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US Trade-Aid Balance:

Implications for Pakistan and the Region

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In Pakistan's early development stages, from the early-1950s to well into the late-1960s, economic growth was considered important. The strategy followed was influenced by the Harrod Domar model. It was one of promoting rapid industrialisation under the ownership and control of the rising capitalist class, with assistance from the government at home, and friendly foreign states. It was presumed that the benefits of growth would 'trickle down' to the more depressed sections of the community. In the words of Dr Mahbubul Huq, the Pakistani planners believed that "it is well to recognise that economic growth is a brutal, sordid process. There are no short-cuts to it. The essence of it lies in the labourer producing more than he is allowed to consume for his immediate needs, and to invest and re-invest the surplus thus obtained". The formulation of detailed development plans, with specific output targets and carefully designed

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investment profits, has often been a necessary condition for the receipt of bilateral and multilateral foreign aid.

At the initial period policy makers favouring external assistance had to battle the influence of a burgeoning intellectual sentiment in the developing world. Its arguments were in sympathy with the 'dependencia' literature whose proponents were the likes of Johan Galtung, Andre Gunder Frank, Samir Amin, and Celso Furtado. They saw the dependence of the underdeveloped countries (satellite/periphery) on the developed countries (metropolis/centre) as a chronic or 'structural condition' which had to be broken if any meaningful development was to be achieved. Otherwise such conditions of this 'exploitative relationship' would result in the exclusive benefit of the metropolis /centre or its 'comprador elite' in the satellite/periphery (such as the '22 families').

To these theoreticians, the remedy lay in either opting out of the capitalist system, if needs be by a revolution. Another option was by adopting such reforms as stimulating demand among more indigent groups for low-grade consumer goods capable of being manufactured domestically. Only such actions could stave off external penetration. The received wisdom among Pakistani policy makers was Paul Rosenstein-Rodan's 'Big Push' theory. It favoured planned large-scale investments in industrialisation in countries with surplus workforce in agriculture in order to take advantage of network effects, viz. economics of scale and scope to escape the low-level equilibrium 'trap'. Hence the need for large doses of funds.

Enter US foreign assistance, initially as a Cold War ally, and later as a partner in the so-called "war on terror". According to statistics available, between 1951 and 2011 the US obligated nearly US$ 67 billion (in constant 2011 dollars) in aid. The flow has 'waxed and waned', year to year, and period to period, in consonance with the nature of bilateral relations and US geopolitical interests. At times, as in the 1990s, there were stoppages. Many, understandably, did not see this donor as an unwavering or reliable partner. Hence there was the perceived need to signal renewed US commitment to Pakistan. In response to that need the US Congress in 2009 approved the Enhanced Partnership for Pakistan Act, also known as Kerry-Lugar-Berman Bill, popularly called KLB. The idea was to put security and development on two separate tracks. This was purported to insulate the development agenda from the uncertainties and vagaries of the politics of security.

It authorised a development-related support to Pakistan of US$ 7.5 billion over the five year period of 2010 to 2014, with the mean figure of US$ 1.5 annually. The goal was to be threefold; first, to improve Pakistan's governance; second, to support its economic growth and, third; to invest in its people. However, as demonstrated in a recent Congressional Research Service report by Susan Epstein and Alan Kronstadt, in only one of the first four years of KLB did the final appropriation of economic-related aid to Pakistan meet or exceed this figure.

It is worth recalling that in the US financial system the executive proposes, and the legislature disposes. With regard to Pakistan, the executive, that is the White House, has always been more supportive than the legislature, that is the Congress, which has often been less kind to this country. The situation may exacerbate if President Obama's Democratic Party, which has an edge of 55-45 over the Republicans in the Senate, loses that majority in the upcoming November polls. If the Republicans can pick up 6 extra Senatorial seats – a distinct possibility – they will control both houses of the Congress, hugely reducing any Presidential predilections to act in Pakistan's favour.

In the pre-KLB period, as between FY 2002 and FY 2009, only 30%of US aid to Pakistan was allocated to development-related needs, with the rest, i.e. 70% going to security. Post-2009, with the KLB, it was raised to 41%. It was argued that the increase demonstrated the strengthened commitment to Pakistan's development. But, as we have seen, its flow was intermittent, particularly in 2011 which witnessed a set of unsavoury bilateral incidents. Even in the best of times, much of what was to have flowed remained with US-based contractors in that country. So in the event the KLB is discontinued, and in any case it is ending in 2014, any tears shed would not necessarily be Pakistani.

Factors such as these, compounded by the limited absorption capacity of local partners, hesitation to allocate in sectors such as energy in the absence of systemic reforms, and disruptions caused by natural disasters such as the 2010 floods, severely constrained actual disbursement. According to Congressional reports, between 2010 and 2012 only US$ 2.2 billion out of $4 billion, appropriated for economic-related assistance was spent. Even if the anticipated US$ 1.5 billion was provided and spent annually, as was not the case, mathematically it would amount to only US$ 8 per capita, and its absence would diminish Pakistan's GDP growth by less than 0.2%. The government of Pakistan (GOP) is now also tapping alternative sources. Though the GOP had scrapped the IMF programme in 2011, the new government after the elections of May 2013 has entered into an agreement with the Fund for a package worth US$ 6.6 billion for FY 2013-2016 as a bail-out for the balance of payments crisis and to shore up the depleting foreign exchange reserves.

