

Country Update

The WTO Agreement on Trade in Services: Main Issues Faced by SMEs in Pakistan and Their Solution

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Context

This study was carried out from the 3rd to 24th June 2016 by PRIME (Policy Research Institute of Market Economy), Islamabad as a part of a CUTS International and Australia Aid Project entitled “Geneva Trade and Business Connexion: South and South East Asia”. The main objective of the project is to improve the capacity of the small and medium enterprises (SMEs) to provide input into their government and their WTO delegations so as to make their negotiating positions more fully aligned with on the ground conditions faced by small scale enterprises.

Methodology

In order to obtain the views of various stakeholders on the issues that SMEs faced when trading services with other countries, primary data was collected through personal interviews, visits and telephonic contacts with

several individuals and SMEs. In addition a questionnaire (Annex A) was also circulated but response to the questionnaire was not encouraging. Furthermore, the previous work done on export of services from Pakistan was also reviewed.

Background

Small and Medium Enterprises (SMEs) play a critical role for Pakistan's economy. Their number is estimated at 3.2 million, which accounts for over 90% of all businesses in Pakistan. They employ 80% of the non-agricultural labour force. Their contribution to the national gross domestic product (GDP) is estimated at about 40%.

Services is the fastest growing sector of Pakistan's economy and now constitutes 59 per cent of Pakistan's GDP . During 2015-16, this sector grew by 5.71 percent. However, in terms of international trade, the share of services is less than 20 percent of the total trade with

exports being US\$ 5,880 billion and imports being US\$ 8,843.

Lower share of exports in overall trade could also be due to the fact that services, which constitute significant share of GDP such as retail trade, wholesale trade, restaurants, hotels and construction are mostly domestically generated and supplied. There are also significant barriers for export of several services.

The most important issues for Pakistan's economy are high unemployment, stagnant exports and relatively low economic growth compared to its neighbours. The GDP growth has shown some improvement, now reaching about 4.7% during 2015-16 financial year, but exports for goods and services have continued to stagnate at around US\$ 30 billion per year for the last 5 years.

This note is intended to highlight the issues that SMEs in Pakistan face when trading services with other countries and provide input to Pakistan's delegation to the WTO GATS (General Agreement on Trade in Services) of those problems. Another objective is to familiarize SMEs with the on-going Trade in Services Agreement (TiSA) negotiations at Geneva and whether SMEs can point out any specific services where Pakistan could seek further liberalization through those negotiations.

Awareness about the WTO GATS and TiSA

There is almost no familiarity with the WTO GATS and the proposed TiSA Agreements. This could be partially due to the fact that the share of trade in services is rather low and unlike goods, there is very little interaction with the government. Furthermore, GATS being a relatively recent agreement, very few are aware of its' being a part of WTO agreements. Not a single SME interviewed had any idea about the

current status of the TiSA or the nature of issues being discussed there.

GATS and SMEs

Main issues faced when trading services

An overwhelming number of SMEs only concentrate on the domestic market. Those interested in exports, mostly rely on exporting online through Mode 1. However, there were sizeable numbers who were interested in Mode 2 (consumption abroad) and Mode 4 (temporary movement of persons). One of the major problems noted by many SMEs was the difficulty in accessing finance and regulatory issues in Pakistan and the destination country.

Although commercial linkages exist between services exported through various modes, for ease of discussion main issues when trading services are discussed in terms of the four modes of delivery of services as recognized by GATS.

Mode 1 – Cross Border Supply

In Mode 1, cross-border supply, only the service crosses the border. The delivery of the service can take place, for example, through telecommunications (telephone, fax, television, Internet, etc.), or the sending of documents through email or hard copies.

This is the most well-known and common method of supply of services from Pakistan. In order to find out the current status and barriers to export, several professionals including software developers, computer programmers, lawyers, doctors, engineers, architects, town planners and designers were interviewed.

