GENERAL AGREEMENT ON

TARIFFS AND TRADE

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Committee on Balance-of-Payments Restrictions

REPORT ON THE 1989 CONSULTATION WITH PAKISTAN

1. The Committee consulted with Pakistan on 17 April 1989, in accordance with its terms of reference, pursuant to Article XVIII:12(b) of the General Agreement and the Declaration of the CONTRACTING PARTIES on Trade Measures Taken for Balance-of-Payments Purposes (BISD 26S/205). The consultation was held under the Chairmanship of Mr. J.-F. Boittin (France). The International Monetary Fund was invited to participate in the consultation in accordance with Article XV of the General Agreement.

2. The Committee had the following documents before it:

Basic document by Pakistan	BOP/288
Secretariat background paper	BOP/W/124
International Monetary Fund "Recent Economic Developments" dated 17 December 1988	

Opening statement by the representative of Pakistan

3. The opening statement by the representative of Pakistan is attached as Annex I.

Statement by the representative of the International Monetary Fund

4. At the invitation of the Committee, the representative of the International Monetary Fund made a statement, which is attached as Annex II.

Balance-of-Payments position and prospects: alternative measures to restore equilibrium

5. Members of the Committee recognized that Pakistan continued to face balance-of-payments problems which warranted the imposition of trade measures under Article XVIII:B. Members noted that some of the underlying factors were structural in nature. Among the elements cited by some members as contributing to the balance-of-payments difficulties were the impact of Pakistan's fiscal and monetary policies on the relationship between domestic output and expenditure; Pakistan's narrow production and export structure; deterioration in the terms of trade; the continuous decline in workers' remittances in recent years and external factors such as subsidization of agricultural products and restrictions under the Multifibre Arrangement. Some members said that the Committee should pay particular attention to the difficulties caused for Pakistan by the instability of world markets and trade distortions and barriers in major importing countries. The concentration of exports in a few product areas

made Pakistan particularly vulnerable to adverse trends on world markets, as well as to increases in trade barriers on certain products. For this reason, the reduction of obstacles and distortions to trade was an essential part of the solution to Pakistan's problems. Other members, while noting the growth in the overall value of Pakistan's exports over the past three years, recognized the vulnerability of its export structure and stressed the critical importance for Pakistan of diversification of both products and markets.

6. The Committee welcomed the reform programme being pursued by Pakistan. Such reforms were regarded as critical for improvement of the balance of payments on a sound and lasting basis. Pakistan's development programme during recent years had been ambitious and successful although imbalances had arisen. In this connection, one member asked what action had been taken or was envisaged to encourage revenue growth and contain expenditures. The existence of a three-year programme of macro-economic and structural reform was a positive step; in this connection, Pakistan's medium-term trade policy programme and the commitments made within it to continue reducing trade barriers and rationalizing tariffs were regarded as providing stability, predictability and a sound basis for progress. The introduction of floating exchange rates and the marketing of foreign exchange bearer certificates were also seen as positive elements. One member noted, however, that even though progress had been made in the reduction of trade barriers, there was still a large number of banned or restricted goods and a substantial volume of trade channelled through Government agencies, as well as other restrictions in the fields of shipping, foreign exchange allocation, and so forth. Some members encouraged Pakistan to continue to act as strongly as possible to reduce trade barriers and domestic constraints.

7. Replying, the representative of Pakistan thanked members for their appreciation and encouragement. Despite sustained economic growth of 6-7 per cent in the 1980s, the fiscal deficit had reached 8.1 per cent of GNP in 1987/88. The current adjustment programme sought to reduce this deficit to reasonable limits. The new government was seeking new avenues for tax revenue, through the creation of a broader-based tax system, controlling current expenditures, giving priority to developmental spending and seeking to increase the efficiency of tax collection. Through these combined efforts the deficit was expected to be reduced to around 6.5 per cent of GNP in the current year and this was expected to continue in the medium term, under the 7th Plan and the programme agreed with the IMF. There were many factors beyond Pakistan's control in the balance-of-payments situation, including declining terms of trade, falling world prices for major export commodities and trade barriers and measures maintained by importing countries. A more favourable external environment was urgently needed to assist Pakistan in the recovery of its balance of payments.

System, methods and effects of restrictions

8. Members of the Committee welcomed the changes which had taken place in Pakistan's import régime since 1983; in particular the move to a negative list system, the reduction in the number of commodities covered by import restrictions, the simplification of the import system and the

rationalization of the tariff structure. It was noted that these reforms should contribute to a more favourable export performance, increase allocative efficiency and promote optimal production and investment decisions. Some members urged Pakistan to continue the process of reducing non-tariff measures.

9. Some members felt that greater clarity was needed concerning the number of restricted lists, the reasons for their maintenance, and criteria for the inclusion of items in the lists. One member recalled that criteria which had been mentioned included health and security questions, temporary protection of domestic industry and concerns related to reciprocity. These were not covered by Article XVIII:B. It was clearly stated in the 1979 Declaration that balance-of-payments restrictions should not be used to protect a particular industry or sector. He reserved his rights under the General Agreement with respect to these restrictions. Some members asked Pakistan to indicate which trade restrictions were taken for balance-of-payments purposes and which for other reasons including temporary protection of local producers; in particular, whether all the items on the negative and restricted lists were restricted for balance-of-payments purposes.

