADE

	1948-49	1949-50	50-51	51-52	52-53	53-54	54-55	55-56	56-57	57-58	58-59	59-60	60-61
Chemicals, Drugs and medicines	3.7	3.5	3.0	3.2	4.5	6.1	5.2	7.6	7.9	10.0	9.1	8.4	7.4
Machinery & mill work	5.3	7.2	7.8	8.9	14.6	22.6	34.5	18.4	26.3	32.4	38.7	32.8	22.9
Metals and ores	3.4	5.1	4.9	9.3	8.8	10.5	8.7	14.3	19.3	29.6	26.2	15.3	22.8
Mineral oils	2.2	3.1	4.4	5.0	9.5	12.9	11.7	11.5	10.0	8.7	12.9	14.2	12.4
Cotton twist and yarn.	11.8	13.8	14.4	13.1	6.1	8.7	3.0	1.5	0.9	0.7	0.2	0.5	1.0
Cotton piecegoods	28.1	18.8	23.1	18.1	9.5	0.4	4.0	6.4	1.1	0.2	0.1	0.2	0.1
Vehicles	4.6	5.1	4.5	5.7	4.5	3.7	4.8	6.9	8.9	14.9	11.8	9.1	12.0

Based on table 2-A

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countries in 1948-49, each with trade exceeding Rupees ten crore and together accounting for some 77 per cent of her total trade.<sup>14/</sup> Dependence on India was found to be especially unreliable after shortfalls occurred in the supply of essential imports to Pakistan from that source. Similarly, India's unwillingness to accept agreed quantities of Pakistan jute and cotton was manifested quite early. The deadlock of trade between India and Pakistan arising out of the non-devaluation decision of Pakistan in September 1949 made it obligatory for Pakistan to look to other markets for the disposal of its exportable commodities as well as its own purchases. Hence, the blockade of its natural market necessitated that Pakistan resort to bilateral trade and commodity agreements as an important instrument in its commercial policy, in order both to ensure markets for its products and to procure supplies of domestically needed goods. These agreements helped to provide a formal basis for new avenues of trade, though at times they served the objective of necessity. The movement of diversification was aided and strengthened substantially by the unexpected rise in demand for Pakistan's jute and cotton originating with stockpiling programmes at the eve of the Korean War. This trend towards diversification continued in later years, with the establishment of trade relations with a number of countries, including some from the Soviet Bloc, and helped to reduce Pakistan's dependence, in its international trade, on a few countries only.

## II

For a review of the commercial policy of Pakistan since Partition the period between August 1947 to the end of 1961 can be divided into a number of sub-periods.

### I. August 1947 - September 1949

This period is characterised by the efforts at adjustment to Partition and the transition to a post-partition trade pattern. Few data are available regarding trade during the period August 1947 to 1948. The disruption of economic activity following Partition, the wholesale migration to the Indian

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<sup>14/</sup> Government of Pakistan: Economic Appraisal Enquiry Committee Report, op. cit. p. 3, para 5.

Dominion, of the group which managed foreign trade and business in pre-Partition India and a severe dislocation of banking services, plus numerous other difficulties made it almost impossible to maintain records about the movement of goods across Pakistan borders. Also Pakistan's trade during this period consisted chiefly of exchanges between India and Pakistan, and this trade was treated for some time under a special agreement as domestic trade. In fact, no exchange control was imposed between the two dominions until February 1951 and the Reserve Bank of India managed exchange Control on behalf of Pakistan until 30th June 1948.<sup>15/</sup>

The year 1948-49<sup>16/</sup> is the first complete trade year for which balance of payments data are available though the official records do not include transactions with India until the beginning of 1951. These transactions with India were regulated by a number of stand-still and payments agreements covering the periods August 1947 - February 1948, June 1948 - June 1949, and April 1950 - September 1951. The import policy during 1948-49 was somewhat liberalized as compared to that of the preceding year. This was done, in spite of the necessity to conserve foreign exchange, in order to alleviate the shortage of some essential consumer's goods, coupled with the fact that very few imports had taken place during the earlier part of the year 1948. A part of the imports was placed on Open General Licence (O.G.L.) which provided general permission to all persons to import any of the goods on this list. This step was necessitated in view of the disordered state of trade during this period, as few established importers were available. The O.G.L. imports

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<sup>15/</sup> Government of Pakistan: Monetary System and Reserve Bank Order 1947: Amendment of 1948 as reported in the State Bank of Pakistan Report of the Central Board of Governors, September 1949.

<sup>16/</sup> Trade year is July-June, unless otherwise specified.



however, covered shipments from soft-currency areas only, other than the sterling area<sup>17/</sup> until the end of 1948, while some sterling area imports were also included in the O.G.L. from January 1949.

Most of the customs duties in effect had been inherited from the pre-Partition customs schedule. They were contributing almost sixty percent of government revenue during 1948-52, but it is difficult to ascertain what portion of these duties was imposed primarily for revenue purposes. Considering the state of industrial activity and the balance of payments situation of the country during this period, it is safe to conjecture that a major part of these duties was meant to serve the revenue purposes only.

On the export side jute was placed on an export O.G.L. for the dollar area while it was freely licensable for the non-dollar areas, though destination quotas were imposed. ✓ However, 68 percent of the total jute exports went to India during this year, but this quantum dwindled to almost nothing following the trade deadlock with India after Pakistan's non-devaluation decision in September 1949. The export of cotton was regulated by the issue of export licences to individual exporters but without any restrictions as to destination. Partition seriously disturbed the acreage and quality of cotton, while world factors such as a bumper United States cotton crop and a mild recession in the textile industry in United States

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<sup>17/</sup> Govt. of Pakistan. Press Communique, Pakistan's Import Trade Control Policy: No. 8(48)/(I); for purposes of commercial policy, all currencies are soft except the following: 1) North, Central & South America, excluding territories which are part of the Sterling Area, the Dutch Monetary area, and the French France area. 2) The Belgian Monetary area, 3) Japan, 4) the Philippines, 5) The Portuguese Monetary Area excluding Portuguese India, and 6) Joint U.K./U.S. zone of Germany.

in 1948 contributed to instability and price fluctuations in the cotton export market. This affected the crop in the next season also. Exports of the other main commodities i.e. wool, hides and skins, and tea, were also governed by export O.G.L.

