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PAKISTAN

Key Economic Indicators

(Billions of U.S. dollars unless otherwise indicated)

	1998	1999	2000 1/
Income, Production and Employment:			
Nominal GDP 2/	57.4	54.0	56.5
Real GDP Growth (pct)	4.3	3.1	4.8
GDP by sector (pct):			
Agriculture	25.2	24.5	25.9
Manufacturing	18.3	18.6	16.8
Services	9.7	8.9	9.3
Government	6.1	6.1	6.3
Per Capita GDP (US$)	441	406	415
Labor Force (Millions)	37.7	38.6	39.4
Unemployment Rate (pct)	6.1	6.1	6.1
Money and Prices (annual percentage growth):			
Money Supply Growth (M2)	14.2	3.5	3.2
Consumer Price Inflation	7.8	6.1	3.4
Exchange Rate (Rupees/US$)			
Official	43.2	50.2	51.7
Parallel	52.2	54.2	54.2
Balance of Payments and Trade:			
Total Exports FOB 3/	8.4	7.7	8.56
Exports to U.S.	1.7	1.7	2.1
Total Imports CIF 3/	10.3	9.3	10.3
Imports from U.S.	1.1	0.7	0.647
Trade Balance 3/	-1.9	-1.6	-1.75
Balance with U.S.	0.6	1.0	1.4
External Public Debt	29.7	28.6	31.04
Fiscal Deficit/GDP (pct)	7.7	6.0	6.5
Current Account Deficit/GDP (pct)	3.2	4.1	2.4
External Debt Service Payments/GDP (pct)	5.0	6.3	5.1
Gold & Foreign Exchange Reserves	1.54	2.3	1.9
Aid from U.S. (U.S.$ millions)	307	42	50
Aid from All Other Sources 4/	2.8	2.3	1.5

1/ Data are for the corresponding Fiscal Years ending June 30. Rupee exchange rates used to convert to dollars are 43.2 for 1998, 50.2 for 1999 and 51.7 for 2000.

2/ GDP at factor cost.

3/ Merchandise trade.

4/ No military aid is believed to be included in these figures. Figures are for loans and grants contracted.

Sources: Various government sources, including the State Bank of Pakistan, the Federal Bureau of Statistics and the Ministry of Finance.

1. General Policy Framework

During 1999-2000 Pakistan's economic performance picked up from the financial crisis of 1998-99 as gross domestic product (GDP) grew at the rate of 4.8 percent as against 3.2 percent during 1998-99. The modest recovery in growth has been supported by a strong performance in agriculture and a slight pick up in the services sector. The large-scale manufacturing sector continued to be in recession registering a growth rate of only 0.04 percent. Inflation remained low at 3.4 percent during 1999-2000. Both exports and imports increased during 1999-2000 after a significant downturn in 1998-99 with a trade deficit of $1.7 billion during 1999-2000. Pakistan faces a critical balance of payment situation with foreign exchange reserves of just $1.11 billion as of October 2000. The government and the IMF are negotiating a Stand By Arrangement (SBA), which would pave the way for further Paris Debt rescheduling needed for Pakistan to avoid defaulting on over $3 billion in payments due in 2001. Additional lending from other IFIs, the World Bank and Asian Development Bank (ADB) would also likely follow the conclusion of an SBA.

Pakistan's economic performance has been handicapped in recent years largely because of ineffective governance and weak policy implementation. Pakistan has the potential to achieve higher growth levels if the Government of Pakistan takes effective measures to achieve macro-economic stabilization and increases economic efficiency by introducing financial sector reforms and restructuring its power sector. The biggest challenge facing American firms in Pakistan is inconsistent, sometimes contradictory policies, and a recent record of not adhering to contracts reached with foreign investors. There is also a lack of transparency in government decision-making, coupled with allegations of systemic corruption. The new military government, which took over on October 12, 1999, has made economic revival a main priority. Its stated goals are restoring investor confidence through stability and consistency in economic policies, increasing domestic savings, carrying out tax reforms, turning around state enterprises, boosting agriculture, and reviving industry. To date this government has been able to make significant progress on tax documentation and is beginning to adopt comprehensive policy reforms in many areas. Actual results, however, remain to be seen, particularly in reviving foreign and domestic investor confidence.