However currently ‘trade not aid’, or more appropriately ‘trade in preference to aid’ is the favoured ‘mantra’ of the GOP. This has great political appeal in Pakistan. When Prime Minister Nawaz Sharif travelled to Washington in October 2013, he apprised President Barack Obama of this. Earlier Foreign and Security Adviser Sartaj Aziz had expressed the hope to Secretary of State John Kerry that bilateral trade could be doubled to “something like US$ 11 billion in the next five years”.

What are the possibilities? Let us look at some numbers. In 2013 the two-way total was US$ 5.3 billion in goods trade. US imports from Pakistan totalled US$ 3.7 billion that year, a 1.6% increase from 2012 and 46% from 2003.The five largest import categories were Miscellaneous Textile Products, Knit Apparel, Woven Apparel, Cotton and Yarn Fabric and Leather. The US exports to Pakistan amounted to US$ 1.6 billion, up 7.7 % from 2012 and 95% from 2003. The top categories were Machinery, Cotton, Yarn and Fabric, Iron and Steel, Aircraft, and Electrical Machinery. US agricultural exports to Pakistan were to the tune of US$ 374 (cotton, dairy products and planting seeds) and imports from Pakistan were worth US$ 121 million (mainly rice). During the first three months of 2014, the US exported to Pakistan goods worth US$ 378 million and imported to the amount of US$ 899.6 million.The numbers do show a slight upward curve, but even the most optimistic would see the aspired figures as much beyond the rim of the saucer.

There are some obstacles that stand in the way of a preferential trade pact between the two countries. US Congressional lawmakers are extremely chary of any measures that would hurt their textile manufacturers. The previous President, George W. Bush, had failed to sway them despite Pakistan’s critical strategic alliance following the twin-tower attacks in 2001. Even if President Obama wants to put himself forcefully and squarely behind such a deal, his existing animus with the legislative arm would render it difficult. Also, outside of textiles there would be problems. For instance US agricultural regulations are stringent and numerous that impose standards on production, packaging, labelling, transportation and more. Even if the Pakistani agro-businesses were prepared to bear the high capital costs needed to meet the American standards, and it is not at all certain they would be, it is quite possible Pakistan will be wanting in terms of the regulatory infrastructure and technology that would also be required to accompany the conclusion of a successful and comprehensive trade deal with the US. This would be the case in spite of the obvious strategic importance of Pakistan to the US and its NATO allies a in the wake and aftermath of draw-down in Afghanistan this year.

The fact is often cited that South Asia persistently remains one of the least integrated regions of the world. This runs counter to economic theory, in particular what is called 'the gravity model of trade'. This posits trade with neighbours, especially when the neighbours have large mass, meaning large markets. Pakistan is the only large country in the world that shares borders with China and India, two of the largest economies of the world. Given that, Pakistan and India would provide each other markets of 180 million and 1.2 billion people respectively.

Bilateral trade shows some sad statistics. It is only 20% of regional trade, though the two countries account for 92% of South Asia's GDP and 85% of its population. The World Bank lists a set of 'doable' actions that could elevate two-way trade to US$ 8-10 billion annually. A respected colleague of mine at ISAS, also formerly of the CSP and ex-Finance Minister of Pakistan Shahid Javed Burki, has argued that unimpeded bilateral trade, or significant relaxation of constraints at any rate, would raise Pakistan's GDP by two percentage points. This is also at a time when America, as Robert Kaplan would have us believe, is in 'elegant decline'. The current big story, in Fareed Zakaria's view, is 'the rise of the rest', for 'the rest' read 'Asia'. Indeed the World Bank has forecast that, in purchasing power parity terms, China will be the world's largest economy by the end of this year. So, Asia may be set to become the new Rome to America's Greece.

This resurgence of Asia, certainly of East Asia, and I say this from the vantage point of being located in Singapore at present, is something that Pakistan should seek to profit from, with regard to trade and other economic linkages. It already enjoys excellent relations with China. Elsewhere in East Asia, the Trans-Pacific Partnership (TPP) and the Regional Comprehensive Economic Partnership (RCEP) have potentials of taking that part of the world closer to the goal of a Free Trade Area of the Asia-Pacific. This will pave the way for much higher living standards for all concerned, and all boats that are linked will rise with the tide, including Pakistan.

This equally sharpens the argument for greater intra-mural trade and cooperation within South Asia. India would do well to provide Pakistan access to Bangladesh, Nepal and Bhutan, and allow these countries facilities to trade among themselves. Pakistan could be a conduit to India to establish links with Central Asia, China and the Middle East, through Afghanistan. The new Modi-led government of India will be focussed on domestic development which should encourage it to develop good relations with neighbours to create an enabling ambience. With the warmth generating from the recent meeting between Prime Ministers Modi and Nawaz

Sharif in New Delhi, there are stirrings of a positive development in that respect already. It has been decided that the Foreign Secretaries of both countries would meet in the spirit of the 1998 Lahore Declaration (on the last occasion the Muslim League-Nawaz and BJP led by Atal Behari Vajpayee met in Lahore) to carry forward negotiations. The Commerce Ministries are also likely to relate to each other to draw up mechanisms for greater market access.

So now is a good time as any for better intra-regional relations in South Asia. The aim, as was envisioned in Europe in the 1970's, could be the ultimate creation of a 'South Asian Home'. All this, I admit is still within the realm of *hochpolitik* or 'high politics' as the Germans say. But such higher politics must be addressed, and the sooner the better. As always in South Asia, time is of the essence, for there is the constant risk that new negative events may suddenly occur to wipe away past positive achievements. In South Asia forward movement is only achieved by riding the tide.

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