2. October 1949 - June 1950

This was a difficult period for the foreign trade of Pakistan, for a major policy decision about the non-devaluation of the Pakistan rupee created problems of a far-reaching nature. The Pound Sterling, and about thirty other currencies of the Commonwealth including the India Rupee were devalued in September 1949. Pakistan, however, decided to maintain the par value of her rupee vis-a-vis the United States dollar and other non-devalued currencies.

The non-devaluation decision depended on four main considerations;<sup>18/</sup> first, it was felt that the prevailing balance of payments position gave no cause for concern, and was likely to remain strong for some time at least. Second, such a move was considered unnecessary as no material advantage from devaluation was in sight because of the relatively inelastic supply of Pakistan's exports and the almost surely inelastic demand for imports from Pakistan. Internal price stability and industrialization with low-cost capital-imports were the other two objectives in this regard. It is for later sections, however, to analyse the advisability and impact of this decision.

Maintaining the value of the Rupee however, created certain difficulties, and doubts were expressed by many countries, especially from those in the sterling area, about how long the rupee could be maintained at its unchanged level. For a short period, these countries adopted an attitude of "wait and see" hoping either for devaluation or a steep fall in prices of

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<sup>18/</sup> State Bank of Pakistan; Annual General Meeting, Speech by the Governor, September 1949.

Pakistan's exports due to accumulated supplies, but they agreed to the new rate of exchange soon afterwards. India, however, persisted in her refusal to accept the new parity between the two currencies and a complete trade deadlock ensued between the two countries. The strain on the economy due to this development was considerable for the next few months. The exports of jute suffered especially, as India was its main customer. The switchover to other markets could not be made readily, and the Government established the Jute Board entrusted with the task of protecting the grower's interests, and also fixed minimum prices.<sup>19/</sup> The adverse effects on cotton exports were softened due to such other factors as the world boom in cotton prices (due both to a small United States crop and the stockpiling programmes originating with Korean hostilities) starting from mid-1950. An important policy measure undertaken during this period was the conclusion of new bilateral trade agreements with some (five) and of renewal with other (four) countries. The most important of these were made with Japan, France, W. Germany, and Italy. Imports were necessarily more restricted during this period, as export earnings immediately after the non-devaluation decision became uncertain. However, the relative share of imports in Pakistan's sea-borne trade rose because of the need for replacing land-borne imports from India. The need for financing imports and the devaluation of sterling resulted by the end of this period, in a drawing down of Pakistan's Sterling balances to nearly half the level of June 1949. The general difficulties encountered specially in import trade rather sharply focused attention on the need to establish industries within the country, and the first Tariff Commission of Pakistan was established in April 1950 to consider and recommend the grant of protection to industries requiring such assistance for their establishment.

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<sup>19/</sup> Government of Pakistan, Ministry of Finance. Fin.

3. June 1950-December 1951:

The full effect of the Korean war boom made itself felt by October 1950, but the boom conditions were already apparent by June 1950, and eased the pressure on Pakistan's foreign exchange reserves. The earnings from Pakistan's main exports rose steeply during this period, despite only modest changes in the volume of exports of jute, and insignificant changes in that of cotton. The improved foreign exchange position greatly facilitated a liberalization of imports, so that nearly 70 to 85 percent of all imports were placed on O.G.L.<sup>20/</sup> The rest were imports from the dollar area, and even for these imports liberal licensing was allowed. The advance deposit requirements imposed earlier as a selective credit control measure in the import sector were first reduced and later abolished in March 1951 as another step in the import liberalization process.<sup>21/</sup>

Export duties on both jute and cotton were raised, in view of the high earnings from exports due to the rise in their prices.<sup>22/</sup> These adjustments were made to regulate the purchasing power in the hands of the cultivator and the exporter so as to

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<sup>20/</sup> GATT: The Use of Quantitative Import Restrictions to Safeguard Balances of Payments (Geneva, October 1951) p. 61 places the figure at 70 per cent in the earlier part of the period.

Andrus and Muhammad in The Economy of Pakistan (Oxford 1958) p. 264 place the figure at 85 per cent, probably an average of the whole period.

<sup>21/</sup> U.K. Senior Trade Commissioner in Pakistan; Economic and Commercial Conditions in Pakistan, (H.M.S.O. 1954) p. 10.

<sup>22/</sup> Export duties on two different varieties of jute were raised from Rs. 6 and Rs. 20 per bale at the end of June 1951, to Rs. 10 and Rs. 35 per bale respectively, and continued at this level till June 1952. Export duty on Desi and Stample varieties of raw cotton was raised from Rs. 40 and Rs. 60 per bale respectively, in 1949-50 to Rs. 180, and later Rs. 300 per bale for both in October and November 1950 and continued till September 1951, when it was lowered to Rs. 100 and Rs. 180 respectively, and reduced still further a year later.

avoid unnecessary inflationary pressures in the country. The high increments in export duties as well as larger import duty collections due to a bigger volume of imports boosted government revenues as well.

By March 1951, the gains from the boom had reached a peak for Pakistan. On the basis of these fortitious circumstances the par value of Pakistan rupee was finally accepted by India (in February) and the International Monetary Fund (I.M.F.) in March 1951.<sup>23/</sup> Foreign exchange reserves rose considerably during this period, and the liberal import policy that was thus made possible facilitated the growth of a number of new industries in the country; especially important were developments in the cotton textile industry.

#### 4. January 1952-March 1953

The post Korean depression in the prices of primary commodities in the world markets had started by the beginning of 1952. Though it affected some of the exports of Pakistan rather late in that year, the downward trend in prices generally was visible quite early. Jute prices registered a notable decline during the first quarter of 1952, but the only action taken by government resulted in stabilising the internal market, through the introduction of a price support scheme, in March 1952. The rate of export duty on jute was revised in July 1952 (from Rs. 35.00 per bale in 1951-52, to Rs. 15.00), when export prices had fallen to almost half of the prices ruling during 1951. In spite of these measures, the export of Jute fell considerably, and government had to end up with an approximate loss of Rs.90.00 million due to the price support scheme for jute during the year 1952-53.

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<sup>23/</sup> International Monetary Fund: Annual Report, (Washington, September 1951) p. 44. Pakistan became a member of I.M.F. in June 1950, but the decision on the par value of her rupee was postponed for some time.