Monetary Policy: The Government of Pakistan has followed a liberal monetary policy during 1999-2000 in order to provide cheap credit to the sagging industrial sector by reducing interest rates on Treasury bills that act as a benchmark for the lending rates of banks. Although domestic credit expansion was higher in 1999-2000 due to large borrowing by the government sector, conversion of non-resident foreign currency accounts into rupees and an increase in liquid reserves, actual growth in money supply has remained stagnant at just 3.2 percent against the target of 9.4 percent, due to low credit demand from the private sector. There has been a recent tightening of monetary policy to stem the slide of the rupee. The government and the State Bank of Pakistan (SBP) are attempting structural reforms in an effort to move toward more indirect, market-based methods of monetary control along with greater autonomy for the SBP. Other government monetary reforms include efforts to rationalize staff, enhance competition in the banking sector, and improve prudential regulation and supervision. Prior to the coup, however, state-owned development finance institutions had continued to make politically influenced lending decisions and, partly as a result, have weak balance sheets. In December 1999 the Supreme Court ruled that interest (riba) is prohibited under Islam and struck down a number of laws and ordered that Pakistan is to implement an interest-free financial system by June 30, 2001. The Government of Pakistan has created two commissions, one at the State Bank of Pakistan and other at the Ministry of Finance, to study the implementation of this decision.

Fiscal Policy: A central element of Pakistan's economic reforms has been the effort to reduce persistent government fiscal deficits. The government, however, has succeeded only marginally in its efforts, as the size of the fiscal deficit was higher than previously reported for 1998-99 due to weak budgeting and poor reporting and accounting procedures. In light of these factors, the revised fiscal deficit for 1999-2000 is 6.5 percent of GDP, while the projected fiscal deficit for 2000-2001 is 4.6 percent of GDP. Improvement in fiscal deficits have been due to reduction in development expenditures rather than through increased revenues. Defense spending and debt repayments absorb 67 percent (80 percent of current expenditures) of total federal spending, leaving little for other basic government functions and improving the long-neglected social sectors. Meanwhile, the country has a very narrow tax base; perhaps 1 in 100 Pakistanis pays income tax. The new government has made compliance with the tax regime, including a 15-percent General Sales Tax (GST), a keystone of its economic reform program. Early results from a recently initiated tax amnesty scheme netted a record $190 million. In order to document the economy the Government of Pakistan has completed a tax survey of industrial, residential and commercial areas in Pakistan's thirteen largest cities and is extending the survey to the whole country. Maximum import tariffs have been reduced from 70 percent in 1994-95 to 35 percent in March 1999, with a further pledge this year to reduce tariffs to 30 percent by June 2001.

2. Exchange Rate Policy

The rupee was floated in May 1999 only to be informally controlled by the State Bank of Pakistan within a narrow range of 52.10-52.30 rupees to the dollar. After the nuclear tests in 1998 the government extended its control to the curb market, which helped to regulate the differential between the curb market rate and the inter-bank exchange rate. The State Bank of Pakistan removed the trading band of rupees 52.10-52.30 to the dollar on July 20, 2000. Under the new exchange rate regime, the rupee exchange rate is a managed float with a spread of 50 paisa maintained between the buying and selling rates. Each bank quotes its own exchange rate depending on its short and long positions. Strong competition among banks, however, means the exchange rates quoted by them vary little.

In years previous to the foreign exchange crisis of 1998, Pakistan significantly liberalized foreign exchange controls. In response to the foreign exchange crisis of 1998, however, the government froze existing foreign currency accounts and denied access to official reserves. Subsequently, these foreign exchange controls were removed. The rupee is now “fully convertible” on current account, foreign firms investing in Pakistan (other than banks and insurance companies) may remit profits and capital without prior approval, and foreign currency accounts can be opened in commercial banks, but the State Bank does not provide forward cover for such accounts.

3. Structural Policies

Pakistan is implementing structural reforms, in consultation with the IMF, to achieve sustainable growth. These include: (a) reducing the fiscal deficit by broadening the tax base; (b) reducing the current account deficit through promoting exports and introducing a market-based exchange rate system; (c) maintaining inflation rate at low levels through reducing government borrowing from the banking sector; and (d) deregulating and increasing the role of private sector through a two-phased privatization program expected to be completed through June 2002. In principle, the Government of Pakistan has been pursuing a long-term strategy of deregulation, reduction of the public sector role in the economy, and opening the economy to international competition. While some progress has been made, the state remains an important player in the Pakistani economy.

Pricing and Tax Policies: Pakistani government agencies and public sector companies allow only exclusive agents to submit bids for tenders as an assurance that they receive only one quotation from each supplier. In the market, pricing is often complicated by the country's complex tax structure, which often includes a number of taxes and customs duties that marketers must build into their final sales prices. These include landing charges, customs duty, bank charges, insurance, and the recently introduced GST. The government has recently done away with the "octroi" tax (a municipal toll tax). Exemptions or relief from import duties have been allowed on imported machinery. Tax relief has also been provided for expansion and balancing, modernization and replacement in existing industries.

