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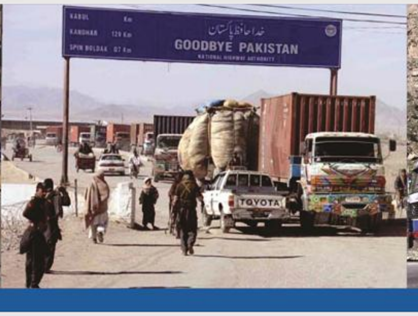
Pakistan-Afghanistan Cooperation on Trade

Political Economy Analysis*

Dr. Mohammad Zubair Khan



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Abbreviations & Acronyms

ADB	Asian Development Bank
APTTA	Afghanistan-Pakistan Transit Trade Agreement (2010)
APTTCA	Afghanistan Pakistan Transit Trade Coordination Authority
ATTA	Afghan Transit Trade Agreement (1965)
CARs	Central Asian Republics
CAREC	Central Asia Regional Economic Cooperation
CPEC	China-Pakistan Economic Corridor
EBRD	European Bank for Reconstruction and Development
EFE	Electronic Form-E
EU	European Union
FPCCI	Federation of Pakistan Chamber of Commerce and Industries
GATT	General Agreement on Tariffs & Trade
GDP	Gross Domestic Product
IMF	International Monetary Fund
IRU	International Road Transport Union
LPI	Logistics Performance Index
NEG	New Economic Geography
PAJBC	Pakistan Afghanistan Joint Business Council
PAJCCI	Pakistan Afghanistan Joint Chamber of Commerce & Industry
PBC	Pakistan Business Council
RKC	Revised Kyoto Convention
TIR	International Road Transports
UN	United Nations
UNCOLS	United Nations Convention on Law of the Sea
UNCTAD	United Nations Conference on Trade & Development
UNDP	United Nations Development Project
UNODC	United Nations Office on Drugs & Crime
WB	World Bank

WCO	World Customs Organisation
WeBOC	Web Based One Customs
WTO	World Trade Organization

About the Author

Dr. Mohammad Zubair Khan has a doctorate from Johns Hopkins University in Political Economy. After working for the World Bank, he was on the staff of the International Monetary Fund from 1981 to 1992, assigned to a wide range of countries, including industrial countries in Northern Europe, developing countries in South Asia and Turkey, the oil exporting states in the Middle East and countries in the South Pacific region. Since returning to Pakistan, he has been consulting for the World Bank, Asian Development Bank, UNDP, JBIC and other international organizations on a range of issues. He also lectured at the Central Banks of Egypt and Sri Lanka, NIPA Lahore, Pakistan Administrative Staff College, and the National Defence University in Islamabad.

During this period, he has also served as the Federal Minister for Commerce, and represented Pakistan at the first ministerial conference of the WTO. He has served as Member National Finance Commission, Member Advisory Board Securities and Exchange Commission, Pakistan, Member Provincial Finance Commission KPK, Member Board of Directors Bank of Khyber for many years. He is also Member of Boao Forum for Asia, Hainan, China. Dr. Zubair Khan is also an active advocate of good governance and the rule of law in Pakistan on the electronic media. He is the founder and CEO of Bela Power Pvt Ltd. that produces O1 Naturally Pure, premium natural mineral water, certified internationally by NSF.

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The responsibility for the analysis and the conclusions are the author's. The author is indebted to excellent support from Akbar Khan Durrani and Mohammad Umair Khan in helping to review the literature, collection of data, tabulation and charts. Akbar Khan Durrani conducted useful interviews of officials and businessmen in Kabul to record their views on the political economy of Pak-Afghan trade.

Executive Summary

Trade between Afghanistan and Pakistan carry vastly different importance for the neighboring countries. While Afghanistan is a land locked country reliant on Pakistan for transit and bilateral trade, Pakistan is located advantageously on the open seas and Afghanistan is relatively less significant a trade partner. For Pakistan, the development of trade links with Afghanistan acquires somewhat enhanced importance in the regional context. The potential of the CAREC program puts regional trade relations for both Pakistan and Afghanistan on a much larger scale, together with funding from multilateral institutions that can convert economic potential into reality in the medium term. In the near-term, the emerging security situation in Afghanistan will be critical for improving access of Central Asian countries to global markets and for Pakistan to reach the CAREC markets.

Trade relations between Pakistan and Afghanistan have been the victim of historically strained political relations between the two countries. In recent years, illegal trade and the unauthorized movement of people and contraband across the porous common border have further contributed to tensions, although considerable trade has started to flow across the border. Afghan-Pak trade has three dimensions, transit trade, bilateral trade and illegal trade. Strains in economic relations reflect Afghanistan's claim that Pakistan has not removed 'impediments' to trade, while Pakistan claims that illegal trade under the cover of Afghan trade hurts Pakistani business interests and cause losses in government revenue. Many attempts have been made to identify the difficulties and address the grievances of the two sides but to no avail. The impediments identified in various studies relate to issues of trade facilitation, transit and transport, en route security, customs procedures, illegal trade, tariffs, banking and payments, competitiveness, and infrastructure.

This paper suggests a strategy to adopt international best practices and address difficulties in the context of the institutional and legal framework of international commitments of Pakistan and Afghanistan, and through formal structured negotiations.

The solution to issues related to transit trade between Afghanistan and Pakistan lies in the full adoption of international best practice in this regard, the TIR Convention. Transit trade can move smoothly and illegal trade can be reduced by improving border procedures, strengthening the bonded transport and guarantee system, especially build the institutional and financial apparatus to implement the TIR Convention system. Mere accession to the TIR Convention is not enough, to utilise the convenience of the TIR system, both Pakistan and Afghanistan need to develop the five pillars of the TIR Customs transit system. Developing the five pillars will be essential if both countries intend to benefit from the regional trade that the CAREC program promises. Tariff harmonization is not the answer to reducing illegal trade. With diverse approaches to tariff determination, the two countries are unlikely to reach agreement on tariff harmonization.

Prospects for bilateral trade are limited in the backdrop of the overall economic prospects of Afghanistan, nevertheless, bilateral trade can benefit by addressing issues related to trade facilitation. Again, these reforms are important for both countries, not only in the bilateral context, but also and more so in the regional context. Trade facilitation reform in Afghanistan and Pakistan can be undertaken with technical assistance from multilateral organisations. Pakistan is addressing trade facilitation shortcomings with the help of ADB and the World Bank.

With better representation of all private sector stakeholders in Afghan-Pakistan trade in PAJCCI, particularly from regions in Pakistan that actually conduct trade with Afghanistan, and from industry that has been hurt by illegal trade, and from transporter associations whose jobs are at stake in concessions demanded by Afghanistan, the input into APTTCA can be made more effective.

The assessment of the investment environment in Afghanistan is not favorable, and there is large-scale capital flight out of the country. Pakistani investors are unlikely to invest in industry in Afghanistan under these circumstances, especially when there is a persistent political trust deficit between the two countries with security related undertones.

1. Introduction

Cross-border trade between Pakistan and land-locked Afghanistan has many dimensions; transit trade to Afghanistan, bilateral formal trade, illegal trade, transit trade to other double land-locked countries, and regional trade. The multi-dimensional trade across the Afghanistan-Pakistan border has been the subject of political debate, negotiations and bilateral agreements, but also a source of tensions between the neighboring countries. Attempts to remove impediments have been mired in repeated negotiations because issues relating to different dimensions have been mixed, making discussions and negotiations complex and unending. Consequently trade relations between the neighbors have suffered, marred by unmet expectations and implementation problems, causing distrust between the governments. Since each dimension of cross-border trade is governed either by bilateral, regional or multilateral agreements or by commitments of the two countries to international charters, untangling of the main issues and discussion of these within the relevant format could help resolve the impediments and issues to mutual benefit.

This report analyses cross-border trade in the context of agreements and commitments made by the two counties to provide the relevant legal and institutional framework for a meaningful discussion and understanding of the outstanding issues.

2. Economic Geography of the Region

Prior to the 15th century when travel and trade was mostly across land, Afghanistan and Central Asian Republics (CARs) lay at the crossroads of the Silk Road, a trading route linking great civilizations and economic powers. Changes in technology shifted the trade routes centuries ago to the sea lanes around the land mass of Asia. The once thriving regions along the Silk Route were transformed into landlocked regions cut off from the major maritime trade routes by national boundaries and difficult terrain. First geography location disadvantages were compounded by second geography disadvantages of difficult terrain and weak communication infrastructure in the region in the terminology of the New Economic Geography (NEG) literature.

Now in the 21st century, Afghanistan, land-locked deep in the landmass of Asia, is dependent on Pakistan and Iran in the south for access to the sea and international markets. The Central Asian Republics of Turkmenistan, Uzbekistan, Tajikistan and the Kyrgyz Republic are double land locked north of Afghanistan, facing multiple border crossings to the south and west before reaching the open seas. All these countries currently have access to the seas and to each other's markets but the region as a whole remains one of the most remote and least integrated regions of the world.

Afghanistan's main transit trade route for links with the rest of the world is through Pakistan, and Pakistan was the largest destination for Afghan exports (33% of total exports) in 2014. Pakistan was also the second largest source of Afghan imports (17%) in that year. For Pakistan, Afghanistan is relatively less significant as an export destination and declining (7% of total exports), and not a source of imports of any note. In the years ahead, Afghanistan as a major export destination for Pakistan remains uncertain and will depend on continued economic growth, political stability and improved security conditions in Afghanistan. According to the IMF,[1] "The future path of the (Afghan) economy is highly dependent on the authorities' delivering on their economic reform commitments, continued donor support, and improvements in security." The IMF further notes that "security challenges have led to higher-than-projected security expenditure, delaying the attainment of fiscal sustainability. Volatile aid flows have also complicated policymaking."

As a result, trade between Afghanistan and Pakistan carry vastly different importance for the neighboring countries. In addition, Afghanistan's market size is much smaller than the Pakistani market, at less than 8.5% of Pakistan's GDP (Table 1 below), and prospects for Afghan economic growth are clouded by near-term risks which are mostly on the downside.[2] Moreover, while

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1 IMF Staff Report December 2015, IMF Country Report No. 15/324.

2 "Risks are mostly on the downside and are related to adverse domestic or regional security developments, political instability, inadequate implementation of economic policies, and donor fatigue." IMF Staff Report December 2015, IMF Country Report No. 15/324.

Afghanistan is a land locked country reliant on Pakistan for transit and bilateral trade, Pakistan is located advantageously on the open Arabian Sea, having access to world markets from the country's seaports. In contrast to Afghanistan, development of bilateral trade links is not vitally important to the economic future of Pakistan. While the border provinces of Pakistan have benefitted from trade with Afghanistan, the economies of the bordering provinces are more strongly linked to the growth centers and markets of Pakistan and the flow of traded goods is facilitated by the country's trade corridors, governed by domestic spatial advantages and driven by national priorities.

Nevertheless, for Pakistan, the development of trade links with Afghanistan acquires somewhat enhanced importance in the regional context, because Afghanistan remains the shortest and most accessible transit route between Pakistan and the CARs. The economies of Afghanistan and its four Central Asian neighbours together are a somewhat larger market, about 60% of the size of Pakistan's economy. Pakistan's proximity to Afghanistan and the CARs gives Pakistan an advantage of lower transport costs over most other countries when the region is viewed as a potential export destination. More importantly accessing the surplus energy in the CARs is attractive for energy-starved Pakistan.