The case of cotton was not very different. Though the decline in prices started about the same time as that in jute prices its offtake had fallen somewhat during the later part of 1951, necessitating some revision in export duties. In September 1952, the duty on Desi Cotton was removed altogether, while that on staple varieties was reduced further (from Rs. 300.00 per bale during November '50-September 1951, it came down to Rs. 180.00 and then to Rs. 90.00 per bale in September 1952). The price support scheme for cotton, too, resulted in a loss of Rs. 50.4 million for the government during the same year. All these changes in export duties, unaccompanied at the same time by adjustments in import duties resulted in reducing the share of customs in the total revenue receipts of the government from 61.3 per cent in 1951-52 to 54.6 per cent in 1952-53.<sup>24/</sup>

No revision of import policy took place, however, it was only in August 1952 that, under the full impact of the depression, imports were curtailed to some extent. The O.G.L. was finally abolished in November 1952, but since provision was made for honouring the previous commitments on O.G.L., (e.g. machinery and chemicals shipped until 31st of December 1952 remained exempted from import licensing)<sup>25/</sup> imports were not effectively controlled until about six months from the date of cancellation of O.G.L. Both the volume and value of imports shrank considerably after 1952, and all imports were brought under licensing control. Import duty on cotton piece goods and other foreign manufactured cloth (a major import item until 1951-52) was sharply increased, and the scarcity of foreign exchange resources reduced the imports of cotton piece goods and yarn averaging over Rs. 510.6 million during the three years 1949-52 to an

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<sup>24/</sup> The fiscal year was April to March upto 1958; then it was changed and brought in conformity with the trade year, i.e. July-June.

<sup>25/</sup> Government of Pakistan: Chief Controller of Imports and Exports: Notice No. 21 (52)/9.

average of Rs. 66.4 million during 1953-55.<sup>26/</sup> In fact, the two moves undertaken due to balance of payments difficulties provided a highly sheltered market not only to the domestic textile industry,<sup>27/</sup> but gave an impetus to the emergence and establishment of various other industries too.

Efforts to reorganize import trade on a restricted basis included the re-introduction of advanced deposit requirements for imports in June 1952 with severe curtailment of overdraft facilities. Categorisation of importers was started in November 1952 to facilitate the issue of licences later. The situation was well in hand by the end of this period. Nevertheless, the great reduction in foreign exchange earnings as well as reserves led to quite a number of difficulties later.

Apart from the generally state-imported defence-stores requirements, the Pakistan Government dealt in some consumer's goods imports in earlier years upto 1953. Specially to be mentioned are import of coal, which was used mostly by railways (a government operated commercial department) oil, some food-grains, sugar and salt (for East Pakistan). The necessity to import these goods on state account has been greatly reduced by now, for one reason or another.<sup>28/</sup>

##### 5. April 1953-July 1955

This period is characterised by a sharp drop in export earnings and highly restricted import expenditures. The persistent balance of payments deficit, and the need for conservation of the already depleted foreign exchange reserves necessitated a policy of great austerity. The difficulties encountered

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<sup>26/</sup> P. Hasan: Balance of Payments Problems of Pakistan. The Pakistan Development Review, Autumn 1961, p. 29.

<sup>27/</sup> Government of Pakistan: Ministry of Industries; Report of the Textile Enquiry Commission (Karachi, March 1960)-p. 4. The textile industry was referred to the Tariff Commission for grant of protection, but formal protection was not given.

<sup>28/</sup> Imports of coal were reduced due to gradual changeover by Pakistan Railways from coal to diesel-operated engines

encountered during this period originated mainly with the wearing off of the Korean boom, which brought about a drastic fall in the volume of exports due to accumulation of stocks with the buyers. The economy adapted itself quickly to the changed circumstances, and considerable import substitution was made possible on the basis of capacity installed during the boom period, but shortages were apparent in a number of sectors.

One of the factors contributing to pressures on the balance of payments during these years was the food shortage in the country. This problem was resolved to a great extent with the help of foodgrain aid from friendly countries. Nevertheless, imports of goodgrains on government account were considerable.

The need to encourage exports of manufactured goods was felt, in view of the limited exchange earning capacity of primary exports due to their low prices, and because these manufacturing enterprises were absorbing domestically some part of the exportable surpluses. Hence, the first export promotion scheme was introduced in July 1954. Some twenty primary commodities of minor importance and a few cottage industry products were placed under the scheme, which altogether covered less than four per cent of the total export trade at the time. The scheme was to allow exporters of these commodities to utilize 30 per cent of their export earnings for the import of a limited number of goods. However, an additional qualification to the scheme required that this 30 per cent import entitlement should amount, as a minimum, to no less than Rs. 5,000.<sup>29/</sup> Since the commodities placed on the export list could be marketed probably only in small lots, few favourable results could be expected under the restriction which placed a ceiling on the minimum earnings that would permit the use of such an allowance. The scope of the scheme was enlarged

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<sup>29/</sup> Government of Pakistan, Ministry of Commerce, Export Promotion Bureau, Pakistan Trade. July and August 1954, pp. 11 and 60 respectively.



by the beginning of 1955, by placing some more commodities on the export O.G.L. but no significant results were achieved.

An important step to reduce invisible payments was taken in December 1953 by making compulsory the insurance of imports by Pakistani Companies.<sup>30/</sup> Though the efforts at export promotion import substitution by domestic industry and drastic cuts in imports had improved the situation somewhat during 1954-55, the strains operating on the balance of payments necessitated a revision of the par value of Pakistan's currency, and the Rupee was finally devalued as of first August 1955.<sup>31/</sup>

#### 6. August 1955-October 1958

The devaluation of the Pakistan rupee by 30 per cent in July 1955 re-established the pre-September 1949 parity with the pound sterling and the other commonwealth currencies. The economy of Pakistan had undergone considerable changes during 1952-55. The foreign exchange earnings had been falling progressively; the crop failures of 1953-54 had necessitated heavy imports of foodgrains, an extra drain on the foreign exchange resources; and whatever industries had been established during 1950-52 were operating under capacity due to lack of imported raw materials and spare parts. The need for devaluation of the rupee under the circumstances was evident. The newly achieved export potential in jute goods, cotton yarn and textiles and a few other minor industries was also to benefit from devaluation by enabling these goods to be more competitive in the world markets. On the other hand, the increase in industrial capacity marked by the achievement of self-sufficiency in cotton-textiles, paper, and a number of consumers goods<sup>32/</sup> was considered

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<sup>30/</sup> Government of Pakistan, Chief Controller of Imports and Exports, Notice No. 54(53)/I.

