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Report- Roundtable Discussion

Pakistan-Afghanistan Cooperation on Trade: Political Economy Analysis

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Pictures of the Event





Pakistan-Afghanistan Cooperation on Trade: Political Economy Analysis

The Institute of Strategic Studies Islamabad (ISSI) organised a Roundtable Discussion on March 21, 2016 with Dr. Muhammad Zubair, former Federal Minister for Commerce on his report "*Pakistan-Afghanistan Cooperation on Trade: Political Economy Analysis*". Federal Minister for Commerce, Engineer Khurram Dastgir Khan was the Chief Guest at the Roundtable. Other keynote speakers at the occasion included Mr. Mansoor Ahmad Khan, Director General (Afghanistan & ATDC), Ministry of Foreign Affairs, and Mr. Javed Ghani, Director General Customs (Transit & Trade), Ambassador Ayaz Wazir, Dr. Mansoor Akbar Kundi, former Vice Chancellor Gomal University, and Mr. Akhlaque Khattak, Chief Customs, Federal Board of Revenue.

The Roundtable Discussion was formally opened by Director General ISSI, Ambassador Masood Khan, who introduced the author and the report. He appreciated the report as very timely and on a subject which is very important for Pakistan-Afghan Relations. He said that the report covered all aspects of the relations- economic, political, and also strategic.

In his presentation of the report, Dr. Zubair said that cross-border trade between Pakistan and landlocked Afghanistan has many dimensions: transit trade to Afghanistan, bilateral formal trade, illegal trade, transit trade to other double landlocked countries, and regional trade. The multi-dimensional trade across the Afghanistan- Pakistan border has not only been the subject of political debate, negotiations and bilateral agreements, but also a source of tensions between the neighbouring 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 neighbours have suffered, marred by unmet expectations and implementation problems that have been a cause of mistrust between the two 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.

Trade between Afghanistan and Pakistan carry vastly different importance for the neighbouring countries. While Afghanistan is a landlocked country reliant on Pakistan for transit and bilateral trade, Pakistan is located advantageously on the open seas and Afghanistan is relatively less significant as a trade partner. However, Pakistan is the largest destination for exports from Afghanistan. Afghan exports to Pakistan constitute 33% of the country's total exports, whereas Pakistan's exports to Afghanistan are merely 7% of its total exports, and these too are declining.

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 Central Asian Republics (CARs). The economies of Afghanistan and its four Central Asian neighbours together are a somewhat larger market - about 60 per cent of the size of Pakistan's economy. Pakistan's proximity to Afghanistan and the CARs gives the country 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.

Even so, the importance of CARs for Pakistan's economy should not be overstated, especially in view of Pakistan's much bigger share of trade (90 per cent of total trade) with much larger markets in Europe, USA and East Asia. 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 programmes 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 programme 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) programme 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 landlocked and rely almost exclusively on overland transport for trade within the region and with markets outside. The CAREC 2020 programme aims to expand and develop the current underdeveloped network of roads and railways within the region into six major transport corridors. Two CAREC corridors 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 programme 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 future, CPEC can provide alternative interlinking route to by-pass conflict-stricken Afghanistan.

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 recognised the 2,400 km 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. In recent years, illegal trade, unauthorised movement of people and contraband smuggling across the porous common border has further contributed to tensions. But trade between the two countries has grown over the years.

There is a long list of strains in economic relations between the two countries. These strains reflect Afghanistan's claims that Pakistan has not removed 'impediments' to trade. Pakistan

claims that illegal trade under the cover of Afghan transit trade hurts Pakistani business interests and causes losses in government revenue. Various government committees, business forums and studies have identified Pak-Afghan transit and bilateral trade complaints; these issues are related to: trade facilitation, transit and transport, en route security, customs procedures, illegal trade, tariffs, banking and payments, competitiveness, and infrastructure.

