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WTO And India Pakistan Trade Relation

Javid Ahmad Khan[1]

1. Introduction

Bilateral trade between India and Pakistan is as old as the two countries are, but the volume of trade between them is minuscule relative to the size of their economies. Bilateral trade relations of India and Pakistan are influenced by their political relations much more than anything else. After the India Pakistan war in 1965, trade was almost negligible for a period of nine years. Bilateral trade did resume in 1975-76, following the 1974 protocol for the restoration of commercial relations on a government to government basis, signed by the two countries after the 1971 war but it remained at an insignificant level. In the year 1991-92 both countries adopted the policy of economic reforms and made attempts to increase the bilateral and multilateral trade. The trade barriers between India and Pakistan take the form of both formal and informal barriers. Formal trade barriers are comprised of, tariff barriers and non-tariff barriers. These consist of, quota restrictions; trade bans, such as the denial of MFN status. Informal barriers are defined as transaction costs and they fall into three categories namely: procedural costs; transport costs; rent seeking. In the same way that formal barriers have restricted trade, informal barriers in the shape of high transactions costs have forced much of the trade, even in commodities that are legally tradable, to flow through informal channels. Many short, medium and long term measures were taken for increasing economic and political ties between two countries. However the agreements were limited in scope and were not implemented fully. SAFTA (South Asian Free Trade Agreement) came into existence in Jan 2006, provided a framework for removing some obstacles to trade but its implementation would not dramatically improve economic integration. SAFTA calls for tariff rates within the region to be zero by 2012, but it is highly unlike that these targets will met. In terms of their global trade, both India and Pakistan have abolished quota restrictions and reduced tariff rates steadily in conformance with their obligations under the WTO. World Trade Organization (WTO), equipped with authority of enforcing the commitments, rules and norms of discipline came into existence on January 1, 1995. The new institution WTO is equipped with legal authority and provision of enforcement of rules and disciplines of the new trading system. The basic principles (of the WTO) make the system economically more efficient and cut the production and marketing costs. It gives consumers more choice, and a broader range of qualities to choose from. These are the basic benefits of world trading

[1] *Ph.D. Research Scholar M.S University Baroda*

given by the WTO (WTO 2003). A number of studies have explained implications of the WTO with reference to developed and developing countries. How much trade has been increased by nations after the implementation of the WTO remained an ambiguous estimation. The increase in trade can result into benefits of the WTO. Generally, it is taken that developing economies have taken lesser tranche of the global trading.

1.1. Review of literature

Ghuman (1986), examined Indo-Pak trade relation with respective to different items of the exports and imports, estimate the mutual gains and explore the possibility of the regional cooperation. It was opined that the strengthening of the mutual cooperation could help in big way to ease tension between two countries and both the countries could play a good role in strengthening the regional cooperation in south Asia.

IMF (2005), in an effort to study the trade liberalization and its impact conduct the study. The study found that Indians trade restrictiveness measures eight (on scale from one to ten), while Pakistan’s index stand at six.

Qamer Abid (2005), conducted a study to identify potential of trade and identify the items. A comparison of Pakistan’s exports with Indian imports indicates various potential sectors that can be explored in case trade between the two countries is liberalized.

Garey (2006), in an attempt to quantify the welfare impact of trade liberalization, based on an analysis of market conditions and trade policies in the two countries, argues that restoration of normal trade relations in textiles would likely have a small but beneficial impact on both India and Pakistan. Eliminating all barriers to intraregional textiles trade would likely induce some limited specialization and trade in intermediate inputs for use in exports of cotton textiles to high-income countries. Study suggested that abolition of Pakistan’s “positive list” system, and the restoration of trade across the land borders, would have clear economic benefits for India and Pakistan, especially in the Punjab-Faisalabad region of Pakistan and in northwest India.

Hossain (2006) was of the view that the relationships between India and Pakistan are major hindrance for the success of any regional or unilateral trade agreements and conflicts between India and Pakistan threaten the future of SAFTA in South Asia.

Naqvi and Nabi (2007), estimate that, at best, the two nations “are exploiting only a third to a tenth of the potential that exists” for bilateral trade. The opportunities for greater bilateral trade flows are immense; the authors argue that “in the most optimistic scenario” greater Pakistan- India commerce could restore pre-1947 trade patterns and benefit all of Pakistan’s provinces.