Table 1: Pakistan and Central Asian Economies GDP 2014

Country	GDP US$ billion, current 2014	Population million 2014
Pakistan	246.8	185.1
Afghanistan	20.8	31.2
Turkmenistan	47.9	5.3
Uzbekistan	62.6	30.7
Tajikistan	9.2	8.4
Kyrgyz Republic	7.4	5.8

Source: WTO, www.wto.org

Even so, the importance of CARs for Pakistan's economy should not be overstate, especially in view of Pakistan's much bigger share of trade (90% of total trade) with much larger markets in Europe.

USA and East Asia. After all, Pakistan is a lower middle income country with serious resource constraints. Pakistan's ability and capacity to develop physical and institutional infrastructure on its own to reach markets in the CARs and Afghanistan will remain limited in the near future. A more realistic and calibrated development strategy should acknowledge Pakistan's priority to develop its trade links with the bigger markets, and explore multilateral and bilateral donor supported regional programs like the Central Asia Regional Economic Cooperation (CAREC) and the China-Pakistan Economic Corridor (CPEC) for developing links with Afghanistan and Central Asia.

The potential of the CAREC program puts regional trade relations for both Pakistan and Afghanistan on a much larger scale, together with funding from multilateral institutions that can convert economic potential into reality in the medium term. Initiated in 1997, The Central Asia Regional Economic Cooperation (CAREC) Program is a partnership of 10 countries (Afghanistan, Azerbaijan, People's Republic of China, Kazakhstan, Kyrgyz Republic, Mongolia, Pakistan, Tajikistan, Turkmenistan, and Uzbekistan), supported by 6 multilateral institutions (ADB, EBRD, IDB, IMF, UNDP and WB), to promote development through regional cooperation in four priority areas: Transport, Trade Facilitation, Energy, and Trade Policy.

Most CAREC countries are land-locked and rely almost exclusively on overland transport for trade within the region and with markets outside. The CAREC 2020[3] program aims to expand and develop the current underdeveloped network of roads and railways spanning the region into six major transport corridors. The six corridors will link the region's key economic hubs to each other, and connect the land-locked CAREC countries to other Eurasian and global markets through the warm-water ports of Karachi and Gwadar in Pakistan. The CAREC program also aims to reduce border-crossing time and costs and make transshipment operations

[3] CAREC Transport and Trade Facilitation Strategy (TTFS 2020), covering 2014– 2020: About $27.7 billion invested in transport, trade facilitation, and energy projects, from 6 projects in 2001 to 166 projects in 2015. www.adb.org/countries/subregional-programs/carec

as seamless as possible through harmonization of transport and trade procedures and processes.

Two CAREC corridors,[4] which connect the regional economies to warm water ports of Gwadar and Karachi, both in Pakistan, for onward access to global markets pass through Afghanistan. In the near-term, the emerging security situation in Afghanistan will be critical for the success of the CAREC program in improving access of Central Asian countries to global markets and for Pakistan to reach the CAREC markets. Since prospects for peace in Afghanistan seem uncertain in the near-term (see box 1 below), Pakistan and the eight countries north of Afghanistan should also develop alternative interlinking routes to by-pass conflict stricken Afghanistan if the security situation does not improve. One such alternative for Pakistan to reach China and the Central Asian economies is the China-Pakistan-Economic Corridor (CPEC).

Box 1: A Recent Report on the Security Situation in Afghanistan

October 6, 2015, Washington (AP): Violence in Afghanistan is on the rise, according to a new Pentagon report to Congress that says the Taliban ware emboldened by the reduced U.S. military role and can be expected to build momentum from their 2015 attack strategy. The number of effective insurgent attacks rose this year, causing increased casualties among Afghan security forces, the report said. While Afghan forces have demonstrated a will to fight and to learn from their battlefield mistakes, the report said the Taliban’s resilience has made security fragile in key areas and at risk of deteriorating in others. Sen. Bob Corker, chairman of the Senate Foreign Relations Committee, told reporters that it was "probably the most depressing assessment" of the direction in which the country is headed that he has heard in a “long, long time.”

[4] Corridor 5 & 6

Complaints and Impediments in Pak-Afghan Trade

Trade relations between Pakistan and Afghanistan have been the victim of historically strained political relations between the two countries. Since the independence of Pakistan in 1947, Afghanistan has not formally recognized the 2,400 kilometer long Durand Line as the legitimate border between the two countries which together with opposing international alignments of the two countries during the cold-war era have been at the root of their estrangement. More recently, "Cross-border infiltration, refugees, drug trafficking, militant groups, and disputes over counterterrorism policy and dialogue with terrorist networks have contributed to an entrenched trust deficit and have eroded relations" (Hussain & Elahi, 2015). Illegal trade and the unauthorized movement of people and contraband across the porous common border have further contributed to tensions between Pakistan and Afghanistan. Pakistan has proposed to fence the border on a number of occasions to prevent the illegal movement of smugglers and people and infiltration by militants. Afghanistan has opposed the idea,[5] but Pakistan has commenced digging a 1,100 km long trench[6] along the Afghan border in northern Balochistan. In the next phase, the trench will be extended to the entire border.

There are a number of formal border crossing points on the border. In recent years considerable trade has started to flow across the border. Afghan-Pak trade has three dimensions, transit trade, bilateral trade and illegal trade. Although Pakistan has signed formal transit trade agreements with Afghanistan as far back as 1965 and now more recently in 2010-11 giving Afghanistan access to international markets and Pakistan is a major bilateral trading partner for Afghanistan, economic relations between the countries have remained strained. Afghanistan claims that Pakistan has not removed 'impediments' to trade, while Pakistan claims that illegal trade under the cover of Afghan trade not only hurts Pakistani business interests, it causes losses in revenue of billions of rupees to the Pakistani government.

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5 Afghanistan contends that the installation of a physical barrier would make this border permanent

6 11 feet deep, 14 feet wide

Many attempts have been made to address the grievances of Afghan traders and Pakistani businesses and the government revenue departments, but to no avail. Complaints, accusations and grievances continue to build up, further aggravating relations between the two countries. The dilemma is that because illegal trade under cover of Afghan transit trade is pervasive and large, Afghan demands for reducing border controls and monitoring make it difficult to achieve the Pakistani objective of reducing illegal trade.

In recent years a number of government committees, business forums and studies have examined Afghanistan's transit and bilateral trade with Pakistan with a view to suggest ways to enhance trade.[7] These examinations have identified various 'impediments' and difficulties faced by traders onboth sides of the border over recent years. This section has consolidated and categorized the identified impediments according to their nature to allow a more systematic and structured discussion of ways to address these in the next few sections of this report. This paper does not suggest putting out a bush-fire here and another one there by providing a computer at one border crossing and an electric generator at the other or addressing the difficult attitude of the security forces at some particular check point.

The strategy suggested here is to adopt international best practices in the movement of trade transport and address difficulties in the context of the institutional and legal framework of international commitments of Pakistan and Afghanistan and through formal structured negotiations. This approach will lower tensions, reduce acrimony and further trade in the interest of both countries. Efforts to address the difficulties will be limited by the resource and capacity constraints in the two countries but those shortcomings can be overcome with the resources and technical support of international multilateral organisations. The gains for both Afghanistan and Pakistan in undertaking reforms to reduce

[7] *Consolidated Report of Post Afghan Visit Review Committee*, Government of KPK (May 7, 2015); (Ahmed, 2015); (Shabbir & Ahmed, 2015); (Hussain & Elahi, 2015); (USAID Pakistan, 2014); (PILDAT, 2011).

impediments to cross-border trade will far outweigh those associated with bilateral trade expansion as reforms facilitate regional integration as well.

The impediments identified in various studies (duly noted here) relate to issues of trade facilitation, transit and transport, en route security, customs procedures, illegal trade, tariffs, banking and payments, competitiveness, and infrastructure. For a complete list of impediments identified, refer to Annex 1.

3. Agreements, Conventions Governing Pak-Afghan Cross-Border Trade

A. Transit Trade of Afghanistan via Pakistani Sea-Ports

I. The UN Convention on Transit Rights of Land Locked Countries[8]

The Convention defines "land-locked State" as a State which has no sea-coast; and a "transit State" means a State, with or without a sea-coast, situated between a land-locked State and the sea, through whose territory traffic in transit passes; and "traffic in transit" means transit of persons, baggage, goods and means of transport across the territory of one or more transit States, begins or terminates within the territory of the land-locked State. Land-locked States and transit States may, by agreement between them, include as means of transport pipelines and gas lines. (For details see Annex 2).

In various commentaries on the UN Convention, it is stated that though land-locked states are given with legal right of access to and from the sea and freedom of transit under Article 125 (1), such rights are put along with significant practical restrictions. Accordingly, Article 125 (2) states that ‘the terms and modalities for exercising freedom of transit shall be agreed between the land-locked States and transit States concerned through bilateral, sub

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[8] UN Division for Ocean Affairs and the Law of the Sea, *United Nations Convention on the Law of the Sea of 10 December 1982*; www.un.org/depts/los/convention_agreements/texts/unclos/UNCLOS-TOC.htm

regional or regional agreements.' This is clearly articulated by Shaw (Shaw, 2008) "it will thus be seen that there is no absolute right of transit, but rather that transit depends upon arrangements to be made between the land-locked and transit states. Nevertheless, the affirmation of a right of access to the sea coast is an important step in assisting landlocked states."

Afghanistan's access to the open seas through Pakistan was first consolidated and formalised under the 1965 Afghan Transit Trade Agreement (ATTA), years before the United Nations Convention on the Law of the Sea (UNCOLS)[9] was signed in December 1982. In view of the limitations of ATTA,[10] the two countries signed a more comprehensive and updated agreement, the Afghanistan-Pakistan Transit Trade Agreement (APTTA) on October 28, 2010. By clearly defining the transit routes and the mode and nationality of transport in these agreements together with the bank guarantees and insurance cover from traders and transporters, Pakistan has exercised its rights under the UN Convention by ensuring that APTTA "in no way infringe(s) (on its) legitimate interests."

The APTTA has attracted attention of other land locked countries in the region as well; Uzbekistan has proposed a Pakistan-Afghanistan-Uzbekistan Trilateral Transit Trade Agreement[11] since a route through Afghanistan and Pakistan to the port of Gwadar is the shortest route to the high seas from Central Asia. More recently Tajikistan requested to be part of APTTA. In a meeting of the Commerce Secretaries from seven Central Asian countries (held on 7th March 2015 in UAE and facilitated by the World Bank), Pakistan has offered similar arrangement to these countries (Shabbir & Ahmed, 2015).

The rights of access to the seas articulated in the UNCOLS also apply to the land locked Central Asian countries transiting through

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9 See Annex 2

10 ATTA did not provide Pakistan access to Central Asia through Afghanistan, and it gave rise to large scale smuggling into Pakistan hurting local businesses and government revenue

11 Source: http://defence.pk/threads/pakistan-and-uzbekistan-celebrate-20-years-of-diplomatic-relations.212528/#ixzz3tvPIIF8S

Afghanistan (and eventually Pakistan) with the agreement of the transit countries.

Article V of the GATT 1994 also provides for freedom of transit with the transit country determining the route and custom procedures to protect its legitimate sovereign rights (see Annex 3).

