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THE EUROPEAN COMMUNITY AND PAKISTAN

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INTRODUCTION

In the 10 years since Pakistan and the European Community signed a commercial cooperation agreement on 1 June 1976, their relationship has developed in a steady if unspectacular fashion. Trade remains its cornerstone, of course. The EC is Pakistan's main trading partner. Some 20% of its foreign trade is with the Community, as against roughly 11% with the United States and around 12% with Japan. Pakistan's exports to the EC amounted to ECU 892m. in 1985, its imports to ECU 1,603m.

Pakistan is an important beneficiary of the EC's trade promotion programme for South Asia. In the framework of this programme the EC has undertaken to help it develop its exports of such items as leather, light engineering goods and jewellery. It has also organized seminars to help Pakistani exporters take greater advantage of the Community's generalized system of preferences, under which manufactured products and a wide range of agricultural products enter the EC either duty-free or at reduced rates.

Pakistan is a beneficiary of the Community's development aid programme for developing countries in Asia and Latin America and is receiving project aid and direct food aid (mainly skimmed milk powder and butteroil since deliveries of cereals stopped in 1981). Project aid is being used to finance a number of projects. New areas of cooperation include science and technology and energy.⁽¹⁾

This expanding relationship is reflected in the new EC/Pakistan commercial, economic and development cooperation agreement, which was put into force on 1 May 1986. In the Preamble to the Agreement the two sides call for "closer cooperation across the whole range of commercial and economic endeavour. Cooperation in the trade field is reinforced and extended to take in economic and development cooperation. In this context the Community and Pakistan undertake to encourage industrial cooperation and the transfer of technology between their economic operators and to promote scientific and technological cooperation. Provision is also made for development cooperation, with the EC undertaking to intensify its support for Pakistan's development programmes.

Such, in brief, is the development of EC/Pakistan relations over the last 10 years or so. The rest of this Information Note is devoted to filling in the picture sketched here in broad outline.

⁽¹⁾ The EC's development aid is in addition, of course, to that provided bilaterally by individual member states.

PAKISTAN - AN ECONOMIC PROFILE

Land area: 804,000 sq. km. (roughly that of France and the Federal Republic of Germany put together).

Population: 96.2 million (mid-1985)

Density: 120 inhabitants per sq. km.

Gross National Product: Total - US \$33,490 million (in 1984/85)

Per capita - US \$ 350 (1984)

Annual rate of growth (% - constant prices)

<u>1975/76</u>	<u>1983/84</u>	<u>1984/85</u>
7.1	4.2	7.8

Labour force:

	<u>Million</u>	<u>%</u>
Agriculture	14.1	51
Industry	5.2	19
Services	8.3	30
TOTAL	<u>27.6</u>	<u>100</u>

Indices of Manufacturing Output

1975/76 - 100

	<u>1979/80</u>	<u>1983/84</u>	<u>1984/85</u>
Total manufacturing	133	200	217
Selected items			
Vegetable products	168	225	240
Cotton yarn	104	123	136
Cotton cloth	66	57	54
Fertilizers	136	354	367
Cement	105	141	145
Mild steel products	182	284	317

External trade (goods)
(US \$ million)

	<u>1980/81</u>	<u>1983/84</u>	<u>1984/85</u>
EXPORTS	3,461	3,439	3,241
IMPORTS	6,466	7,058	7,028
BALANCE	- 3,005	- 3,619	- 3,787

Principal exports (%)

	<u>1983</u>	<u>1984</u>
Textile yarn, fabrics	43	39
Rice	14	13
Cotton	10	6
Clothing	7	9

External Public Debt
(outstanding and disbursed)

	<u>1970</u>	<u>1984</u>
US \$ million	3,060	9,953
As percentage of GNP	30.5	29.6
Interest payments (US \$ million)	76	314

RECENT DEVELOPMENTS IN PAKISTAN

Economic: Pakistan's economy was hard hit by the second oil shock in 1979, in that oil imports accounted for as much as 30% of total imports by 1983/84 (as against 16% in 1978/79). But rising incomes in the Middle East meant not only increased Pakistani exports to these markets but also increased remittances from Pakistanis working in the Middle East and Gulf States. Thus, despite higher oil prices Pakistan was able to maintain the level of imports.