Regulatory Policies: As part of an integrated investment promotion strategy, Pakistan has undertaken a comprehensive program to bring the economy into a fully market-oriented system. In an investment policy announced in April 1997, foreign investment on a repatriable basis is now allowed in the manufacturing, infrastructure, hotel/tourism, agriculture, services, and social sectors. Key features of Pakistan's investment climate include a general policy of permitting foreign investors to participate in local projects with up to a 100-percent equity basis, easing of work permit and remittance restrictions on expatriate managers and technical personnel, no requirement of government approval to set up an industry (with a few very limited exceptions), statutory protection against expropriation, and no restrictions on borrowing by foreign entities.

4. Debt Management Policies

Pakistan remains dependent on foreign donors and creditors to finance its balance of payment deficits. The increased liability of debt service payments has reduced the net inflow of foreign resources. Pakistan was a net exporter of $533.8 million in capital to the international financial institutions during 1999-2000. Gross external public debt is over 50 percent of GDP while debt servicing has hovered around 3 percent of GDP during the 1990s with the exception of 1999-2000 when it was 2.2 percent due to debt rescheduling. However, the long and medium term debt as a ratio of GDP has risen from around 37 percent during the second half of the 1990s to above 39 percent during 1999-2000 due to the accumulation of capitalized interest on debt stock as a result of rescheduling.

5. Significant Barriers to U.S. Exports

Pakistan is a member of the World Trade Organization (WTO).

Import Licenses: In recent years Pakistan has significantly reformed its previously restrictive import regime. Former import licenses have been abolished on all "freely importable" goods, i.e. on all items not on the negative list (48 items banned mostly for religious, health or security reasons). All importing firms in the private sector must register as importers with the Government of Pakistan's Export Promotion Bureau and must have valid registration at the time of the import. Certain import restrictions, such as "questionable" fees, have continued. U.S. pharmaceutical manufacturers have faced discriminatory application of the internal sales tax between imported pharmaceutical raw materials and the same domestically produced raw materials. Imported raw materials receive preferential tariff rates if the same materials are not manufactured locally.

Services Barriers: The new 1997 investment policy promised liberalization in services. In this regard, the social sector which includes education, technical and vocational training, human resource development and medical and diagnostic services has been opened for foreign investment with 100-percent ownership of equity. However, the minimum amount of foreign equity investment in these sectors shall not be less than $0.5 million. Other services like wholesale distribution, retail trade, transportation, technical testing facilities, audio-visual services have also been opened for foreign investment with the requirement that a minimum foreign equity investment of $0.5 million be made. Foreign ownership of 100-percent equity is allowed at the onset of the investment in these sectors, which has to be reduced to 60 percent within two years with the condition that the repatriation of profits be restricted to a maximum of 60 percent of total equity or profits.

Pakistan's offer in the WTO financial service negotiations in December 1997 included the right to establish banks and grandfathered acquired rights of foreign banks and foreign securities firms. In the past foreign banks generally have been restricted to a few branches, faced higher withholding taxes than domestic banks, and experienced restrictions on doing business with state-owned corporations. The general insurance and life insurance sectors are now open to foreign investors; they are entitled to hold a 51-percent stake in companies in these sectors. Foreign investors in the insurance sector, however, are required to make minimum equity investment of $2 million in foreign exchange and raise an equal amount in equity in the domestic market. There are no restrictions on repatriation of profits; the original capital invested in the insurance sector can not be repatriated. Under the WTO Agreement on Basic

Telecommunications Services, Pakistan made commitments to provide market access and national treatment for all local, domestic long distance and international basic voice telecommunications services and private leased circuit services as of January 1, 2004. E-mail, Internet, electronic information services, data communication network services, trunk radio services, cellular mobile telephone services, audiotex, voice mail and card-pay services, close user group for banking operations, international satellite operators for domestic data communication, paging services, vehicle tracking system and global mobile personal communication systems are now open for 100-percent foreign ownership on a repatriable basis. However, the amount of foreign equity investment shall not be less than $0.5 million in these services. Other telecommunication services can be provided only through the network facilities of the Pakistan Telecommunication Company Limited (PTCL). Up to 100-percent foreign investment on licensed services may be permitted; there will be no foreign ownership restrictions as of January 1, 2004. Pakistan also adopted some pro-competitive regulatory principles regarding transparency of regulations, interconnection and numbering, and competitive safeguards. Motion pictures face high tax rates; the practice of including the royalty value in the dutiable value of films imported for showing in theatres have sharply cut their export to Pakistan. Theater owners also lack the authority to set admission prices according to market conditions.