II. Afghanistan Pakistan Transit Trade Agreement (APTTA)

The first transit trade agreement with Afghanistan (ATTA) gave rise to large-scale illegal trade that hurt local industry and caused losses in revenue to the government. A new transit agreement, APTTA was designed to improve Afghanistan's access to Pakistani ports while restricting the associated illegal tradein conformity with the UN Convention. APTTA is a more comprehensive transit trade agreement than its predecessor, giving both signatory countries access through each other's territory (USAID Pakistan, 2014). APTTA allows Afghanistan greater access to Pakistani ports and identifies new transit corridors for Afghan trade:

- To three Pakistani ports: Port Qasim, Gwadar and Karachi;
- To China via Sost/ Tashkurgan border points; and
- To India via Wagha border point (Afghan trucks are allowed access on designated routes to Wagah where cargo can be transferred to Indian trucks, but the Afghan trucks are not allowed to carry Indian exports on return).

APTTA also provides Pakistan access to regional countries through designated corridors although Afghanistan has not yet notified its customs transit rules required under the Agreement. Despite repeated requests by Pakistan, the Afghan Government has not provided the notification of the customs transit goods. Pakistan needs to impress upon the Afghan side to notify the customs transit rules soon. This would create transparency for Pakistani traders to use the territory of Afghanistan for transit to Central Asia. The routes agreed upon are:

- To Iran via Islam Qila and Zaranj border;
- To Uzbekistan via Hairatan;
- To Tajikistan via Ai Khanum, Sher Khan Bandar; and
- To Turkmenistan via Aqina and Torghundi.

While APTTA removed clauses like the "Negative List" for Afghan imports,[12] and removed the monopoly of Pakistan Railways /NLC on Afghan transit trade by allowing Afghan trucks to carry Afghan export consignments and allowing Afghan importers to select their freight options, APTTA also introduced significant provisions[13] aimed to reduce illegal trade that can take place under cover of transit trade, which followed the guidance provided by the customs procedures and trade facilitation in conformity with the Revised Kyoto Convention.[14]

- Only trucks owned by licensed customs bonded carriers are allowed to carry international transit trade, where licenses are issued on specified terms and conditions,[15] and against a bank guarantee and a revolving insurance guarantee from a reputable insurance company;
- To ensure the fulfillment of any customs obligation arising out of transit trade, Afghan importers must furnish Custom Security in the form of insurance guarantee, valid for a year and en-cashable in Pakistan; and if the transporter is Afghan as well, an additional bank guarantee (or guarantees from Afghan Ministry of Communication) equal to ten percent of leviable duty on merchandise;

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12 (Pakistan Business Council, 2015)

13 APTTA Protocol *One International carriage by road of goods and baggage in transit*

14 UN Economic Commission for Europe (UNECE), *Revised Kyoto Convention 2006,* www.unece.org/contents/revised-kyoto-convention.htm

15 APTTA Protocol One *International carriage by road of goods and baggage in transit*

- APTTA also requires containerization of cargo and the installation of tracking devices on vehicles carrying Afghan transit trade.

According to a study undertaken by the PBC (Pakistan Business Council, 2015) to evaluate the impact of APTTA, the volume of Afghan transit trade through Pakistan has declined between 2011 and 2014 [16] in the post APTTA period, "but this appears to be more a reflection of the overall drop in Afghan imports as opposed to diversion of transit trade through other routes". And the difference in the value of transit trade reported by Pakistan and Afghanistan (reflecting illegal trade) remained high at $1.0 billion in 2014 (post APTTA) but much less than $2.9 billion in 2010 (the last year of ATTA). The reduction indicates that the provisions of APTTA to curb illegal trade are having some impact but needs to be made more effective.

APTTA is a more comprehensive transit trade agreement than ATTA, and it has reduced the risk of illegal trade as well as facilitating transit trade considerably, but it has failed to satisfy the critics on both sides of the border. APTTA is still seen to be cumbersome, time consuming and costly for Afghan traders on the one hand and failing to stop illegal trade on the other hand. Both Pakistan and Afghanistan have met numerous times to remove 'impediments' and reduce illegal trade, seeking the views of the business communities on both sides of the border through the APTTCA, but with limited success due to the fundamental conflict of objectives related to reduction in illegal trade and reduction in monitoring.

One of the persistent demands of Afghanistan has been to allow Afghan trucks to transport goods to India and back, across the land border at Wagah.[17] First, Afghanistan's demand of access to India overland Pakistan through Wagah is not rooted in the UN

[16] In 2014, imports through Pakistan accounted for 58% of Afghanistan's transit imports

[17] Under APTTA Afghan trucks are allowed access on designated routes to Wagah where cargo can be transferred to Indian trucks, but the Afghan trucks are not allowed to carry Indian exports on return

Convention UNCOLS, (the one way export facility for fruits and perishables addresses a genuine need of Afghan exporters to save the perishable export product) and secondly, agreeing to the Afghan demand will mean loss of thousands of jobs for people living in KPK and Balochistan provinces. A recent study shows that "cargo and commercial trade with Afghanistan is important for the large portion of Pakistan's population employed in the trade, transport, warehousing, and communication sectors (TTWC sector) (Shabbir & Ahmed, 2015). During the period 2004– 2011 employment in Balochistan and Khyber Pakhtunkhwa provinces increased in TTWC sectors. This increase in employment was particularly significant in the poorest quintiles". Making concessions to Afghanistan on this demand will carry a large employment cost for Pakistan. In view of this finding, it is important that the relevant transporter association be represented at the PAJCCI which reports to APTTCA.

India has also shown interest to join the APTTA and use the land route across the Wagah border. India's interest is not rooted in the UN Convention since India is neither land locked nor enroute from land-locked Afghanistan to the sea. Apart from the security considerations while relations with India are strained, unless India gives Pakistan reciprocal access to Nepal, Bhutan and Bangladesh, Pakistan will lose the locational advantage and competitive edge vis-à-vis Afghanistan and the central Asian markets if India is granted this access.

In April 2015, Pakistan's Commerce Minister announced the following steps to reduce delays experienced by Afghan transit trucks:

- Allowing a system-based partial shipment of Afghan transit goods instead of manual processing;
- A reduction in the share of Afghan cargo that is scanned, from 100 percent to 20 percent;
- A goal of increasing the clearance of almost 90 percent of Afghan cargo on the first day, with 80 percent cleared

without scanning;

- Establish joint customs and clearing points for more efficient movement of cargo across borders.

Unfortunately these measures are likely to meet resistance from Pakistani businesses and government officials who will find that the proposed measures will lead to more illegal trade. The Minister's proposals do not address all the legitimate concerns on both sides of the border. The difficulty arises due to the apparently conflicting objectives of trade facilitation and reducing illegal trade under the guise of transit trade. The solution to issues related to transit trade between Afghanistan and Pakistan lies in the full adoption of international best practice in this regard, i.e. the TIR Convention.

III. Illegal Trade Across the Border

Illegal trade across Pakistan's borders with neighboring countries and the coastline is widely acknowledged. It contributes to the informal economy which evades taxes, deals in contraband, and other criminal activities. The size of the informal economy in Pakistan is large. A State Bank of Pakistan study [18] concludes that the size of the informal economy in Pakistan has been around 30% of GDP in the 2000s (Arby, Malik, & Hanif, 2010). The SBP estimate means that Pakistan's informal economy was approximately US$ 34 billion in 2009/10 according to a UNODC funded study in 2011.[19] "While the illegal economy raises the cost for conducting legal economic activities, it also weakens states, threatens development opportunities, undermines the rule of law and keeps countries trapped in a cycle of poverty and instability. Proceeds of the illegal economy find their way into the world's formal economies every year through money-laundering and acquisitions of legal assets. Illegal economic activities also fund the activities of international organised crime groups and finance insurgent groups active in conflict zones throughout the world".

The UNODC study adds further that "Pakistan is uniquely

18 (Arby, Malik, & Hanif, 2010)
19 (SDPI & UNODC, 2011)

challenged by the nexus between crime and the illegal economy due to its geographic location. The country's relations with its neighbors, particularly Afghanistan, are complicated by cross-border criminality, which in turn creates a thriving regional illegal economy orchestrated by complex informal and formal organized criminal networks." (SDPI & UNODC, 2011)

Illegal trade across the Pakistan-Afghanistan border is nothing new to the porous border. Renewed focus on illegal trade in discussions between Afghanistan and Pakistan stems from evidence that illegal trade has flourished in the cover of Afghan transit trade. Illegal trade associated with transit trade is conducted in two ways:[20] transit diversion (in which goods in transit through Pakistan, never reach the destination and are diverted for sale in Pakistan; and illegal re-export (where goods reach Afghanistan but are subsequently smuggled back into Pakistan across the porous border). There is no consensus on the estimate of illegal trade associated with Afghan transit trade, and estimates vary from study to study. The Pakistan Business Council study concludes that the difference in the value of transit trade reported by Pakistan and Afghanistan (reflecting illegal trade diversion) remained high at $1.0 billion in 2014 (post APTTA) but much less than $2.9 billion in 2010 (the last year of ATTA). There are few estimates of illegal re-exports from Afghanistan which make their way to Pakistan across the porous border over mountainous passes and through FATA.[21]

As always, the incentive for illegal trade comes from a price differential (or quantitative restriction) between the domestic economy and across the border. Studies have concluded that for some goods transiting through Pakistan, the level of Afghan imports bear no relevance to the consumption levels in Afghanistan and that many of these goods are primarily meant for Pakistani markets to benefit from the tariff differential between the two countries. "Pakistan's tariff rates are generally higher, particularly for the types of goods where it is argued that substantial amounts of unauthorized trade are taking place. Pakistan's average tariff rate is 14.5 percent, about 2.5 times the average tariff for Afghanistan (i.e., 5.65

[20] (USAID Pakistan, 2010).
[21] Akbar Khan Durrani, *Informal trade with Afghanistan*

percent)”.

Whatever the size of the illegal trade across the Afghanistan-Pakistan border and whatever methods are used, its impact on Pakistan’s economy is significant. One, it causes a loss to the government in tax revenues and duties, and two; it adversely impacts legal businesses and industry (USAID Pakistan, 2014). Pakistan’s concerns about illegal trade in discussions about transit trade are genuine and serious. There is a need to take effective steps to reduce illegal trade without restricting transit trade. Illegal trade can be reduced by improving border procedures, strengthening the bonded transport and guarantee system, especially build the institutional and financial apparatus to implement the TIR Convention system.

Suggestions to harmonise tariff rates between the two countries to reduce incentives for illegal trade are unrealistic in general although on a few items it’s possible. Pakistan’s tariff rates are set in view of the protection considerations of a complex economy with a relatively large industrial base, and in other cases with a view to raise revenues for a government of a large economy. In contrast, Afghanistan has no industrial base in relative terms, and tariffs have been set at low levels to stimulate trade and lower the burden on consumers.[22] Revenue generation is an important consideration for Afghanistan as well, but till recently it has been dependent on donor assistance and own revenue generation has been low. With such diverse approaches to tariff determination, the two countries are unlikely to reach agreement on the level of tariffs on all items in tariff structure. There will always be some items for which there is a strong price differential between the two countries, creating an incentive for illegal trade. And in any case illegal trade will continue if smugglers can avoid paying customs in Afghanistan where government control and tax administration is relatively ineffective in the war torn country. The answer lies in better border controls, and strengthening the bonded transport and guarantee system.

[22] Afghanistan is one of the more open economies in the region and its tariff structure is below average among LDCs. Few products are taxed above 15 percent, according to the World Bank

IV. TIR Convention[23]

International best practices in transit trade have a long history of successful implementation. The Customs Convention on the International Transport of Goods under cover of TIR Carnets (TIR Convention 1975) is one of the most successful and only universal international transport conventions. The TIR Convention facilitates the international carriage of goods from one customs office of departure to another customs office of destination through as many countries as necessary. As a rule, the vehicle remains sealed throughout the TIR transport. This, of course, requires a number of precautionary measures, such as strict customs control and secure sealing at the customs office of departure and guarantees to cover risk of customs liability.

