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AN EMPIRICAL CRITIQUE OF NATIONAL TARIFF POLICY 2019-2024

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Policy Paper

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EXECUTIVE SUMMARY

This paper provides a holistic view of our trade data and tariff structures by assessing Pakistan's first National Tariff Policy (NTP) 2019-24, its impact, and incidence on changing the trade policy direction. NTP 2019-24 was introduced to depart from using tariffs as a revenue collection measure and focuses on promoting competitive import substitution by providing time bound protection to local industry. It highlights that a complex tariff structure is detrimental to consumer welfare and industrial growth. It proposed changes to simplify the tariff structure by introducing an inclusive decision-making process for simplifying the tariff structure and for minimizing exemptions given in the fifth schedule.

This study finds that the National Tariff Policy (2019-24) was a step in the right direction but remained ineffective in removing rigidities and simplifying the tariff structure. This study also highlights that there is a need to increase the import base as 43 percent of the imports are in the exempted products list. It is further noted that around 71 percent of customs duty were collected from 10 product groups. In year 2022-23, the base of dutiable imports further shrunk to 18 percent (FBR year book 2022-23). A complex tariff structure causes delays and inefficiencies in the promotion of manufacturing exports from Pakistan.

NTP 2019-24 became dormant soon after its enactment in 2019 as the Federal Board of Revenue (FBR) continued to use imports as a revenue measure. Import duties contribute 24 percent to indirect taxes, and 75 percent of custom duties are being collected from 15 product groups. FBR, Ministry of Commerce, and regulatory bodies are trying to manage imports with cumbersome and vague procedures of imposing and availing exemptions given in the fifth schedule.

NTP 2019-24 outlined a complex formation of the tariff board. The Tariff Policy Board, due to its structure and voting pattern, remained ineffective and mostly inconclusive in taking timely decisions. Pakistan's trade policy framework is complex, with multiple non-tariff barriers (NTBs) and tariffs affecting international trade. The government aims to gradually remove protectionist policies to address market failures.

However, high tariff rates, complexity, and corruption lead to under-invoicing and smuggling, which are some of the challenges the government tried to correct through National Tariff Policy 2019-24. National Tariff policy used cascading as a principal objective to protect the local industry. After analysis, it appears that the policy to protect local industry is curbing trade in Pakistan and promoting a rent-seeking culture.

Cascading principle is having a selectivity bias as small and medium industries are unable to avail duty exemptions. For example, iron, steel and paper commercial importers are benefiting from duty exemptions. This report indicates that the SRO culture and exemptions given in the fifth schedule have increased the complexity of the tariff structure in Pakistan.

Multiple rates and non-tariff barriers (NTBs) affect international trade in Pakistan. Custom duty continues to be the major revenue spinner. Sales tax on imports contributes significantly to the total sales taxes in Pakistan, with a 61% share in FY 2022-23.

Non-Tariff Measures (NTMs) cover 33.12% of imports, exceeding the frequency ratio, indicating significant NTM costs. NTM-affected trade is worth USD 32.93 million, with USD 30 million lost due to licensing, certification, and labeling requirements. Sector-specific regulations and accreditation requirements add complexity.

The Granger VAR Model, Impulse Response Function, and Double Log Model used in this study showed that tariff imposed is adversely affecting GDP growth and has caused the depreciation of PKR. By addressing these challenges, Pakistan can improve its tariff structure, increase trade efficiency, promote economic growth, reduce corruption, and enhance the business environment.

Qualitative analysis reflects that future directions of the policy must be based on real time data rather than using tariff as a revenue spinner. Non-Tariff Measure and imports sales tax were not the purview of National Tariff Policy. Future tariff policies must take a holistic view and work on the single object of improving trade competitiveness rather than discussing tariff in isolation.

ACRONYMS

AHS	Effectively Applied Weighted Average
BND	Bound Tariff
CPEC	China-Pakistan Economic Corridor
DRA	Drug Regulatory Authority
ECC	Economic Coordination Committee
ERP	Effective Rates of Protection
FBR	Federal Board of Revenue
FDI	Foreign Direct Investment
HHI	Hirschman Herfindahl Index
IRF	Impulse Response Function
LPI	Logistics Performance Index
MFN	Most Favored Nation
MIGA	Multilateral Investment Guarantee Agency
NOCs	No Objection Certificates
NTB	National Tariff Board
NTC	National Tariff Center
NTM	Non-Tariff Measure
NTP	National Trade Policy
OTRI	Overall Trade Restriction Index
PBC	Pakistan Business Council
PCT	Pakistan Customs Tariff
PEC	Pakistan Engineering Council
PNAC	Pakistan National Accreditation Council
POL	Petrol, Diesel and Kerosene Oil Products
PRF	Preferential Tariffs
PSQCA	Pakistan Standards and Quality Control Authority
PTA	Pakistan Telecommunication Authority
RD	Regulatory Duties
SAM	Social Accounting Matrix
SBP	State Bank of Pakistan

SMEs	Small and Medium Enterprises
SRO	Statutory Regulatory Order
TIFA	Trade and Investment Framework Agreement
TPB	Tariff Policy Board
TPC	Tariff Policy Center
TRI	Trade Restrictiveness Index
UNCTAD	United Nations Conference on Trade and Development
VAR	Vector Autoregression
WITS	World Integrated Trade Solution

1 INTRODUCTION

Pakistan's trade policy aims to collect revenue and protect local industry by frequently changing the tariff structure. Tariffs are taxes imposed on imports and exports. In Pakistan, import duties contribute 24% of indirect taxes (FBR Year Book 2023). The yearbook reveals that almost 46% of import items are either on the banned list of imports given in import policy order issued by Ministry of Commerce or exempted from import duties issued by FBR (FBR Year Book 2023). Almost 73% of import duties are concentrated around 15 major product groups. Moreover, the interplay between regulatory bodies implementing quality standards, vague custom rules, limitations in determining the value of declared imported items, exemptions given in 'respective headings' of the custom tariff fifth schedule of FBR and special powers of the Ministry of Commerce to ban imports and exports through import orders, create an uncertain and unsupportive environment for trade in Pakistan.

The frequent changes in tariff structure in Pakistan can be attributed to the complex and fragmented regulatory framework of controlling trade in the country. Various regulations and acts, such as the Imports & Exports (Control) Act, 1950, Tariff Schedules of the Customs Act, 1969, and others, provide the government with the authority to regulate trade. Additionally, institutions like the State Bank of Pakistan (SBP) and ministries such as Law & Justice, Commerce, and the Federal Board of Revenue (FBR) have the power to issue instructions, guidelines, and notifications that can alter trade rules and regulations. Moreover, ambiguous quality standards cause delays and results into various interpretation of the import duties. Most of the time these regulatory frameworks create an environment of uncertainty and unpredictability, making it challenging for businesses to navigate and comply with the regulations.

The frequent changes in rules and regulations can be driven by various factors, including political considerations, pressure from special interest groups, and short-term revenue goals, rather than a coherent long-term strategy. This, in turn, hinders the achievement of trade policy objectives, such as promoting industrialization, exports, and consumer welfare. The complex structure of Pakistan's trade regulations does not provide a level-playing field to all businesses. Big businesses and influential stakeholders benefit from the complexity of the system. Moreover, the mandate of all these institutions is not to tailor rules for promoting industrialization or exports from Pakistan, except for the Ministry of Commerce, but to manage imports to ensure government revenue stability and control import bills.

Pakistan's customs structure also favors a few oligopolistic industrial importers. These importers gain undue profits by using complicated tariff structures in their favour. Small and Medium Enterprises (SMEs) are not fully conversant with the frequent changes made in tariff policy. Most of the time, SMEs are not even aware of exemptions given in the fifth schedule. These SMEs prefer to pay above average market price to commercial importers rather than dealing with FBR or Ministry of Commerce and Customs officials. The industrial importers know the market conditions, act like monopolists and benefit from exemptions and sudden changes in tariff structure. Over

and above Non-Tariff Measure (NTM) works like quotas and licenses having import licenses and quotas.

Traders import raw materials and earn profits by saving on duties or twisting rules and regulations with the help of custom officials. They can create shortages and pass all taxes to local industries by selling to small local businesses. It is almost impossible for small businesses to engage in exports or imports in Pakistan. That is why Pakistani businesses have not become part of many important global value chains (except textiles) or export goods by adding value to imported raw materials or intermediate goods. Businesses usually prefer to sell in the domestic market rather than plan to sell in international markets. As a result of this complex policy structure, we collected 24% of indirect taxes from imports, but the industry is not growing or competing with fast-paced industrialization worldwide. The cumbersome process and procedures have damaged the capacity to sell in international markets.

In this paper, our objective is to assess Pakistan's first National Trade Policy (NTP) 2019-24 by measuring its impact and incidence. NTP 2019-24 departed from using tariffs as a revenue collection measure, focusing on promoting trade. It highlights that a complex tariff structure is detrimental to consumer welfare and industrial growth. It proposed changes to simplify the tariff structure by minimizing tariff slabs. Secondly, we will examine the success of NTP 2019-24 in achieving its objectives. Thirdly, this paper will provide important information about the direction of our trade policies for maximizing the benefits of international trade.

Based on empirical evidence, countries started trade liberalization strategies after the inception of WTO in 1995. Developed economies, by and large, removed tariff and non-tariff barriers and became part of global chains. These policies increased trade's share in GDP, and globalization swept the world. Financial crises slowed down integration, but world-trading centers emerged as global chains. It seems that reversing globalization and trade openness policies is impossible, and the world is connected through value chains and competitiveness.

Empirically speaking, tariffs do not reduce trade volume but curb trade and retard domestic consumption. Scholars have shown that tariffs create monopolies and oligopolies. Majune and Stolzenburg (2023) estimated that 19% of global exports have few suppliers but a large market share. Moreover, their share in global trade has doubled over the past two decades. It means value chains are highly concentrated, and countries with effective policies achieved specialization and comparative advantage.

Trade provides access to new technologies and products for which there is hardly any domestic substitute. Conventionally, there are three main arguments for imposing tariffs: the infant industry argument, encouraging tariff-jumping investment, and linking local industries. High and complex tariff structures create a rent-seeking class by intervening in social incentives structures. The cost of implementing a high tariff wall results in low industrialization levels and a tax structure highly dependent on indirect measures of tax collection.

Is a tariff policy a revenue measure or should it promote consumer welfare and industrialization? Tariff policy as a revenue collection measure increases inequalities and inefficiencies by creating distortions in society, creating rent-seeking industrialists

who may earn profits by passing on taxes to consumers and not investing in innovation and competition. Development and industrialization do not follow a linear progression. Integration, partnerships, and building value chains are crucial for industrialization in a global world. Restrictive trade policies isolate countries, and trade complexities hinder growth.

COVID-19 and the war in Ukraine have disrupted global supply chains. Due to latest technologies like AI and 3-D printers, conflicts, and pandemics, countries are showing interest in onshoring, and the thrust in trade liberalization seems to be waning. It's time to show diversity and flexibility in trade and tariff rules worldwide (IMF, 2023). Countries are adopting flexible approaches, including plurilateral agreements among like-minded countries, allowing members to adopt new rules (IMF-WB-WTO 2018).

Compared to its competing economies, Pakistan relies heavily on increasing tariffs. In a country with a low level of development, trade is the primary means of introducing new skills and technology to the domestic market. It is also the primary source of creating demand for transport logistics, communication, and financial services. However, Pakistan uses a complex tariff structure as a barrier to trade. Tariffs on imports violate the concept of comparable cost, limiting the growth potential.

Pakistan's trade policy framework includes the Imports and Exports (Control) Act, 1950, and the Customs Act, 1969. The Ministry of Commerce regulates trade through Statutory Regulatory Orders (SROs).

Following this section, this report reviews literature, providing information on the theoretical framework and data sources, qualitative and quantitative research methods used to enrich our analysis. In Section 3, We provide some holistic information about trade and its various performance indicators to explain the stagnation in trade as a percentage of GDP in Pakistan. We analyzed the tariff structure, comprising customs duties, import sales tax, regulatory duties, and additional regulatory duties imposed on imports. This section also explores how trade is managed through various Statutory Regulatory Orders (SROs).

Section 4 examines Non-Tariff Measures (NTMs) and trade losses due to restrictions in Pakistan. NTMs and import sales tax were not in the purview of the National Tariff Policy 2019-24.