10. The ongoing process of removal of items from the negative list was welcomed. However, it was noted by some members that a considerable number of products were still subject to prohibitions, which were not permitted under Article XVIII:B. One member asked for clarification of the discrepancy between the 475 items mentioned in the secretariat paper as being on the negative list and the 240 items mentioned by Pakistan.

11. Questions were also asked by some members concerning the licensing system. It was understood that, while all imports required a license, many items were imported freely under licence. Pakistan was asked what proportion of import items were in this category. In addition, one member asked whether the monitoring functions played a part in moving goods on or off the negative or restrictive lists, what procedures were involved in obtaining a licence and how many agencies must approve a licence under normal conditions. He encouraged Pakistan to remove the licensing requirement in cases where licences are freely granted: no reason was seen for such a licensing requirement, which was likely to undermine reform by perpetuating an administrative mechanism for restricting imports.

12. Pakistan was also asked by a member to give an outline of its future programme of phasing out of import restrictions with a time-frame if practicable.

13. Some members requested Pakistan to provide the Committee, by its autumn meeting, with an up-to-date list of the products on which import restrictions were maintained for balance-of-payments purposes. One member emphasized that without an up-to-date list of such products on an eight-digit Harmonized System basis, it was difficult to determine how extensive Pakistan's balance-of-payments restrictions were.

14. Questions were also asked by some members concerning the level of and justification for import surcharges. In this context it was recalled that surcharges were to be preferred to quantitative restrictions as a

balance-of-payments measure, and that duplication of different types of import measures was to be avoided.

15. In reply, the representative of Pakistan said that Pakistan's import policy was completely transparent, published in the Official Gazette which was available to the public and a copy of which had also been supplied to the GATT Secretariat. The discrepancy in the number of items in the two lists was due to use of different classifications. The purpose of import licensing in Pakistan was to monitor the flow of imports and the balance-of-payments situation; licences are issued within 24 hours of the application. The only agency involved in the process of issuing import licences was the office of the Chief Controller of Imports and Exports. Import licensing was not, therefore, an instrument of restriction or protection. An additional advantage for exporters to Pakistan was that all imports were allowed against confirmed letters of credit.

16. The main purposes of the import restrictions maintained by Pakistan were firstly, balance-of-payments reasons, and secondly, security, cultural or religious purposes. Tariffs were the only instrument of protection in Pakistan and a major source of revenue: The surcharges in force were for fiscal purposes: in particular the "Iqra" surcharge was to provide revenue for educational and literacy programmes. Restrictions were basically for balance-of-payments purposes; if there were other effects these were incidental. Pakistan would continue the process of liberalization with the improvement in its external and reserves position.

17. In respect of notifying the products under restriction, the representative of Pakistan said that the full details had been supplied to the Secretariat under the provisions of the Agreement on Import Licensing Procedures and were available in the Secretariat for consultation by any interested party. In addition, Pakistan would, in due course, be updating its notification to the Technical Group on Quantitative Restrictions. This would contain full information, classified under the Harmonized System, on the status of Pakistan's restrictions and their GATT justifications.

18. Some members stressed that the Committee could not rely only on materials supplied to other GATT bodies for other purposes. In this specific case, such other notifications were outdated, based on a different customs classification system and did not reflect accurately the present situation or did not contain all relevant information necessary for the specific tasks of the Balance-of-Payments Committee.

19. There was an exchange of views on the notification requirements for use by the Committee on Balance-of-Payments Restrictions. The representative of Pakistan said that his understanding of the provisions of Article XVIII was that the obligation under Article XVIII:B related to the general level of restrictions and not to individual measures or products. Similarly, the reference to "all restrictive measures" in paragraph 3 of the 1979 Declaration could not be construed as extending the coverage of notifications to individual "products" on which restrictions may be maintained by a consulting party on account of balance-of-payments reasons. Pakistan's import system was basically for balance-of-payments purposes. The notifications made in the context of the Agreement on Import Licensing provided information on the general level of restrictions. In addition,

Pakistan had regularly notified its restrictions with their GATT justifications in the Technical Group on Quantitative Restrictions. This information was available to all contracting parties including members of the Committee. In his view, it was not therefore necessary to notify to the Committee, or to discuss in the Committee each and every item on an individual basis.

20. Some members of the Committee said that the notification requirements of paragraph 3 of the 1979 Declaration contained fundamental and very specific obligations for contracting parties, i.e. to notify promptly to the GATT the introduction or intensification of all restrictive import measures taken for balance-of-payments purposes. This requirement in their view was essential for the Committee to carry out its tasks, inter alia, under Article XVIII:B, paragraphs 9, 10, 11 and 12 as well as under paragraphs 1, 4, 8, 11 and 13 of the 1979 Declaration on Trade Measures Taken for Balance-of-Payments Purposes. In their view, the notifications made for other purposes were not always appropriate for the specific tasks of the Balance-of-Payments Committee and could not in any way be regarded as waiving obligations under the 1979 Declaration or other relevant GATT provisions and procedures.