<sup>31/</sup> State Bank of Pakistan, Annual General Meeting, Speech by the Governor, September 1955, p. 4

<sup>32/</sup> State Bank of Pakistan; Governors Speech, September 1955, p. 5.

capable both of keeping the internal price level more or less stable, and of substantially alleviating any hardships to the consumer.

Though the extent of the devaluation (30 percent) in relation to the severe balance of payments pressures was questionable, it helped to improve the payments situation favourably, and the year 1955-56 recorded an appreciable rise in earnings of foreign exchange. This improvement, however, cannot be wholly attributed to the devaluation decision; other factors, especially the recovery of the world markets after the post-Korean recession, and a boom in the United States economy played their part. There was a short-lived spurt in prices of staple varieties of cotton and the export duty was accordingly adjusted from Rs. 90 per bale to Rs. 135 per bale but later (August 1956) reduced to Rs. 115. The price and duty changes for jute for 1955-56 were minor.

The favourable balance of payments developments did not last long; pressures emerged soon after, which tended to persist during the years 1956-57 and 1957-58. The food situation remained poor, despite larger foodgrain aid from various countries. Further industrial expansion, and hence import-substitution was limited during this period. Additional restrictions of consumers goods imports in favour of industrial raw materials and capital goods, coupled with other difficulties in the domestic monetary sector created a highly unstable situation. The inflationary pressures also had an adverse effect on the export earnings of the country by making the domestic market more attractive, and raising the cost of exports.

The export promotion scheme was revised in view of the changed circumstances in October 1956. An "Export Industries Special licensing Scheme" was introduced in May 1957 for the import of raw materials and other essentials needed by export industries. This scheme provided that a predetermined ratio of

these industrial users' import license value will be exported within six months of the issue of such licenses. The performance under this scheme too was not very encouraging.

All these measures had, by the beginning of 1958 brought a considerable change in the structure of Pakistan's import trade. Apart from the fact that restrictions on imports were made very severe, the composition had changed too; out of a total of 193 licensable import items in January-June 1957, 39 were exclusively industrial, and by the first half of 1958 this figure had risen to 60 out of a total of 206 items. The fact remains however, that the years 1956-58 witnessed a deterioration in the overall balance of payments situation as the index of import prices had risen considerably due to the devaluation, but the export prices did not register any significant improvements.

#### 7. October 1958-December 1961

The years 1956-57 and 1957-58 were particularly difficult as evident from the discussion above. The export receipts dropped to the lowest level ever, necessitating drastic cuts in imports, while imports under commodity aid (other than food) were not very substantial.<sup>33/</sup> The change in policy which came with the changed government in 1958 restricted imports still further; imports of all textiles, cotton, woollen, and silk, as well as most other high priced luxury items were banned. At the same time most of the unutilized licenses were frozen, and revalidated only in 1959. In the beginning of January 1959 an Export Bonus Scheme was introduced with a set up different from the previous export

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<sup>33/</sup> Government of Pakistan: Office of the Chief-Controller of Imports and Exports, Notice No. 7, (55)/I. Imports had been classified, from 1955 onwards, between those from country's own resources called cash-licensing, and those against U.S. economic aid and counterpart funds, called aid-sub-authorisations. The flow of this aid was not very well regularized during the years 1955-57; hence hardships in import sector.

promotion schemes. This was done in view of the evidence that the commercial sector in the economy had tended to concentrate on imports where gains were abnormally high, and neglected the export sector. According to this scheme the exporters of certain specified commodities<sup>34/</sup> receive a freely transferable voucher entitling its owner to purchase foreign exchange equal to 10, 20 or 40 percent (depending on the commodity exported) of the amount earned. The transferability of the voucher at a market determined price places a premium on it, since the imports allowed under bonus vouchers are varied and large (more than 200 in number). This scheme operates, thus, in the nature of a subsidy for the exporters of the specified commodities, while at the same time taxing the consumer of the bonus imports, through the market mechanism, because of the high premium on bonus vouchers. There is thus an element of discrimination between goods imported under regular license, at the official exchange rate, and those imported after the payment of a premium on bonus vouchers, which has ranged between 80 to above 150 per cent. This in effect means the operation of a multiple exchange rate system in the economy, or an invisible devaluation of the currency for the purpose of some imports. The export Bonus Scheme, though initially introduced as a short-term measure, was later extended to June 1965 and made co-terminus with the Second Five Year Plan.<sup>35/</sup>

The imports under bonus, however, were primarily meant to relieve the industrial sector of shortages of raw materials and spare parts. During the year 1959-60, 80 per cent of the industrial sector was enabled to obtain 100 per cent of its requirements of these essentials.<sup>36/</sup> ~~The improvement in the foreign~~

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<sup>34/</sup> Items placed on the bonus export list, include all exportables and manufactures of Pakistan except raw jute, raw cotton, raw wool, raw hides and skins, tea and rice. The composition of the list has been changing however, in view of the needs and developments of the domestic industrial sector.

<sup>35/</sup> For further exposition of the Export Bonus Scheme, see Bruton and Bose, the Export Bonus Scheme, a Preliminary Report, the Pakistan Development Review, September 1962.

<sup>36/</sup> Government of Pakistan: White Paper on the Central Govt

exchange position during this year lead to some import liberalization. Eleven items were placed on a restricted O.G.L. for the period January-June 1960, and another 28 items in July-December 1960, while a number of imports were placed on automatic licensing. The working of the new O.G.L. was restricted, however, to include only categorised importers, whose permissible imports were placed on banned list. They could import specific items on O.G.L. within a fixed "ceiling" in terms of value or quantity. This trend has continued during the year 1960-61 though changes have been introduced from time to time in the pattern of imports according to the availability of foreign exchange.

Special attention has been given during this period to reduce the burden of customs duties on goods, capital or otherwise, meant for industrial uses. Thus, the customs duty on all machinery and some other industrial items was reduced, between 1959-61 from 50 per cent or more to a level of 25-30 per cent, and later to a uniform  $12\frac{1}{2}$  per cent with a special concessionary rate of  $7\frac{1}{2}$  per cent for East Pakistan.<sup>37/</sup>

Tariff protection was granted, over the period 1950 to end 61, to 53 industries, notable among which are electric lamps, fans, and electric motors, cycle tyres and tubes, some drugs and pharmaceuticals, dyestuffs, paints, colours and varnishes, matches, lathes, steel castings and steel-re-rolling.<sup>38/</sup> It is surprising to note that the major industries of Pakistan, like cotton and jute textiles and yarn and paper emerged without the formal grant of protection though embargoes on imports of these goods for balance of payments purposes were placed and did provide them with sheltered domestic markets.