In order to remove these tensions in Pak-Afghan trade relations, both countries should adopt international best practices and address difficulties in the context of the institutional and legal framework of their international commitments through formal structured negotiations. This approach will lower tensions, reduce acrimony and further trade in the interest of both countries. The gains for both Afghanistan and Pakistan in undertaking reforms to reduce impediments to cross-border trade will far outweigh those associated with bilateral trade expansion, as reforms facilitate regional integration as well

The issue of transit trade figures prominently in Pak-Afghan relations. Afghanistan's access to open seas through Pakistan was formalised in 1965 through Afghan Transit Trade Agreement (ATTA), years before the United Nations Convention on the Law of the Sea (UNCOLS) December 1982. A more comprehensive agreement was reached in 2010, called Afghanistan-Pakistan Transit Trade Agreement (APTTA). The APTTA defines: transit routes, mode and nationality of transport, bank guarantees and insurance cover for traders and transporters. Pakistan has exercised its rights under the UNCOLS, ensuring that APTTA "in no way infringe(s) (on its) legitimate interests." Afghanistan's demand of access to India overland Pakistan through Wagah is not rooted in the UN Convention UNCOLS. The rights of access to the seas articulated in the UNCOLS also apply to the landlocked Central Asian countries transiting through Afghanistan.

The problems with regard to Transit Trade mainly relate to transport vehicles, routes, security, customs procedures, bank guarantees, and illegal trade. Difficulty arises due to conflicting objectives of smooth movement of transport and reducing illegal trade under the guise of transit trade. The solution to these problems lies in full adoption of international best practice for transit trade, 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, and building the institutional and financial apparatus to implement the TIR Convention system. As both Afghanistan and Pakistan are now signatories to the TIR Convention, they can utilise it to overcome the impediments in their bilateral ties. However, mere accession to the TIR Convention is not enough, and both Pakistan and Afghanistan need to develop the five pillars of the TIR customs transit system, which are:

- 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; and

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

Another major issue in Pak-Afghan economic relations is that of illegal trade. Illegal trade across Pakistan's borders and the coastline is widely acknowledged. Illegal trade has many adverse implications for both countries' economies as it is informal economy which evades taxes, deals in contraband and other criminal activities, raises the cost for conducting legal economic activities, threatens development opportunities, undermines the rule of law and keeps countries trapped in a cycle of poverty and instability. 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. There is a need to reduce illegal trade without restricting transit trade. The solution to this problem can be found by improving border procedures, strengthening the bonded transport and guarantee system, and, especially, building the institutional and financial apparatus to implement the TIR Convention system.

As far as the issues in bilateral trade are concerned, prospects for growth in Pakistan's exports are limited in view of the assessment of the IMF and World Bank that Afghanistan's economy in the years ahead is likely to be driven more by donor spending and priorities than competitiveness and market forces. Nevertheless, bilateral trade can benefit by addressing issues related to trade facilitation. Trade facilitation contains provisions for expediting the movement, release and clearance of goods. It needs to be emphasised that reforms are important for both countries in the bilateral context, and more in the regional context. Trade facilitation reform can be undertaken with technical assistance from multilateral organisations.

Both countries should find solutions for expediting the movement, release and clearance of goods. They need to bring their customs and border procedures in conformity with international norms as adopted in international conventions and agreements. Pakistan has formally accepted the WTO Trade Facilitation Agreement (TFA), and submitted commitments under the category "A" provisions. Pakistan has also acceded to the Revised Kyoto Convention (RKC). The Revised Kyoto Convention (RKC) is the main trade facilitation Customs Convention. Moreover, Pakistan is addressing trade facilitation shortcomings with ADB and the World Bank assistance. Afghanistan also has undertaken extensive reforms of its customs procedures and border operations according to the World Bank. 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.