Section 5 presents a quantitative data analysis using Vector Autoregressive Technique (VAR) and Granger VAR to determine the direction of causation between variables. The analysis is further strengthened by qualitative data analysis, highlighting the need for rationalizing the national tariff structure and addressing policy missteps due to protectionist policies in Pakistan.

Section 6 discusses the National Tariff Policy, major policy gaps, and the efficacy of the tariff board. The final section presents conclusions and policy recommendations.

2 RESEARCH DESIGN

Our research design is based on a mixed-methods approach, combining qualitative and quantitative techniques for data analysis. These methods were used to address two overarching questions: What are the policy gaps in designing Pakistan's tariff policy, and how can we tailor a tariff policy that incorporates diverse views, or alternatively, how to transition away from using tariff policies for revenue collection or import control in Pakistan?

To pursue these questions, a literature survey was conducted to identify global trends and domestic issues explored in local research.

Quantitative data techniques included descriptive analysis of official documents and Vector Auto Regressive (VAR) analysis to establish direction of causation, revealing policy missteps. Additionally, we conducted qualitative research through structured interviews with business leaders, academia, experts in public policy, journalists, and relevant government officials. The quantitative findings were strengthened by qualitative data analysis, enabling us to consider diverse perspectives, policy processes, and procedures to understand the missteps in Pakistan's tariff policy.

2.1 LITERATURE SURVEY

Can protectionist policies promote growth? Scholars such as Dong et al. (2022), Antràs and Chor (2021), Fajgelbaum et al. (2020), Furceri et al. (2019), and recent influential scholars like Amiti et al. (2020), Autor et al. (2020), and Pierce and Schott (2020) have examined the impact of tariff increases on output growth. They found that tariffs lead to a decline in output growth due to a substantial reduction in efficiency after five years. Additionally, tariffs result in increased unemployment.

The negative effects of tariffs arise from increased costs of imported inputs and appreciation of the real exchange rate, with a small and insignificant impact on the trade balance. Antràs and Chor (2021) showed that tariff increases target intermediate goods, leading to the rise of global value chains and fragmentation of the production process. This results in increased prices across all sectors of the economy. In contrast, Dong et al. (2022) found that a gradual decrease in tariffs leads to gradual growth in imports.

Before 2018, there was a consensus against using tariffs as a policy measure to protect local industries. However, in 2018, the US government imposed a $50 billion tariff on imports from China, leading to retaliatory tariffs from China. Scholars have discussed how tariff changes can shift imports in advance of the rate increase, driving up import prices before the tariff imposition and leading to a large decline in import prices afterward.

The literature suggests that trade openness is directly related to the competitiveness of local industries. Scholars like Bown (2018), Krugman (2018), Baldwin (2018), and recent contributors like Freund et al. (2020), and Reyes et al. (2020) have analyzed the retaliatory tariffs imposed in the US to restrict trade. They found that antidumping duties, countervailing duties, and safeguards restrict trade and cause unemployment. These studies concluded that tariffs matter in the early phase of development but not in mature economies.

Furthermore, scholars have discussed how insider information can lead to increased

domestic prices of imported goods, curbing demand which may likely to contract economic growth. Hummels and Klenow (2005) found that tariffs significantly impact trade flows. A high tariff rate can substantially reduce trade. This decrease in demand can lead to decreased prices of imported goods in the international market. Mill's theory of reciprocal demand highlighted these challenges that import duties are usually applied to raw materials and commodities that a country can substitute. Import duties always fall on domestic consumers, resulting in decreased demand for the product.

Scholars like Bhagwati (1999), Krueger (1997), and recent scholars like Irwin (2019), and Bagwell and Staiger (2020) have discussed the importance of effective trade liberalization reforms, including reducing tariff rates and non-tariff barriers. They have also emphasized the importance of institutional effects, scale effects, spillover effects, and technological change in enhancing a nation's competitiveness.

There is a consensus that protectionist policies may benefit a few but are harmful to a country's competitive advantage and growth. Tariffs can be a tool for revenue collection but reduce consumer welfare and shrink reciprocal demand. Protectionist policies cause smuggling and a large informal economy. With low tariff rates, a country can discourage smuggling and under-invoicing, contributing to revenue and enhancing consumer welfare.

In today's globalized world, where global value chains are reshaping trade flows, it is no longer true that tariffs are imposed only on imported goods. Countries depend on each other for exports, and balance of payments and gross value of trade are inadequate to reflect perspective comparative advantages.

2.2 LITERATURE REVIEW ON PAKISTAN

In Pakistan, economists have been studying tariff walls and calculating protectionism rates since 1960. The debate between nominal protection rates and effective rates of protection (ERP) has been ongoing. In Pakistan, researchers have typically estimated nominal protection rates (NRP) or ERP.

Naseem and Balasa (1971) identified errors in measuring effective tariff rates and noted that the two definitions of ERP—the percentage difference between value added at domestic and world prices, and the percentage difference in value added per unit of output at two sets of prices—are not equivalent. Haque and Siddiqui (2007) calculated ERP in Pakistan and found that protectionist policies harmed labor intensity, comparative advantage, and export orientation.

Recently, Zeeshan (2023) used ERP to examine import substitution strategies and found that average ERP decreased from 53% to 21% in Pakistan between 2011 and 2020. ERP reductions were observed in agriculture (3.6% to 1.2%), manufacturing (99.8% to 39.7%), and services (-2.8% to -0.7%).

Rizwana and Iqbal (2001) analyzed the impact of protectionist policies on income distribution using a social accounting matrix (SAM). They found that import controls and inefficient exchange rate policies led to a 28.63% decline in government revenue and a 10% increase in industrial imports, while other imports declined. Tariffs negatively affected government revenue collection and demand.

Chaudhry (2011), high tariff rate shows weak institutional capacity, and it reduces GDP growth through spillover effects of labour in protected sectors.

Pursell, Khan and Gulzar (2011) in their report suggested that custom duties in Pakistan must hover around 5 percent and maximum bound tariff inclusive of all duties should not exceed from 29 percent.

Pervez and Malik (2013) concluded that lower tariff structures may increase GDP, inflation rates, and foreign direct investment (FDI). Amjad and Naeem (2017) noted that customs duty shares decreased from 43% to 7% over three decades, and tariff cuts on machinery imports, tax holidays, and fiscal incentives for domestic exporters led to revenue losses in Pakistan. They used the Gravity model to show that trade policies adversely affected trade flows in Pakistan between 2006 and 2015.

Qadir (2020) while analyzing the national tariff policy concluded that tariff could affect the product mix and process of industrialization. He was of the view that tariff cascading in the national tariff policy may promote rent seeking. He was critical about the protection given to the cars industry. Hafsa (2021) found that import demand elasticity is inelastic, making depreciation ineffective in reducing import demand. Imposing tariffs would only raise domestic goods prices, leading to marginal quantity adjustments and attenuation bias.

In conclusion, research on trade and tariff policies in Pakistan, despite methodological limitations, suggests that tariffs harm competitiveness and consumer welfare, contributing to stagnation and de-industrialization.

2.3 THEORETICAL FRAMEWORK

Traditionally, protectionism can be measured in two ways: first, a trade restrictiveness index (TRI), which approaches the question from the standpoint of import, demand and second the effective rate of protection (ERP).

The empirical work of Anderson and Neary (1996) has shown that countries rarely face world supply curves with infinite elasticities. By assuming perfect pass-through, conventional ERPs may overestimate the degree of protection to domestic producers. Moreover, as the production process becomes increasingly fragmented across international borders, thus, assuming a simple one-step production process and directly applying input intensities from input–output tables may result in a misleading estimate of protection.

Tariff protection on intermediate inputs strongly counteracts protection on final output, and this effect only increases as the stages of production multiply. In this study, we are using various indicators proposed by UNCTAD, WITS and Trade map to assess the effect of tariff policy in Pakistan.

According to the comparative advantage theory, tariff rates can lead to inefficient allocation of resources and reduced economic growth. However, higher tariff rates may provide short-term protection and growth, but they lead to long-term negative consequences, including influencing exchange rates through trade balance and pass-through effects. General Equilibrium Theory (Léon Walras, 1874): analyzes the impact of tariffs on the overall economy, including effects on prices, output, and trade. In new growth theory, Krugman (1979) understands the impact of tariffs on trade and growth. He highlighted the importance of product differentiation in a monopolistic economic environment.

2.4 QUANTITATIVE METHODS

The basic question is how the change in tariff rate affects the GDP growth rate, trade, and domestic prices and demand. Theoretically

speaking, tariff rates can significantly influence economic growth and exchange rates. There is a consensus that higher tariff rates can lead to increased protectionism, reduction in trade, and lower economic growth in the long run. However, tariffs can increase economic growth in the short run. Policymakers must carefully consider these relationships when setting tariff rates.

In this study, we used tariff rate as the dependent variable and saw how trade, exchange rate, inflation and total duties, which includes customs duties, excise, regulatory and additional custom duties and domestic prices affect the tariff rate. It will simply show that policy makers consider all these dimensions while setting the tariff rate and what is the direction of the causation between these variables in Pakistan.

$$\Delta \log \text{tariff rate} = a + b\,\Delta \log (1+t)_t + \mu \Delta \log(GDP)_t + g\Delta \log(\text{Exchange rate})t + e_t$$

(1+ t) is the elasticity of substitution and a set of controls include GDP, Trade, Inflation rate and Exchange rate. Trade to GDP ratio, Real GDP Growth at constant factor cost, GDP at current prices (US$), Inflation rate, Nominal exchange rate, Tariff rate, Custom duties, Total Duties, Tariff as a percentage of total taxes.

We employed the methodology outlined by Furceri et al., (2022) and employed VAR and Impulse response function to know the aftermath of tariff shocks.

2.4.1 THE VECTOR AUTOREGRESSION MODEL (VAR)

The vector autoregression (VAR) model most commonly used multivariate time series analytic technique to explain causal relationships among multiple variables over time, as well as predict future observations (lütkepohl, 2005).

2.4.2 VAR GRANGER CAUSALITY TEST

Granger Causality Test states that *"if the prediction of one time series is improved by incorporating the knowledge of a second time series, then the latter is said to have a causal influence on the first."* (Granger, 1969; Lütkepohl, 2005, p. 41). Granger called a variable *x* causal for a variable *y* if the lagged values of *x* are helpful for improving forecasts of *y* (*y* at future times).

The VAR framework is flexible and provides an environment for implementing this type of analysis. Granger Var is used to see the bidirectional causation in the above-mentioned variables. The Granger VAR Test, developed by Toda and Yamamoto (1995), is a modified Wald (MWALD) test procedure that determines causality regardless of the unit root problem in the data. This test utilizes Augmented VAR settings, regardless of the order of integration. Toda and Yamamoto (1995) proposed the augmented VAR(p+d) model for testing causality between integrated variables, where:

- p is the assumed order of the process
- d is the maximum order of integration of the variables

The kth element of yt does not Granger-cause the jth element of yt if the following hypothesis is not rejected.

2.4.3 IMPULSE RESPONSE FUNCTION (IRF)

Impulse Response Function (IRF) describes the reaction of a set of variables to a shock in one or more variables. IRF traces the transmission of a shock which enables us to assess the impact of economic policies.

2.5 QUALITATIVE RESEARCH DESIGN

To incorporate diverse perspectives into our analysis of Pakistan's trade and tariff policy structures, as well as the roles of various government departments and ministries, we employed content analysis. Structured interviews were conducted with a diverse group of professionals, including academics, policymakers, journalists, businessmen, and consultants.

The study utilized NVivo software and an interview inspection method to systematically code, categorize, and visually represent the data. Nodes and child nodes were constructed to represent the various perspectives on Pakistan's tariff policy. Through coding recorded interviews with these individuals, the study identified major themes and concerns associated with Pakistan's trade policy environment.

Following the coding and thematic analysis of these interviews, this study aims to analyze the challenges in implementing tariff policy and identify key recommendations for its improvement. The experts who participated in this study are: Senator Zeeshan Khanzada, Dr. Robina Athar, a former Chair of the National Tariff Commission; Dr. Safdar Sohail, the Executive Director of Social Protection Centre; Mr Mehtab Haider, a senior economic journalist; Mr Imtiaz Rastgar, a leading businessman; Mr Saud Bangash, a representative from the Pakistan Business Council (PBC); Mr Zaheeruddin Dar, an expert consultant; Mr Ashfaq Ahmad[1], Joint Secretary at the Ministry of Commerce; and Dr. Aadil Nakhoda, an academic. Each expert added a unique set of experiences and a rounded perspective on how tariff policy is developed, implemented, and perceived in Pakistan.