Banik, N. and John Gilbert (2008), analyzed the augment gravity model in context of the south Asia. The recommendation of the study was because of political difference (such as Kashmir issue related to India and Pakistan) member countries have refused to participate in mutually gainful situations, much less try to give any unilateral concession.

Taneja, Nisha (2008), in an effort to promote trade and economic relations between India and Pakistan focuses on identifying bilateral trade possibilities and identifying non-tariff barriers to Indo-Pak trade. The study shows that there is large untapped trade potential between the two countries of US $11.7 billion. The export potential from Pakistan to India is US $ 2.2 billion while that from India to Pakistan is to the tune of US $ 9.5 billion.

Rahpoto (2009),in an attempt to quantify and analyze the relative impact of South Asian Free Trade Agreement (SAFTA) over the global economic welfare. The simplified static analysis by using CGE model for policy implication reveals that Pakistan will gain benefit from Pak-India trade on SAFTA.

1.2. Need of the study

The establishment of the WTO itself represents the policy change in the world economy. India was the founding member of the WTO. Giving the volatile environment between India and Pakistan trade remains hidden. The need arise to study statistically the problem whether the policy implementation (WTO) has any impact on India Pakistan bilateral trade or not. The importance of the study is to highlight how for the WTO has succeed in increasing the bilateral trade of India and Pakistan.

1.3. Objectives of the study

1. To know the Indo-Pak bilateral trade relation.

2. To analyze the impact of WTO on Indo-Pak bilateral trade.

3. To suggest the measure to increase the bilateral trade.

2. Research Methodology

The present study is based on secondary data. The annual time series data are used for the entire period present work is from 1983-84 to 2008-09, which is divided into two sub periods from 1983 to 1995, before WTO and from 1995 to 2008, after WTO/ Both non -Econometric and Econometric approaches have been used. Data were collected from world economic outlook database oct.2009, IMF &

Import export data bank, ministry of commerce govt. of India and Economic surveys of two respective economies.

2.1. Non-econometric approach

In this approach calculation of the chain index, graphs and tabulation, ratios, percentages, growth rates all these techniques were used for analysis. The shares in percentage terms have been calculated.

2.2. Econometric approach

Under this approach GDP of three economies are taken as independent variables and bilateral trade flow as dependent variable. The reasons for taken these three variables are to analyze it in context of the size of three economies at large. In this way the model is restricted gravity model of the trade which supported that trade is positively related with the size of the economies and inversely with distance. Simple test of stability of parameters has worked out to know the impact statistically.

Model specification

$$Y_T = \beta_0+\beta_1 GDP_W+\beta_2 GDP_I+\beta_3 GDP_P +\mu \quad (1)$$

Where

Y_t = Bilateral trade flow of two countries

GDP_W = gross domestic product of the world

GDP_I = gross domestic product of the India

GDP_P = gross domestic product of the Pakistan

And β's are the coefficients from

$N= 26 = n_2 + n_2$

The numbers of observations are 26. We have divided the entire sample into two different periods one before WTO one after WTO. We thus obtain the two estimations of the same model for two different time periods. We want to test whether the estimated relationships differ significantly or not in that case we conclude that relationship is changing from one sample to another. We have applied the test of equality between sets of coefficients in two linear regressions to get the results.
We pooled together the two samples and thus forming the sample of $(n_1 + n_2)$

$$Y_P=\beta_0+\beta_1 GDP_W+\beta_2 GDP_I + \beta_3 GDP_P +\mu \quad (2)$$

And we have estimated the unexplained variance

$$\sum e^2_p = \sum y^2_p - \sum y'^2_p \quad (3)$$

With $(n_1 + n_2 – K)$ degree of freedom
Where p stands for pooled and K for total number of β's in our case 4. We perform the regression analysis on each sample separately
From the first sample we have

$$Y_I=\beta_0+\beta_1 GDP_W+\beta_2 GDP_I + \beta_3 GDP_P + U \quad (4)$$

And compute unexplained variance as

$$\sum e^2_i = \sum y_i - \sum y'^2_i \quad (5)$$

With (n1 – K) degree of freedom
From the second sample we obtain similarly and unexplained variance is estimated as