And last but not the least, both countries should strive to improve implementation of APTTA. APTTA established the Afghanistan Pakistan Transit Trade Coordination Authority (APTTCA) which includes private sector representatives, to monitor effective implementation of APTTA and measures adopted to curb illegal trade. APTTCA 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 (Pakistan-Afghanistan Joint Chamber of Commerce and Industry) needs to be broadened and made more inclusive on the Pakistan side to include: giving a seat to PAJBC (Pakistan-Afghanistan Joint Business Council) at APTTCA. Specifically, stakeholders involved in transit trade, bilateral trade, the industries

hurt by illegal trade and transporters who lose jobs if Afghan demand for permission to use Afghan transport inside Pakistan is accepted, should be consulted.

The Chief Guest at the Roundtable Discussion, Engineer Khurram Dastgir Khan speaking on the occasion said that earlier, many people used to see Afghanistan as extension of FATA (Federally Administered Tribal Areas) with both the regions having one economy. However, since 9/11, Pakistan is no longer ready to tolerate its western frontier as beyond laws and regulations of the State. Successive Pakistani governments had to decide social and economic policy framework for FATA. Prime Minister Nawaz Sharif's vision is that Pakistan must become part of shared prosperity through regional economic integration and therefore, trade with all neighbours is important. The Prime Minister has, on several occasions, expressed his commitment that Pakistan will fully respect Afghanistan's sovereignty and will not interfere in Afghanistan's internal affairs. The government of Prime Minister Nawaz Sharif has abided by this vision and commitment. Pakistan did not interfere in recently held Afghan elections. Today, an Afghan government reflecting the wishes of Afghan people is in place, and Pakistan is working with it. President Ashraf Ghani's visit to Islamabad in 2014 was a very positive development, and progress is being made in bilateral relations. Pakistan supported Afghanistan in international trading organisations and welcomed Afghanistan's entry into the World Trade Organization.

However, Engineer Khurram Dastgir Khan highlighted that a tension between Pakistan's desire to facilitate Afghan trade and the suspicion that this transit trade would hurt Pakistan's interest exists. Though, APTTA, signed in 2010, put lots of safeguards on Afghan transit traders so that Pakistan could regulate it. Following the visit by President Ashraf Ghani, some major steps were taken that included giving access to Afghan traders up to border areas like Wagah and Karachi, and after unloading their goods they can take Pakistani goods to Afghanistan on their way back. Secondly, the percentage of scanning of Afghan trucks has been reduced. Initially, it was hundred per cent, but now it has been reduced to twenty per cent to facilitate Afghan traders and expedite the flow of Afghan trade. Further, according to 2010 transit trade agreement, trade was to be conducted in dollars only but now, perishable items can be traded in Pakistani currency as well.

Commenting on the challenges, the Federal Minister said that any effort by Pakistan to regulate the flow of goods or movement of people to Pakistan is resisted by Afghanistan. Both countries have formal agreements on customs and information sharing. Pakistan and Afghanistan also need to address this issue and reach some kind of understanding as it is important to regulate the borders to get the exact sense of quantum of movement between the two countries. He said new infrastructure at Chaman and Torkham is being developed to facilitate and regulate the flow of goods and people and if successful, Pakistan would be willing to open new crossing points as well.

Pakistan is also working towards regional economic integration. In this regard, Pakistan has offered the Central Asian States to have a regional transit trade agreement and sign FTAs with regional countries. Pakistan is testing waters through projects like CASA1000, and there are high hopes from the TAPI gas pipeline. He once again reiterated Prime Minister Nawaz Sharif's vision and said that regional economic integration is the only road to peace and prosperity for the entire region. With this goodwill and improving trade with Afghanistan and Central Asian countries, prospects are bright for Pakistan.

Mr. Mansoor Ahmad Khan, Director General (Afghanistan & ATDC), Ministry of Foreign Affairs appreciated the report, which, he said, was timely, objective and comprehensive. He concurred with the observation made by Dr. Zubair that growth in Pak-Afghan trade during the last 10 years was mostly donor-driven. However, Pakistan continues to attach great significance to the improvement in its trade relations with Afghanistan in the years ahead. The most important factor in the improvement of Pak-Afghan bilateral relations, including trade and economic ties, will be peace in Afghanistan. Pakistani government is following a holistic approach to help the Afghan government to restore peace in their country, while fully respecting its sovereignty. He noted that Pak-Afghan trade had become stagnant and there was immense need to enhance bilateral trade between the two neighbouring countries.