2.6 INDICATORS FOR TRADE POLICY EFFECTIVENESS

2.6.1 AD VALOREM EQUIVALENT

To overcome the problem of overestimating the rate of protectionism, Kee, Nicita and Olarreaga (2009) calculate their ad valorem equivalent.

$$tave=100\ t/p$$

For calculating the advalorem equivalent, divide trade values by volumes. This gives unit value of imports. Since the unit value changes systematically. Its interpretation may have a systematic bias. P is the international price of the commodity.

2.6.2 OVERALL TRADE RESTRICTION INDEX (OTRI)

OTRI captures the trade policy distortions that each country imposes on its import bundle. It measures the uniform tariff equivalent of the country tariff and non-tariff barriers (NTB) that would generate the same level of import value for the country in a given year.

2.6.3 BOUND VS. APPLIED TARIFF RATES

Bound MFN tariff levels indicate the upper limit at which the government is committed to set its applied MFN tariff.

2.6.4 TARIFF RATE QUOTAS

Tariff rate quotas are low tariff rate on an initial increment of imports and a very high tariff rate on imports above that initial amount. These could be simple aggregation of trade quota regime or a weighted quota of imported items.

$$t = S_k w_k t_k$$

[1] Mr Ashfaq Ahamd participated in interviews in his personal capacity and views expressed in the report are his personal views.

2.6.5 DISPERSION

The higher dispersion of tariffs means as higher distortion. Standard deviation σ and the coefficient of variation (standard deviation / tariff mean) shows the level of distortion. The proportion of tariff peaks also shows the distortions.

2.6.6 EFFECTIVE PROTECTION AND TARIFF ESCALATION

Effective Protection rate measures the net protective effect of the whole tariff structure on domestic producers in a particular sector. ERP can be negative, when the import tariff on the final good is positive, because of protection on inputs.

2.6.7 TRADE ELASTICITY

There is a long tradition in estimating trade elasticity. Trade elasticity is the key variable in international economics, which determines welfare gains from trade and transmission of shocks across countries (expenditure switching effect).

2.7 DATA SOURCES

Data sources include:

- Trade Map
- UNCTAD trade policy analysis
- WITS/Trains websites
- State Bank of Pakistan Annual Reports (nominal exchange rate)
- Pakistan Bureau of Statistics (GDP growth rate and inflation rate)
- World Bank (logistics performance indicators, ease of doing business ranking, GDP at Market Price, and unit value of imported goods in the domestic market)
- World Development Indicators (GDP at Market Price and unit value of imported goods in the domestic market)

3 TRADE IN PAKISTAN

Pakistan is passing through a low growth phase in its economic history. The average GDP growth rate is 2.64 percent in the last five years. The GDP growth rate was -0.94 percent in 2019-20 and -0.21 percent in 2022-23. In a country where population growth is 2.55 percent, this is an alarming situation. During the same period, inflation rates were the highest.

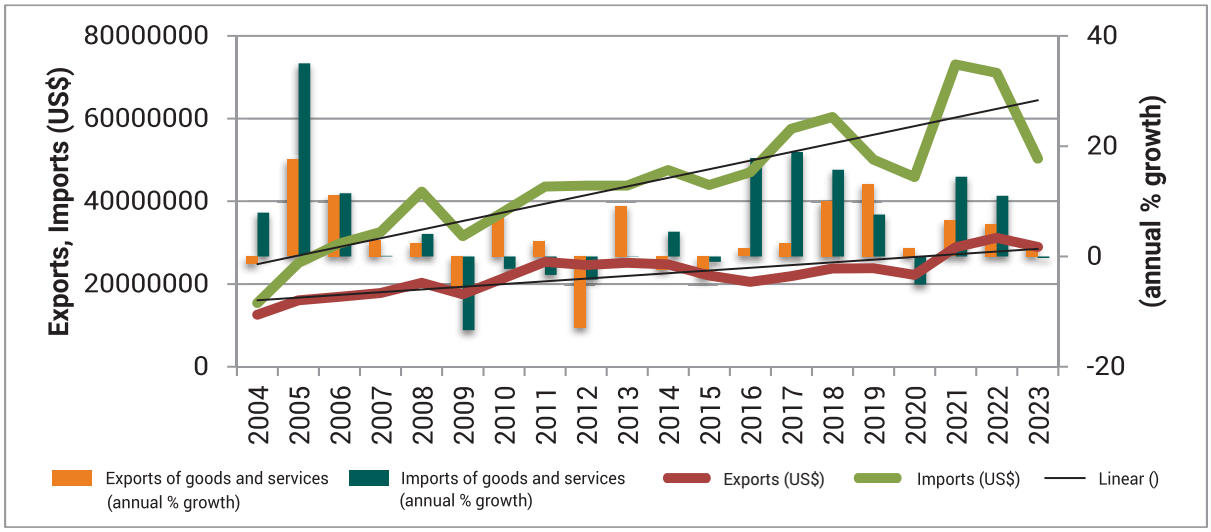
Trade is an opportunity that can generate growth in low-performing sectors, especially large-scale manufacturing. Pakistan's exports value for 2023 is Rs 6.8 trillion, and imports stand at Rs 13.4 trillion. The trade deficit is around Rs 6.6 trillion (Pakistan Bureau of Statistics, 2024). Trade openness, on average, stands at 33 percent of GDP. After liberalization of the economy, the share of trade in GDP has not increased.

To control the trade deficit, the government restricts trade by imposing tariffs on imports. Pakistan's exports data reveal inadequate foreign value addition and a high value of domestic intermediate goods. Out of Rs 6.8 trillion of exports, Pakistan re-exports only Rs 74.2 billion. This is because of high tariffs and duties imposed on the import of intermediate goods (World Bank, 2020).

Pakistan's import data show that major imports are crude oil, palm oil, and some other consumer products. Pakistan's re-imports[2] are Rs 16.8 billion in FY 2023. Pakistan does not import its own commodities back again after value addition due to high tariff walls. Historical trade data shows that high tariff rates make the import of essential intermediate goods expensive, and the industry finds it difficult to compete with the world market.

Figure 1 reflects the trade data of Pakistan. Imports and exports are sluggish to grow and follow inconsistent growth. The liner trend shows that gap is increasing with the passage of time between imports and exports of Pakistan.

Figure 1: Trade in Pakistan



Source: Pakistan Bureau of Statistics

[2] Re-exports means to export after adding value after importing from various locations. Re-import means to bring back to the country from which it was imported.

Table 1 shows Pakistan's imports distribution shows that 28.9 percent are consumer goods, 32 percent are intermediate goods, 18.4 percent are capital goods, and 20 percent are raw materials (Trade Map, 2024). The low share of capital goods and raw materials imports reflects a weak industrial base and a complex tariff policy. Pakistan's top imports are petroleum oil, natural gas, palm oil, and pharmaceuticals.

These are basic inputs or necessities, and the demand is highly inelastic. These essential items are highly inelastic commodities with very few substitutes. Using basic raw materials and inelastic products as a revenue spinner only minimizes consumer welfare and increase domestic prices.

Table 1: Trade intensity indicators 2022

Product categories	Import (US$ Mil)	Import Product share (%)	Export (US$ Mil)	Export Product share (%)
Consumer goods	23882.20755	28.7141	17938.97924	62.2986
Intermediate goods	20930.16429	32.764	6861.029955	23.827
Capital goods	13376.06982	18.3506	1024.039199	3.5563
Raw materials	14663.89326	20.1174	2968.750525	10.3099

Source: Trade Map

Our export's structure shows that Pakistan exports only 3.6 percent of capital goods. Moreover, Pakistan is still trying to rationalize the tariff structure, while our competitors have forged ahead and become part of global value chains. Comparing the last five years' import data reveals that during FY19 to FY23, imports of machinery and transport equipment increased by 13 percent from FY19.

Manufactured goods and materials imports have increased by 35 percent, while food and live animals' imports contracted by 67 percent. Chemicals imports contracted by 45 percent, minerals and lubricants imports contracted by 52.5 percent, and animal and vegetable oil imports contracted by 72 percent (PBS, 2024). Import contraction has direct implications for GDP growth and food security.

3.1 TRADE PERFORMANCE INDICATORS

In a country where the logistic performance index is 2.2, indicating poor quality of infrastructure related to trade, it is not surprising to see a low share of trade in GDP. As previously discussed, Pakistan's trade policy has been criticized for its complex tariff structure and high tariff barriers, which can further exacerbate the issue. The poor trade performance is evident from the trade ratings, institutional and governance ranking and competitiveness structure.

Table 2: Trade intensity indicators 2022

2021	No. of Tariff Agreement	8
2021	No. of Import partners	211
2021	No. of Import products	4011
2021	No. of Export partners	199
2021	No. of Export products	2761
2018	CPIA Trade Ratings	3.5
2019	Ease of Doing Business Rank	108
2013	No of NTM Affected Products (HS 6 Digit)	28
2013	No of NTM Measures	2
2009	Overall Trade Restrictiveness Index - MFN Tariff	0.073
2019	Trading Across Borders Rank	111
2009	Overall Trade Restrictiveness Index - Applied Tariff	0.073
2016	LPI Score	2.92
2013	Temporary Trade Barriers in Effect - Weighted Average	1.30

Source: WITS

Pakistan's 'Ease of doing business' ranks 108 and 111 in trading across borders in 2020 (World Bank), highlighting the challenges faced by businesses in the country. Furthermore, Pakistan's Hirschman Herfindahl Index (HHI) is 0.07, and the Index of export market penetration is 9.23, indicating low market concentration and low competitiveness of Pakistan's trade. The trade restrictiveness index of Pakistan is also at 0.07, showing a highly restricted trade ratio. This, combined with the low share of Pakistan's trade in the world market, largely based on low-value-added goods, poor competitiveness structure, and low institutional quality, creates a bleak scenario for trade in Pakistan.

The high tariff barriers in Pakistan, as mentioned earlier, further compound these issues, making it essential to address these challenges to improve the country's trade performance. Pakistan is also not part of regional blocks. Its share of trading within the region is very low, its logistics and infrastructure are not fully utilized and has not developed to facilitate the major trading routes. Weak governance and capacity to produce are posing another set of challenges.

Table 3: Trade Restrictiveness Indices

OTRI	*ALL*	7.4%	MAOTRI	ALL	0.14729
	AG	5.8%		AG	0.4692447
	MF	7.5%		MF	0.1169579
OTRI_T	*ALL*	7.4%	MAOTRI_T	*ALL*	8.3%
	AG	5.8%		*AG*	32.9%
	MF	7.5%		*MF*	6.0%

Source: IMF

Table 3 shows Trade Restrictiveness Index of Pakistan. It depicts highly restricted trade in Pakistan. OTRI explains that tariffs or NTBs are causing more welfare loss. OTRIs are found to be higher in manufacturing. It means manufacturing protection is larger than agriculture protection. The MA-OTRI captures the restrictiveness of its agriculture export bundle is on average almost 4 times as high as the MA-OTRI for manufacturing. This suggests our agriculture exports are more likely to face market access problems than manufacturing products.

4 TARIFF STRUCTURE IN PAKISTAN

The complexity of Pakistan's tariff structure extends beyond the variation in rates across different slabs. It also varies based on product usage and origin, leading to a difficult policy that fosters misuse of concessions, creates anomalies, and results in valuation lapses. The involvement of multiple regulatory bodies further exacerbates the issue, leading to corruption and bureaucratic hurdles. This complexity causes significant delays in custom clearance at ports, with Documentary Compliance for imports taking around 60 hours and border compliance requiring 131 hours (World Bank Ease of Doing Business Indicators).

After the implementation of the National Tariff Policy, it was expected that the Federal Board of Revenue (FBR) would issue Statutory Regulatory Orders (SROs) only in dire circumstances for correcting an anomaly or for trade promotion. On 1July 2024 FBR issued SRO 929(I)/2024 and imposed Additional Custom Duty (ACD) on 2,200 items and increased/imposed regulatory duties (RD) on the import of 657 luxury items. In 2022 S.R.O. 966 (I) 2022 was issued to levy regulatory duty on import of goods specified. S.R.O. 678 was issued that import under Chapter 99 of First Schedule of the Customs Act are exempted from regulatory duty under Temporary Importation Scheme or import under Fifth Schedule to the Customs Act, 1969.