21. Some other members said that the Committee's task was not to carry out a detailed line-by-line discussion of individual restrictions. One member, recalling the provisions of paragraph 3 of the 1979 Declaration, said that Pakistan appeared to interpret "measures taken for balance-of-payments purposes" as policy measures, without giving emphasis to product coverage. He thought that the product coverage would also be important for the Committee to conduct its analysis. It was clear to him that the Pakistan authorities had not prepared themselves at this stage for such an examination: he wondered whether a future occasion could be set at the convenience of Pakistan for such a discussion. Another member said that as far as quantitative restrictions were concerned, contracting parties provided GATT regularly with information on these measures to the Technical Group on Quantitative Restrictions. He wondered whether this information would serve the Committee's purposes. Another member said that in her view, the major task of the Committee was to assess whether the balance-of-payments difficulties of a consulting country justify the application of restrictions for balance-of-payments reasons. Her delegation did not think that an item-by-item examination was the task of this Committee. Duplication of notifications should also be avoided. Another said that he agreed that the main purpose of the review should be to judge whether the balance-of-payments position of a consulting country justified its access to the provisions of Article XVIII. Such situations occurred and thus measures which would normally be contrary to the General Agreement were permitted. The Committee should not examine every restriction on every product; in practice it would be extremely difficult to come to an agreed judgement on the justification for each restriction. Concerning information, he suggested that other appropriate GATT notification procedures such as those of the Technical Group on Quantitative Restrictions could be used by members of the Committee.

22. The representative of Pakistan said that the debate in which a large number of delegations had participated clearly showed that there were genuine differences of opinion in the interpretation of various GATT

provisions and procedures. These differences, he said, needed to be recognized.

Aspects relating to Paragraph 12 of the 1979 Declaration

23. The representative of Pakistan, calling attention to the preamble and Paragraph 12 of the 1979 Declaration, stressed two major constraints on Pakistan's exports. First and foremost were trade distortions in world markets caused by subsidization of cotton and rice by major producers. Secondly were the increasing restrictions imposed on Pakistan's textile and clothing exports under the MFA. Cotton was one of Pakistan's major exports. Prices had tended to fall steadily over the years. Subsidization by a major producer had played a major rôle in depressing these prices. Similarly, subsidization had been intensified on world markets for rice, Pakistan's second export, in recent years: the practices of developed countries had again depressed prices for Pakistan's exports. He cited figures illustrating the impact of subsidization in depressing the prices of cotton and rice. With regard to cotton, official figures of one major producer showed government expenditure averaging $639 million per year during 1980-84, rising to $1.6 billion in 1985 and to $2.1 billion in 1986. For 1987 and 1988 they were projected to be $1.4 billion and $740 million respectively. He noted that the World Bank annual report for 1987 attributed the 20 per cent reduction in cotton prices in that year to those subsidies. Pakistan had seen the export price for its cotton decline in direct correlation to them, falling from $1.35 per kg. in 1983-84 to $1.06 in 1984-85, $0.80 in 1985-86, and $0.70 in 1986-87. Intensified subsidization practices were also responsible for driving down world prices for rice: over the period 1984-87, the export price of Pakistan's rice had fallen steadily from $334 per ton to $236 per ton, while annual subsidies by the two major producers rose respectively from $664 million to $1,062 million, and from ECUs 47.8 million to ECUs 103 million. These measures by developed countries had produced and continued to produce serious adverse implications for the economy of Pakistan. They were clearly counter to the preamble of the 1979 Declaration. In MFA textiles and clothing, which constituted major exports from Pakistan, restrictions were maintained under the MFA by the United States, Canada, EC, Finland, Sweden and Norway. The continued intensification of these restrictions had given rise to serious adverse implications for Pakistan's balance of payments, economy and growth. He hoped the Committee could make an immediate recommendation which could help to alleviate Pakistan's balance-of-payments problems.

24. A number of members strongly supported the statements made by Pakistan. It was clear that Pakistan's economy was seriously affected by external developments. They expressed concern on the constraints facing exports and agreed with the need to make strong recommendations concerning the removal of distortions and improved access to markets for products of major interest to Pakistan.

25. Some members pointed out that the IMF had identified the positive contribution of export earnings to Pakistan's balance of payments, due to sustained export growth. This growth was to a large extent made possible by the openness of their respective markets, thereby making an important positive contribution to Pakistan's balance of payments. Some others