Thus, an account of the Commercial Policy of Pakistan has to cover widely fluctuating events. There have been sudden and

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<sup>37/</sup> Government of Pakistan, Investment Promotion Bureau, Ministry of Industries, Guide to Investment in Pakistan, 1961, and supplement to brochure entitled Investment Opportunities in Pakistan, 1961, p. 9.

drastic changes in policy, largely motivated by the inability of domestic supply conditions to adapt to changes in world demand or prices. Its trade relations with neighbouring countries, particularly India, have played a major role in shaping the policy in the earlier period. Later, domestic instability, political and economic, was a key factor in determining the course of its policy. It remains for the last section to attempt an assessment of the achievements of policy in terms of success or failure in the fulfilment of policy objectives.

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With the foregoing analysis of the commercial policy of Pakistan, as given in the preceding section, we are now in a position to draw conclusions about the effectiveness of policy in the achievement of objectives as set out in Section 1 of this paper. To simplify the procedure of analysis, we will examine the performance of policy in the same order as the objectives set up.

#### 1. Revenue Purposes

Customs duties are an important source of government revenue of Pakistan as mentioned earlier. The accompanying table-3 shows, however, that their share in total government revenue has been declining over time falling from an average of about 62 percent during the first four years (1948-49 to 1951-52) to less than one third of the total during the last four years listed (1958-59 to 1961-62). The fact that total tax revenue of the government (Column 1, Table 3.) from the four other principal heads of revenue viz: personal income tax, corporate income tax, excise and sales tax, has constantly been on the rise points up the lag in yields from customs duties. Whereas the tax yield of these other four almost doubled over time, that of customs fell absolutely in 1953-1954, and though it recovered later, it never reached the levels achieved earlier.

Let us examine import duties first. Excise duty collections were supposed to fill the gap created by the shrinking of tax revenue from import duties, as these were imposed on domestic manufactures, most of which were substitutes for imports. It is to be noted, however, that the fall in import duty collections was not replaced fully by excise taxes on domestic manufactures. Quite a number of these new industries were exempted from the from the imposition of excise taxes, while their imports formerly were subject to import duties. On the other hand, even the domestic manufactures taxes, like cotton textiles and yarn, pay in terms of excise only a fraction of what they used to pay in terms

Table 3

## Customs Duties as Part of Total Tax Revenue\* Collected by the Centre

Years	Total Taxes*	Customs	Export	Import	Percentage share of		
	(1)	(2)	(3)	(4)	Customs in total tax revenue 2 ÷ 1	Export duties in customs 3 ÷ 2	Import duties in customs 4 ÷ 2
1948-49	639.2	382.8	186.5	196.2	59.9	48.8	51.2
49-50	814.6	482.8	122.3	360.5	59.2	25.3	74.7
50-51	1231.3	843.9	427.7	416.2	68.5	50.7	49.3
51-52	1438.7	919.4	365.5	553.8	63.9	39.7	60.3
52-53	1286.7	695.3	235.0	460.3	54.0	33.8	66.2
53-54	1000.9	440.0	183.3	256.6	44.0	41.7	58.3
54-55	1088.0	492.8	126.0	366.8	45.3	25.6	74.4
55-56	1225.3	635.3	206.5	428.8	51.8	32.5	67.5
56-57	1258.5	561.1	165.5	395.0	44.6	29.5	70.5
57-58	1312.2	549.1	133.3	415.8	41.8	24.3	75.7
58-59	1741.5	606.2	163.2	442.8	34.8	26.9	73.1
59-60	1618.0	542.1	127.8	414.3	33.5	23.6	76.3
60-61	1947	625.3	75.6	549.6	32.0	12.1	87.9

## Source:

Column I: Budget Documents of the Government of Pakistan.

\* Date includes tax revenue from five principal heads only, viz, Personal Income and Corporate income tax, Excise tax, Sales tax, Customs, and Sell, before allocation to Provinces.

Columns 2,3 and 4: Courtesy of the Central Board of Revenue: Also available, for some years in the Taxation Enquiry Committee Report.

39/ Government of Pakistan: Taxation Enquiry Committee Interim Report, (Karachi, 1959) p. 43. Some of the industries which do not bear excise duty are food products, glassware, electric bulbs, soap, paper etc. Most of these are also given protection.



The highest tax collections, during this period, from import duties (Column 4, Table 3.) were realized during 1951-1952. However, the turnover of trade in that year was also at the peak, total private account imports standing at Rs. 192.8 million. Comparing roughly the total value of imports and import duty collections, however, one comes to the conclusion that the average height of the import tariff in that year was about 28 per cent. The comparison of some selected later years is as follows:

Year	Average Unweighted (percentage) height of tariff
1951-52	26.1
1953-54	36.4
1956-57	89.1
1957-58	121.2
1959-60	85.0
1960-61	57.7

Source: Table 4.

The year 1953-54 represents the trough period for both imports and duty collections (table 3). The year 1957-58 is significant because it stands at the end of a long period of trade and balance of payments difficulties and the year 1960-61 represents the position as it stands now with the import schedule including more of low duty development oriented goods (nearly 60 percent of total imports on private account) and less of high duty consumption goods. This table and the preceding discussion point up the fact that both the volume of trade and the average height of tariff though important, do not have a significant meaning for purposes of collections of tax revenue in a developing economy. More important in such a case is the composition of imports, i.e. what type of goods are imported. Referring back to table 2-B, which clearly shows the trend away from the import of consumers goods towards the import of capital goods and industrial raw materials, the reasons behind this falling trend in import duty collections become evident, since only the former are liable to pay high import taxes, while the import of the latter has to be encouraged for development purposes, and thus taxed at low rates. It might be suggested thus, that a developing

country like Pakistan has little scope of development

of tax revenue is a problem of fiscal policy, however, and not in the scope of this discussion.