In NTP, it was decided that any matters related to imposing or suppressing duties would be presented to the National Tariff Board. The Board would then submit its proposals to the cabinet for approval. Although, there were significant tariff rate changes, but the applied tariff rates remained non-uniform. These rates are subject to frequent changes, often at the discretion of authorities or based on factors such as usage and origin of import, making the process cumbersome.

Certain sectors, like iron and steel, enjoy complete protection, resulting in anti-export bias. Furthermore, the applied tariff rates are augmented by various exemptions listed in the fifth schedule of custom tariffs and the imposition of regulatory duties (RD) on imports, as well as additional regulatory duties. This complex tariff structure creates uncertainty and obstacles for trade.

4.1 CUSTOM DUTIES IN PAKISTAN

Customs duty is an important source of tax collection in Pakistan. It is paid to the Government at the time of Customs Clearance. Every commodity imported in Pakistan, if not exempted through an SRO or part of the fifth schedule of custom tariff or not in 'respective tables' heading, usually has to pay multiple duties, including customs duty, additional customs duty, regulatory duty, sales tax on imports, withholding income tax, excise duty, and CESS. On average, a commodity has to pay 69% of its value as duties and taxes.

Table 4 shows the trend of Customs duties in Pakistan. The trend is upward in all types of indirect taxes during 2014-23. If we look at the growth rates, it is clear that after the NTP, regulatory duties increased by 139.92% compared to 804.71% for the last decade. The increase in regulatory duty was less than the average increase of regulatory duty, which is 160.9%. After NTP, the pace of increase in regulatory duty has decreased, but we are still not able to remove these duties.

The data also reveals that custom duties

contributed 13% towards the overall FBR's collection and around 24% in indirect taxes during FY 2023. The net collection from customs duty during FY 2019-20 was Rs. 627 billion and around Rs. 932 billion in FY 2022-23. It has declined from Rs. 1011 billion from FY 2021-22. The trend is upward, but it remained volatile. According to FBR Year Book (2022-23), custom duty recorded a negative growth of 7.8 percent.

However, imports volume in US dollar terms contracted by 30.95 during the same period (Pakistan Bureau of Statistics, 2023). Moreover, this custom duty is collected from only 53.8% of total products imported in Pakistan during FY 2022-23 (FBR Year Book 2022-23). The nominal tariff rate, (total tariff collected divided by the total imports value in Pakistan) has increased significantly during last five years. FBR is collecting more custom duties with a lower volume of imports. The mean tariff rate (including regulatory duties and additional custom duties) and dispersion rate has increased. The distortion rate in revenue collection has increased gradually. This means NTP 2019-24 has created more distortions in the tariff policy.

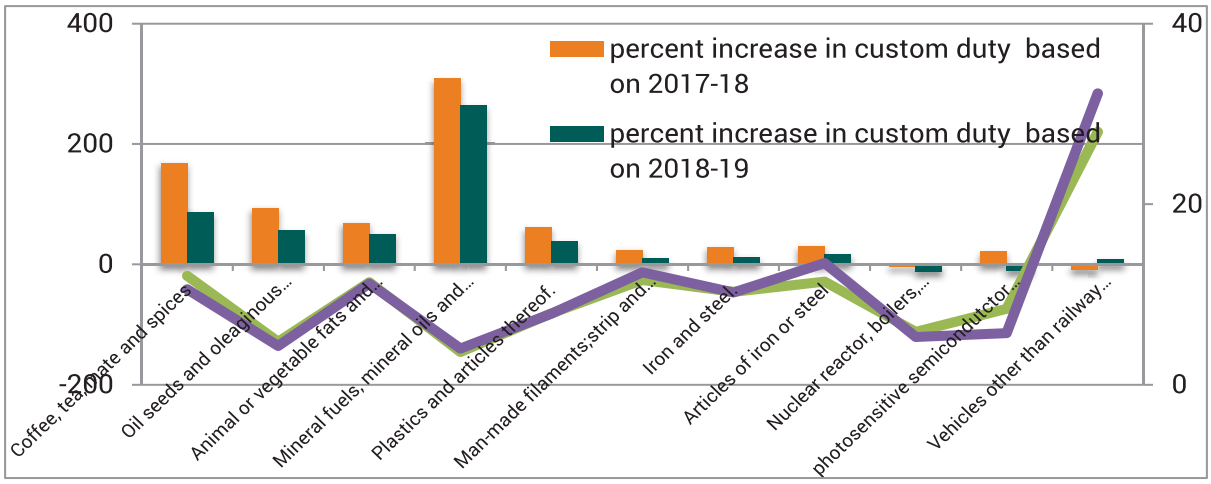
Table 4: Customs duty as Revenue Spinner

Years	Total Import Duties	Miscellaneous	Warehouse Surcharge	Regulatory Duty
2014-15	283946	5066.68	808.69	19128.26
2015-16	377416	4019	648	28550
2016-17	454814	8750	552	37772
2017-18	538019	13679.93	853.22	63584.41
2018-19	605677	15688.49	1063.99	71207.57
2019-20	538076	18458	699	72128
2020-21	654673	21902	835	86948
2021-22	924784	20974	1210	86060
2022-23	763644	16961	1147	173056
GROWTH* RATE IN% (2014-23)	168.94	234.76	41.83	804.71
GROWTH* RATE IN % (2019-2023)	41.92	-8.11	64.09	139.92

**Author's Calculation* *Source: FBR*

Customs duty in Pakistan is imposed on an ad-valorem basis. FBR also imposes duties in specific terms in custom tariff schedule on certain products. For example, Pakistan charges Rs. 10800 per metric ton on Animal fat with HS code 1518 plus 20 percent ad valorem basis. The government of Pakistan also charges 17.0 percent sales tax on the duty-paid value of various goods produced in or imported into the country. This tax burden falls on local consumers due to the inelastic nature of these commodities. Imposing tariffs on such commodities reduces consumer welfare, increases production costs for local industries, and makes them less competitive, creating anti-export bias and generating anomalies.

Figure 2: Composition of Custom duties and growth rate



Author's Calculation *Source: FBR*

Figure 2 shows that how the composition of customs duties and changes in nominal and effective protection rate before and after the enactment of NTP. All the custom duties decreased after the enactment of the policy. However, the rate of growth in changing the effective and nominal protection remains the same. The descriptive statistics showed that standard deviation has increased. Changes in customs duty are more volatile after the enactment of NTP. Increase in dispersion and reduction in mean tariff rate indicates more distortions in the policy.

Table 5: Descriptive statistics of major revenue spinners

Indicators	2018-19	2019-20	2020-21	2021-22	2022-23
Mean	24,005	22,229	35,176	53,868	46,979
Standard Error	5,198	5,016	8,260	18,711	18,155
Median	11,983	10,720	16,896	19,229	22,457
Standard Deviation	23,247	22,432	31,992	72,468	70,313
Range	75,337	78,968	100,929	246,295	279,066
Minimum	6,122	4,257	9,931	10,380	9,934
Maximum	81,459	83,225	110,860	256,675	289,000
Sum	480,103	444,578	527,640	808,022	704,679
Distortion rate	0.96842	1.00913	0.90948	1.34529	1.49669

**Author's Calculation* *Source: FBR*

Table 5 reveals the descriptive statistics of 15 product groups contributed around 73% of the total Customs Duty collection during FY 2022-23. Although, customs duty's share in the total FBR revenues declined from 16.4 percent to 13 percent during the 2022-23 but it is higher in absolute terms when compared it with the base year 2019.

Table 6: Increased Protectionism

Chap #	Commodities	% increase in Imports Value	% increase in CD	Nominal Protection rate*
27	POL Products	-31.4	7.5	-4.19
87	Vehicles (Non Railways)	-43.9	-51	0.86
72	Iron & Steel	-29.9	-17.3	1.73
15	Edible Oil	42.9	22.8	1.88
85	Electric Machinery	-25.5	-33.8	0.75
84	Machinery and Mechanical Appliances	-26.9	-26	1.03
39	Plastic Resins etc	4.3	7.1	0.61
9	Tea & Coffee	16	13.9	1.15
48	Paper & paperboards	16.4	11.3	1.45
73	Articles of iron or Steel	9.1	9.4	0.97
	Sum	-68.9	-69.5	0.99
	Overall	-18	-7.8	2.31
	Mean	-6.89	-5.61	1.23
	Standard Deviation	28.23	24.58	1.74

**Author's Calculation* *Source: FBR*

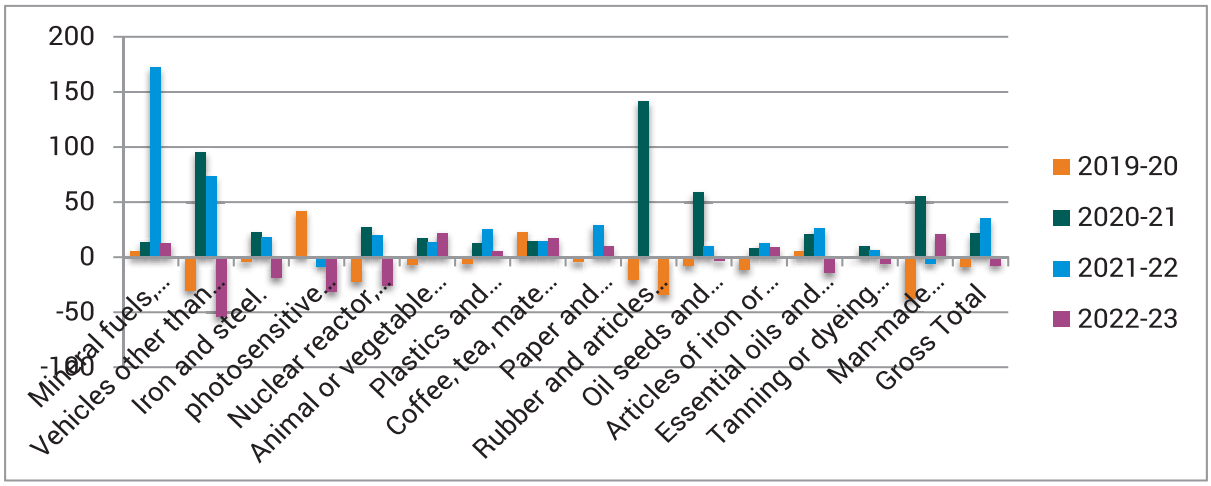
Table 6 showed the growth pattern of imports value and growth of customs duty. Despite there is decrease in value of imports custom duty has not decreased proportionally.

Due to Import policy orders (2020, 2022) government in order to curtail current account deficit-controlled import. Further it has increased the duty rates to collect more revenue from imports. According to FBR, collection from MS (Petrol), High Speed Diesel Oil, Kerosene and Light Diesel Oil (POL) products showed negative growth of (31.4) percent followed by Vehicles (Non-Railway) with (43.9) percent negative growth, Iron & Steel recorded (29.9) Electrical Machinery (25.5) percent negative growth and Machinery & Mechanical Appliances (26.9) percent negative growth. To offset the negative effect of imports contraction policy, FBR increased the nominal protection rate in all these sectors.

Table 6 shows that the duty collected from POL Products increased by 7.5 percent, edible oil contributed 22.8 percent, paper and paperboard contributed 11.3 percent more in customs duty. The negative growth in these sectors have reduced their share in the overall Custom duties. (FBR Yearbook, 2022-23)

To overcome the deficit in duty FBR revised the regulatory duty and additional customs duty in Pakistan. The automobile sector contributes around 9% to the overall Customs Duty collection. Similarly, the iron and steel sector registered negative growth of around 20% due to a decline in its dutiable imports. On the other hand, the collection of edible oils has recorded growth of around 22% owing to a 42.4% growth in its dutiable imports in FY 2022-23.

Figure 3: Composition of the Custom Duty



As far as electrical and mechanical machinery is concerned, the collection of Customs duty declined during FY 2022-23 due to a decline in the value of dutiable imports. In the case of plastic, tea, paper & paperboard, iron & steel, and man-made filament, the Customs Duty went up due to a surge in dutiable imports. Specifically, the increased rates of Customs Duty in the case of paper & paperboard and man-made filaments partly contributed to their increased collection of Customs Duty as well.

The tariff structure is overly complex due to the numerous Statutory Regulatory Orders (SROs) and frequent changes to regulatory duties. This complexity provides unnecessary protection to inefficient industries, leading to misuse and anomalies that adversely affect domestic industries, particularly small and medium-sized enterprises, and hinder competitiveness.