Advantages for Customs administrations:[24]

- Reduces the normal requirements of national transit procedures.

- Avoids the need for physical inspection (expensive in manpower and facilities) in transit other than checking seals and the external conditions of containers.

- It also dispenses with the need to operate national guarantees and national documentation.

- The international transit operation is covered by a single transit document, the TIR Carnet, which reduces the risk of presenting inaccurate information to Customs administrations.

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[23] The Convention on International Transport of Goods Under Cover of TIR Carnets (TIR Convention) is a multilateral treaty that was concluded at Geneva on 14 November 1975 to simplify and harmonise the administrative formalities of international road transport. (TIR stands for "Transports Internationaux Routiers" or "International Road Transports".)

[24] UN Economic Commission for Europe (UNECE), www.unece.org/tir/system/tir-system-countries.html

- In exceptional cases where irregularities are suspected, Customs authorities have the right to inspect the goods under Customs seal at any time and, if necessary, to interrupt the TIR transport and/or to take adequate measures in accordance with national legislation.

Advantages for the Transport Industry:

- Goods may travel across national frontiers with minimum interference from Customs.

- By removing traditional impediments to the international movement of goods, the TIR system encourages the development of international trade.

- By reducing delays in transit, it enables significant savings to be made in transport costs.

- Its international guarantee chain, and relatively simple access to the required guarantees, benefits the transport and trade industry.

- By reducing the impediments to international traffic by road caused by Customs controls enables exporters and importers of land locked countries to expand trade.

In order that transporters of any country can utilize the TIR system, these must fulfill five basic requirements of the TIR system – the five pillars of the TIR Customs transit system:

- Goods should travel in Customs secure vehicles or containers;

- Duties and taxes at risk should be covered by an internationally valid guarantee;

- Goods should be accompanied by an internationally accepted Customs document (TIR Carnet), opened in the country of departure and serving as a Customs control document in the countries of departure, transit and destination;

- Customs control measures taken in the country of departure should be accepted by all countries of transit and destination;

- Access to the TIR procedure for national associations to issue TIR Carnets to act as guarantor.

Box 2: What is the TIR Convention?

"The TIR Convention[1] facilitates the international carriage of goods from one or more customs offices of departure to one or more customs offices of destination (up to a total of four customs offices departure and destination) and through as many countries as necessary. As a rule, the vehicle remains sealed throughout the TIR transport and, thus, goods are generally not inspected at border crossings. However, customs authorities remain entitled to perform inspections whenever they suspect irregularities or randomly. The Convention applies to transports with road vehicles, combinations of vehicles as well as containers and allows for the use of the TIR Carnet for all modes of transport, provided that some portion of the journey is made by road".

"This, of course, requires a number of precautionary measures, such as strict customs control and secure sealing at the customs office of departure. The TIR Convention also contains specific technical requirements for the construction of the load compartments of vehicles or containers, in order to avoid smuggling. In addition, only carriers authorized by customs are allowed to transport goods under the TIR procedure"

"To cover the customs duties and taxes at risk throughout the journey, the Convention has established an international guaranteeing chain which is managed by the International Road Transport Union (IRU). IRU is also responsible for the printing and distribution of the so-called TIR Carnet, which serves both as international Customs document and proof of guarantee".

"For more than sixty years, the TIR Convention significantly contributes to the facilitation of international transport and trade throughout the UNECE region. In addition, more and more countries from beyond the UNECE region (North Africa, Middle East, Asia) have joined the TIR Convention in recent years or are considering acceding to it."

V. TIR Convention in Afghanistan, Pakistan and Central Asia

On 21 July 2015 the Government of Pakistan deposited its instruments of accession to the TIR Convention, 1975. The Convention will enter into force for Pakistan on 21 January 2016. With the accession of Pakistan, the TIR Convention will have sixty-nine Contracting Parties including Afghanistan (re-activated since 2013), Azerbaijan, Iran, Kazakhstan, Tajikistan, and Turkmenistan.[25] Many bordering countries in the region are also signatories to the Convention including Armenia, Georgia, Mongolia, the Russian Federation and Turkey. China's accession is in the process. Thus the central Asian region is poised to take advantage of the conveniences offered by TIR Convention.

The success of the TIR System may be judged not only by the number and geographical scope of its Contracting Parties but also by the number of TIR Carnets distributed and issued every year.[26] Central Asian countries have shown extremely dynamic growth in their use of the TIR System over the past few years, in spite of the global economic downturn. The increasing use of TIR carnets can be explained by the special features of the TIR System which offers transport operators and Customs authorities a simple, flexible, cost-effective and secure Customs regime for the international transport of goods across frontiers.

Afghanistan[27]has been a member of IRU since 1983 and its membership was re-activated in 2013. However Afghanistan has issued only 2 Carnets throughout this period, while 337 TIR terminations [28]took place there. There are lessons in these statistics. Mere accession to the TIR Convention does not enable the country to reap full benefits of membership especially to enable the country to send its products through other countries in its own transport (generating jobs and income) with the ease of TIR transport. However, accession provides other countries the facility to move

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[25] UN Economic Commission for Europe (UNECE), www.unece.org/tir/system/tir-system-countries.html

[26] (IRU, 2014)

[27] (Asayesh, 2015).

[28] (IRU, 2014).

through the home country with ease. New comer Pakistan must realise that acceding to the TIR is easier than creating the system required for its utilisation. To utilise the convenience of the TIR system, both Pakistan and Afghanistan need to develop the five pillars of the TIR Customs transit system described above, including

- Appropriate transport vehicles and containers;
- Internationally valid guarantee system to cover duties and tax at risk;
- The institutional system to issue internationally acceptable customs document called TIR Carnets;
- Custom control measures which are accepted by customs in transit and destination countries;
- Access to the TIR procedure for national associations to issue TIR Carnets.

Looking beyond bilateral transit trade, developing the five pillars will be essential if Pakistan and Afghanistan want to benefit from the regional trade that the CAREC program promises. The development of good road network is essential, but corridors alone will not suffice, the countries need to improve trade facilitation and the transport system in accordance with the TIR Convention. The multilateral and bilateral donors can contribute towards helping both countries in establishing the transport and guarantee systems.

Table 2: Number of TIR CARNETS issued to ECO associations from 2005 to 07/2015

Country	Association	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015*
Azerbaijan	ABADA	5,000	5,500	9,000	9,500	7,600	7,800	9,100	11,400	10,300	4,800	2,300
Iran	ICCIMA	33,000	48,000	52,000	48,000	58,000	54,000	78,000	85,000	105,000	90,000	45,000
Kazakhstan	KAZATO	19,600	32,650	39,050	32,150	31,000	30,050	24,500	19,000	25,000	24,200	12,500
Kyrgyzstan	AIRTO-KR	6,250	11,450	18,100	17,050	15,050	14,050	20,700	17,100	22,200	20,900	7,100
Tajikistan	ABBAT	50	300	500	400	900	700	1,500	2,950	3,500	4,000	1,500
Turkmenistan	THADA	400	1,000	1,000	1,000	2,000	3,200	4,700	6,000	7,500	11,000	6,000
Turkey	TOBB	589,000	689,000	788,500	765,000	490,000	701,500	672,000	685,000	540,500	385,500	246,500
Uzbekistan	AIRCUZ	1,800	4,500	7,000	5,000	6,500	9,000	14,100	17,500	7,500	9,000	6,000
Total issued to group during year		655,100	792,400	915,150	878,100	611,050	820,300	824,600	832,950	721,500	549,400	326,900

**figures for months 1-7 of 2015 Source: IRU 2014.*

B. Bilateral Trade

Prospects for Pakistan's bilateral trade with Afghanistan are bound by Afghanistan's global trade prospects and its balance of payments projections. According to a World Bank study:[29] "Afghanistan's import-heavy trade balance reflects the large aid flows to the country's reconstruction and recovery efforts:

- The relatively high import level has been driven in the last five years mostly by the demand for goods in donor-funded projects—particularly oil, machinery, household items and food (80 percent of incoming goods);
- Import values today are more than 13 times the size of exports;
- Imports declined by 4% in 2013 and 11% in 2014 (WTO data);
- The current account deficit, ($6.7 billion in 2013) excluding grants, went from 70 % of GDP in fiscal year 2007 to 34% in 2012 (and 33% in 2013, WTO), and was financed, as in previous years, by grants;
- These grants are spent mostly on imports of goods and services; thereby not only financing the trade deficit but contributing to it.

Relative to its GDP, Afghanistan is under-performing in exports and their survivability is a challenge.

- Export/GDP ratio was 2.7% in 2014 (compared to Pakistan's exports/GDP of 10%);
- Afghan export flows to individual countries between 2005 and 2009 have often faltered and disappeared, especially those to the EU that accounted for about 20 percent of the country's export growth;
- Growth in carpet exports to Pakistan, also, dropped by 45 percent;
- Afghanistan's export base is unusually narrow, with few tradable products going to few markets;

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29 (The World Bank, 2012)

- Carpets and dry fruits account for close to three-quarters of total exports;
- The composition of exports has changed in the last 10 years, with dry fruits & seeds becoming the largest official Afghan export.

Prospects for growth in Pakistan's exports to Afghanistan are limited in view of the assessment of the IMF and World Bank about Afghanistan's economy and donor support in the years ahead. Pakistan's exports to the neighboring country are likely to be driven more by donor spending and priorities than competitiveness and market forces. A self-explanatory summary of the level, composition, and recent trends in bilateral trade with Pakistan appears in the tables and charts in Annex below.

Against the backdrop of the overall economic prospects of Afghanistan, nevertheless bilateral trade between Afghanistan and Pakistan can benefit by addressing issues related to trade facilitation. These reforms are important for both countries not only in the bilateral context, but also and more so in the regional context as regional connectivity develops in the context of CAREC program. Trade facilitation contains provisions for expediting the movement, release and clearance of goods. Both Pakistan and Afghanistan need to bring their customs and border procedures in conformity with international norms as adopted in international conventions and agreements.

In this context Pakistan has formally accepted the WTO Trade Facilitation Agreement (TFA) and submitted commitments under the category "A" provisions.[30] This means Pakistan is already moving to update its trade facilitation procedures in conformity with the WTO requirements. The TFA will come into force once two-thirds of the WTO membership has formally accepted the Agreement.[31] At the recent Trade Policy Review of Pakistan undertaken by WTO, Members were satisfied that with a view to facilitating trade and investment, Pakistan implemented a number of

[30] Provisions that the member will implement by the time the Agreement enters into force

[31] Currently (January 4, 2016) 65 ratifications submitted, 104 required

reforms, including further liberalization of the foreign investment regime, development of Special Economic Zones, enhanced competition policy, upgraded port infrastructure, and setting up a national single window.[32]

Pakistan has also acceded to the Revised Kyoto Convention (RKC). The Revised Kyoto Convention (RKC) is the main trade facilitation Customs convention. It was developed by the World Customs Organization and entered into force on 3 February 2006. It is an update and revision of the International Convention on the Simplification and Harmonization of Customs Procedures (Kyoto Convention) adopted in 1973-1974. The RKC aims at facilitating trade by harmonizing and simplifying Customs procedures and practices. To this end the Convention provides standards and recommended practices for modern Customs procedures and techniques. The RKC commits contracting parties to the following key principles:

- Transparency and predictability of Customs actions;
- Standardization, simplification of goods declaration, supporting documents;
- Simplified procedures for authorized persons;
- Maximum use of information technology;
- Minimum necessary Customs control to ensure compliance with regulations;
- Use of risk management and audit-based controls;
- Coordinated interventions with other border agencies; and
- Partnership with the traders.