Standards: The Pakistan Standards Institution (PSI) has established about 4,600 national standards for agriculture and food, chemicals, civil and mechanical engineering, electronics, weights and measures, and textile products. Testing facilities for agricultural goods are inadequate, and standards are inconsistently applied, resulting in occasional discrimination against U.S. farm products. Sometimes a U.S. exporter will encounter difficulty with "quality" standards, usually in the context of protecting some domestically manufactured product.

Investment Barriers: Pakistan has liberalized its foreign investment regime and officially encourages investment. Investors often face unstable policy conditions, however, particularly on large infrastructure projects. The Government of Pakistan has resolved operating contract disputes with all IPPs except one. In June 2000 the Supreme Court of Pakistan held that an arbitration clause in a contract with an independent power producer need not be honored due to allegations of corruption. These actions have severely damaged Pakistan's climate for foreign investment. Security concerns can also be disruptive factors influencing company choice of location of facilities and areas of operation. Local content requirements occur in the automobile, electronics, electrical products, and engineering industries under Pakistan's "deletion program." Although this deletion policy was to have ended on December 31, 1999, pursuant to the requirements of the WTO TRIMS agreement, Pakistan has sought a seven-year extension of the waiver of these requirements from the WTO and this request is pending.

Government Procurement: The government, along with its numerous state-run corporations, is Pakistan's largest importer. Work performed for government agencies, including purchase of imported equipment and services, is often awarded through tenders that are publicly announced or issued to registered suppliers. Lack of transparency, however, has been a recurrent and substantial problem. The Government of Pakistan nominally subscribes to principles of international competitive bidding, but political influence on procurement decisions has been common, and decisions have not always been made on the basis of price and technical quality alone. The current government has, however, established an office for procurement reform in an attempt to introduce and enforce better procurement practices in Pakistan.

Customs Procedures: Investors sometimes complain that the incentives advertised at the policy level are not implemented on the ground, particularly with respect to customs. The government canceled its controversial pre-shipment inspection (PSI) valuation system in March 1997. In January 2000 the government began implementing a transactional valuation system where 99 percent of import valuation is based on invoices pursuant to the WTO's Customs Valuation Agreement.

6. Export Subsidies Policies

Pakistan actively promotes the export of Pakistani goods with measures such as government financing and tariff concessions on imported inputs, and income and sales tax concessions. The government is looking at phasing out many of these programs due to the strain on the national budget. These policies appear to be equally applied to both foreign and domestic firms producing goods for export. Pakistan has established export processing zones with benefits such as tax holidays, indefinite carry forward of losses, exemption of imports from taxes and duties, and exemption from labor laws and various other regulatory regimes.

7. Protection of U.S. Intellectual Property

Pakistan is party to the WTO's Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), and is currently revising its laws to become TRIPS compliant. New laws on copyright, industrial designs and layout of integrated circuits have been recently enacted and new laws on trademarks, patents and plant breeders' rights are in the pipeline. Pakistan is a member of the Bern Convention for the Protection of Literary and Artistic Works, the Universal Copyright Convention, and the World Intellectual Property Organization, but is not a member of the Paris Convention for the Protection of Industrial Property. Pakistan has been on the U.S. Trade Representative's "special 301" Watch List since 1989 due to widespread piracy, especially of copyrighted materials.

Patents: Current law protects only process patents, though the government has stated its commitment to eventually offering product patents in accordance with WTO obligations.

Trademarks: Since 1994, Pakistan has required that pharmaceutical firms label the generic name on all products with at least equal prominence as that of the brand name. This trademark labeling requirement makes it difficult for consumers to assess the differences in quality, efficacy and safety among different products. There also have been occasional instances of infringement, including for toys and industrial machinery.

Copyrights: The markets for imported computer software and, until recently, film videos, were nearly 100-percent pirated. Piracy of copyrighted textile designs is also a serious problem. Some counterfeit products made in Pakistan are exported to other markets. At least one local firm, however, is now distributing legitimate, copyrighted videotapes produced by U.S. film studios. As a result of strengthened law enforcement, some other pirate outlets are taking steps to offer legitimate products. Sustained stronger enforcement needs to be paired with action by the courts to prosecute and sentence violators. The new copyright law provides for much higher penalties for piracy.

New Technologies: The impact on U.S. exports of weak IPR protection in Pakistan is substantial, though difficult to quantify. In the area of copyright infringement alone, the International Intellectual Property Alliance estimated that piracy of films, sound recordings, computer programs, and books resulted in trade losses of $80 million in 1998.