4.2 IMPORT REGULATIONS

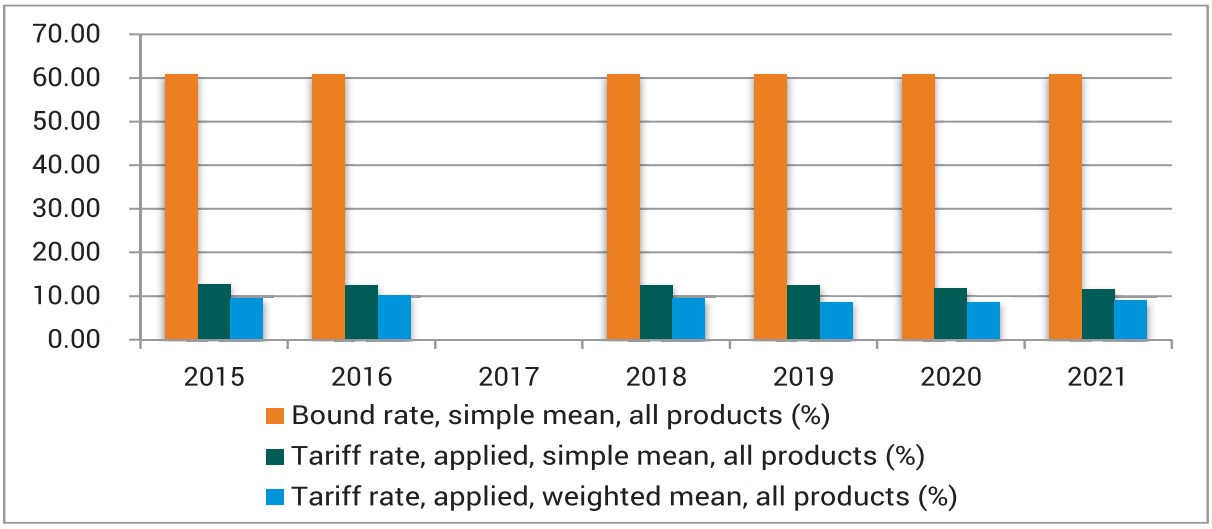
The Import Policy Order, 2022, under the Imports & Exports (Control) Act, 1950, allows the Ministry of Commerce to control imports. Import Policy Orders from time to time allow the government to ban any product from being imported into Pakistan. Pakistan's 2022 Import Policy Order bans the import of 52 categories of products, mostly on religious, environmental, security, and health grounds.

In 2013, there were 44 categories in the banned list. 71 products are in the restricted list, and NOCs are required for importing these products. Part II of the list reflects the 36 goods that have procedural requirements. Part III and IV introduced non-tariff barriers for the import of agriculture commodities and livestock subject to approval from the Plant Protection Organization, Ministry of National Health, and related organizations. Import of medicines is subject to the standards imposed by Drug Regulatory Authority (DRA).

Figure 4 shows that bound rate remains same over the years whereas the simple applied rate and weighted average rate is declining. It reflects that policy is becoming more complex over time.

In the budget 2015-16, concessions on raw materials/input granted to twenty-four (24) domestic industries were withdrawn by removing them from SRO 565(I)/2006. Concessions allowed in customs duty to the remaining twenty-five different industries on the import of raw materials/input under SRO 565(I)/2006 were withdrawn from July 2016.

Figure 4: Tariff rate (bound rate and simple rate)



On 16 October 2017, FBR through SRO 1035(I)/2017 imposed a new RD on 26 items only (137 tariff lines), including new cars (less than 1800 cc), plastic articles, dry fruits, sunglasses, cigarette paper, tobacco, wallpaper, etc. Moreover, rates of RD have been increased on 21 imported items only (219 tariff lines), including betel nuts (Supari), betel leaves (Paan), cosmetics, fruit juices, tiles, footwear, tires, handbags, tableware, kitchenware, and home appliances like air conditioners, refrigerators, etc. The rates of RD range from 10% to 30% on different items.

Since 2016-17, imports of raw materials/ input at concessionary rates of duties have been transformed to statutory rates of customs duty of either 2% or 5%. There are also broad decreases in rates on 2,436 tariff lines, with duty cut from 20% to 6% or 7%. These reductions largely apply to imported raw materials used in the textile industry. In addition, importers of polyester, woven fabrics of synthetic staple fibers and artificial staple fibers, and yarn of artificial staple fibers and manmade staple fibers will now only need to pay 2% duty. The FBR also announced the extension of the exemption from duty on 61 imported medical devices and equipment used in the treatment of Covid-19 until 31 December of that year.

4.3 SALES TAX ON IMPORTS

Sales tax at the import stage is another major contributor to indirect taxes. Sales taxes on imports contributed 61% of the total Sales Tax during FY 2022-23, indicating that domestic producers only contribute 39% to sales tax. This again highlights the multiplicity and burden of import duties. By imposing a ban on imports, the net collection declined by about 8%, mainly due to a 5% decline in the value of imports in FY 2022-23. The government increased the Sales Tax rate from 17% to 18% and 25% on certain luxury items in FY 2022-23.

Petroleum products continue to be the top revenue spinner of Sales Tax on imports, forming about 19% of the total collection of Sales Tax on imports. However, its share has declined from 26% in 2021-22 to around 19% in 2022-23. Sales Tax on the import of edible oil displayed a massive growth of about 45% during FY 2022-23, taking its share in the overall collection of Sales Tax (imports) to 10% compared to 6.5% in the previous financial year. This growth is due to a 42.4% increase in the dutiable imports of edible oil.

In contrast, the collection of Sales Tax on imports for iron & steel, electrical & mechanical machinery, and automobiles

sectors exhibited negative growth due to a decline in the value of imports during FY 2022-23.

Table 7 presents the changes in tariff structure after the enactment of NTP 2019-24. In case of Live animals effectively applied tariff rate increased from 1.13 to 5.17. standard deviation, which is a measure of dispersion and volatility has been doubled from 3 to 6.26. This is because of changes in maximum duty rate for effective rate which hovers between 16.25 in 2018 to 25 in 2022. As a result of these fluctuations, total tariff lines reduced from 69 in 2018 to 54 in 2022. However, there is a decline in bound rate and preferential duty rate. Imports' value decreased from $65048.7 to 79.114.

Table 7: Tariff structure of live animals

Tariff Year	2018	2018	2018	2018	2022	2022	2022	2022
Duty Type	AHS[3]	BND[4]	MFN[5]	PRF[6]	AHS	BND	MFN	PRF
Simple Average	1.13	27.8	2.15	8.13	2.53	48.2	3.47	5.17
Weighted Average	3.67	20.17	3.67	16.22	2.09	95.3	2.43	4.7
Standard Deviation	3	27.83	6.71	7.04	5.1	42.05	6.83	6.29
Minimum Rate	0	0	0	0	0	5	0	0
Maximum Rate	16.25	100	30	16.25	25	100	25	15
# of Total Lines	69	56	69		54	12	54	
#of Domestic Peaks	0	0	0		0	1	0	
# of International Peaks	1	39	4	1	1	11	5	0
Imports Value in 1000 USD	65048.7	65048.7	65048.7	85.583	1504.95	957.271	1504.95	79.114
Binding Coverage		84.62				19.05		

Source: WITS

Tariff structure of live animals shows the gap between bound rate and MFN rate has increased in last 05 years. It is called a large binding overhang which indicates less predictable polices. The tariff structure of live animals becomes less predictable, and we have fewer binding coverage in last 05 years. It indicates more exemptions or bans of imports.

In case of meat and edible meat there is decrease in duty rate, standard deviation and binding coverage and there is a considerable decline in volume of imports as well during the study time. For dairy products, the effective applied rate has increased, dispersion and binding overhang has increased with value of imports decreased. Coffee effective tariff rate increased as well as imports volume and its binding overhang and dispersion. For cereals, milling and malts

[3] AHS stands for Effectively Applied
[4] BND stands for Bound Tariff
[5] MFN stands for Most Favored Nation
[6] PRF stands for Preferential Tariffs

starches effective tariff rate has increased, and imports have also increased. For animal and vegetable fats, the effective duty rate decreased but binding overhang increased. In case of tobacco, the effective duty rate on average decreased with a marginal increase in volume of imports.

All these tables depicting changes in tariff rates can be seen in appendix-I.

4.4 STATUTORY REGULATORY ORDERS (SROS) / EXEMPTIONS AND BANS

In this section, we are discussing some of the important SRO's issued in the last five years.

After the enactment of NTP 2019-24, It was thought that the need to issue SROs will taper off. FBR issued SROs without discussing these in the TPB. Ministry of Commerce also issued import and exports orders through SROs under its power given in Import Act 1950. From time to time, the Ministry of Commerce amended these orders, and every amendment had to be routed through the board for formal submission to the cabinet. Unfortunately, due to the structure of the board there are delays and most of the decisions on countervailing duties took some extra time and resulted into wastage of resources.

In February 2019, the Government of Pakistan through the FBR issued a Statutory Regulatory Order (SRO) 237 (1) 2019, which banned the import of processed food products without labeling in the local language and halal certification. Pakistan's 2020 Import Policy Order continues to ban goods from India and Israel. In addition, there is a negative list of various products that are banned, mostly on religious, environmental, security, and health grounds.

On 30th June 2021, FBR issued an S.R.O. 840(I)/2021, the powers conferred by sub-section (3) of section 18 of the Customs Act, 1969 (IV of 1969), and in supersession of its Notification No. S.R.O. 680(I)/2019, dated the 28th June, 2019, act to levy regulatory duty on the import of goods given in the first schedule of the customs act.

S.R.O. 545 (I) 2022 declares that new imported cars/ vehicles will be those that have been driven up to 2,000 kilometers instead of 500 kilometers, aimed at avoiding detention by Customs at the ports. The Cabinet Committee for Relaxation of Import/ Export-related Prohibitions, constituted vide notification No. 1(13)/2018-AC (TP) on October 11, 2022, considered such cases of "One-Time Condonation of Extra Mileage." The Economic Coordination Committee (ECC) approved the proposal of the Ministry of Commerce. The Federal Cabinet has also endorsed the decision.

SRO 928(1)/2024 Customs Act, 1969 (IV of 1969), the Federal Government has imposed regulatory duty on 611 imported goods. The duty ranges between 5 percent to 90 percent. It imposes regulatory duty on fruits, vegetables, pharmaceuticals, vehicles, etc., at the same time it protects exemptions given in S.R.O. 678 (I)/2004 dated the 7th August, 2004. Imports under chapter 99 of the first schedule of the custom tariff and fifth schedule to the custom tariff, import under PCT codes 1202.4200 and 1517.9000, by registered manufacturers of the food and confectionary industry; and import of input materials used for manufacturing auto parts by local vendors under Notification S.R.O.655(I)/2006, dated the 5th June, 2006.

5 NON-TARIFF BARRIERS (NTBs)

Trade economists typically argue that these non ad-valorem tariffs are less transparent and more distorting, i.e. that they drive a bigger wedge between domestic and international prices. UNCTAD defines Non-Tariff Measures (NTMs) as policy measures, excluding ordinary customs tariffs, that can potentially impact international trade in goods by changing quantities traded or prices. If the coverage ratio exceeds the frequency ratio, it indicates a high NTM impact on that sector. NTBs may be intrinsically protectionist, but they can also address market failures, such as externalities and information asymmetries between consumers and producers. NTMs that address market failures may restrict trade while improving welfare. Other NTMs, like certain standards or export subsidies, may expand trade.

With the implementation of NTP 2019-2024, it was expected that protectionist NTBs would be gradually removed, and NTBs would be used to address market failures and externalities like asymmetric information between consumers and producers. As a signatory to the WTO Customs Valuation Agreement, Pakistan must ensure uniformity in custom valuation. However, Pakistan's custom officials lack explicit minimum valuation methodology and expertise, leading to reliance on declared transactional values. NTBs in Pakistan include labeling and marking requirements, which cause delays and corruption. Import Order 2022 identified banned and restricted product lines, requiring clearances or NOCs from various ministries.

Pakistan's coverage ratio for NTMs is 33.12%, exceeding the frequency ratio of 15.24%. This indicates significant NTM costs. Fuels, Hides & Skins, Transportation, and Footwear are highly impacted sectors. NTM-affected trade is worth USD 32.93 million, with USD 30 million lost due to licensing, certification, and labeling requirements.