expressed their sympathy with the problems presented by Pakistan's narrow export base, but said that Pakistan's primary need was to seek greater diversification into exports which would find ready markets. One member noted that Pakistan's exports to the markets which he represented had increased considerably. While his markets maintained some subsidies on exports of rice, the small quantity involved was unlikely to affect world market prices; moreover, specific import reliefs for rice from Pakistan had already been introduced. Textile export growth from Pakistan to his markets had been around 250 per cent between 1985 and 1987 in dollar terms, from US$266 million to over US$600 million. This could not be said to have had an adverse effect on the Pakistan's economy; rather the reverse. Another member recalled that his delegation had in the Uruguay Round proposed the elimination of agricultural subsidies; although this had not met with a particularly favourable response from some contracting parties, there was now a mechanism for dealing with this widespread problem in the Uruguay Round. His country's MFA agreement with Pakistan was a balanced package which in many respects exceeded MFA standards. Imports of textiles and clothing from Pakistan had grown by 27 per cent in volume between 1987-88; Pakistan was the ninth largest supplier to his market. He agreed with the need for Pakistan to diversify out of its heavy reliance on products with high price volatility. A third member noted that imports of clothing from Pakistan into his market had increased by 398 per cent in value terms in the period 1984-88. Moreover, clothing imports from Pakistan rose considerably faster than total imports of the same products in 1987 and 1988. Pakistan was the ninth largest supplier of clothing. Imports of textiles from Pakistan rose five-fold over the period 1984-88. No restraints were imposed on raw cotton or cotton yarn which formed some 25 per cent of Pakistan's exports to his market. Pakistan had used the flexibility provisions available under its bilateral agreement and his government had responded positively to requests for special flexibility. He also stressed the importance for Pakistan to expand its export base and emphasized the importance of efforts to liberalize trade in the Uruguay Round context.

26. The representative of Pakistan thanked delegations for their understanding of the problems and the adverse implications in the areas referred to by him. He said that the practices mentioned in the 1979 Declaration covered not only border measures but also other trade measures such as subsidization of production and exports. Pakistan's external problems were mainly due to such factors, which constrained the possibilities of increased investment and diversification. He expressed concern on the intensification of restrictions in cotton-based textiles where Pakistan had a natural comparative advantage: he emphasized that whenever industry diversified within this area, new restrictions were introduced, thus adversely affecting diversification efforts. For example, in the new MFA agreement with the United States, the coverage of the agreement was extended from cotton to man-made fibres and new areas; the number of specific limits was substantially increased to 25; for two fabric categories where Pakistan was the most competitive supplier, growth rates were reduced to 5 per cent, affecting the small-scale weaving sector very seriously. For one other category the base level was reduced by 50 per cent. Liberalization of some textile items undertaken in the EC market had been counteracted by five new restrictions introduced in 1987. The representative of Pakistan said that the figures relating to growth in

Pakistan's exports as mentioned by some delegations in paragraph 23 were not relevant for the purposes of paragraph 12 of the 1979 Declaration, which owed its origin to the recognition in the preamble of the Declaration that the impact of trade measures taken by developed countries on the economies of developing countries can be serious. He again emphasized that the 1979 Declaration required the Committee to recognize the problems posed for consulting developing countries by external factors and to make recommendations concerning measures which might be taken to alleviate them, and urged the Committee to make a strong recommendation to the CONTRACTING PARTIES in this connection.

Conclusions

27. The Committee recognized that Pakistan continued to face serious balance-of-payments difficulties which warranted the invocation of Article XVIII:B. It also recognized that in the period under review, and particularly since 1987, Pakistan had taken major steps in adjusting imbalances in its economy, reducing import restrictions and rationalizing its tariff structure. The Committee welcomed the statements by Pakistan and the IMF concerning the Pakistan authorities' policy of continuing the process in the medium term. It took note of the justifications mentioned by Pakistan for the maintenance of remaining import restrictions.

28. The Committee noted that Pakistan would notify to GATT, by 1 November 1989, an updated list of the import restrictions maintained by it for balance-of-payments purposes.

29. With respect to import prohibitions, the Committee recalled the provisions of Article XVIII:10 relating to minimum commercial quantities of imports, while also noting the provisions of paragraph 1 of the 1979 Declaration.

30. The Committee noted that Pakistan's exports remained highly concentrated in the three sectors of rice, cotton, and textiles and clothing. It observed that this high concentration made Pakistan's trade, growth and investment possibilities particularly vulnerable to external distortions and restrictions. The Committee invited Pakistan to seek greater diversification of export products and markets, while, at the same time, recognizing the short-term difficulties involved. The Committee noted that, for the longer term, the current negotiations in the Uruguay Round offered a significant opportunity for alleviating distortions and constraints in external markets. Pending that, and bearing in mind the provisions of the preamble and paragraph 12 of the 1979 Declaration on Trade Measures Taken for Balance-of-Payments Purposes, and taking into account the particular structure of Pakistan's exports, the Committee recommended contracting parties to give particular attention to the possibilities of alleviating and correcting the balance-of-payments problems of Pakistan through measures which they might take to facilitate an expansion of Pakistan's export earnings.

ANNEX I

Opening Statement by Pakistan

The full consultations with Pakistan under Article XVIII:12 are being undertaken almost after a decade. However, as simplified consultations have been undertaken regularly on almost an alternative year basis, the Balance-of-Payments Committee is familiar with and appreciative of the developments in Pakistan's external sector. It may be recalled that during the last balance-of-payments consultations held in 1987, the Committee had noted with appreciation the steps taken by Pakistan to reduce import barriers despite a difficult balance-of-payments position. We are grateful for the understanding shown by the Committee and are looking forward to similar useful discussions in this meeting.