$$\sum e^2_2=\sum y_i-\sum y'^2_2 \quad (6)$$

With $(n_2 –K)$ degrees of freedom
We add together the unexplained variance of the two samples one before and other after WTO

$$(\sum e^2_i + \sum e^2_2) \quad (7)$$

With $(n_1 - K) + (n2 - K) = (n1 + n_2 - 2K)$ degrees of freedom

$$\sum e^2_p - (\sum e^2_{i} + \sum e^2_{2)} \tag{8}$$

With $(n_{1\,+}\, n_2 - K)$ - $(n1 + n_2 - 2K)$ degrees of freedom

$$F^* = \frac{\sum e^2_p - (\sum e^2_{i} + \sum e^2_{2)} / K}{N (\sum e^2_{i} + \sum e^2_{2)} / (n1 + n_2 - 2K)} \tag{9}$$

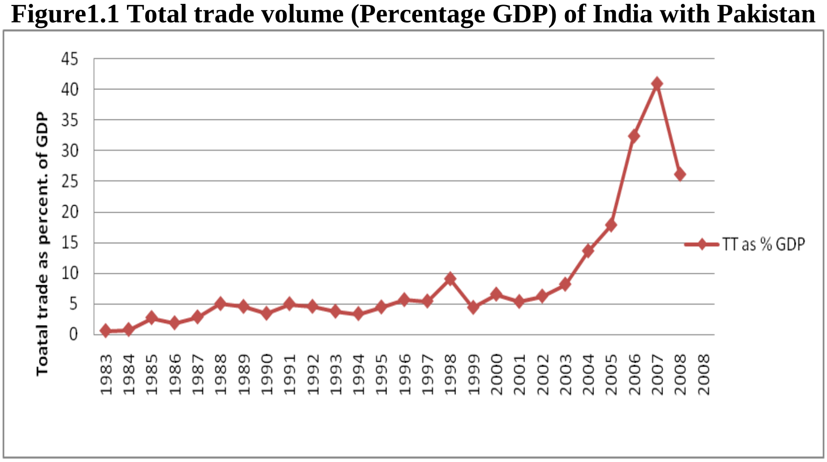
The test of equality between sets of coefficients in two linear regressions.

3. Results and discussion

3.1. Non-econometric approach results

India's total trade (export and import as a percentage of the GDP) is shown in the table 1.1. The trend of trade volume (as percentage of GDP) of India with Pakistan before and after the WTO has been shown in figure 1.1. The trade volume was low before the WTO and remains near to same trend after, till 2002, reached maximum in 2007 and again decreased from 2007.as shown in the fig 1.2 based on data from table1.1. The important point is that before the WTO maximum occurrence was trade deficit in account of India but after the WTO it remains in favors of India. The calculated chain index results are provided in the table 1.2. The chain index of trade (percentage of GDP) of India with Pakistan before the WTO was 118 and after the WTO was 80, which shows that trade, has been reduced after the WTO.The result revealed that India Pakistan bilateral trade has not obtained the advantages of trade liberalization.

Figure1.1 Total trade volume (Percentage GDP) of India with Pakistan



Source: Based on the figures in table 1.1

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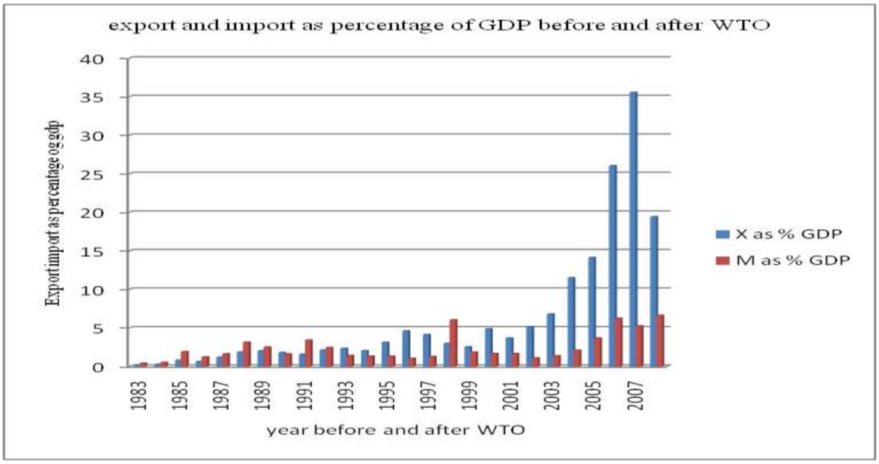
Table 1.1 India's trade as percentage of GDP with Pakistan