The Pakistan Standards and Quality Control Authority (PSQCA) is the WTO-TBT National Enquiry Point, responsible for conformity assessment, testing, inspection, and product certification. The Pakistan National Accreditation Council (PNAC) handles accreditation matters. Various statutes govern trade, including the Pakistan Animal Quarantine Act, Pakistan Plant Quarantine Act, and Drugs Act.

Disputes can be settled through arbitration under the UN Commission on International Trade Law, World Bank's International Center for Settlement of Investment Disputes, or the Court of Arbitration of the International Chamber of Commerce. Pakistan is a member of the Multilateral Investment Guarantee Agency (MIGA) and has signed a Trade and Investment Framework Agreement (TIFA) with the United States.

Sector-specific regulations include:

- Foreign engineering consulting companies must register with the Pakistan Engineering Council (PEC).
- Foreign banks and financial institutions must comply with State Bank of Pakistan (SBP) regulations.
- Telecommunication services require licensing approvals from the Pakistan Telecommunication Authority (PTA).

Table 8 depicts that due to ambiguous non-tariff barriers, a huge amount of trade activity is affected.

Table 8: Losses Caused by Trade Policy Distortions

Sector	NTM Coverage ratio	NTM Frequency ratio	NTM affected product – count	NTM affected trade	NTM partial coverage	Traded products - total	Total Trade	Trade loss
Animal	100	100	147	252681.58	10	147	252681.58	0%
Vegetable	34.06	48.34	146	1733983.86	5	302	5090861.23	-194%
Food Products	4.17	23.53	44	35450.47	0	187	850717.05	-2300%
Fuels	86.16	8.11	3	10310686.69	0	37	11966470.57	-16%
Chemicals	25.75	15.29	111	1471589.49	40	726	5715494.52	-288%
Plastic or Rubber	0.54	3.33	7	13474.84	0	210	2517343.27	-18582%
Hides and Skins	65.53	57.63	34	79065.79	0	59	120658.63	-53%
Wood	10.26	6.76	15	103602.34	0	222	1009297.19	-874%
Textiles and Clothing	1.05	8.77	67	32497.84	0	764	3083910.25	-9390%
Footwear	38.64	31.91	15	39795.18	0	47	102982.52	-159%
Stone and Glass	14.73	17.24	30	66410.26	0	174	450836.63	-579%
Metals	0.1	2.04	11	4012.71	0	538	4169830.26	-103816%
Mach and Elec	1.9	0.65	5	173191.19	0	766	9097511.62	-5153%
Transportation	54.44	25.41	31	1691447.97	6	122	3107155.23	-84%
Miscellaneous	15.79	15.8	55	188928.47	2	348	1196180.92	-533%
All sectors	33.12	15.24	721	16196818.69	63	4732	48896333.09	-202%

Source: WITS/TRAINS

The table above shows that trade can be doubled by removing rigidities and anomalies. See appendix for loss in trade caused by each NTM.

6 QUANTITATIVE ANALYSIS

In this section, we are presenting the quantitative data analysis and results of various economic models used to identify policy misperceptions.

6.1 GAPS IN TARIFF POLICY

Growth in income or stability in prices and consumer welfare has never been the policy objective in Pakistan. Below table shows the results of double log regression model adjusted for robust results.

After determining the level of integration, we estimated the first equation of our model. The first equation estimates the relationship between tariff rates and GDP at current prices in dollars. Increasing tariff rates are negatively related to GDP and positively related to trade duties. This suggests that tariffs are being used as a revenue-generating tool.

In the second model, we tested the relationship between tariff rates, GDP, nominal exchange rates, and inflation rates. All variables were significant, indicating that tariffs contribute to inflation and exchange rate volatility in Pakistan. The low elasticity of substitution suggests that increases in tariff rates are passed on to domestic consumers, adversely affecting consumer welfare.

The third model verifies that tariff rates are determined by their lagged values, indicating that policymakers adopt an incremental approach to collecting revenue without assessing the impact of these tariff increases.

Table 9: Results of Double Log Models (Tariff rate, the Dependent Variable)

VARIABLES	Model 1	Model 2	Model 3
Lgdpc	-.7585132 ***	-0.7549301***	
	.1192366	.0897861	
Ltrade duty	.3007979 **	0.7139552 **	.2369027**
	.0775182	0863051	.0795079
Lnxr		-0.8132714 ***	-0.510486**
		0.1386981	0. 172514
Ltrade		-0.4789275**	-.3714572*
		0.2024026	0.1888946
L.inf		0.0776869**	.0829505*
		0.036999	.0419658
$L.tariff_{t-1}$			.8359003 ***
			.0831082
Constant	19.67531***	19.09759***	-0.615***
	2.119265	1.810335	-0.0606
Observations	32	32	31
R-squared	0.82	0.93	0.95

*Robust standard errors in parentheses *** p<0.01, ** p<0.05, * p<0.1*
Author's Calculation

Our study, which analyzed aggregated annual data from 1991 to 2023, reveals that tariffs have a significant and lasting negative impact on output growth. The effects of tariffs are not only statistically significant but also economically substantial, with a one standard deviation increase in tariff rates leading to a 0.75% decline in output three years later.

The decline in output can be attributed to several factors, including reduced efficiency in labor use across sectors, an appreciation of the real exchange rate that hampers competitiveness, and higher imported input costs that raise production costs. Additionally, anticipated tariffs can bring forward consumption and output once the tariff is imposed, leading to inter-temporal effects.

Notably, our findings suggest that the costs of tariffs are likely a lower bound on the costs of protectionist policies more generally, as non-tariff barriers are likely to have even higher costs than price-based restrictions. Our results align with previous studies, which have found that higher tariff rates indicate weak institutional capacity to collect taxes through imports. Furthermore, high tariff rates can reallocate labor from the export goods sector to highly protectionist industries, ultimately hampering growth, exports, and innovation through spillover effects. In contrast, lower tariff rates are associated with increased growth and effective institutional quality.

6.2 VAR-GRANGER TEST

The Wald test was employed to determine the bilateral causation between the variables. A concern with using the double log regression model and tariff rate as the dependent variable is that, in an economy where tariff rates are used as a revenue generator, reverse causality may occur, potentially overestimating the negative relationship between tariff changes and depressed economic performance.

Table 7 presents the results of our Granger causation test. A significant bilateral causation was found between tariff rates and GDP. However, no causation was detected between trade and tariff rates, which is a surprising result. This can be attributed to the nature and composition of our imports and the elasticity of substitution. An increase in tariff rates does not appear to be a shock, as commodities like crude oil, palm oil, coffee, and tea remain inelastic to changes in tariff rates.

The contraction in trade and GDP due to an increase in tariff rates leads to a depreciation of the Pakistani Rupee. No direct causation was found between the exchange rate and tariff rate. However, a unilateral causation exists between the inflation rate and tariff rate, running from inflation rate to an increase in tariff rates. This is an interesting result, as inflationary shocks lead to an increase in tariff rates, which depresses GDP and causes a depreciation of Pakistan's Rupee.

Tariff rates, customs duty, and all other regulatory duties are bilaterally causing, indicating that imports are income and demand inelastic, with no close substitutes existing for these products. The causation results show that tariff shocks are adversely affecting the economy by reducing demand. The burden of tariff increases is passed on to consumers, causing a significant reduction in consumer welfare.

This further proves our hypothesis that a bilateral causation between tariff rates and GDP adversely affects consumer welfare. It also proves that the policy of using tariffs as a revenue spinner by the Federal Board of Revenue (FBR) is a major reason for curbing exports from Pakistan. The spill-over effects need to be measured by examining data on productivity and inequalities.

Table 10: VAR GRANGER CAUSATION RESULTS

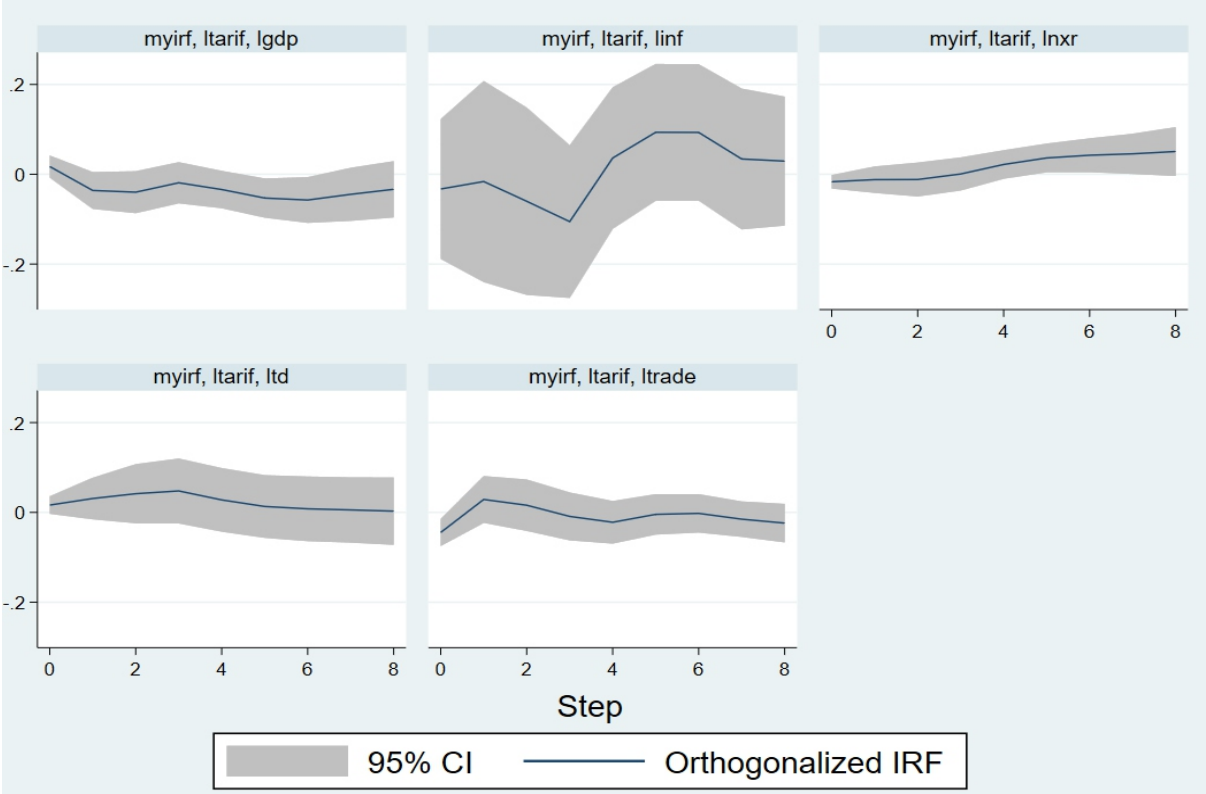
Equation	Excluded	chi2	df	Prob > chi2
Ltarif	1gdp	5.1362	2	0.077
ltarif	ltrade	.50951	2	0.775
ltarif	1nxr	4.3911	2	0.111
ltarif	linf	.45366	2	0.797
ltarif	1td	6.9116	2	0.032
ltarif	ALL	10.624	10	0.388
1gdp	ltarif	7.9785	2	0.019
1gdp	ltrade	.45355	2	0.797
1gdp	1nxr	7.7795	2	0.020
1gdp	linf	.15601	2	0.925
1gdp	1td	.96076	2	0.619
1gdp	ALL	40.761	10	0.000
Ltrade	ltarif	2.0259	2	0.363
Ltrade	1gdp	3.6868	2	0.158
Ltrade	1nxr	12.595	2	0.002
Ltrade	linf	11.755	2	0.003
Ltrade	1td	6.2476	2	0.044
Ltrade	ALL	27.026	10	0.003
1nxr	ltarif	2.6256	2	0.269
1nxr	1gdp	9.7361	2	0.008
1nxr	ltrade	.34554	2	0.841
1nxr	linf	.96772	2	0.616
1nxr	1td	1.7389	2	0.419
1nxr	ALL	36.411	10	0.000
Linf	ltarif	5.7537	2	0.056
Linf	1gdp	4.3882	2	0.111
Linf	1trade	3.5977	2	0.165
Linf	1nxr	3.6834	2	0.159
Linf	1td	2.4641	2	0.292
Linf	ALL	12.48	10	0.254
1td	ltarif	13.007	2	0.001
1td	1gdp	1.9592	2	0.375
1td	1trade	10.912	2	0.004
1td	1nxr	32.6	2	0.000
1td	linf	11.912	2	0.003
1td	ALL	68.333	10	0.000

6.3 IMPULSE RESPONSE FUNCTION

Impulse Response Function (IRF) describes the reaction of a set of variables to a shock in one or more macro-economic variables. IRF traces the transmission of a shock which enables us to assess the impact of economic policies.