8. Worker Rights

a. *The Right of Association:* The Industrial Relations Ordinance of 1969 (IRO) gives industrial workers the right to form trade unions but is subject to major restraints in some employment areas. The IRO prohibits anti-union discrimination by employers. Under the law, private employers are required to reinstate workers fired for union activities. However, workers usually do not pursue redress through the courts because they view the legal system as slow, prohibitively expensive and corrupt. The Essential Services Maintenance Act of 1952 (ESMA) restricts union activity in sectors associated with state administration, i.e., government services and state enterprises. The government lifted a ban on union activity in the Water and Power Development Authority (employing 130,000 workers) through a Presidential Ordinance in July 2000.

b. *The Right to Organize and Bargain Collectively:* The right of industrial workers to organize and to freely elect representatives to act as collective bargaining agents is established in law. Legally required conciliation proceedings and cooling-off periods constrain the right to strike, as does the government's authority to ban any strike that may cause "serious hardship to the community or prejudice the national interest." The government also may ban a strike that has continued for 30 days. The government regards as illegal any strike conducted by workers who are not members of a legally registered union. Police do not hesitate to crack down on worker demonstrations. The law prohibits employers from seeking retribution against leaders of a legal strike and stipulates criminal penalties for offenders. The law does not protect leaders of illegal strikes.

c. *Prohibition of Forced or Compulsory Labor:* The constitution and the law prohibit forced labor and slavery, including forced labor by children. The 1992 Bonded Labor System (Abolition) Act outlawed bonded labor, canceled all existing bonded debts, and forbade lawsuits for the recovery of existing debts. However, provincial governments, which are responsible for enforcing the law, have failed to establish effective enforcement mechanisms. The government of Punjab, has now reportedly enhanced its activities, particularly in regard to bonded and child labor. Illegal bonded labor is widespread. It is common in the brick, glass, and fishing industries and is found among agricultural and construction workers in rural areas as well.

d. *Minimum Age of Employment of Children:* Child labor is common and widespread and there are insufficient resources as well as an inconsistent commitment to stop it. The Constitution prohibits employing children aged 14 years and under in factories, mines, and hazardous occupations. The 1991 Employment of Children Act prohibits employing children under age 14 in certain occupations and regulates working conditions. Under this law, no child can work overtime or at night. Enforcement is a serious problem, with few inspectors and low fines and penalties imposed. According to a 1996 survey by the government and the ILO, 8.3 percent (over 3.6 million) of children between ages of 5 and 14 work. Few regard this survey as accurate, however, believing it understates the true dimensions of the problem. The government has recently issued a National Policy and Plan of Action to Combat Child Labor.

e. *Acceptable Conditions of Work: The* federal minimum wage for unskilled workers is rupees 1,976 ($36) per month, but it applies only to industrial and commercial establishments employing 50 or more workers. Federal law provides for a maximum workweek of 48 hours (54 hours for seasonal factories) with rest periods during the workday and paid annual holidays. These regulations do not apply to agricultural workers, workers in factories with fewer than 10 employees, and contractors. In general, health and safety standards are poor. Provinces have been ineffective in enforcing labor regulations, because of limited resources, corruption, and inadequate regulatory structures.

f. *Rights in Sectors with U.S. Investment:* Significant investment by U.S. companies has occurred in the power, petroleum, food, and chemicals sectors. U.S. investors in industrial sectors are all large enough to be subject to the full provisions of Pakistani law for worker protection and entitlements. In general, multinational employers are more diligent in fulfilling their legal obligations, providing good benefits and conditions, and dealing responsibly with unions. The only significant area of U.S. investment in which worker rights are legally restricted is the petroleum sector, where the oil and gas industry is subject to the Essential Services Maintenance Act. That act bans strikes and collective bargaining, limits a worker's right to change employment, and affords little recourse to a fired worker.

Extent of U.S. Investment in Selected Industries—U.S. Direct Investment Position Abroad on an Historical Cost Basis—1999

(Millions of U.S. dollars)

Category		Amount
Petroleum		229
Total Manufacturing		13
Food & Kindred Products	27	
Chemicals & Allied Products	(1)	
Primary & Fabricated Metals	(1)	
Industrial Machinery and Equipment	0	
Electric & Electronic Equipment	0	
Transportation Equipment	0	
Other Manufacturing	0	
Wholesale Trade		41
Banking		139
Finance/Insurance/Real Estate		65
Services		2

Other Industries	-2
TOTAL ALL INDUSTRIES	488

(1) Suppressed to avoid disclosing data of individual companies.
Source: U.S. Department of Commerce, Bureau of Economic Analysis.