Thus Pakistan has made significant international commitments to trade facilitation. The Electronic Form-E (EFE) module in the Pakistan Customs' electronic system called WeBOC (Web based One Customs) has been developed in consultation with relevant stakeholders. The EFE is available for use at border controls except for Pakistani exporters through land routes. "At present, majority of goods exported from Pakistan are handled through WeBOC.

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32 The World Trade Organization, www.wto.org/english/tratop_e/tpr_e/tpr_e.htm

However, a small percentage of goods such as those exported through land route or categorized as bulk cargo are currently being exported through Pakistan Customs' previous goods clearance system called 'One Customs'. Efforts are underway by Pakistan Customs to extend WeBOC system to export of such goods as well, in a phased manner throughout Pakistan" according to the SBP.

Box 3: State Bank of Pakistan, FE Circular No. 10 of 2015

1. Attention of Authorized Dealers is invited to Chapter XII of Foreign Exchange (FE) Manual 2002 which, inter alia, sets out rules for issuance of Form-E for export of goods from Pakistan.

2. In order to streamline issuance of Form-E, State Bank of Pakistan in collaboration with Pakistan Customs have automated issuance of Form-E. The Electronic Form-E (EFE) module in the Pakistan

   Customs' electronic system called WeBOC (Web based One Customs) has been developed in consultation with relevant stakeholders.

3. At present, majority of goods exported from Pakistan are handled through WeBOC. However, a small percentage of goods such as those exported through land route or categorized as bulk cargo are currently being exported through Pakistan Customs' previous goods clearance system called 'One Customs'. Efforts are underway by Pakistan Customs to extend WeBOC system to export of such goods as well, in a phased manner throughout Pakistan.

Afghanistan also has undertaken extensive reforms of its customs procedures and border operations according to the World Bank [33]"Customs Reform Will Strengthen Trade Facilitation." The customs reforms, which were ongoing in 2012, had:

[33] (The World Bank, 2012)

- Reorganized customs procedures;
- Improved border facilities; and
- Expedited clearance.

According to the WB, "when fully operational, the modified customs department, the Asycuda system and new customs procedures will further lower transaction costs, and improve trade facilitation and security". The World Bank in 2012 adds that "Customs efficiency has improved dramatically in recent years, with various indicators suggesting real progress in facilitation and movement of goods across Afghanistan. In the long term, however, Afghanistan needs to strengthen its border management institutions, change transport regulation policy, and invest in trade-related infrastructure".

Major customs reforms implemented by 2012 in Afghanistan:[34]

- Introduction of the Afghanistan National Tariff Schedule; which classifies goods according to international standards;
- Procedures to control and monitor exemptions;
- Roll-out of the Automated System for Customs Data (ASYCUDA);[35]
- Capacity-building and training of customs officials;
- Infrastructure development at main customs stations; and
- The establishment of regional customs valuation and post-clearance control units in the major provincial centers.

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[34] (The World Bank, 2012)

[35] In 2011, implementation of Asycuda had expanded to cover 95 percent of customs houses (and 90 percent of foreign trade value processed), according to the World Bank

As a result, the Customs reforms had significantly improved trade and logistics indicators for Afghanistan. But according to the most recent World Bank's Logistics Performance Index scores for Afghanistan, performance had declined over the last five years. Pakistan with a better score had nevertheless remained stagnant since 2006.

Table 3: Pakistan & Afghanistan Logistics Performance Index (LPI) Score

	2006-2010	2011-2015
Afghanistan	2.30	2.07
Pakistan	2.83	2.83

Source: World Bank LPI

Box 4: What is LPI?

Logistics Performance Index overall score reflects perceptions of a country's logistics based on efficiency of customs clearance process, quality of trade and transport related infrastructure, ease of arranging competitively priced shipments, quality of logistics services, ability to track and trace consignments and frequency with which shipments reach consignee within scheduled time. The index ranges from 1 to 5, with a higher score representing better performance.

Looking ahead, the WB had suggested in 2012 that "The customs reform (in Afghanistan) needs to be consolidated,...there were opportunities for improving customs administration"… "grouped into three themes: (i) Improved customs procedures (ii) Better organisation and human resource management, (iii) Greater interagency coordination". The decline in LPI suggests that the reform process may have faltered.

Trade facilitation reform in Afghanistan and Pakistan can be undertaken with technical assistance from multilateral organisations. Afghanistan is a member of the World Customs Organisation (WCO) but has not yet ratified the Revised Kyoto Convention (RKC) for committing to international best practices in custom procedures.[36] In addition, Afghanistan is about to become a member of the WTO; recently ministers formally approved Afghanistan's WTO membership terms at a special ceremony held at the WTO's Tenth Ministerial Conference (MC10) in Nairobi on 17 December 2015[37]. Afghanistan will have until 30 June 2016 to ratify the deal and would become a full-fledged WTO member 30 days after it notifies the acceptance of its Protocol of Accession to the WTO Director-General. Once Afghanistan joins the WTO, it can seek technical assistance for Trade Facilitation.

Technical assistance for trade facilitation is provided by the WTO, WTO members and other inter-governmental organisations, including the World Bank, the World Customs Organisation and the United Nations Conference on Trade and Development (UNCTAD). In July 2014, the WTO announced the launch of the Trade Facilitation Agreement Facility,[38] which will assist developing and least-developed countries in implementing the WTO's Trade Facilitation Agreement.

The 2014 LPI report of the World Bank finds that "low-income, middle-income, and high-income countries will need to take different strategies to improve their standings in logistics performance. In low-income countries, the biggest gains typically come from improvements to infrastructure and basic border management. This might mean reforming a customs agency, but, increasingly, it means improving efficiency in other agencies present at the border, including those responsible for sanitary and phyto-sanitary controls. (This would be particularly important for Afghanistan for which fruits, nuts and vegetables are important

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[36] UN Economic Commission for Europe (UNECE), *Revised Kyoto Convention 2006,* www.unece.org/contents/revised-kyoto-convention.htm

[37] (WTO, 2015)

[38] (WTO, 2014)

exportable items.) Often, multiple approaches are required. The LPI report adds that "*You can'tjust do infrastructure without addressing border management issues"*. Middle-income countries,by contrast, usually have fairly well-functioning infrastructure and border control. They generally see the biggest gains from improving logistics services, and particularly outsourcing specialised functions, such as transportation, freight-forwarding, and warehousing".

Pakistan is addressing trade facilitation shortcomings with the help of the World Bank and ADB. The Asian Development Bank (ADB) approved a $250 million loan in December 2015, to boost cross-border trade activity with its neighbouring countries by reducing customs processing time for cargo and goods at the three key border points of Chaman, Torkham, and Wagha[39] (which will directly facilitate Pak-Afghan trade).

"Customs operations have improved substantially since 2010, but border point performance has lagged due to:

- Poor infrastructure and facilities;
- Weak governance;
- Insecurity and remoteness;
- Lack of Internet access".

"The project is part of the ADB-supported CAREC program. To improve border services with other CAREC countries, Pakistan will streamline transport, trade, logistics, customs, and other trade-related border control operations. The project will construct modernised border point infrastructure and facilities, compliant with internationally accepted standards including ICT equipment and connectivity to link each border point with the central customs database, security, trade facilitation equipment, and the construction of border point infrastructure." The government will also establish the Pakistan Land Port Authority to manage national land border

[39] Asian Development Bank (ADB), www.adb.org

points. The project will also train officials and professional staff from relevant agencies to adequately run the modernized border point infrastructure and facilities, and to provide quality border point services. The project will run for 5 years, with a target completion date of December 2021.

C. Role of Private Sector Chambers

"To ensure effective and consensual implementation of APTTA, the agreement establishes the Afghanistan Pakistan Transit Trade Coordination Authority (APTTCA) which is required to meet once every six months".[40] The authority is co-chaired by representatives of Government of Afghanistan and Government of Pakistan, and includes the private sector including the Pakistan – Afghanistan Joint Chamber of Commerce and Industry (PAJCCI),[41] freight forwarders, and road transporters. The APTTCA is tasked to monitor effective implementation of APTTA and the implementation of measures adopted to curb un-authorized trade among other similar tasks. APTTCA is potentially an effective forum to undertake the tasks and responsibilities assigned to it in both Afghanistan and Pakistan, by the status and recognition given to it by the bilateral agreement, APTTA. However it needs to be strengthened by providing a voice at its deliberations to all relevant private sector stakeholders in the Pakistan Afghanistan trade environment. Specifically, the membership of PAJCCI needs to be broadened and made more inclusive on the Pakistan side as explained below, and in recognition of the different but important view of large scale businesses, the Pakistan Afghanistan Joint Business Council could also be made a member of APPTCA.

Pakistan's private sector's commercial and industrial interests are diverse and geographically widespread. It is unlikely that any one Chamber, even the Federation of Pakistan Chamber of

40 (USAID Pakistan, 2014)

41 PAJCCI was formed with the collaboration of Karachi Chamber of Commerce (KCCI), Chaman Chamber of Commerce (CCCI), Khyber Pakhtunkhwa Chamber of Commerce (KPCCI) and Afghanistan Chamber of Commerce (ACCI), recognized and licensed by the GoA and GOP.

Commerce and Industry (FPCCI) or a new chamber, can represent the diverse interests of large and small businesses from all regions. Creating one more Chamber is not likely to resolve the issue of full representation on diverse issues nor will the new chamber be able to compete with the clout of existing Chambers which have established recognition amongst their members. For this reason it is understandable that representation on PAJCCI has also been a contentious issue from its inception, with many complaints on the Pakistani side that the PAJCCI does not take the views of Chambers of various regions. In the context of the analysis above, it is recommended that all stakeholders on the Pakistan side should be included, one by broadening the base of PAJCCI and secondly by giving a seat to PAJBC at APTTCA. Among the stakeholders, there are those involved in transit trade, others in bilateral trade, then there are the industries which are hurt by illegal trade which are also important stakeholders, and finally transporters whose jobs are on the line by the Afghan demand for permission to use afghan transport inside Pakistan.

Furthermore, the private sector has a role to play in the following recommendations of this report as well:

- To overcome problems of illegal trade associated with transit trade, both Pakistan and Afghanistan need to develop their transport and guarantee system in accordance with the TIR Convention.

- To ensure the smooth and efficient flow of transit trade and bilateral trade, both countries need to upgrade their trade facilitation procedures.

With trade relations between Afghanistan and Pakistan historically under the shadow of strained bilateral political relations, the role that the private sector can play in furthering trade and economic relations at this juncture in time is secondary. The role of the private sector can be more precisely defined:

- The PAJCCI, with better representation of Chambers from regions in Pakistan that actually conduct trade with

Afghanistan, can monitor the development of trade facilitation system and report to the governments through the APTTCA.

- PAJCCI should include representatives of Chambers from the Punjab province as well since industrial units hurt by illegal trade are mostly based in the Punjab, and their views should be considered when designing Afghan trade monitoring methods to curb illegal trade.

- The reformed PAJCCI and PAJBC can play a role in forming the national association that will be part of the international guarantee chain supported by IRU, to issue the TIR Carnet.

The transport association(s) which are relevant for the transport of goods involved in transit trade and bilateral trade, should be represented on the PAJCCI, and provide their own view point to the APTTCA on matters related to giving Afghan trucks the right to transport goods inside Pakistan.