Collections of revenue from export duties, on the other hand, as given in Column 3 of table 3, show an almost persistent downward trend, even though the volume and value of total exports has not fallen much. However, only a limited number of exports bear an export duty, and even among these, raw jute and raw cotton are the major sources; goods like raw wool, hides and skins, and tea have borne only a minor burden of duty payments, being exempted from any such payments from time to time. Revenue collections from export duties are very closely linked with the price of exports in the world markets, the state of foreign demand and the extent of competition faced. Pakistan's raw jute was produced almost in monopoly circumstances in the first few years. Even though this hardly warranted any exploitation of the situation as the number of markets at its disposal was limited, with India its main customer, the scope for raising substantial tax revenue from this source was evident. Since the wearing off of the high demand conditions of the Korean war boom, however, Pakistan's jute has been facing increasing competition from the growth in jute cultivation that has since taken place in India. Pakistan is thus no longer in an enviable position of near-monopoly as regards its jute. Apparently, judging from the trend of average jute prices since 1952-53, it also faces a relatively inelastic demand in the world markets. At home, its supply is sensitive to the price of rice, a crop which can be alternately grown in place of jute; a number of studies have shown the high correlation between the prices of jute and the price of rice.<sup>40/</sup> Since the imposition of an export duty tends to lower the remuneration to the domestic cultivator, it is imperative that the price and demand factors be taken into account before the rate

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<sup>40/</sup> See for example Ralph Clark "The Economic Determinants of Jute Production", FAO Monthly Bulletin of Agricultural Economics and Statistics, Vol. VI, No. 9, September 1957

of duty is fixed. In spite of the recover of jute prices during the years 1960 and 1961, no great reliance can be placed on it as a source of revenue in future.

Raw Cotton export on the other hand, is becoming less and less important for purposes of revenue as its volume has gone down substantially due to its consumption by domestic textile industry. In fact, an export duty on raw cotton, by lowering the domestic prices, provides incentives to the industry to consume larger quantities of cotton, so that little is left for export. Perhaps manufactures of both jute and cotton will in the long run be ready to bear the burden of export duties; for the present, in view of all the other incentives being provided to boost up the export of manufactures, any policy aiming at this source yielding some revenue for the government exchequer would be in conflict with the objective of development.

We might conclude, then that the objective of reaching a sufficient level of tax revenue from customs duties has had to be worked out (and will remain so for some time to come) under a number of constraints, important among which are: no appreciable rise in exports, and in fact fall in some, lower export duties in view of subdued markets facing the export products of the country and shifts within the import schedule so as to favour development needs to the detriment of the revenue objective. Thus, the scope of this objective can be enlarged only if the commercial policy is conducive to reducing and minimizing the rigidities of these constraints; in fact, such a policy would be helping in other areas too.

## 2. Protection or Resource Allocation

A country like Pakistan must accord protection to some industries which have some natural advantages, and which might be expected to dispense with the necessity of protection within a reasonable period of time. This is a difficult task, however; to assess the claims of an industry to the right of being shielded from foreign competition needs a number of factors to be looked

into such as the capacity of the industry to expand and meet domestic demand, and the loss to the consumer perhaps in terms both of price and quality. It is interesting to note that none of the major industries of Pakistan, like jute and cotton textile and paper which had most of the natural advantages in terms of raw materials were given formal protection. The fact that some of these, e.g. Jute textiles and paper industries started as government enterprises and were thus given special privilege in the granting of foreign exchange for the procurement of machinery and other capital equipment, is beyond the point here. A study of the industries given protection so far shows that the emphasis has been on import substituting industries. This had entailed additional expenditure of the foreign exchange earnings of the country in so far as the establishment of these industries required purchases from abroad of machinery, other equipment and some raw materials also (e.g. in the case of steel rerolling, steel castings and cycle tyres and tubes) while they did not contribute anything to earnings of foreign exchange. It may be that some savings in the import of these goods did take place, but it is difficult to determine the extent of any such saving.

The trend of resource allocation from the list of industries protected seems to be in favour of light machinery and industrial user's goods, while only about one third of these are consumers' goods industries. Data about such questions as performance of the protected industries in terms of total goods manufactured, as well as flow of additional private capital to these industries is lacking. These questions need to be looked into thoroughly for any concrete assessment of the usefulness of such a policy. It is also necessary in order to determine the long run gains that such resource allocation may be expected to yield.

3. Defense of the balance of Payments.

The details set down in section 3 of the present paper bring out rather prominently the fact that all policies aiming at correction of balance of payments disequilibria have leaned rather heavily on restricting imports. Comparatively little attention has been paid to the other side of the problem - till 1959 - of framing really dynamic policies aiming at encouragement and promotion of exports. An analysis of table I-B reveals that no great change was brought about in the structure and composition of the export trade of the country until 1958-1959, when the export-bonus scheme started with sizable subsidization of the jute and cotton textile exports and thus a spurt in their percentage share in the total export earnings of Pakistan is witnessed during the years 1958-59, 1959-60, and 1960-61. It is to be noted, however, that the share of cotton and its manufactures taken together has fallen considerably, whether we take account of the total volume or value exported. Here is a clear case of export stagnation. Measures aiming at curbing domestic consumption and increase in the acreage and yield of cotton in order to improve the supply position would be useful in this regard, without any significant effects on the international prices of cotton, as Pakistan is a small supplier in the world market. If left to itself the cotton situation may deteriorate so that Pakistan might move on to the position of a net importer of raw cotton rather than an exporter.

The Jute position has been subject to a fluctuating price situation throughout. The Korean boom period was followed by generally subdued markets for this fibre - too and the domestic supply was subjected to acreage controls in order to strengthen prices. It is only since 1959-60 that the index of export price for jute has again gone up.

The case of the two major cash crops of Pakistan and the consequent deterioration of the terms of trade brings the vulnerability of the balance of payments to outside influences rather sharply into focus. The continued balance of payments difficulties through 1954-55 upto 1958-59, with a brief period of relief after the devaluation of 1955 show that something more than mere control of imports is required. It is interesting to note in this regard that the devaluation in 1955 was able to exert only a temporary influence on the balance of payments situation. The need to build up sizable foreign exchange reserves and their safeguard is imperative in this regard; a policy of drawing down of such reserves to dangerously low levels, as was evident, for example during 1954-55, not only deteriorates the balance of payments situation but also disturbs the balance in the domestic monetary sector. It is thus evident that the commercial policy followed during these years has failed to meet the challenge that the balance of payments situation presented.