We welcome this opportunity to explain Pakistan's external economic situation. The background paper provided by Pakistan and circulated as GATT document BOP/288 provides a detailed exposition of Pakistan's balance-of-payments position as well as its import system. I may also draw attention to GATT secretariat document BOP/W/124, which details the general evolution of Pakistan's trade and economic situation. I should clarify that figures presented in the documents may vary a bit, depending on the source and/or definitions used. But they do not materially alter either the content or the character of the data. As these documents outline the developments during the past decade, my statement will concentrate more on the current problems and perspective. I would, therefore, like to give only an overview of the developments in Pakistan's balance-of-payments, its salient features, the external constraints and the manner in which the Government has persisted in its efforts to liberalize the import régime - notwithstanding the restrictions and constraints to which I shall refer in some detail later on.

It may be recalled that the 1987 consultations were held at a time when Pakistan was under severe balance-of-payments pressures. The current account in 1976-77 was in deficit of some $890 million. It had been reduced to that level from $1,082 million in 1974-75 which in itself was the consequence of the oil price shock - and had reached that level from a mere $481 million only a year ago, i.e. in 1973-74: a phenomenon experienced by most oil importing countries. In 1977-78, we were able to reduce the current account deficit to $605 million. Then came the second oil shock which caused a major upheaval in our external economic situation. The trade deficit increased to $2,172 million in 1978-79, and to $2,516 million a year later.

Faced with an external shock of this magnitude, the Government of Pakistan undertook a far-reaching programme of adjustment aimed at re-orientating public investment towards priority sectors of agriculture, irrigation, energy, rural development and social services. Simultaneously, a major step was taken to correct the exchange rate disequilibrium. The Rupee was unpegged from the US dollar, and a managed floating rate system was introduced in January 1982.

The cumulative effect of the various measures adopted by the Government helped reduce the current account deficit to 1.8 per cent of GNP in 1982-83 from 3.2 per cent in 1980-81 and 4.9 per cent in 1981-82. Unfortunately, the improvement was short-lived as the position of the current account again weakened in 1983-84 and deteriorated still further to 5 per cent of GNP in 1984-85. The major factors underlying this deterioration were a severe drought in Pakistan which resulted in lower exports of our main agricultural commodities, namely, rice and cotton. The situation was exacerbated by a slackening of the economic activity in the Middle East resulting in a decline in Pakistani emigrant workers' remittances. I should mention here that these remittances which stood at $2,886 million in 1982-83 (and were more than the earnings from merchandise exports) declined to $2,737 million in 1984-85 and to $2,446 million in 1985-86.

In 1985-86 the current account deficit improved to a deficit of 3.5 per cent of GNP, followed by a further improvement to 2 per cent of GNP in 1986-87. This had been made possible by a strong improvement in exports, which grew at the rate of 20 per cent a year, though this improvement was partly counter-balanced by a further drop in remittances from abroad. Exports continued their strong performance in 1987-88, but the current account again worsened to 4.1 per cent of GNP. This deterioration resulted under the combined impact of a large increase of some 18 per cent in imports and a further decline of 12 per cent in remittances from workers overseas which amounted to only $2,015 million as compared to an average of some $2,800 million in 1982-83 to 1983-84.

In the current financial year 1988-89, the balance of payments has come under renewed pressure. The current account deficit is expected to increase to $1.9 billion as against the projection of $1.25 billion. The current account deficit to GNP ratio instead of improving is expected to decline from 4.1 per cent in 1987-88 to 4.3 per cent in 1988-89. This deterioration is mainly on account of surge in imports, and relatively slower growth in exports as also stagnation in workers remittances. During the first nine months of the year (i.e. July to March 1988-89) exports have increased only by 2 per cent as against projection of 14 per cent for the year and imports have risen by 14 per cent as against 6 per cent projected for the year. Mainly exogenous factors have contributed to this situation. Prices of major exports have declined while those of imports have increased. Consequently, the terms of trade have deteriorated and trade gap widened. All this is happening when the economy is maintaining a positive growth despite damages due to floods and disturbances during the current year. The growth in GDP in the current year is expected at 5.2 per cent as against over 6 per cent in previous year.

I have gone at some length in explaining the balance-of-payments situation: this only to stress the protracted nature of Pakistan's external account difficulties.

As would have been noticed by members of the Committee from our background document in BOP/288 as well as the one circulated by the GATT secretariat as BOP/W/124, the major reasons for our difficulties are a

large imbalance between exports and imports. Export earnings continue to rely heavily on agricultural commodities which are prone to adverse climatic conditions and international factors. (In relation to the causes of the adverse international factors, I shall revert later in my statement.) In addition, a large proportion of our manufactured exports consisting of cotton-based products remain constrained by restrictions in our major export markets. Finally, remittances from Pakistani workers abroad have witnessed a consistent decline due largely to the slow down in economic activity in the oil-exporting countries of the Middle East. All these factors are beyond the control of Pakistan.