The unexpected setback in agriculture in 1983/84 had adverse effects on the country's cotton and textile exports. Workers' remittances fell also. There was a sharp recovery in 1984/85, however, largely because of the recovery in the agricultural sector. But growth in manufacturing industry continued to be adversely effected by cotton and energy shortages.

The following Table shows the composition of Pakistan's imports in recent years:

Composition of Imports
(US \$ million)

	<u>1979/80</u>	<u>1983/84</u>	<u>1984/85</u>	<u>Average growth %</u>
-Merchandise	4,850	5,997	5,937	4.1
-Consumer goods	754	796	947	4.7
-Capital goods	1,685	1,809	1,901	2.5
-Raw materials	2,298	3,081	3,061	5.9
-Merchandise, excluding oil	3,965	4,717	4,671	3.3

To ensure sustained economic growth with better income distribution, Pakistan will have to strengthen the process of structural adjustment begun during the late 1970s. There is an urgent need to reform trade policy in a direction conducive to high export growth, especially in manufactures; increase public investment in the country's economic and social infrastructure; improve domestic resource mobilisation and remove controls as far as possible to ensure higher levels of private investment and productivity.

Significantly, in his first address to the nation on 31 December 1985 the Prime Minister, Mohammed Khan Junejo, announced a number of policy measures. Among them were measures to increase growth in agriculture and industry; speed up rural development; raise investment in education; develop energy resources, through the exploitation of coal and a peaceful nuclear programme, and to promote a greater role for science and technology.

Political: 1985 was a crucial year for Pakistan, for it was marked by the transition from military to civilian rule. The first general elections since 1977 were held on February 25, on a non-party basis.

Martial law was lifted on 30 December 1985. The Constitution of 1973 was restored and the 20-year old state of emergency ended. The Prime Minister announced a 5-point manifesto. It provides, among other things, for the establishment of a strong Islamic democratic order; the promotion of an equitable economic system; the elimination of illiteracy; a fight against bribery, corruption and injustice and the consolidation of national integrity through the establishment of a strong national defense and a balanced foreign policy.

EC/PAKISTAN RELATIONS
The first commercial cooperation agreement

Trade has always been central to EC/Pakistan relations. In establishing diplomatic relations with the 6-nation Community in 1962, Pakistan was concerned mainly with safeguarding its exports to the U.K., then engaged in the first entry negotiations. When these were broken off in 1963 Pakistan, like India, sounded out the Community with a view to entering into a comprehensive trade agreement.

This was the solution which had been adopted during the entry negotiations for India and Pakistan, but it had now lost all relevance from the Community's point of view. It was not revived until the 1970-71 entry negotiations. But the situation had changed meanwhile. The Asian Commonwealth was less dependent now on the U.K. market for its exports. And access to the Community market for Asian exports was favoured by the Generalized System of Preference (GSP), which the Community had introduced in favour of 91 developing countries on 1 July 1971. (The Community's GSP scheme provides for duty-free entry for manufactures, and on preferential terms for a growing list of agricultural products.)

But it was politically difficult for the enlarged Community, having agreed to accommodate the developing Commonwealth outside Asia within the framework of the existing association agreement with French-speaking Africa, to refuse to enter into an agreement with India and Pakistan.

The search for a new type of agreement was therefore undertaken by the European Commission with India to begin with. Together they invented the commercial cooperation agreement (CCA), which could be seen as a development, at the bilateral level, of the multilateral generalized system of preferences. The problem of tariffs having been largely settled through the GSP, as it were, the CCA sought to provide the institutional machinery which would allow the Community to help countries like India and Pakistan, both to take full advantage of the GSP and develop new trade opportunities.

The CCA between the Community and Pakistan came into effect in 1976. A non-preferential agreement, it provided for tariff adjustments and most-favoured-nation treatment. But the CCA also set up a Joint Commission, with a mandate to:

- (1) study the means of overcoming trade barriers and
- (2) encourage cooperation between the EC and Pakistan in developing and diversifying their two-way trade.

Since it first met in 1977, the Joint Commission has promoted a wide range of activities, principally with a view to helping Pakistan increase and diversify its exports. Under the EC/Pakistan trade promotion programme the Community has helped Pakistan exporters take part in trade fairs and sales missions, organized seminars and workshops for them, and provided experts to advise them on tobacco, leather and sports goods and clothing. The emphasis has been on helping economic operators in Pakistan directly, and on putting them in touch with their European counterparts.