It would be relevant to note the role played by foreign economic aid in this regard. Though a complete evaluation of the effects of foreign aid on the economy would be out of place here, it must be taken note of for the role that it has played in relieving the balance of payments pressures of the country. To take an instance, there have been sizable imports of foodgrains under aid during periods of food shortages. It is evident that the burden on the balance of payments would have been much greater in absence of the food imported under aid, which amounted to a total of nearly Rs. 1800.00 million (utilised) from 1954 upto end December 1961.<sup>41/</sup> On the whole it financed about one third of the total imports of the country during the first plan period.<sup>42/</sup>

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<sup>41/</sup> Government of Pakistan, Ministry of Finance, Foreign Economic Aid: a supplement issued with the Budget 1962-63 (Rawalpindi, 1962) ch:3 (for foodgrains aid under U.S. P.L. 480 Title I and II) and Appendix I, p.110-111 (for foodgrains aid from other countries).

<sup>42/</sup> Government of Pakistan, the Second Five Year Plan, 1960-1965 (Published June 1960) p.87.

#### 4. Stability of the Domestic Economy

The balance of payments position has a definite impact on the domestic price level, specially in a country like Pakistan, where imports cater both for consumption as well as production and development activities in the country. As such any policy aiming at a regulation and control of imports must take into account the broader impact of such a policy on the domestic price level through an interference with the level of import prices. The volume of exports, through its foreign exchange earnings, fixes, to some extent the policy determined level of imports during the short-run,<sup>43/</sup> and thus needs consideration too.

Changes in foreign exchange reserves have some direct relationship with the total availability of money supply in the country, too, as gold, dollar and sterling reserves serve as a part (30 per cent) of the assets of the issue department of the State Bank of Pakistan, as currency backing. It is difficult to deduce from available data however, the extent of the direct relationship between changes in money supply and the foreign exchange reserves. Stability in the domestic economy is, thus, linked with the foreign sector but not much attention has so far been paid, in policy formulation, to a coordination of the two. This is a sector needing more thoughtful research than it has been given so far.

#### 5. Maximisation of income from exports:

The objective of maximisation of income from exports was not given much consideration in the commercial policy of Pakistan up till 1959. Mention has been made earlier of the occasional

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<sup>43/</sup> Foreign aid and loans can fill the gap after some time, and in fact have been doing so in Pakistan but they can be acquired only with some lag. More about this will be discussed in the evaluation of the last policy objective viz, economic development.

attempts at export promotion that were made during the period 1953-57. The coverage was very insufficient however; "the value of exports included in the Export Incentive Scheme which expired on the 30th of September 1955, amounted to over Rs. 2 crores as compared to about Rs.6.9 million and Rs.8.4 million respectively during the years 1952-53 and 1953-54."<sup>44/</sup> This means that the schemes covered only about 1.7 per cent of the total value of exports on private account for the year 1954-55, whereas the percentages were almost negligible for the two earlier years mentioned. The incentives provided, also, were not highly effective since they worked under conditions of a minimum effort in export performance.

The more recently introduced (in the beginning of 1959) Export Bonus Scheme has had better results however. This scheme covers all exports except raw jute, raw cotton, wool, hides and skins, tea and some varieties of rice. Imports allowed with foreign exchange earned through the export bonus scheme are varied and large (more than 200). Whereas this scheme, on the one hand, encourages exports of all manufactures, cottage industry products and some semi-manufactures, it nevertheless has a destabilising influence on the domestic price level and the commodity market situation. This is because a keen competition arises between the domestic purchaser and the exporter of raw commodities in the domestic market. Hence, a decided fall in the absolute quantity of both raw jute and cotton exported, as well as in the relative share of export in the total produce of the two, is witnessed during these two years. No exhaustive official evaluation of the net loss or gain from the scheme has been made so far, in terms of earnings foregone due to reduced exports of raw commodities and the additional earnings from items covered by export bonus list which

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<sup>44/</sup> Government of Pakistan: Ministry of Finance: White paper on the Budget for 1956-57, p:24.



may be attributable entirely to the operation of the scheme. This is not all that can be done in this field, however. Efforts at stabilization of both domestic and world market prices for the primary exports of the country should be an essential feature of any programme for the maximization of income and foreign exchange earnings from exports. Whereas the former can be looked after through specific domestic policies, the latter requires international cooperation, and can be achieved only through occasional airing of the country's views in the relevant international forums. A creditable performance in the achievement of this objective, is most essential not only from the view point of maximising income, but also for balance of payments purposes, and to help finance the foreign exchange component of the development programmes of the country.

6. Economic Development:

Economic development of the country is a major professed goal of all national policies today in Pakistan and especially so in areas covered by the First and the Second Five Years Plans aiming at raising national and per capita incomes in the country. The commercial policy of the country, under these circumstances, has to play a vital role, though subservient to the over-riding objectives set out in the Plan.

It is a matter of some concern that the present Five Year Plan projections for 1960-65 of the total foreign exchange earnings of the country at Rs.11,250 million fall considerably short even of the projected non development imports of Rs.13,750 million.<sup>46/</sup> This gap of Rs.2500 million for the financing

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45/ See Bruton and Bose, *op. cit.* which gives a preliminary report on the findings of a research project on this topic.

46/ Government of Pakistan: The Second Five Year Plan (Revised estimates) November 1961, p.26.

of the non-development imports must be added to the other requirements of foreign exchange for development purposes (Rs.8450 million), for the Indus Basin Replacement Works (Rs.2240 million) and to cover expected shortages of food and other commodities (Rs.3440 million, under P.L.480).<sup>47/</sup> Thus, out of the total projected development expenditure of Rs.27,900 million (the revised Plan estimates plus Indus Basin and Works programmes) during 1960-65, the foreign exchange component not financed from the country's own resources amounts to Rs.16630 million, or nearly sixty per cent of the planned development expenditure. It is evident, then that the foreign sector, in an underdeveloped country like ours, is expected to make a major contribution to the development effort of the country. The fact, however, that the current earnings of foreign exchange by the country are insufficient to meet the non-development expenditure, invites special attention towards the role of commercial policy. The extent to which foreign aid, loans and investment should contribute to the development efforts of a country is a controversial matter. The developing countries may put forward the criteria of their "need" forming the basis of any such assistance, which may consist of the total foreign exchange component of development, more than that or less. The countries contributing foreign exchange, however, may depend on any criteria - from political to socio-economic to purely economic ones such as the absorptive capacity of a country (though this last concept may not lend itself to any concrete measurements). Much can be done, however, through the country's own efforts, at reducing its dependence on foreign sources of financing its development expenditures. This is the area, then, where the commercial policy can be maneuvered to reduce the non-essential imports to a minimum, to budget and allocate the foreign exchange

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<sup>47/</sup> Ibid, pages 16 and 17.

resources among various uses in a manner most advantageous for the development of the country, and to aim at enhancing the earnings of foreign exchange, specially by developing new exports.