year	X as % GDP	M as % GDP	TT as % GDP
1983	0.181	0.421	0.602
1984	0.273	0.520	0.794
1985	0.812	1.917	2.729
1986	0.637	1.244	1.881
1987	1.194	1.647	2.842
1988	1.861	3.154	5.016
1989	2.021	2.527	4.548
1990	1.793	1.630	3.424
1991	1.573	3.421	4.994
1992	2.111	2.452	4.563
1993	2.345	1.410	3.756
1994	2.050	1.333	3.383
1995	3.139	1.322	4.461
1996	4.600	1.058	5.658
1997	4.146	1.287	5.434
1998	2.997	6.057	9.054
1999	2.532	1.858	4.391
2000	4.883	1.673	6.556
2001	3.694	1.661	5.356
2002	5.125	1.115	6.240
2003	6.805	1.366	8.170
2004	11.505	2.097	13.602
2005	14.134	3.682	17.816
2006	26.054	6.240	32.295
2007	35.574	5.266	40.840
2008	19.434	6.634	26.069

Source: Calculated from data world economic outlook database oct.2009, IMF &Import export data bank.

Figure 1.2 Import and export volume of India with Pakistan before and after the WTO



Source: Based on the figures in table 1.1

Table 1.2 Chain indices volume of total trade, imports and exports with pakistan

year	export	import	Total trade
Volume of trade WTO			
1983	100	100	100
1995	133.8	5.02	118.76
Volume of trade after WTO			
1996	100	100	100
2008	74.59	106.31	80.72

Source: Authors own calculation based on the data in table 1.1

3.2. Econometric approach results

The Econometric approach was employed to know the impact of the WTO on the bilateral trade of India and Pakistan. Data was taken for the time period 1983 to 2009 from the IMF. The data is presented in the table 1.3. The data is in nominal terms. From the data given in the table three regressions were estimated. Regression for whole time period called pooled regression was estimated for the time period 1983 to 2008. The second regression was estimated for the sample period before the WTO and third regression were estimated or the time after the WTO. The results of the pooled estimated regression are presented in the table 1.3.1.

Table 1.3 Variables taken for analysis

YEAR	Total trade	GDP of world	GDP Pakistan	GDP India
1983	48.45	12107.66	32.339	212.527
1984	66.48	12474.08	33.762	213.843
1985	53.5	12897.82	34.941	220.972
1986	37.45	15245.15	36.432	243.001
1987	36.3	17483.23	38.983	267.793
1988	74.8	19595.45	42.241	293.067
1989	62.9	20579.48	43.869	290.836
1990	89.03	22851.07	48.457	313.731
1991	136.93	24045.51	55.007	278.533
1992	134.92	24282.56	59.407	280.933
1993	112.46	24887.4	62.88	274.651
1994	105.08	26719.48	63.389	311.813
1995	145.33	29638.43	74.066	353.964
1996	193.38	30378.81	77.345	364.802
1997	187.6	30252.48	76.261	408.27
1998	320.55	30017.15	75.966	411.546
1999	161.16	31175.2	71.248	439.433
2000	250.86	32103	74.08	461.913
2001	208.77	31891.91	72.268	473.044
2002	251.01	33186.8	72.685	495.008
2003	344.59	37301.21	83.501	573.153
2004	616.03	41974.19	98.093	669.407
2005	868.79	45385.48	109.595	784.254
2006	1671.56	49115.35	127.489	875.435
2007	2233.06	55270.1	143.203	1100.986
2008	1454.47	60917.48	164.557	1206.684

Source: World economic outlook database oct.2009, IMF

Table 1.3.1 Result for pooled regression

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-304.824	127.415		-2.392	.026
	Gdp_w	-.049	.020	-1.109	-2.398	.025
	Gdp_p	14.295	8.504	.861	1.681	.107
	Gdp_i	2.433	.599	1.159	4.062*	.001