4. Policy, Institutional, and Legal Climate Impacting Investment inAfghanistan

A. Assessment of Investment Environment in Afghanistan

"The government of Afghanistan has stated a commitment in principle to fostering private-sector-led economic development and increasing domestic and foreign investment, as reflected in the Afghanistan National Development Strategy (ANDS). However, its efforts

- to build an enabling environment for a competitive private sector;
- to expand the scope of private investment by developing natural resources and infrastructure;
- and to promote investment

have been limited by institutional capacity, rent seeking behavior, and the political will to undertake necessary reforms" according to the US State Department Assessment of Investment Environment, 2015.

According to the same report, which is the most recent detailed assessment of the investment environment in Afghanistan for 2015,[42] the investment environment requires improvement. The main points in the executive summary are the following:

- The Afghan economy experienced steady economic growth averaging 10% between 2005 and 2013;

- Growth was driven largely by the international presence, including spending by international security forces and international aid agencies;

- As international assistance declines, growth is expected to be 1-2% annually in the short term and 3-4% per year in the medium term;

- The success of private sector led development will depend on the government's ability to convince reluctant investors of the business opportunities in the country and that security risks are manageable;

- At present, Afghanistan's legal and regulatory frameworks and enforcement mechanisms remain underdeveloped and irregularly implemented;

- Much of the framework necessary for encouraging and protecting private investment is not yet in place;

- The existence of three overlapping legal systems Sharia (Islamic Law), Shura (traditional law and practice), and the formal statutory system instituted under the 2004 Constitution can be confusing to both investors and legal

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[42] US Department of State, *Afghanistan Investment Climate Statement 2015*

professionals;

- Corruption affects the consistency of the application of the laws;

- Security threats limit investors' opportunities to develop businesses in some provinces;

- Certain sectors, such as mining and hydrocarbons still lack a regulatory environment that fully supports investment;

- Domestic and foreign investors rank corruption high on the list of impediments.

Table 4: Afghanistan's Ranking on some Global Investment Indices		
Measure	**Index or Rank**	**Year**
TI Corruption Perceptions index	172 of 175	2014
WB Report "Ease of Doing Business"	183 of 189	2015

Source: Transparency International, transparency.org/cpi2014/resultsThe World Bank, doingbusiness.org/rankings

B. Capital Flight Out of Afghanistan

The assessment of the investment environment is supported by news of capital flight out of Afghanistan. News reports out of Kabul over the recent years sums up what the Afghan elite think about investing in Afghanistan:

- 2012: A Financial Times Report of March 18,2012 (by Matthew Green in Kabul)[43]

"The $4.6bn of declared dollar exports via Kabul airport last

[43] Financial Times, www.ft.com/cms/s/0/a888d1fc-6f12-11e1-afb8-00144feab49a.html#ixzz3wk6s9P69

year (2011) was almost equivalent to Afghanistan's 2010-11 state budget of $4.8bn. Officials suspect that large quantities of cash also leave the country without being recorded. Noorullah Delawari, the central bank governor, said he had imposed a new rule that restricts passengers to carrying a maximum of $20,000. Anyone wishing to move more money abroad will have to make a wire transfer through a bank. Mr Delawari said the rule, introduced this month, closed a loop-hole in Afghan law that allowed passengers to carry as much money as they liked out of the country provided they filled in a form."

- The Economist Intelligence Unit has a similar report: EIU May 30th 2012: The government acts to curb capital flight [44]

- 2014: TSG Intel Brief: Afghanistan's Capital Flight and Post-2014 Future,[45] January 8, 2014

"As of early January 2014, the continued transfer of capital by Afghanistan's elites to the UAE points to persistent uncertainty among them about their country's future as US and allies prepare for draw down post-2014. …These elites appear unconvinced that the national military and police forces will be capable of countering the likely escalation in the Taliban's insurgent warfare, leading to continued—and possibly worsening—political and economic instability throughout the country.

Well before the announcement of the 2014 date for departure of Western forces, Afghan businessmen have been concerned with the lack of safe investment opportunities in Afghanistan, where corruption and infrastructural inefficiencies are widespread. The Afghan elite's capital flight has been accompanied by a slowdown in new building construction in Kabul and an increase in the number

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44 The Economist Intelligence Unit www.country.eiu.com/article.aspx?articleid=1109075895&Country=Afghanistan&topic=Economy&subtopic=Forecast&subsubtopic=Policy+tren ds&u=1&pid=1873762971&oid=1873762971&uid=1

45 www.soufangroup.com/tsg-intelbrief-afghanistans-capital-flight-and-post-2014-future

of high-end houses up for sale, with their owners reportedly seeking to shift assets abroad. As a result, the prices of such properties have declined by as much as 35 percent since 2011, according to a September 2013 *NBCNews* report".

C. State Bank of Pakistan Rules About Investment Abroad

The laws in Pakistan allow investors to invest abroad in Afghanistan and the rest of the world, as the SBP circular below states clearly. But the question is that with alternative investment avenues in Dubai, and all over the world, will Pakistani investors go to Afghanistan where the prospects are very uncertain in the assessment of multilateral institutions like the IMF, World Bank and even the US State Department.

The State Bank of Pakistan's F.E. Circular no. 12, September 1, 2001 [46]contains Rules about Investment Abroad by Residents of Pakistan. The rules relevant for this discussion are reproduced here:

> *"In supersession of the instructions contained in F.E. Circular No.11 of 1995, it has been decided to allow residents of Pakistan including firms and companies to make equity based investment (other than portfolio investment) in companies (whether incorporated or not)/Joint Ventures abroad on Repatriable basis, with prior permission of State Bank of Pakistan and subject to the following guideline (among others):*
>
> - *Investment abroad is allowed only for those countries that allow repatriation of profits, dividends and capital.*
>
> - *Funding for the proposed investment abroad would be allowed only from the inter-bank market or from funds available in the foreign currency accounts of investors opened in terms of FE 25 of 1998, or out of funds available in the incremental deposits of frozen foreign currency accounts, or from Foreign Currency accounts maintained by exporters in terms*

[46] State Bank of Pakistan, www.sbp.org

of Para 29 Chapter XII of Foreign Exchange Manual/FE 25 of 2000 (net of amount paid to foreign importers/agents).”

Afghanistan’s Foreign Exchange Conversion and Transfer Policies [47]state that Private investors have the right to transfer capital and profits out of Afghanistan, including for off-shore loan debt service. There are no restrictions on converting, remitting, or transferring funds associated with investment, such as dividends, return on capital, interest and principal on private foreign debt, lease payments, or royalties and management fees, into a freely usable currency at a legal market clearing rate.

Thus there are no legal restrictions on Pakistani investment in Afghanistan as long as these conform to the rules above and those in F.E. Circular no.12.

D. Prospects of Pakistani Investment in Afghanistan

There needs to be a sense of realism when discussing Pakistani investment in industry in Afghanistan. Private sector investment has been declining even in Pakistan during the last five years due to the security situation and weak infrastructure in Pakistan. It will be difficult to expect that Pakistani investors will invest in industry in Afghanistan under the present circumstances and assessment described above, especially when there is a persistent political trust deficit between the two countries with security related undertones. In the future as peace efforts gain momentum and the legal and institutional framework improves, investment in Afghanistan could become more attractive.

[47] *Afghanistan Investment Climate Statement 2015*, US Department of State

Annex 1

Impediments in Pak-Afghan Trade

I. Trade Facilitation

- Permits issued by the Political Agent Khyber Agency are issued to non exporter / traders (Consolidated Report of Post Afghan Visit Review Committee (May 7, 2015) KPK government).

- Delay in clearance of the goods is faced due to procedural hiccups i.e. PRAL, WeBoC.

- For the purpose of Registration of Goods Documents (GD), there is no dependable computerised system available, and during power break-downs non-availability of back-up power supply.

- Insufficient space is available, for goods clearance and handling.

- Valuation Committee is prone to indecision resulting problems and discrepancies in export and import.

- For regular exporters to Afghanistan, the process should be simplified in order to facilitate consignments. Previously the process was completed within a single day, now, in the present regime, the process has started taking considerable times / delays.

- Registration of Pharmaceuticals products in Afghanistan are delayed due to administrative matters, sometimes it takes years register products, which is too costly.

- Also, some companies that are already registered in Afghanistan are being asked to re-validate their registration requiring documents and company products.
- Trolleys and trucks are sometimes delayed by 2 to 3 days

because the system installed at Torkhum is not very organised and systematic. At the time of this study the customs automated We boc facility on the Pakistani side of the borders does not synchronise with the automated facility at the border crossings in Afghanistan (Shabbir & Ahmed, 2015).

- Time and cost are of critical importance in international transit. On both fronts, Pakistan has significant scope for improvement. To effectively participate in corridor 5 and act as an access point for CAR, improvement in both parameters is imperative for Pakistan (USAID Pakistan, 2014).

- Major delays in transit are due to delays in filing, processing of goods declaration forms.

- Time consuming registration of a bonded carrier and poor infrastructure.

- Lack of harmonisation and inadequate communication between the Pakistan and Afghanistan customs departments also hinder in the timely completion of transit.

- Pakistan's non-accession to TIR convention also encumbers its connectivity with Central Asia. Afghanistan and the Central Asian Republics (CAR's) have acceded to the TIR convention. Accession to TIR is vital for Pakistan to connect with CAR's and beyond.

- Similarly non-existence of risk management system in customs operations leads to time-consuming examination even on low risk consignments.

- Complaints regarding road and customs clearance, infrastructure in both countries. According to business community, the current practice of checking all containers rather than a randomised selection slows the transit process, and repeats checks on both the Afghan and Pakistan side of the border add additional transit time (Hussain & Elahi, 2015).

II. Transit and Transport Issues

- Monopoly of bonded carrier, on charging exorbitant freight fare as NLC has been deleted in the new APTTA.[48]

- Compensation by the carriers not being given to the owner of goods in case of theft, pilferage and damages.

- Computerised system at check posts en-route i.e. Hyderabad, Multan and Kohat are mostly out–of–order, and creates delay / passage problems.

- NLC other than routine processing charges is now been charging additional sum of Rs. 2500 per truck to Kabul.

- There is a Government Backed transporter union on Afghan side, which creates problems in smooth flow of transport for their personal benefits.

- Guarantee / Securities taken to the extent of 110%.

- Transit time of the truck / container is only 5 days with no special relaxation in breakdown is allowed.

- Afghan Gov. does not allow Tajik trucks beyond their border and similarly Pakistani trucks not permitted to deliver goods at Afghanistan. This is one of the main hurdles to the transit trade and establishes the monopoly of the Afghan trucks dealers.

- Afghan Transit Trade issues addressed on daily basis in Karachi instead revolving basis.

[48] KPK Committee

- Lack of reliable road or rail infrastructure, transportation bottlenecks (Shabbir & Ahmed, 2015) .

- High cost of transit through Pakistan and Afghanistan in comparison to other international routes is also a foremost concern in using corridor 5 as a transit route (USAID Pakistan, 2014).

- Under Article 3 of Protocol 2, a bank guarantee, revolving bank guarantee or Carnet-de-Passage is required for the temporary admission of commercial vehicles. The banks in both countries are reluctant to issue such guarantees, thereby hampering the movement of transport units carrying transit goods. This issue was temporarily resolved during the third APPTCA meeting, where Pakistan provided special dispensation to Afghan trucks to enter Pakistan on the production of letter of guarantee from Afghanistan Ministry of Transport. Both sides need to develop a permanent solution. Once Pakistan accedes to the TIR convention, this issue could be resolved, as TIR Carnet allows temporary admission of commercial vehicles carrying transit goods (USAID Pakistan, 2014).