It is hardly surprising that the scope of a work programme of this kind should be constantly expanding. To meet the requirements of a very demanding market such as the Community market the exporter must up-grade his technology, for example. A transfer of technology can take place under a licensing agreement or in the framework of a joint venture. Industrial cooperation can facilitate both forms of transfer, paving the way in fact to economic cooperation in general.

Industrial cooperation can also stimulate other forms of cooperation, notably cooperation in science and technology - and vice-versa. As the EC has been providing development aid to Pakistan and other so-called "non-associated" countries since 1976, there has been a natural tendency to extend it from rural development to cooperation in agriculture, tropical medicine, energy, especially solar energy, protection of the environment, etc.

India was the first to feel the need for a more wide-ranging cooperation agreement, although the first such agreement was signed with ASEAN. (1). As mentioned earlier, the new commercial, economic and development cooperation agreement between the Community and Pakistan, having been approved by the Council of Ministers on 22 April 1986, came into effect on 1 May 1986.

THE COMMERCIAL, ECONOMIC AND DEVELOPMENT COOPERATION AGREEMENT

The scope of the new agreement is summed up in its title. It sets out the various ways in which commercial and economic cooperation can be encouraged. The emphasis is on increased contacts between economic operators of both sides and greater and more effective exchanges of information on trade, industry and economic matters. As regards cooperation in the fields of science and technology, energy and "other fields of common interest" (e.g. agriculture, fisheries, transport, and communications ...) the two sides agree to encourage joint programmes of research.

Under the provisions for development cooperation, the EC has undertaken "to intensify its support ... for Pakistan's development programme" by providing technical assistance, concessional aid and finance from "institutional and other sources." Equally important, perhaps, is the undertaking to "seek a coordination of the development cooperation activities of the Community and its Member States in Pakistan".

The role of the Joint Commission is obviously even more crucial to the success of the new agreement, which lists some of the activities that can be undertaken.

(1) The six members of the Association of Southeast Asian Nations are Brunei, Indonesia, Malaysia, the Philippines, Singapore and Thailand.

Thus the Joint Commission can

- (1) study and devise ways of overcoming trade barriers;
- (2) find ways of encouraging economic and commercial cooperation;
- (3) encourage information exchanges;
- (4) make recommendations on the use of Community funds, and the efficient utilization of all available instruments, to promote trade in items of interest to both sides.

The success of the new agreement depends, therefore, on the ability of the European Commission and the government in Islamabad to (1) establish an on-going exchange of views on all subjects covered by it and (2) mobilize their business, industrial and financial interests. Given the importance of the private sector in the Community, the Commission's role is that of a catalyst rather than a prime operator.

TEN YEARS OF EC/PAKISTAN TRADE (*)
Main Trends

The steady rise in the 2-way trade between the EC and Pakistan emerges clearly from the following Table:

<u>EC Trade with Pakistan, 1975 and 1982-85</u>					
(ECU million)(**)					
	<u>1975</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>
EC IMPORTS	227	541	585	672	892
EC EXPORTS	427	1,077	1,307	1,471	1,603
BALANCE	+200	+536	+722	+799	+711

The Community's imports rose by 290% and its exports by 275% over the period 1975-85. Its trade surplus rose by 300% between 1975 and 1984, when the surplus reached a peak of ECU 799m.

Changes in the composition of imports from Pakistan are shown in the following Table:

<u>EC: Main Imports from Pakistan, 1979 and 1984-85</u>					
(ECU million)					
<u>SITC</u>	<u>Brief description</u>	<u>1979</u>	<u>1984</u>	<u>1985</u>	
03	Fish, shrimps	7	15	13	
06	Sugar, sugar preparations	22	35	69	
26	Raw cotton	12	55	143	
29	Raw material, animal/ vegetable	15	21	25	
61	Leather, leather manufactures	40	97	113	
65	Yarn, cloth	166	242	280	
84	Clothing	25	97	135	
85	Footwear	6	9	12	
87	Scientific equipment	5	17	15	
89	Other manufactures	15	29	31	

(*) The following analysis is based on trade between Pakistan and the 10-nation Community - i.e. the EC prior to the entry of Spain and Portugal.