Pakistan-Afghanistan trade has stagnated after reaching its peak at US\$2.5bn in 2011. Pakistan had set the target of US\$5 billion, but it could not be achieved due to a number of factors. But the significance of bilateral trade remains immense. Pakistan should focus on improving the competitiveness of its industry and build institutional linkages with Afghanistan. The two countries should make their banking channels more effective. While Pakistan is legally bound to provide Transit Trade facilities to Afghanistan, its concerns about smuggling and informal trade are justified. It is true that informal trade happens across many borders, such as India-Nepal, but a particularly worrying thing about informal trade across the Pak-Afghan border is that it is more than the formal trade. It's difficult to tackle this problem through unilateral means alone; it requires bilateral means. Both countries should make efforts to harmonise their tariffs, develop infrastructure for trading and incentivise formal trade, particularly in those products which are prone to be smuggled.

For regional economic integration, connectivity projects, and reforms, including the development of border areas are very crucial. Pakistan government is fully abreast of these needs and is already working on these issues. Pakistan is already working on political reforms in FATA, and will be focussing more on economic reforms in the years ahead. In their bilateral interaction, both Pakistan and Afghanistan should seek win-win situation.

Speaking on the occasion Mr. Javed Ghani, Director General Customs (Transit & Trade), said that many ambiguities and nuisances which had become an established practice under the 1965 Pak-Afghan Transit Trade Agreement have been taken care of under APTTA. Now, Pakistani custom authorities maintain regular contact with their Afghan counterparts. He declared APTTA a major development, which demonstrated strong economic and political cooperation between the two countries. APTTA, he said, had helped frame policy, infrastructure and issues related to logistics.

There have been some challenges that Pakistan Customs faced. For example, there were fragmented customs offices, flawed custom clearance, en route theft, impediments in custom clearance and inadequate legal provisions. But now, many of these problems have been taken care of. A dedicated directorate general Transit Trade was in 2013, and now the cargo moves through licensed bonded carriers, except perishable goods. Pakistan customs have also established connectivity with Afghan customs and now Afghanistan trade office electronically acknowledges receiving cargo. The speaker also talked about other improvements regarding the

designated routes and weighing of cargo at exit and entry points and clearance of more than 90 percent cargo consignment on same day. Mr Ghani said that still there are issues which need to be addressed, for instance delays caused by terminal operators due to lack of given space and equipment, infrastructure issues at Chaman/Torkham Pakistan-Afghanistan border due to non-availability of customs scanners and weighing bridges.

Mr Ghanisaid that the expected benefits and opportunities which will come through China-Pakistan Economic Corridor. He underlined the need for better road infrastructure up to the exit stations for swift movement of the transit trade consignments needed. He was of the view that smooth and efficient handling of transit cargo across Pakistan and to the Central Asian States is the key for successful transit trade.

Ambassador Ayaz Wazir was of the view that Pakistan should refrain from raising controversial issues such as that of Durand Line, otherwise the two governments would not be able to improve their bilateral ties. It is difficult for any Afghan government to recognise the Durand Line: it is to Afghans what Kashmir is to Pakistan. Though the border is there and is respected by two sides. Moreover, there is trust deficit between the two sides. As long as this deficit is there, both sides will continue to blame each other. On the issue of smuggling, he was of the view that it was more of Pakistan's responsibility. We cannot simply ask the other state not to import certain things because these subsequently are smuggled back into Pakistan. To tackle this problem, reforms in FATA and empowerment of FATA people was absolutely necessary. Any reforms in FATA must be introduced after taking the people of FATA on board.