- The Agreement uses financial securities for the release of goods transiting through the territory of the contracting parties. This created problems for traders since bank charges for such guarantees were very high. This issue was temporarily resolved by APTTCA when Pakistan agreed to release Afghan transit goods on the production of insurance guarantees. A large number of insurance guarantees are pending release with Pakistan customs authorities despite the fact that the goods have reached their destination. The delay has been due to non-production of goods declaration being demanded by Pakistan customs authorities. This issue has also been temporarily resolved after Pakistan agreed to release the insurance guarantees on production of T-1 document by Afghan customs. The successful implementation of EDI by both sides would help expedite the release of insurance guarantees being submitted by Afghan traders as security for the release of transit consignments (USAID Pakistan, 2014).

- Afghanistan has not yet notified its customs transit rules required under the Agreement. Despite repeated requests by Pakistan, the Afghan Government has been providing assurances for notification of the customs transit goods soon. Pakistan needs to impress upon the Afghan side to notify the customs transit rules soon. This would create transparency for Pakistani traders to use the territory of Afghanistan for transit to Central Asia (USAID Pakistan, 2014).

- Pakistan is maintaining a sensitive list of the products for which transit is not allowed. This list includes auto parts and cigarettes. With proper risk management system in place, Pakistan may consider eliminating the sensitive list to facilitate the transit trade of Afghanistan (USAID Pakistan, 2014).

- The agreement uses three layers of security to ensure there are no leakages during transit. The release of goods requires production of insurance guarantees equal to the leviable duties and taxes. The transport is to be carried through bonded carriers only. The containers and transport units are to be installed with tracking devices. These excessive security layers have increases the cost of transit for Afghan traders. Pakistan may consider easing these layers to facilitate the Afghan transit trade (USAID Pakistan, 2014).

- Removal of Shipping Restrictions. In April 2015, it was also agreed that Afghan trucks bound for India would be allowed to reach the Wagah border crossing, and on their way back would be allowed to carry Pakistani exports to Afghanistan, a provision removing previous restrictions. This should help Afghan businessmen significantly reduce the cost of transportation. Similarly, Pakistan-origin trucks are allowed to transit through into Afghanistan without reloading. It is expected that customs revenues for Pakistan will increase as a result of more trade through Wagah. The truck companies in Afghanistan can become the major beneficiaries of this relaxation by investing in the trucks and the transport systems (Hussain & Elahi, 2015)

III. En Route Security Issues

- KPK: 03 security check posts of F.C viz at Jamrud, Takhta Bag-Michini and Torkham.
- Border tensions (Shabbir & Ahmed, 2015).
- Furthermore, excessive checks on the transit consignments by the law enforcing agencies other than customs of both countries also cause delays in the movement of traffic and increase the transactional cost for trade (USAID Pakistan, 2014).

IV. Customs Procedures

Pakistan (KPK) side:

- Bank Guarantees are on consignment-to-consignment basis and not on revolving basis.
- Customs Act 1969 allow for 10% check, but frequent and excessive checks up to 110% and verifications of goods in transit are applied.

- Scanner Machine is mostly found out of order

Afghan side:

- Value of goods is being done arbitrarily by the custom in Afghanistan at Gumrak.

- Truck weightage allowances vary from time to time.

- Delay in clearance from Afghanistan occurs.

- All medicine's export via Torkham border are scrutinised intensely and cumbersome export documentation at times delay the shipments on border for days.

- Live Broiler Chicken export is banned to Afghanistan but all other products are allowed including processed chicken, layer, breede.

- On the Afghan side, traders complain that Afghan-origin products are sold back to Afghanistan from Pakistan at higher prices, forcing Afghanis to pay custom duties on their own goods. Afghan merchants also accuse Pakistani customs officials of regularly extracting bribes to clear the border or to obtain necessary visas or other paperwork. There are as well Afghan concerns about low-cost imports from Pakistan displacing Afghan production of agricultural and other goods (Hussain & Elahi, 2015).

- Many of the respondents believed that their businesses were adversely impacted due to the inefficient and opaque practices of customs (Ahmed, 2015).

- Similarly more than 50 percent were not satisfied by the examination of goods undertaken by the customs authorities.

- Only 15 percent of the firms had been able to file any complaints against APTTA due to the cumbersome grievance redressal mechanisms (entailing high transactions costs).

- There also appears to be a communication gap between the business community and the relevant authorities, as the relevant authorities never addressed 80 percent of the complaints.

V. Illegal Trade

- KPK: There is a huge Illegal movement on border of Afghan to Pakistan that needs to be restricted.

- Half of the respondents reported that APTTA has led to an increase in informal trade and smuggling (SDPI & UNODC, 2011).[49]

- Thriving trade via informal channels reduces incentives for formal trade (Hameed, 2012). Estimates of informal trade between Afghanistan and Pakistan vary across anecdotal evidence. This amount is said to be equivalent to or greater than formal trade between both countries.

- Smuggling and Spillover. Afghan proposals to allow the transit of imports from India through Pakistan have been met with resistance, in part owing to Pakistani concerns that they may be dumped instead in Pakistan, affecting local industry. Illicit trade between Afghanistan and Pakistan is a long-standing concern on the Pakistan side; a 2011 study by Pakistan's Federal Tax Ombudsman noted that several high-tariff goods, including vehicles, cigarettes, and electronic items, were being smuggled from Afghanistan to Pakistan.7 Officials estimate that three quarters of all goods smuggled into Pakistan come through the APTTA before being

[49] Informal trade may not be pure smuggling of goods if it comes under extra-legal trading and tolerated in practice by the State even if illegal by law. Our distinction between informal trade and smuggling follows Taneja and Pohit (2004).

diverted to Pakistani markets, evading the imposition of customs duties.8 Trade Controls. At the same time, efforts to control and combat smuggling and other misuses of the transit trade agreement provoked complaints from traders interviewed on both sides of the border. Requirements that traders obtain certified customs clearance documents, restrictions on partial shipments of goods that require all trucks of a given shipment to be present before trucks can cross into Afghanistan, and heavy security deposits, insurance, and shipment tracker installation costs all increase truckers' costs of operations and strain their limited working capital (Hussain & Elahi, 2015).

VI. Tariff Issues

- KPK: irrational tariff-regime.
- No duty free access.

VII. Banking and Payments Issues

- KPK: Existence of only one bank with no online system and foreign exchange facilities and with no Form-E facility. No proper banking system at Torkham border compels Exporters/Importers to use illegal ways of payment.
- Formal banking ties between Afghanistan and Pakistan remain limited, with traders on each side of the border forced to rely on unofficial transfers, and with inconsistent exchange rates.

VIII. Market Issues

- Pakistani businessmen unaware of Afghan market potential (Shabbir & Ahmed, 2015).

IX. Competitiveness

- $5 billion target cannot be achieved because declining competitiveness of Pakistani products (Shabbir & Ahmed, 2015).

Annex 2

The UN Convention on the Law of the Sea,[50] 1982 Part XRight of access of land-locked states to and from the sea and freedom of transit

- *Article 125: Right of access to and from the sea and freedom of transit*

  - Land-locked States shall have the right of access to and from the sea for the purpose of exercising the rights provided for in this Convention including those relating to the freedom of the high seas and the common heritage of mankind. To this end, land-locked States shall enjoy freedom of transit through the territory of transit States by all means of transport.

  - The terms and modalities for exercising freedom of transit shall be agreed between the land-locked States and transit States concerned through bilateral, sub-regional or regional agreements.

  - Transit States, in the exercise of their full sovereignty over their territory, shall have the right to take all measures necessary to ensure that the rights and facilities provided for in this Part for land-locked States shall in no way infringe their legitimate interests.

- *Article126: Exclusion of application of the most-favoured-nation clause*

  - The provisions of this Convention, as well as special agreements relating to the exercise of the right of access to and from the sea, establishing rights and facilities on

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[50] UN Division for Ocean Affairs and the Law of the Sea, *United Nations Convention on the Law of the Sea of 10 December 1982*; www.un.org/depts/los/convention_agreements/texts/unclos/UNCLOS-TOC.htm

account of the special geographical position of land-locked States, are excluded from the application of the most-favoured-nation clause.

- *Article127: Customs duties, taxes and other charges*

  - Traffic in transit shall not be subject to any customs duties, taxes or other charges except charges levied for specific services rendered in connection with such traffic.

  - Means of transport in transit and other facilities provided for and used by land-locked States shall not be subject to taxes or charges higher than those levied for the use of means of transport of the transit State.

- *Article128: Free zones and other customs facilities*

  - For the convenience of traffic in transit, free zones or other customs facilities may be provided at the ports of entry and exit in the transit States, by agreement between those States and the land-locked States.

- *Article129: Cooperation in the construction and improvement of means of transport*

  - Where there are no means of transport in transit States to give effect to the freedom of transit or where the existing means, including the port installations and equipment, are inadequate in any respect, the transit States and land-locked States concerned may cooperate in constructing or improving them.

- *Article130: Measures to avoid or eliminate delays or other difficulties of a technical nature in traffic in transit*

  - Transit States shall take all appropriate measures to avoid delays or other difficulties of a technical nature in traffic in transit.
  - Should such delays or difficulties occur, the competent

authorities of the transit States and land-locked States concerned shall cooperate towards their expeditious elimination.

❖ *Article131: Equal treatment in maritime ports*

- Ships flying the flag of land-locked States shall enjoy treatment equal to that accorded to other foreign ships in maritime ports.

❖ *Article132: Grant of greater transit facilities*

- This Convention does not entail in any way the withdrawal of transit facilities which are greater than those provided for in this Convention and which are agreed between States Parties to this Convention or granted by a State Party. This Convention also does not preclude such grant of greater facilities in the future.

Annex 3

GATT 1994 Article V: Freedom of Transit

I. Goods (including baggage), and also vessels and other means of transport, shall be deemed to be in transit across the territory of a contracting party when the passage across such territory, with or without trans-shipment, warehousing, breaking bulk, or change in the mode of transport, is only a portion of a complete journey beginning and terminating beyond the frontier of the contracting party across whose territory the traffic passes. Traffic of this nature is termed in this article “traffic in transit”.

II. There shall be freedom of transit through the territory of each contracting party, via the routes most convenient for international transit, for traffic in transit to or from the territory of other contracting parties. No distinction shall be made which is based on the flag of vessels, the place of origin, departure, entry, exit or destination, or on any circumstances relating to the ownership of goods, of vessels or of other means of transport.

III. Any contracting party may require that traffic in transit through its territory be entered at the proper custom house, but, except in cases of failure to comply with applicable customs laws and regulations, such traffic coming from or going to the territory of other contracting parties shall not be subject to any unnecessary delays or restrictions and shall be exempt from customs duties and from all transit duties or other charges imposed in respect of transit, except charges for transportation or those commensurate with administrative expenses entailed by transit or with the cost of services rendered.

IV. All charges and regulations imposed by contracting parties on traffic in transit to or from the territories of other contracting parties shall be reasonable, having regard to the conditions of the traffic.

V. With respect to all charges, regulations and formalities in connection with transit, each contracting party shall accord to traffic in transit to or from the territory of any other contracting party treatment no less favourable than the treatment accorded to traffic in transit to or from any third country.