(**) The ECU (European Currency Unit) is a "basket" unit, based on a certain quantity of each Community currency, weighted on the basis of a 5-year average of the GNP and intra-Community trade of each Member State.

As Pakistan is a major producer of raw cotton, the substantial rise in its exports of textiles and clothing is not altogether surprising. But more interesting than the growth in exports of agricultural products is the rise in exports of manufactured products. Even so, the level of these exports is small in relation to Pakistan's export potential.

With the exception of some agricultural products, some of which are supplied under the EC's food aid programme, the Community's exports to Pakistan consist entirely of manufactured products, as can be seen from the following Table:

EC: Main Exports to Pakistan, 1979 and 1984-85
(ECU million)

<u>SITC</u>	<u>Brief description</u>	<u>1979</u>	<u>1984</u>	<u>1985</u>
0	Food	51	80	63
5	Chemicals	126	246	272
67	Iron and Steel	42	87	99
71	Power generating machinery	28	57	61
72	Specialized machinery	123	233	182
74	Industrial machinery	38	85	139
76	Telecommunications equipment	58	35	58
77	Electrical machinery, appliances	32	65	63
78	Road Vehicles	98	134	150
79	Other transport equipment	41	21	82
87	Scientific equipment	29	39	48

TEXTILES AND CLOTHING

Pakistan's textiles and clothing exports to the EC have been regulated by the GATT Multifibre Arrangement (MFA) and the bilateral agreements the Community and Pakistan have negotiated under it. Despite criticisms of the MFA, and the Community's implementation of it through its bilateral agreements, the fact is that Pakistan has secured a growing share of the Community market. From 1.9% in 1977 it rose steadily to 2.7% in 1983. It fell in 1984 from 2.3% but recovered the following year.

Pakistan clearly attaches considerable importance to this virtually guaranteed share of the EC market, something which has become even more important as the Community's imports from China have grown. This is reflected in Pakistan's readiness to enter into bilateral negotiations, especially in 1981, but also in 1986, although after some initial reluctance.

The following table shows Pakistan's exports to the EC of both textiles and clothing covered by the MFA:

<u>EC:Imports of MFA products from Pakistan</u>				
<u>Tonnes</u>				
	<u>1979</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>
All MFA products	35,114	44,138	39,398	53,687
Textiles	32,722	39,490	33,907	46,912
Clothing	2,392	4,648	5,491	6,775

RICE

Some 13% of Pakistan's exports in 1983 and 1984 consisted of basmati rice. This is a special variety, grown only in Pakistan and India. In an annex to both the 1976 and 1986 EC-Pakistan cooperation agreements, the EC has specifically undertaken to explore possibilities for facilitating imports of basmati rice.

Attempts to do this through the GSP having gotten nowhere, the European Commission proposed in 1986 that the variable levy be reduced by 50%. This reduced rate would apply up to an annual quantity of 15,000 tonnes. Shipments would have to be accompanied by a certificate to ensure that only genuine basmati rice from Pakistan and India benefited from the reduction.

The Commission's proposal was under discussion by the Member States at the end of June, 1986.

THE GENERALIZED SYSTEM OF PREFERENCES

Pakistan has begun to use the Community's GSP scheme more effectively in recent years. In 1984 exports eligible for GSP benefits in the EC rose by 21%, while exports which actually secured preferential entry rose by 17% (as against a rise in total exports of 15%).

But Pakistan's GSP exports remain heavily concentrated on a single sector - leather, leather goods and shoes. These items are all "sensitive" for GSP purposes. Even so, under the 1986 GSP scheme the ceiling for the six items in this sector have been increased by 18% to 33%, while Pakistan's ceiling for leather shoes has been increased by 14% and the quota on canvas shoes abolished altogether.

Carpets have also done well; in 1984 exports worth ECU 99 million entered duty-free. Pakistan now exports only the better quality carpets, on which import duties are rarely reintroduced.

In the agricultural sector, dried mushrooms benefited from the GSP in 1984, but for small amounts. Among Pakistan's exports, shrimps and prawns in fact are the only important food item eligible for GSP benefits. Exports have risen from ECU 9 million in 1982 to ECU 16 million in 1984. The GSP utilization rate is 70 to 90%, depending on the year.