Table 1.3.2 Result for first sample regression (before WTO)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	33.592	58.732		.572	.581
	Gdp_w	.005	.006	.766	.861	.412
	Gdp_p	1.664	1.790	.584	.930	.377
	Gdp_i	-.483	.377	-.527	-1.281	.232

Table 1.3.3 Result for sample regression (after WTO)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	167.715	1389.264		.121	.907
	Gdp_w	14.158	16.540	.644	.856	.414
	Gdp_p	3.975	3.383	1.607	1.175	.270
	Gdp_i	-.086	.100	-1.325	-.859	.413

As indicated by the table the estimated pooled regression becomes

$$Y_p = -304.824 - .049\ (gdp_w) + 2.433\ (gdp_i) + 14.295\ (gdp_p)$$

The R square denotes that 89 % of variation in dependent variable is explained by these independent variables. The unexplained variance is 863622.563.looking to the t value only the Gdp_i is significant.

The estimated regression for the time period before WTO as indicated in the table 1.3.1 is

$Y_i = 33.592 + .005\ (gdp_w) + 1.664\ (gdp_{i)}) - .483\ (gdp_p)$

With R square .832 and unexplained variance 2999.420

The estimated regression for time period after WTO as presented in table 1.3.3 is

$Y_2 = 167.715 + 14.158\ (gdp_{w)}) + 3.975\ (gdp_i) - .086\ (gdp_p)$

With R square .861 and unexplained variance 779212

The test of equality between sets of coefficients in two linear regressions suggested no significant impact of WTO on India Pakistan bilateral trade.

3.3. Findings of research

The non-econometric and econometric analysis we presented above allows us to see the impact of the WTO on international trade of India with Pakistan. The WTO has affected the trade negatively. As a whole we can say that the WTO has not increased the international trade of India and Pakistan as it was expected. The major findings of the study are, the rate of growth of trade bulk (as percentage of GDP) of India with Pakistan has not increased as it was expected. The rate of increase in imports of India from Pakistan was lower relatively than exports to Pakistan. India was facing the trade deficit with Pakistan before WTO, after WTO there is surplus in the account of the India. That is due to the relatively more open policy of Pakistan with India. The bilateral trade of two countries has not benefited by the policies of WTO. The trade restrictions are discriminative which is in contrast of the WTO provision of non- discrimination Increasing share of informal trade makes every policy less effective and WTO is no exceptional. Why bilateral trade was not affected by WTO is because of:

1 First and foremost the political conditions. Trade restrictions are sometime laid down for security purposes which make WTO less effective.

2. India's applied duty customs rates are higher than Pakistan's rates

3. Pakistan not granted MFN status to India (If Pakistan was to grant MFN status to India, it would have to impose the same duty as it does on other trading partners.) and India's MFN status to Pakistan less effective.

4. Most of the trade not liberalized, Increasing share of the global trade,

5. High border barriers

6. Increasing share of informal trade makes every policy less effective and WTO is no exceptional.

3.4. Suggestions/Recommendations

1. Harmonization or mutual recognition of standards across the borders can make trade much easier.

2. Similarly, improving customs and border crossings.

3. Reducing transactions costs, the number of signatures for transaction costs can play a very important role.

4. Transparency and strong enforcement of policies could increase the formal trade and make trade restrictions lesser than prevailing.

5. India should make MFN status practically efficient in order to non-discriminate Pakistan which finally will be helpful to make WTO policies much effective.

6. Pakistan should grant MFN status means open behavior with India in trade as is with other countries.

7. Effective peace building measures to restore political stability will be then effective.

4. Conclusion

Indo-Pak study is the concern of every one because the peace between the two countries is not essential for the south Asia only but for world cooperation as well. Both India and Pakistan open there respective economies with the rest of the world. Both countries followed the road of globalization and were trying to and are in effort to meet with WTO clause at international level but it remains the main concern to study how much open the two countries are with each other after WTO. It was found that there was not a significant impact of the WTO on the bilateral trade of India and Pakistan. The reasons are many but one important reason which the both countries are forwarding before rest of the world is that," if we are discriminating with each other it's because of the political concerns". But this study concludes that in order to make any policy effective the realization of the mutual benefit from the bilateral trade is important. The study also provides clue that to make any policy effective close economic ties are important for both counties which will not have trade effect but restoration of political stability effect as well.

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