In this study, impulse response function was calculated on the basis of the first order Vector Auto Regressive (VAR) Scheme. The model was adjusted for a small data set. It is clearly evident that tariff rates are depressing the GDP.

Figure 5: Impulse Response Function



Author's Calculation

Each of the five panels estimates the baseline response function for GDP, inflation, exchange rate, total custom duties, and trade to a one standard deviation increase in the tariff rate. Time is measured on the X-axis.

The results in the left panel graph show that a one-standard-deviation increase in the tariff rate will lead to a decrease in GDP for three consecutive years before it is absorbed into the system. This brings uncertainty and more fluctuations to the economy.

In contrast, the graph showing the impact of tariff changes on the inflation rate has a wider band, indicating more volatility and a greater increase in the inflation rate.

Panel 3, located at the top right, shows the impact of tariff changes on the exchange rate. It reveals that tariff changes cause a depreciation of the currency. The impulse from the tariff rate brings more volatility to the inflation rate and depreciation of the Pakistan Rupee.

Panel 5 shows that high tariff rate depresses trade as percent of the GDP in long run as well.

6.4 QUALITATIVE ANALYSIS

This content analysis investigates varied perspectives on Pakistan's National Tariff Policy (NTP) through a detailed comparison of views expressed by diverse professionals. The major themes and concerns emerging from the content analysis are competitiveness of trade, tariff policy's procedures and management, and future directions of tariff policy. We categorized these themes into trade promotion, tariff management, and policy effectiveness. Common sub-themes included prioritizing NTP's role in enhancing competitiveness, simplifying bureaucratic hurdles, and the public sector's regulatory role.

Challenges in Trade Policy emerged as a key theme, with experts identifying regulatory barriers hindering effective trade facilitation. Key issues mentioned by experts include policy inconsistencies creating uncertainty for stakeholders and public sector involvement complicating the trade landscape.

These challenges are crucial for understanding the broader context within which NTP operates. Experts view bureaucratic inefficiencies and public sector involvement as critical barriers to achieving desired outcomes within the NTP framework.

Mr. Mehtab Haider criticized the frequent use of SROs as a tool for fiscal adjustments rather than as part of a coherent trade policy. Mr. Saud Bangash highlighted how regulatory duties, initially introduced to regulate trade and protect industries, have become instruments for short-term revenue generation rather than supporting long-term industrial growth.

Tariff Policy and Competitiveness revealed diverse opinions among experts. While there was general agreement that protectionism and competitiveness work at cross-purposes, some experts proposed competitive strategies to improve market positioning, and others believed protectionism may provide short-term benefits. Experts emphasized the need to maintain a delicate balance when formulating tariff policies. They urged domestic industries to enhance their global competitiveness gradually.

Mr. Rastgar noted, "Protectionism must be combined with a plan for capacity building and innovation." Experts like Dr. Manzoor and Senator Zeeshan Khanzada raised concerns about the auto sector's performance, where protectionism led to a lack of innovation and above-average market prices. Senator Khanzada compared car prices in Pakistan with India, illustrating that protectionist policies resulted in overpriced, lower-quality products, and loss of consumer welfare.

The Federal Board of Revenue's (FBR) role was found to be a **major concern.** Experts highlighted that trade promotion and revenue generation are dual objectives. They expressed concern that FBR's prioritization of revenue undermines the conducive trade environment. Experts desired to align imports as revenue spinners with the overall performance and future direction of the policy.

Mr. Ashfaq Ahmad emphasized using tariffs as instruments for industrial protection and trade promotion whereas Zaheeruddin Dar Sahib were of the view that there is no such thing as tariff policy. Tariffs are the tools in the hand of custom officials which helps in achieving the policy objectives of respective polices. Suppose the objective of health for all can be achieved by affordable medicine. FBR can impose low tariff or no tariff on the pharmaceutical raw material or medicines keeping in view the objective of health policy.

Dr. Robina Athar added that FBR's reluctance to cede control over tariff-related matters

leads to delays in implementing pro-industry reforms. Dr. Aadil Nakhoda emphasized that the revenue-driven approach creates disincentives for industries to innovate, as higher tariffs on inputs make upgrading technology or improving productivity more expensive. The NTP performance theme revealed a consensus on the necessity of strategic adjustments to bolster the policy's impact. Experts agreed that NTP has been a notable success, but future policy must enhance the effectiveness of the tariff board and improve stakeholder engagement.

Additionally, there was a consensus that **import substitution** of strategic industries has largely failed to create competitive industries capable of thriving in the global value chain. The import substitution approach needs to be better aligned with international standards, focusing on becoming part of global value chains.

Mr. Saud Bangash viewed that the **cascading tariff system** introduced in NTP has not been effectively implemented, hindering industrial growth. Dr. Aadil Nakhoda emphasized that without embracing export-oriented and open market policies, Pakistan will continue to lag behind regional competitors like Vietnam and Bangladesh.

Dr. Robina Athar and Dr. Safdar Sohail emphasized the need for a data-driven approach to policy formulation, arguing that the current lack of sectoral analysis and economic forecasting makes it difficult to develop long-term policies. Experts highlighted the need for **real-time, high-frequency data** availability and access for better decision-making. They voiced concerns that inadequacies in current data regimes hinder effective decision-making and policy formulation.

The most prominent node was **'Future Directions'** of the tariff policy. Experts highlighted the need for adaptive strategies and dynamism in policy-making to deal with challenges and harness trade opportunities. Dr. Safdar Sohail emphasized a selective industrial policy balancing trade openness with the protection of strategic industries. He suggested conducting sectoral analysis and careful implementation of trade policy, noting that generalized policies have hurt domestic industries in the past.

Furthermore, Labour Productivity surfaced as a concern, with experts noting that low productivity levels significantly impede the potential benefits of trade policies."

Table 11: KEY THEMES AND QUOTES

Themes	Sub Themes	Quotes
Trade Promotion	Protectionism and Competitiveness	"Trade is the shortest, easiest and tested way to reduce poverty". "Pakistan is among the 7 most protectionist countries." "Trade, investment, and aid must go hand in hand, especially in partnerships like CPEC." "Early liberalization of trade with the hope that exports would drive growth proved to be a costly mistake." "Parliament determines the Custom duties whereas federal cabinet imposes regulatory duties. Both of these must aim to balance trade regulations and protection." "Immediate international competition without proper protection risks de-industrialization."

Themes	Sub Themes	Quotes
	Competitiveness Strategies	Competitiveness should come from the specialization and sophistication of exports, not from paying minimum wages to labor. The link between comprehensive social security and labor productivity is undeniable. Local industries need gradual exposure to global markets to scale and compete effectively. Unfortunately, Pakistan never became part of global value chains.
Tariff Policy and Competitiveness	Protectionism and Competitiveness	"Policy formulation is fragmented because key players like FBR, Commerce, and Finance have different objectives. FBR uses tariffs as a revenue instrument, Finance manages the balance of payments, and Commerce focuses on trade facilitation". "The tariff policy has to be defensive. But serious reforms are needed, beyond tariff policy alone, including revisiting foreign exchange and FDI policies with proper regulatory capacity."
	Competitiveness Strategies	"We have allowed tariff policy to become fragmented, even at the sectoral level, and lobbies have exploited this by 'forum hopping' to get better deals from different departments, like the Engineering Development Board or the National Tariff Commission."
Tariff Management and Data Regimes	Data-Driven Tariff Policy	Effective tariff policy requires well-researched analysis of each tariff line and item, something Pakistan often fails to do. Incorrect concessions and misguided negotiations, like those with China, have hindered trade progress.
	Data Accuracy and Accessibility	Data accuracy is the key to develop a forward-looking policy
	Current Data Regimes	National Tariff Policy or other policies—the country risks continued stagnation.
Success Stories, SROs	Positive Impact	"Pakistan's paper industry is robust, but publishers face high costs due to the regulatory duties "
	Negative Impact	"Inefficiencies in industries like the automobile sector, which remain heavily protected by tariffs."
Revenue Collection and Tariff	Tariff as Revenue Tool	"Recent tariff changes were made without involving the National Tariff Policy Board, even though the policy mandates" "Tariff policy should not be used as a revenue spinner but as a tool for trade facilitation and industry growth. High tariffs on imported inputs limit value addition, making it hard for local manufacturers to compete globally."
	Revenue vs. Competitiveness	Custom duties are the parliament's authority, while regulatory duties are set by the federal cabinet, aiming to balance trade regulation and protection.

Themes	Sub Themes	Quotes
Performance of NTP	NTP Review	"In 2019, tariff determination shifted from the FBR to the Ministry of Commerce to promote trade and protect industry, with tariffs used as industrial and trade promotion tools."
	NTP Success	"The National Tariff Commission, which had shown some improvement, has now reverted to an ad-hoc approach, and the FBR is influenced by political masters who control appointments and operations".
	Future Directions for NTP	Pakistan needs to improve its Trade Remedy Laws (e.g., anti-dumping and countervailing duties) to protect local industries from unfair foreign competition.
FBR Role	FBR & Revenue Generation	"The influence of Finance and FBR has been greater than Commerce for several years"
Economic and Social Impact of Trade Policies	Consumer Welfare	The long-term economic plan should aim to improve the standard of living through trade, not just focus on energy projects.
Challenges in Trade Policy	Regulatory Barriers	Export lobbies continue their usual profit-making ways, but it is the government's responsibility to recognize unsustainable practices.
	Public Sector Involvement	Our competitiveness was hindered by a lack of understanding of our sectors and ineffective consultations among government ministries.
	Policy Consistency	"Pakistan needs a merit-based professional group for better outcomes." "Pakistan's economic problems are multi-dimensional, influenced by short-term policymaking, bureaucratic caution, and entrepreneurs' focus on wealth diversion rather than creation." "Consistent policy encourages industries to compete globally".
	Bureaucratic Issues	"Historically, bureaucrats were not adept at understanding the trade dynamics." "Over the years, upright professionals in ministries like Finance, Planning, Commerce, and FBR have been sidelined" "Professionalism can be nurtured through rotations, international exposure, and grooming for higher positions." "The District Management Group (DMG) prioritizes its cadre over specialized professionals".

The content analysis concluded the need for a balance between protectionism and trade liberalization, balance between policy formulation by the Ministry of Commerce and policy implementation by the FBR, the impact of tariff structures on industrial competitiveness, and the broader implications of the NTP on Pakistan's trade policy.

Figure 6: Main themes

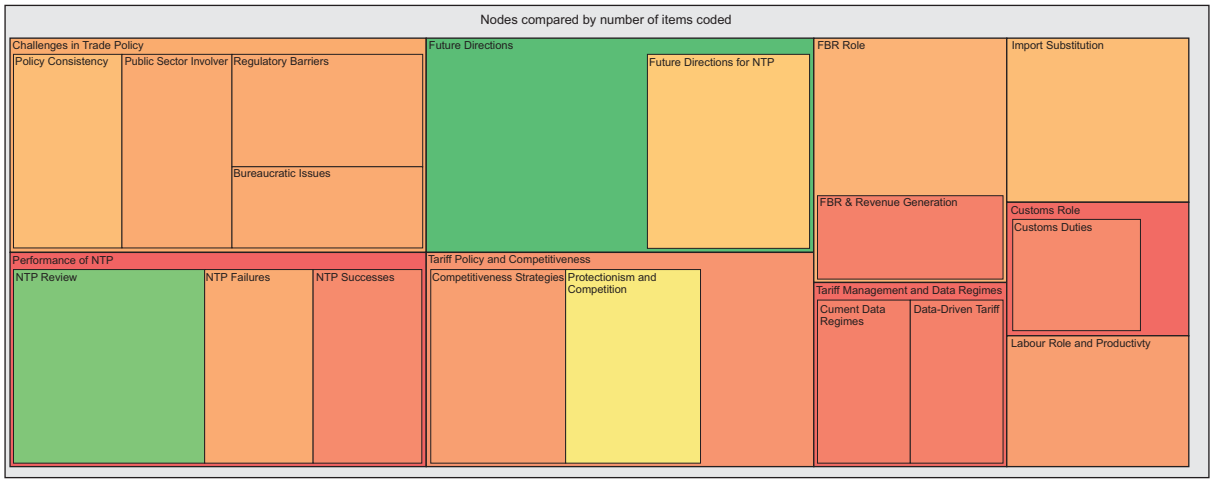


Figure 6 reflects the main themes emerges from our content analysis. All experts were agreed on the review of NTP, and desired to have a holistic and simplified tariff structure for trade promotion. Experts believe that there is need to have minimum and clear role of the public sector departments and ministries. Future direction of the policy must be based on real time data and analysis.