Like with other developing countries going through the process of rapid economic development, Pakistan also has a substantial external debt to service. As indicated in our background submission, Pakistan's long-term external debt stood at $12.6 billion at the end of June 1988 and amounted to some 30 per cent of the GNP. As a ratio of current account receipts the debt service payments increased from 20 per cent in 1982 to 30.4 per cent in 1987-88.

Notwithstanding its balance-of-payments difficulties, Pakistan has persisted in its efforts to simplify and liberalize the import régime. In July 1983, Pakistan administered a fresh and substantial dose of liberalization in the Import Policy. A major reform was undertaken to shift from the so-called "positive" list of imports to a "negative" list system. The liberalization efforts undertaken since 1983-84, (although the process has been on since well before then) have been summarized in our background documentation as well as in that prepared by the GATT secretariat. The impact of our import liberalization measures may be appreciated by comparing the import values as shown in the two statements at pages 12 and 13 of our document BOP/288. The non-oil imports have increased from $3,873 million in 1981-82 to $5,347 million in 1987-88. The total import bill, including petroleum imports, stood at $6,328 million in 1987-88 although Pakistan has attained a self-sufficiency ratio in crude oil of some 35 per cent in 1987-88 compared with 13 per cent in 1983-84.

The persistent balance-of-payments deficits, a large trade imbalance, the cumulation of debt service liability from past obligations combined with the protectionist international economic environment are likely to continue and present themselves as a difficult situation for a prudent management of our external economic sector. The recent subsidy war in agricultural products and the rebounding of oil prices add to our difficulties, severely constraining our import capacity. While we expect to continue with a liberal trend in our import system, the difficulties remain real and veritable.

The Government of Pakistan is not unaware of the need to undertake corrective actions particularly in the areas of export diversifications, as well as in its fiscal and monetary policies. Fortunately we have had relatively moderate rates of inflation during most of the decade. But, as the process of development continues, a prudent management of the fiscal situation would be a necessary component of our economic management. Alive

to that objective, extensive studies are being carried out by the Government to gradually shift from import restrictions to tariffs, to improve collection and broaden the tax base and to reorient spending towards production. The last two years have witnessed far-reaching reforms in these areas.

The principle objective of the fiscal reforms has been to simplify the tax structure, move to a régime of lower tax rates, improve collection and broaden the tax base: in short to foster a stable and predictable tax policy environment and a much greater emphasis on the sue of fiscal policy instruments as compared to physical controls of imports. Changes in the productive sectors are constantly being made with an emphasis on simplifying procedures and removing bottlenecks to capacity expansion as well as balancing and modernization. The private sector is being encouraged to play a greater rôle in the economic sphere.

It would be seen that Pakistan has been progressively relaxing its balance-of-payments restrictions without waiting for improvement in its external financial position. Alternative corrective mechanisms designed to raise productivity and export capacity are being devised and related macro-economic policies, particularly in the area of fiscal management, are being developed and put in place.

As indicated earlier in my statement I would now like to revert to some of the major constraints affecting Pakistan's exports which would require particular attention by this Committee. I should draw the attention of the members to paragraph 12 of the 1979 Declaration on Trade Measures Taken for Balance-of-Payments Purposes which derives its origin from the recognition in the preamble of the Declaration that "the impact of trade measures taken by developed countries on the economies of the developing countries can be serious" and accordingly requires the Committee to give particular attention to the possibilities for alleviating and correcting the balance-of-payments problems that CONTRACTING PARTIES might take to facilitate an expansion of the export earnings of a less developed contracting party.

At the time of the 1987 consultations under simplified procedures, we requested that in preparing its background paper, the secretariat may give particular attention to the constraints facing Pakistan's exports. We had hoped that with its expertise and analytical capacity, it will be possible for the secretariat to assess the cumulative affects on Pakistan's export and investment possibilities of the agricultural subsidy practices and support programmes of the developed countries particularly in the fields of cotton and rice. Similarly, we pointed out to the adverse effects that restrictions under the MFA have on our textiles and clothing exports. We appreciate the secretariat's general exposition of the impact of these measures and restrictions in paragraphs 19, 20 and 21 of its background paper.

To supplement this, I would take the liberty of asking the secretariat to circulate a couple of tables that we have prepared to show the magnitude of the impact that these measures have had on depressing the prices of our

main agricultural exports. A separate statement should suffice to offer a glimpse of the intensification of restrictions in one of our major export markets.

Mr. Chairman, it is hardly necessary for me to say that these factors have caused, and continue to cause, a substantial loss to our exports. We would urge the Committee to recommend the CONTRACTING PARTIES to take effective steps to facilitate the expansion of our export earnings. This will help us to continue to pursue the import liberalization policies and programme with confidence and thus contribute to the growth of trade.

ANNEX II

Pakistan - Statement by the Representative of the International Monetary Fund

I am pleased to have the opportunity to discuss with you recent developments in Pakistan's balance of payments and trade régime. I shall start by describing economic developments prior to the implementation of a comprehensive program of economic reforms beginning in July 1988, which is supported by a Fund stand-by arrangement and structural adjustment facility.