VI. Each contracting party shall accord to products which have been in transit through the territory of any other contracting party treatment no less favourable than that which would have been accorded to such products had they been transported from their place of origin to their destination without going through the territory of such other contracting party. Any contracting party shall, however, be free to maintain its requirements of direct consignment existing on the date of this Agreement, in respect of any goods in regard to which such direct consignment is a requisite condition of eligibility for entry of the goods at preferential rates of duty or has relation to the contracting party's prescribed method of valuation for duty purposes.

VII. The provisions of this Article shall not apply to the operation of aircraft in transit, but shall apply to air transit of goods (including baggage).

Table 5: Pakistan: Composition of Imports from Afghanistan 2010-14 (by sector/goods)										
Goods	2010		2011		2012		2013		2014	
	Import Product Share (%)	Import (US$ Thousand)	Import Product Share (%)	Import (US$ Thousand)	Import Product Share (%)	Import (US$ Thousand)	Import Product Share (%)	Import (US$ Thousand)	Import Product Share (%)	Import (US$ Thousand)
Animal	0.1	198.4	0.2	383.0	0.1	123.0	0.2	555.5	0.0	155.5
Chemicals	1.2	1,670.0	0.0	13.8	0.0	22.5	0.0	1.6	0.0	3.0
Food Products	0.2	233.6	0.1	140.7	0.0	54.4	0.0	20.4	0.1	183.2
Fuels	1.4	1,914.1	18.5	36,823.2	25.4	59,622.5	18.1	55,686.2	22.6	88,509.5
Hides & Skins	2.3	3,136.9	1.2	2,470.5	1.2	2,878.2	0.9	2,681.5	1.3	4,955.0
Mach & Elec	0.2	311.5	0.4	875.1	0.6	1,427.1	0.8	2,299.1	0.8	3,159.6
Metals	22.0	30,477.4	34.9	69,638.1	20.0	47,022.4	13.6	41,841.2	21.7	84,913.3
Minerals	4.4	6,074.5	7.7	15,452.3	1.1	2,642.5	5.4	16,685.1	9.8	38,406.4
Miscellaneous	0.2	333.8	0.0	33.4	0.0	33.1	0.0	28.7	0.0	26.6
Plastic or Rubber	0.0	36.7	0.0	9.0	0.0	6.9	0.0	20.6	0.0	78.3
Stone & Glass	0.0	6.2	0.2	381.8	0.2	380.9	0.0	80.4	0.1	251.4
Textiles & Clothing	45.4	62,840.7	16.2	32,412.5	29.4	69,201.1	41.3	127,139.8	18.0	70,515.6
Transportation	0.1	118.0	0.2	412.5	0.1	195.1	0.1	325.2	0.0	70.3
Vegetable	19.5	27,003.7	18.6	37,011.1	21.3	50,000.1	19.4	59,596.4	25.6	100,354.6
Wood	2.9	4,020.0	1.7	3,472.1	0.6	1,481.1	0.2	635.7	0.2	584.0

Source: World Bank, World Integrated Trade Solution, wits.worldbank.org

Table 6: Pakistan: Composition of Exports to Afghanistan 2010-14 (by sector/goods)										
Goods	2010		2011		2012		2013		2014	
	Export Product Share (%)	Export (US$ Thousand)	Export Product Share (%)	Export (US$ Thousand)	Export Product Share (%)	Export (US$ Thousand)	Export Product Share (%)	Export (US$ Thousand)	Export Product Share (%)	Export (US$ Thousand)
Animal	4.0	67,414.8	3.5	94,303.3	4.3	90,415.5	5.6	112,465.4	5.0	92,997.2
Chemicals	3.4	57,500.4	3.0	80,370.8	5.3	112,027.8	6.4	127,846.1	7.1	132,772.9
Food Products	3.8	63,469.8	4.8	128,323.3	7.4	156,232.2	14.8	294,848.8	16.5	310,789.4
Footwear	0.1	1,417.2	0.1	3,134.4	0.2	3,221.8	0.2	2,918.3	0.3	4,926.1
Fuels	39.3	662,707.1	29.2	776,315.2	0.2	5,092.3	1.3	25,478.9	5.8	108,275.8
Hides & Skins	0.0	71.6	0.0	121.6	0.1	1,696.2	0.0	296.8	0.0	54.5
Mach & Elec	2.5	42,802.6	2.0	54,296.4	2.8	59,674.0	4.3	85,753.5	4.6	87,136.5
Metals	6.9	116,533.6	6.4	170,119.7	10.0	210,629.3	6.2	123,019.3	6.5	122,988.4
Minerals	11.0	185,601.5	9.2	244,795.2	15.4	322,201.3	14.2	282,758.7	12.8	240,211.1
Miscellaneous	0.3	5,197.2	0.4	10,647.9	3.4	71,935.1	0.1	2,515.7	0.5	9,889.0
Plastic or Rubber	3.8	64,540.2	3.8	101,147.8	5.6	117,409.7	4.8	96,411.1	2.7	51,196.1
Stone & Glass	0.7	11,931.6	0.7	18,824.1	0.7	15,282.6	0.6	11,288.7	0.5	9,246.5
Textiles & Clothing	0.4	6,627.2	0.9	23,965.8	1.4	29,857.4	0.6	11,465.6	1.2	23,337.5
Transportation	1.0	16,805.1	0.8	20,668.6	0.6	12,472.8	0.4	7,043.0	0.5	9,662.4
Vegetable	20.9	351,795.6	33.2	883,500.1	40.0	839,429.3	38.1	761,931.5	32.9	617,310.9
Wood	1.8	30,250.6	1.9	49,761.3	2.5	51,705.2	2.6	52,069.2	3.1	58,348.6

Source: World Bank, World Integrated Trade Solution, wits.worldbank.org

Table 7: Afghanistan Import Partners 2010-14										
Rank	2010		2011		2012		2013		2014	
	Country	% share	Country	% share	Country	% share	Country	% share	Country	% share
1	Uzbekistan	21.1	Pakistan	13.7	Unspecified	50.0	Unspecified	76.8	Unspecified	44.3
2	China	13.7	Russia	12.6	Pakistan	14.2	Pakistan	10.4	Iran	19.5
3	Pakistan	11.6	Uzbekistan	11.5	China	11.5	Iran	8.4	Pakistan	17.3
4	Japan	9.6	Iran	9.1	Japan	9.7	Germany	2.0	China	13.5
5	Germany	8.2	China	9.0	Iran	8.0	China	1.6	Japan	3.4
6	Iran	7.5	Japan	6.4	Germany	4.2	India	0.5	India	1.4
7	Kazakhstan	4.0	Turkmenistan	5.5	India	1.9	Japan	0.3	Germany	0.7

Source: World Bank, World Integrated Trade Solution, wits.worldbank.org

Fig. 1: Afghanistan Imports (% partner share) 2010-14

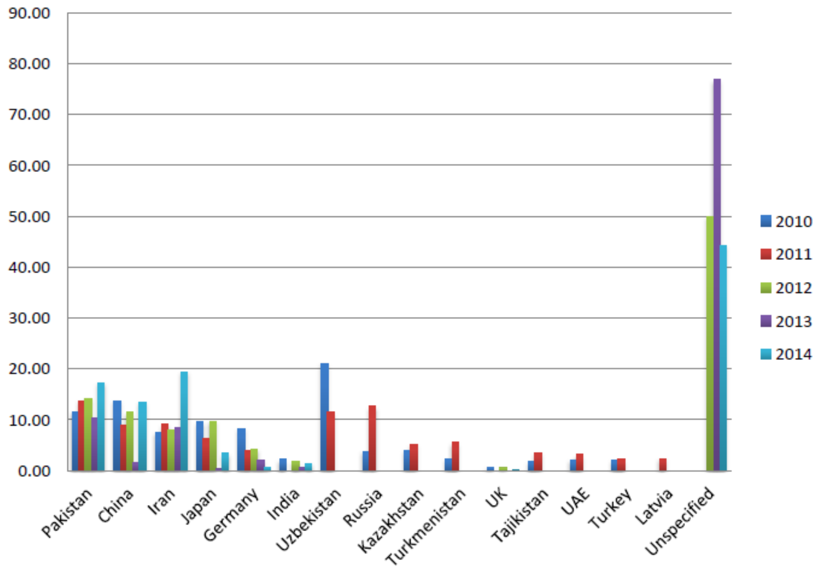

Table 8: Afghanistan Export Partners 2010-14

Rank	2010		2011		2012		2013		2014	
	Country	% share	Country	% share	Country	% share	Country	% share	Country	% share
1	Pakistan	39.0	Pakistan	48.1	Pakistan	47.0	Pakistan	38.5	Pakistan	33.0
2	India	16.8	India	18.7	Unspecified	28.7	Unspecified	27.4	India	28.0
3	Turkey	9.0	Russia	8.8	India	16.3	India	20.0	Unspecified	27.3
4	Iran	8.2	Iran	5.2	Iran	6.2	Iran	8.3	Iran	5.9
5	Russia	7.6	Iraq	4.1	China	1.1	China	3.9	Germany	3.0
6	China	3.0	Turkey	3.1	Saudi Arabia	0.4	Germany	1.8	China	2.7
7	Netherlands	2.4	Finland	1.6	Germany	0.4	Saudi Arabia	0.1	Saudi Arabia	0.1

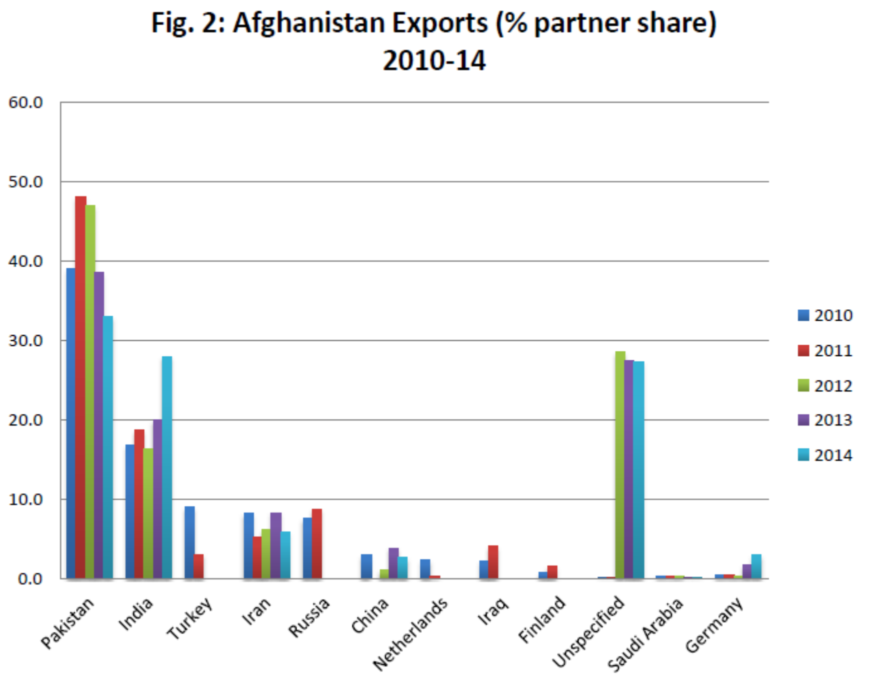

Fig. 2: Afghanistan Exports (% partner share)
2010-14
60.0
50.0
40.0
30.0
20.0
10.0
0.0
Pakistan
India
Turkey
Iran
Russia
China
Netherlands
Iraq
Finland
Unspecified
Saudi Arabia
Germany
2010
2011
2012
2013
2014

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