7 NATIONAL TARIFF POLICY 2019-24

On November 19, 2019, the Federal Cabinet approved the first National Tariff Policy (NTP) 2019-2024. NTP (2019-2024) marked a significant departure from the old practice of imposing tariffs, including customs duties, regulatory duties, and additional regulatory duties. The policy mandates the Ministry of Commerce to submit proposals for tariff changes after consulting with all relevant stakeholders at the appropriate level i.e. Federal cabinet.

According to the Federal Government Rules of Business 1973, amended on December 20, 2021, the Ministry of Commerce is responsible for tariff policy, protection and promotion of local industry, and dispute resolution. The Commerce Division administers trade defense laws related to anti-dumping duties, safeguards, and countervailing duties through the National Tariff Commission.

To implement this policy, a Tariff Policy Board (TPB) was established, chaired by the Minister/Advisor of Commerce. The board comprises representatives from relevant ministries, including the Minister for Industries & Production, Secretary Finance, Secretary Revenue, Chairman FBR, Secretary Commerce, Secretary Board of Investment, and Chairman NTC.

A Tariff Policy Center (TPC) was set up within the National Tariff Commission to consult with stakeholders, invite proposals from businesses, and submit analyzed proposals to the board for approval. Any changes or amendments to tariffs, including regulatory duties and customs duties, must be examined by the Tariff Policy Centre and approved by the Tariff Policy Board before being submitted to the Cabinet or Parliament. Tariffs on imports include customs duty, additional customs duty, and regulatory duty and any other taxes which are imposed on imports or exports.

Parliament is the supreme authority for changing customs duties, as part of the finance bill, while the Cabinet has the final authority to change regulatory and additional regulatory duties based on the Ministry of Commerce's recommendations. To deal with revenue shortfalls, FBR or the Ministry of Commerce can issue SROs.

The policy principles include:

i. Using tariffs as an instrument of trade policy rather than revenue generation

ii. Maintaining vertical consistency through cascading tariff structures

iii. Providing time-bound 'strategic protection' to strategic domestic industry during its infancy phase

iv. Promoting competitive import substitution through time-bound protection

v. Phasing out protection to make the industry competitive for export-oriented production.

To achieve these objectives, the NTP instituted a Tariff Policy Board (TPB). The Board includes all relevant stakeholders including secretaries from all economic ministries. Secretary Commerce acts as

secretary to the Board and a Tariff Policy Centre (TPC), (based in National Tariff Commission) serves as technical arm of the Board. Based on TPC's analysis, the proposals or recommendations are presented before the Board for any changes in tariffs including CD, ACD and RDs.

The objective of NTP (2019-2024) is also to enhance the competitiveness of local industry by providing duty-free access to imported raw materials. A predictable tariff structure is crucial for promoting investment in efficient industries. NTP (2019-24) has proposed changes in institutional arrangements by transferring the power to impose tariffs from FBR to an inclusive forum comprising all relevant ministries, which takes decisions through majority votes. However, it results in complexity and indecisiveness. The Minister of Commerce chairs the board meetings and has one vote, like all other members.

NTP 2019-24 has also changed the principle of imposing regulatory duties and additional regulatory duties, shifting from restricting imports to promoting growth and local industrialization by providing cheap raw materials. NTP planned to study value chains of all imports and based on cascading principle, it was decided to provide cheap raw material to the local industry.

7.1 POLICY PATTERNS AND MISSTEPS

National Tariff Policy was a shift from revenue generation to using tariffs as a tool for promoting trade and industrialization. This was considered as a right step in the right direction because it aims to simplify tariff structure, which would be fairly predictable as well. It would not be easy to manipulate all the members of the board so it was seen that personalized and influential businesses would not try to change the governance of tariff in Pakistan.

After the inception of NTP, it was thought that tariff decisions must be based on rational analytical grounds rather than on ad-hoc basis announced in budget after calling budget proposals. It was a good intent to change tariff measure on strong research footings. Unfortunately, NTC remained deficient in experts to deal with complicated tariff issues.

NTP also aims to provide time-bound strategic protection to strategic domestic industries during their infancy phase, which can help them develop and become competitive. There was a sunset clause, which would allow the protection to be phased out after some time. It uses cascading as the basic principle to implement tariff.

Various departments were the stakeholders in the TPB. However, most of the senior representatives of the ministries and departments remained absent from the meetings. This lack of engagement with the NTP agenda and inadequate meeting preparation significantly results in a fractured decision-making process, causing delays. NTP (2019-2024) did not use the “one member one vote" principle in the TPB decision making. The Chairperson of the board typically makes decisions after gathering input from all members present in

the meeting. However, five years after the National Tariff Policy's (NTP) enactment, its rules and procedures remain undefined.

Stakeholders often attend meetings without grasping the discussed issues or send junior colleagues, lacking the necessary context. Disagreement causes stalemate and delays. In most cases, the Minister of Commerce has to make decisions based on meeting input. Furthermore, some decisions face legal challenges, leading to additional delays and ultimately, the board's ineffectiveness. It would have been better for such a forum to have had adopted rules of business based on the principle of equal representation.

There was no mechanism given in the policy to deal with disagreement. As a result of these hurdles, we see the NTP (2019-24) becoming dormant and less effective. Perhaps, the better solution would be to deal with these challenges rather than discarding the policy. The policy was a right step in the right direction, but it had both implementation and design issues. It remains silent on the use of Statutory Regulatory Orders (SROs) by various ministries for dealing the unusual circumstances. NTP lacks in addressing the implementation mechanism, and there were issues about transparency and accountability mechanisms.

Non-tariff measures (NTMs) are another area which was out of the sphere of the NTP. All other tariff-like measure like imports sales tax and surcharge etc. never been in the scope of NTP. By addressing these challenges, the revised NTP can enhance effective implementation.

8 CONCLUSION

Empirical evidence proves that a uniform tariff rate is the most efficient way to handle trade policy. Differentiating between essential and less essential imports adversely affects resource allocation and import substitution policies. Inflation and exchange rates have a uniform effect; differentiating tariff rates makes it difficult to calculate opportunity costs.

The cost of handling complex tariff structures and involvement of various regulatory bodies and approvals causes delays in customs clearance. Optimizing revenue would be easier at a uniform rate rather than calculating custom duties at different rates. One can calculate the nominal protection rate, but it would be challenging to calculate trade intensity and effective tariff rates.

Pakistan's import structure shows that commodities with low tariff rates have higher trade volumes. This suggests that the government also wants to promote imports and discourage the use of certain products. High tariff rates do not discourage consumption of products; people can't change their habits. This results in under-invoicing and smuggling.

Complex tariff structures are heavily influenced by lobbying from established import substitution producers for low tariffs (and if possible, zero tariffs) on their intermediate inputs. The benefit to them of cuts in tariffs affecting the cost of intermediate raw materials and components often exceeds the benefit of increases in tariffs protecting finished products.

Duty on raw materials was reduced to facilitate local production. However, with a cascading tariff structure, there is no chance that the country will achieve sufficiency in production of the same commodity.

Firstly, the intent and effect of tariffs aimed at protecting local production are to reduce imports, making it possible to balance the current account at a higher (stronger) rupee value in terms of foreign currencies. Secondly, even assuming that duty neutralization schemes could be operated with low or zero transaction costs for exporters, unless explicit export subsidies are paid, exporters have to compete on world markets with no protection.

Moreover, production for export is further disadvantaged by the consequent overvaluation of the exchange rate. Thirdly, many exports are typically also sold as intermediate inputs to processors, which use them for production sold on the domestic market. Unless exporters of these intermediate exportable have market, power and can charge higher prices domestically than when exporting, processors obtain inputs at approximately world prices while benefiting from tariff protection on their sales.

These effects lead to the observations that, in the interests of economic efficiency and taking account of political and administrative feasibility, tariffs should be uniform and low. High duties on imports lead to smuggling. In some cases, smuggling exceeds imports through regular channels. Estimates suggest that smuggling is almost 60% of the regular channel.

Higher duties and a multiplicity of non-tariff measures lead to under-invoicing and

corruption. Mis-declaration at Customs and smuggling can be controlled with a uniform custom duty rate. Estimates of yearly customs duty revealed that the average Custom duty rate is 13% for imported products, with a standard deviation of around 15. So, the nominal protection rate varies from zero to 28%. The maximum bound rate is even higher when including excise duties, sales tax, surcharge, and additional custom duties.

There is a need to simplify the process. Imposition of custom duties, SROs, and exemptions opens avenues for smuggling and under-invoicing. These cumbersome rules create special interest and rent-seeking trader groups who can create shortages and benefit from being insiders, raising artificial prices in the market, as seen in the wheat and sugar crises.

The policy's short-term focus has contributed to its lack of effectiveness, as political and bureaucratic cycles drive decision-making, often ignoring the long-term strategic needs of the economy. Moreover, high tariff rates on inputs have discouraged local production, limited value addition, and stunted industrial competitiveness, particularly in sectors like textiles and automobiles.

9 RECOMMENDATIONS

Simplification of Tariff Structure: Streamline the tariff structure by reducing the number of tiers and slabs. One product, one duty rate may be the golden principle to follow. There is a need to remove all the anomalies and exemptions. SROs may be issued only in extraordinary times. Change in custom duties, regulatory duties and additional regulatory duties through a consultative process must be time bound.

Tariff Rationalization: Rationalize tariffs to ensure balanced protection for domestic industries while avoiding high levels of protection that can lead to inefficiencies. Pakistan is still struggling to find out one optimum tariff rate while the world has moved from rationalization of tariff to offshoring and global value chains. The cost of administering such policies is huge and causes inefficiencies. These are indicators of the weak institutional capacity of FBR to collect revenue from indirect sources. Customs officials have no capacity to assess the tariff except imposing tariff on declared values. This search for rationalized tariff is a source of smuggling and a hindrance to the growth of the small and medium enterprises.

Gradual Tariff Reduction: Gradually reduce tariffs to encourage competition, increase efficiency, and promote trade. Government must plan to simplify tariff structure by introducing a two-pronged strategy. Firstly, it should build the capacity of customs officials to assess the value of declared commodities and second, it should remove rigidities in tariff structure. It can start by removing additional regulatory duties and regulatory duties by the act of parliament and impose a single-digit customs duty in a product group. At the next stage, the rates can be curtailed. Later, it can announce a mechanism for protecting the local industry from countervailing duties as per outlined in WTO framework.

Enhanced Transparency: Enhance transparency in tariff policy by providing clear and easily accessible information on tariffs and trade policies. It will reduce the time required for custom clearance.

Regular Review and Update: Regularly review and update the tariff policy to ensure it remains relevant and effective in achieving its objectives. The broad framework and policy objectives may be reviewed every ten years. This review will help in addressing strategic issues in policy and will also make policy dynamic. There is also a need to address the spillover effects of tariff policy on the labor market and economic growth.

Coordination with Trade Agreements: Ensure coordination between tariff policy and trade agreements to avoid conflicts and ensure compliance. This coordination would help to mitigate the negative effects of contraction in consumer welfare and demand.

Support for Export-Oriented Industries: Provide support for export-oriented industries through targeted tariffs and incentives. Duty drawback facilities are not favoring the small and medium industries. There is a need to have a comprehensive study addressing the issue of countervailing duties. The procedure is lengthy and tedious. A comprehensive study of countervailing duties will help the importers and exports and will also minimize

the need for immediate relief in the form of SROs.

Addressing Revenue Concerns: Address revenue concerns through measures such as improving tax administration and broadening the tax base. Perhaps there is a need to reduce the exemptions given in the fifth schedule. The exemptions given in 'respective headings' are creating many anomalies. There is a dire need to have comprehensive regulatory standards to minimize the role of personalized influence of regulatory bodies. The negative list needs to be revisited for dealing with smuggling and the illegal economy.

Monitoring and Evaluation: Establish a monitoring and evaluation framework to assess the impact of tariff policy on the economy and trade.

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