With the rapid growth and diversification in Pakistan's manufacturing industry, the country is better placed to take advantage of the GSP scheme. While trade statistics show that Pakistan now exports quite a wide range of manufactured products, the quantities involved are still very small. The potential for an increase in such exports - on which tariffs are unlikely to be reintroduced in Pakistan's case - is considerable. Its exporters are now reasonably familiar with the Community's GSP scheme and could take advantage of it, therefore, to increase their share of the Community's GSP imports.

PUTTING THE NEW COOPERATION AGREEMENT TO WORK

The agreement is a framework. Put to work, it can stimulate both trade and the various forms of cooperation it envisages. This should not be too difficult, as the foundations for increased trade and cooperation have already been laid. The following sections look at what has been done.

Trade promotion

Pakistan is an important beneficiary of the EEC's trade promotion programme for South Asia, under which it has been allocated some ECU 2 million between 1983 and 1985. Light engineering, jewellery and leather are the sectors to have benefited. The Karachi Export Promotion Zone has received help with attracting European investments, and the Community is also helping Pakistan prospect the market for fruit and vegetables in the Middle East and Gulf States.

Economic Cooperation

Two projects are likely to be launched in 1986/87. Under the first, some half dozen managers, specialists in finance, would spend 3 to 6 months in either business schools or financial institutions in order to familiarize themselves with European financial and trading practices. Under the second project, a delegation of senior officials and industrialists would visit the EC to explore ways of promoting investments.

Cooperation in Science and Technology

After a slow start, two projects have been selected for 1986. Both have to do with environmental protection. Two Pakistani scientists are to spend two years at the EC's Joint research Centre at Ispra (Italy), while a British scientist is to carry out a feasibility study in Pakistan related to atmospheric pollution in large cities.

The EC has also invited research institutes and laboratories in Pakistan to take part in the Community's ECU 40 million research programme, launched in 1983. Under this programme, institutes in the EC and developing countries are invited to apply for help in funding research in medicine and tropical agriculture, to be conducted jointly by them. In the absence of any projects, the European Commission has envisaged a campaign to alert Pakistani institutes to the next such programme, to be launched in 1987.

Development Cooperation

Between 1976 and 1985 the Community has committed nearly ECU 140 million, including an estimated ECU 75 million for project aid and ECU 58 million for food aid.

Project aid has slowed down in recent years, as the Community has tried to move away from its earlier policy of co-financing with other agencies. As part of a fresh start, the European Commission approved in 1986 both a vocational training and a rural electrification project. Under the first, to be cofinanced with the World Bank's affiliate, the International Development Agency, 11 new vocational training centres will be built in North-West Pakistan. The second project relates to the electrification of 176 villages. The EC's commitment will be an estimated ECU 17 million for the first project and ECU 7 million for the second.

Food aid to Pakistan has fluctuated in the last few years between ECU one million (1983) and ECU 9 million (1981). In 1985 it was ECU 3 million. Until 1981 Community aid consisted of food grains (35,000 tonnes that year), skimmed milk powder and butter oil. Since then no food grains have been supplied as direct food aid, although small quantities of edible oil (500 tonnes) were included in 1984 and 1985.

Aid to Afghan refugees

The influx of up to 3 million Afghan refugees into Pakistan has led the European Community to provide food and, on occasion, medical aid. Between 1980 et 1985 Community aid totalled ECU 110 million and consisted mainly of cereals but included skimmed milk powder, butter oil, vegetable oils and sugar. The food aid package for 1986 includes 45,000 t. of cereals, 2,000t. of sugar and 1,000 t. of butteroil, worth ECU 12 million. The Community in fact accounts for about one-third of the food aid the Afghan refugees are receiving.

CONCLUSIONS

Although the focus of EC/Pakistan relations has always been on trade, their scope has been enlarged progressively to include economic cooperation and, with the 1986 agreement, scientific and development cooperation. This process is likely to be speeded up now, thanks to two developments: the change in the political climate in Pakistan itself and the conclusion of the new cooperation agreement. But while the agreement opens the way to a broadening, as well as deepening, of EC/Pakistan relations, this cannot come about without a firm political commitment to it by both sides.

Statistical material drawn from publications of the Statistical Office of the European Community and international agencies, notably the World Bank.

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