Over the period 1980/81-1986/87 (fiscal years begin July 1), real GDP growth averaged more than 7 per cent a year on the strength of sustained growth in the manufacturing sector and, except in 1983/84 and 1986/87, generally good performance in the agricultural sector. The strong rate of economic growth was facilitated by the implementation of a number of structural measures, many of them during the period of the extended Fund facility arrangement in the early eighties. In particular, active producer pricing policies and deregulation of the pricing and trading of important commodities contributed to major output gains in the agricultural and energy sectors.

Inflation was generally moderate over the period 1980/81-1986/87, with the annual increase in consumer prices declining from an average rate of 9 per cent over 1980/81-1984/85 to less than 5 per cent over 1985/86-1986/87. The performance of the external current account was mixed, however, reflecting protracted structural weaknesses including a narrow export base and heavy dependence on workers' remittances. Following a substantial reduction to under 2 per cent of GNP in 1982/83, the deficit widened to 5 per cent of GNP in 1984/85 when a major drought affected cotton and rice exports at the same time as there was a sharp decline in workers' remittances. The external current account position improved over the subsequent two years, mainly as a result of buoyant exports and substantially lower world prices for major commodity imports. Thus the deficit was reduced to under 2 per cent of GNP in 1986/87.

Reflecting the wide fluctuations in the external current account, the overall balance of payments position remained weak over the period 1980/81-1986/87, and the levels of gross official reserves ranged between only three and seven weeks of imports. Moreover, beginning in 1985/86, the authorities experienced increasing difficulties in external reserve and debt management. In particular, to maintain gross official reserves at manageable levels, they had recourse to heavy short-term commercial borrowing. As a result of this as well as higher medium- and long-term borrowing on nonconcessional terms, Pakistan's external debt service ratio rose from around 23 per cent in 1984/85 to 31 per cent in 1986/87.

In 1987/88 the expansionary stance of fiscal and monetary policies resulted in a strong acceleration of total domestic demand and price inflation and a sharp deterioration of the external current account. With

total absorption increasing more rapidly than output, and workers' remittances declining further, the ratio of the external current account deficit to GNP more than doubled to 4 per cent, from its level in 1986/87. This deterioration resulted mainly from a 19 per cent increase in imports, higher interest payments on the foreign debt, and a further decline in workers' remittances. This more than offset an increase of 24 per cent in the dollar value of exports reflecting sustained foreign demand in 1987/88 and a further depreciation of some 7 per cent in the real effective exchange rate. Despite increased net inflows of foreign aid and further large recourse to short-term commercial borrowing, gross official reserves were again drawn down. By the end of June 1988 official reserves declined to only about three weeks of imports.

In recent years, the authorities have maintained a flexible exchange rate policy with the aim of enhancing the competitiveness of the tradable goods sector. Some steps were also taken in the area of trade liberalization. In 1983 the import régime was changed to a negative list system, in which all items not specifically banned or restricted were freely importable. Overall, however, the import régime remained restrictive and complex and involved a significant antiexport bias. As I will note later, however, major measures to liberalize the trade system have been undertaken since 1987 and further measures are anticipated.

Pakistan has also encountered growing protectionism in foreign markets, particularly in the area of textiles. A number of countries, including member countries of the European Community, Japan, and the United States impose quantitative restrictions on certain categories of imports from Pakistan. In 1987 the European Community tightened restrictions on textiles. As a result there were four consultations between Pakistan and European countries. The restrictions on Pakistan's exports to the United States have become increasingly complicated. A bilateral agreement between Pakistan and the United States was signed in 1986. It covers synthetic textiles as well as cotton, and makes extensive use of discretionary minimum consultation levels for man-made fibers. An additional problem in 1988 disrupted Pakistan's exports to the United States. U.S. estimates of transshipment of Pakistan's textiles to the United States via other countries during the period 1985-87 were deducted from the 1988 quota. As a result the quota for that year was exhausted by September. Pakistan also faces limits on its exports of leather products to Japan.

Rice exports to the European Community face a sharp escalation of tariffs paid on unhusked and husked rice, which deters Pakistan producers from obtaining the additional value added from processing rice. More generally, distortions in world agricultural markets due mainly to policies pursued by major industrial countries create considerable instability and uncertainty for producers of rice and cotton.

These impediments to Pakistan's exports have had the effect of discouraging investment in the affected sectors of the economy and thus could adversely affect the prospects for economic growth.

I would like now to describe the adjustment program which the government has adopted in order to address the major macroeconomic imbalances and structural problems of the economy. This program is designed to sustain strong economic growth while ensuring domestic and external financial stability. In December 1988, in support of the Government's program, the Executive Board of the Fund approved a 15-month stand-by arrangement for an amount of SDR 273 million, and the first annual arrangement under the Structural Adjustment Facility (SAF) of SDR 109 million. Over the three years of the SAF the cumulative resources which will be available to Pakistan are currently projected to amount to about SDR 347 million.