Dr. Mansoor Akbar Kundi, former Vice Chancellor Gomal University, concurred with Ambassador Ayaz Wazir's arguments. He said that there was also a policy deficit. Most of the problems discussed here with regard to Pak-Afghan relations can be solved if FATA is given the status of a province. But the problem is that we cannot increase the number of provinces. Moreover, the smuggling or informal trade on border areas is a source of livelihood for many people. But while the situation has improved, but the trust deficit between Pakistan and Afghanistan is making many efforts by the government of Pakistan seem futile.

Mr. Akhlaque Khattak, Chief Customs, Federal Board of Revenue spoke about the problem of smuggling and the anti-smuggling role of Pakistan Customs, on the basis of his personal experience gained through working at three Custom collectorates. He said when Pakistan Customs was establishing new custom stations on Pak-Iran border, there were already custom stations on the Iranian side and Pakistan could simply replicate the model. But this was not the case when Pakistan was establishing new custom stations on Pak-Afghan border. The people who are inclined to indulge in illicit activities like smuggling do it out of economic motivations. These are the people who are just concerned about making maximum profit. He narrated his personal experience while posted at Peshawar collect orate that some Pakistani traders would come to him, seeking undue favours, and threatening that if they were not provided those favours they would take their next consignment across the border under the garb of transit trade and then bring it back to Pakistan through smuggling, because that would give them higher profits rather than importing into Pakistan legally and paying due taxes.

He said that many people living along the border areas donot have any other livelihood than smuggling. So these people are not smugglers; they indulge in such activities to earn their livelihood. But then there are also people with money who indulge in such nefarious activities to multiply their profits.

As far as Pakistan Customs role with regard to transit trade is concerned, our first responsibility is to ensure that all those things that are imported under transit trade cross the Pak-Afghan border and enter into Afghanistan, and then to ensure that these things do not re-enter Pakistan. To ensure this, we have been devising many ways and policies, including tariff rationalisation. Now, the Afghan government has also realised that taxing the things that enter Afghanistan through transit trade is also beneficial for them as they can generate revenue from this. Secondly, Pakistan Customs has a very advanced, state-of-the art, web-based automation system. There is no human element involved. This system itself decides which consignment to scan. We can now ensure that what enters Karachi goes onto Afghanistan.

We are fully cognisant of growing significance of Afghanistan for Pakistan's security, and are trying to improve our coordination. We are trying to convince them to tax transit trade things at par with Pakistan. There was a time when there were 24 items on negative list, but now there are only two: auto parts and cigarettes. With the introduction of TIR, to which both Pakistan and Afghanistan are signatories, we are hoping for improved coordination with Afghanistan.

Dr. Muhammad Zubair thanked all the commentators and summarised their main points.

Ambassador Khalid Mahmood, Chairman Board of Governors ISSI, highlighted the importance of the subject under discussion. He said that it is encouraging that there are bilateral agreements in place like APTTA, and both Pakistan and Afghanistan are signatories to international agreements as well. It is heartening to see that practical steps are being taken to facilitate trade. Afghanistan on its part wants to have maximum freedom of transit trade, whereas Pakistan's interest is to ensure that this freedom is not abused. It is up to the two countries to harmonise these conflicting interests. He also stressed that the Durand Line is a settled issue now and it is an internationally recognised border between Pakistan and Afghanistan. According to the UN Law of the Sea, he said, landlocked countries have the right to access to the sea, the common heritage of mankind.

Ambassador Masood Khan, Director General ISSI, in his concluding remarks thanked the chief guest, the speakers and the participants. He said that despite some legal issues, Afghanistan is ready to work with Pakistan on border management. The transit trade system need reforms and both the countries need to address the deficits to reduce controversies. He said that illicit trade in narcotics, arms and human smuggling is a big problem and is undermining the economies of both the countries besides bringing a bad reputation. He also emphasised the need for reforms in FATA and mentioned about the US\$250 million grant for the region by the Chinese government. He emphasised the importance of peace and stability in region for better trade relations among the neighbouring countries.