Earlier discussion of policy achievement of the various other objectives, thus, highlights the fact, that much remains to be done both in the field of a better regimentation and control of the current account, the non-development imports of the country, and in the promotion of exports. Following are a few suggestions for a reorganisation of the commercial policy of Pakistan in the light of the foregoing analysis, in terms of the instruments of policy mentioned in section 2.

1. A revision of the tariff structure of the country, of both import duties and export duties in the light of the changes already apparent in the pattern of foreign trade. This would be in order specially because the importers and consumers of goods imported under regular licenses are apparently enjoying large margins of profits (and consumers' surplus) by receiving foreign exchange at a price much below its true value. The government must aim at diverting some of these surplus gains to itself, through a revised tariff structure, so as to utilize them for other development purposes. In the export sector, some of the duties are outmoded and almost injurious to the cause of export promotion. Alternative areas of taxation must be sought to cover the fall in proceeds from this sector.

2. The procedures for licensing of imports, and fixing quotas for them, should be made simpler. Import trade in the country has been monopolised by a small group during the last one decade or so. Already, some efforts are being made to allow new comers in import trade, but more is needed to introduce some element of healthy competition in this commercial sector. A break away from traditional sources of supply as basis of fixing quotas must be sought, in order to exploit the cheapest markets to the best advantage of the country, (unless imports are "tied" and thus committed to come from specific sources).

3. The Exchange control machinery in the country needs further tightening. More stringent controls on the foreign exchange receipts and allocations, by better supervision of the over-valuation and under-valuation of the invoices by importers and exporters, is needed. This is borne out by the fact that declarations under amnesty of foreign exchange illegally held abroad were considerable during 1959-60. Also, it is essential to remove anomalies in foreign exchange regulations which allow only limited drawings of foreign exchange for visits abroad, but disproportionately high imports as "personal baggage" on return, by residents of the country, thus almost inviting misuse of such regulations.<sup>48/</sup> Removal of even such small discrepancies in policy matters can reduce the drain on foreign exchange resources to some extent.
4. Bilateral agreements and state trading have played a limited role in the commercial policy of Pakistan, but most probably in the socio-political set up of Pakistan, they may not be expected to do more than this. Bilateral agreements have been of importance in diverting the direction of trade somewhat, and they may be expected to play the same role in future also.

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<sup>48/</sup> For example, the maximum "basic quota" for travel abroad as a tourist is £ 150, equivalent to about Rs. 2,000, but total imports allowed, free of any import duties, as "personal baggage" amount to about five times the 'basic quota' figure.

Table No:4

Percentage hight of tariff for various Categories of Imports

		Rs. in millions												
		1948-49	49-50	50-51	51-52	52-53	53-54	54-55	55-56	56-57	57-58	58-59	59-60	60-61
Mineral Oils	Imports	27.2	35.3	62.9	97.7	89.1	94.6	108.2	114.2	102.4	81.6	99.9	238.2	263/3
	Duty Collections	39.3	42.6	60.1	68.7	51.4	80.0	65.9	65.4	75.6	83.9	108.7	77.9	96.7
	Percentage hight of tariff.	144.5	120.7	95.5	70.3	57.7	84.6	60.9	57.0	73.8	102.8	103.8	32.7	36.7
Vehicles	Imports	58.1	58.0	65.5	93.0	41.9	27.0	44.6	58.4	91.2	139.6	98.8	152.8	254.5
	Duty Collections	8.5	14.4	18.2	16.8	14.2	8.1	14.9	13.1	18.8	19.5	33.4	18.2	55.4
	Percentage high of tariff.	14.6	24.8	27.8	18.1	33.9	30.0	33.4	22.4	20.6	14.0	33.8	11.9	21.8
Machinery*	Imports	66.8	82.1	111.9	175.3	136.8	166.0	318.5	182.0	268.6	304.7	324.9	551.1	485.8
	Duty Collections	5.6	4.7	5.6	8.8	3.8	4.7	18.1	12.2	15.1	13.0	27.1	39.8	78.2
	Percentage hight of tariff.	8.4	5.7	5.5	5.0	2.8	2.8	5.7	6.7	5.6	4.3	8.3	7.2	16.1

Contd.....

Metals	Imports	42.3	57.4	70.2	183.2	82.8	76.9	80.2	131.8	197.0	278.0	220.0	257.6	484.4
	Duty Collections	3.0	4.5	11.3	18.0	19.0	12.0	8.5	12.5	13.4	19.6	22.4	11.4	42.6
	Percentage hight of tariff	7.1	7.8	16.1	9.8	22.9	15.6	10.6	9.5	6.8	7.0	10.2	4.4	8.8
Textiles & manufacturing	Imports	502.0	369.5	536.0	626.3	145.9	67.4	64.8	78.5	20.1	8.7	2.6	12.9	24.3
	Duty Collections	53.1	100.8	127.5	171.7	152.8	33.2	81.8	76.4	68.1	41.6	50.0	47.7	49.6
	Percentage hight of tariff	10.6	27.3	23.8	27.4	104.7	49.3	126.2	97.3	338.8	478.1	...	369.0	204.1
Average unweighted hight of tariff for the above five categories.		37.04	37.24	33.7	26.1	44.4	36.4	47.3	38.6	89.1	121.2	...	85.0	57.7

Source: for value of Imports: Report on currency and finance, as in table 2.A. For Duty collections: Courtesy of Central Board of Revenue: Statistical office letter C. No. 2(4)-C.st/61.

\*the item 'machinery' is the same as "machinery and will work" in table 2-A

+Not calculable, as duty collections for 15 month period due to change of fiscal year from April March to July-June.

All customs duty figures are provisional and not fully reconciled with Accounts figures.

Data for value of imports on a July-June (Trade year) basis; for duty collections on an April-March basis upto 1958-59, later on July-June basis.

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