In the external sector, the program aims at reducing the current account deficit to a sustainable level while substantially increasing the level of gross official reserves. It involves a comprehensive package of measures that are being implemented over a period of three fiscal years beginning in July 1988. The program concentrates on several key policy areas that are critical to the achievement of the macroeconomic objectives; it also initiates wide-ranging reforms in other sectors that will be important in improving the efficiency and growth potential of the economy in the period after 1990/91. The priority structural reform measures to be achieved by 1990/91 include major fiscal reforms to broaden the tax base; a comprehensive program of trade liberalization including the gradual replacement of non-tariff barriers by tariffs, and external tariff reform; and deregulation of important costs and prices throughout the economy.

In the real sector, the Government is committed to implementing measures to expand both public and private fixed capital formation and to accelerating progress in reallocating its development outlays toward priority areas. The Government is also committed to renewing its efforts toward reducing cost and price distortions. Such efforts - in conjunction with continued flexible exchange-rate management - are expected to provide incentives to efficient domestic producers and exporters in agriculture and industry. These measures also aim at reinforcing the objective of sustaining real growth, with increased reliance on the private sector to carry the growth momentum of the economy and improved export performance.

In the area of public finance, the Government has started to implement measures to ensure a reduction in the overall fiscal deficit to 6.5 per cent of GDP in fiscal year 1988/89 (compared with an estimated average ratio of about 8.1 per cent in the last two fiscal years), with further progress in later years.

The Government has recognized that cautious domestic credit policies are needed to avoid inflationary pressures and achieve the targeted improvements in external sector performance. The Government has embarked on reform of the financial sector supported by a loan from the World Bank, which aims at improving the efficiency of the financial system, and mobilizing domestic savings.

The Government's objectives in the external sector are to achieve a viable overall balance of payments position - defined as an external current account deficit that can be financed largely by net aid

disbursements while maintaining adequate reserves - and to significantly reduce restrictions on trade and payments. To this end, the program envisages a substantial reduction of the external current account deficit to a sustainable level by 1990/91, from nearly 4 per cent in 1987/88. In addition, the program aims at rebuilding gross official reserves to seven weeks of imports by end-June 1991. The program also envisages a substantial strengthening of the structure of the current account and of the debt service profile. In particular, the Government aims at diversifying the export base, thereby reducing reliance on workers' remittances and rice and cotton-based exports. A continuation of the flexible exchange rate policy pursued in recent years will also be essential to achieving the Government's external sector goals, particularly in the context of the intended trade liberalization, and the urgent need to strengthen the external reserves position.

The Government has undertaken a comprehensive trade policy reform. With the "New Trade Policy" of June 1987, measures for export promotion were instituted to help move exporters to free trade status in production. The trade reform, which is viewed as one of the major policy instruments in Pakistan's structural adjustment effort, is expected to continue to enhance the incentives framework for exports. It also involves a comprehensive import policy reform in order to reduce the level and dispersion of protection according to different activities.

Further liberalization of the export system is being implemented during 1988/89-1990/91. On July 1, 1988, in the context of the 1988/89 Export Policy Order, the Government removed a few items from the list of essential commodities that are presently exportable only through public sector agencies. Private sector participation in cotton and rice exports has also been further liberalized.

The Government is implementing a major import policy reform over the three years 1988/89-1990/91. As of July 1, 1988, with the 1988/89 budget and Import Policy Order (IPO), a significant number of existing non-tariff barriers were replaced by tariffs, the maximum tariff rate levied on imports (other than large automobiles and alcoholic beverages) was reduced from 150 per cent to 125 per cent and the first phase of the rationalization of the tariff structure was implemented. Over the rest of the three-year program the Government is committed to further liberalization and rationalization of the tariff system. The average level and dispersion of tariff rates will be reduced.

With the 1988/89 Import Policy Order, the Government has also begun to implement a program of significant liberalization of the import régime. A total of 162 categories of commodities were removed from the negative list and 51 categories were dropped from the restrictive lists. A number of changes have been made in the presentation of the restricted lists to improve the transparency of the trade régime. In addition, the licensing system has been simplified and liberalized by a 20 per cent increase in all value ceilings on imports of machinery and millwork against cash licenses, and by a doubling of the ceiling on imports by actual users. The Government has made specific commitments to further liberalization over the programme period.

The Fund believes that the program to which the authorities have committed themselves for the next several years is properly set in the medium-term framework. It includes measures of a structural nature which will address adequately the long-standing weaknesses of the economy. It also places emphasis on demand restraint that will help to contain the rate of price inflation and improve the balance of payments. A significant reduction in impediments to Pakistan's exports to the major foreign markets and a continuation of external financial assistance on concessional terms would considerably assist Pakistan in the implementation of this program.

Unfavourable developments in 1988/89 largely beyond the control of the authorities may impede the attainment of the external objectives of the Government's program. Floods in late September and early October 1988 have reduced the scope for exporting both raw cotton and rice, and have necessitated some additional imports to compensate for the destruction of food crops. In addition, the prices of some of Pakistan's exports (notably cotton and textiles) have weakened compared to the program assumptions. At the same time, there are some signs that the domestic rate of inflation may be higher than had been assumed in the program. Thus if the objectives of the program are to be achieved, the Fund believes that the authorities will need to adhere strictly to the implementation of the programmed policies.