These consultations showed that the area which faces the least barriers, is relating to export of software and data coding. According to Pakistan Software Export Board (PSEB), there are more than 110,000 highly qualified

professionals working in this field. Of these, about 24,000 are engaged in software export. There are approximately 2000 SMEs working on freelance basis. In 2014, Odesk ranked Pakistan at number 4 in the list of most earning countries in the world. According to the same report, Pakistan was among the countries that saw a 30% increase in freelance income in 2014 than 2013. The top skills offered by companies in Pakistan are website development, software development, web application development, graphic designing, multimedia, finance and management.

Other Mode 1 services such as consultancy or market research reports, tele-medical advice, distance training, or architectural drawings have not developed to the same extent due to various barriers and lack of local capacity. Dr Nisar Ahmad, an independent consulting family physician, explained that he did not see much scope for his profession to give online medical advice as Pakistan Medical Council restricted prescribing through Internet or on telephonic basis except when the physician was cognizant of the individuals past medical history. Similarly a large number of lawyers were asked if they would be interested in giving legal advice on line. There was some interest but most were of the view that it would not be easy due to licensing and payment problems. Several professionals were of the view that there was considerable scope for architects, accountants and tax experts to provide services online but of the several professionals interviewed, none was providing such services.

● *Mode 2 – Consumption abroad*

Mode 2, consumption abroad, occurs when consumers consume services while outside their country. In case of Pakistan, visits by foreigners such as Sikhs to holy places in Pakistan as well as for medical treatment are typical examples.

Interviews with local service providers indicated that indigenous regulatory issues were the

most significant barriers. For example, many tour operators referred to religious and medical tourism that was greatly hampered by strict visa regime applied by Pakistan. According to a recent World Bank study, if the visa was sufficiently relaxed and security situation improved significantly, the number of religious tourists could exceed 300,000 per year and the economic impact could increase from \$5 million to an estimated \$300 million.

In case of medical tourism, currently most patients visiting Pakistan are either from Afghanistan, Central Asia or overseas persons of Pakistani origin. According to Dr. Adnan, a dental implant specialist, “Pakistan is receiving many patients from abroad. In fact, the medical economy around border cities such as Peshawar is based on cash payments made by Uzbek, Tajik and Afghan patients from Afghanistan and other Central Asian countries”. A doctor giving infertility treatment explained that it is the attraction of cost and the expertise of Pakistani doctors that brings in many foreigners for treatment here. While in Pakistan, the cost for infertility treatment is around US\$ 2000; it can be many times more in other countries. Nevertheless, a significant number of richer people travel abroad for treatment (services import). There are no figures as to whether Pakistan is a net exporter or importer in health services.

● *Mode 3 - Commercial presence*

In Mode 3, the service supplier establishes its commercial presence in another country through e.g. branches or subsidiaries. Examples are banking services supplied by a subsidiary of a foreign bank. Since SMEs are not in a position to establish commercial presence abroad due to difficulties with visa, financial resources and trouble in gaining registration for a company; this mode is not too significant for them in terms of setting up export subsidiaries. However, domestic liberalization of this Mode has had a significant impact on the productivity, employment and creation of many

SMEs. Opening up of telecom sector gave rise to the establishment of a large number of mobile phones related businesses including repair shops and mobile banking.

Mian Khalid Aziz, a town planning expert, explained that Pakistani firms are actively providing construction services under Mode 3 in the Middle East and other countries but these are mostly large firms and not SMEs. However, SMEs and individuals move there temporarily to provide consultancy services as he did for the Government of Oman (Mode 4). Therefore in terms of Mode 3, he did not see much scope for SMEs.

Similarly, Mr Tariq Mahmud Jehangiri, the President of the Islamabad High Court Bar Association explained that it was not easy for small law firms to set up representative offices in other countries for the reason that Pakistani lawyers cannot represent clients in foreign courts just as foreign lawyers do not have a right to do so in Pakistan.

● *Mode 4 - Temporary Movement of Natural Persons*

Mode 4, presence of natural persons, occurs when an individual has moved temporarily into the territory of the consumer in the context of the service supply, whether self-employed or as an employee of a foreign supplier. For instance, architects moving abroad to supervise construction work are providing services under this mode of supply.

Mode 4 is of key interest to Pakistani SMEs. According to many SMEs if temporary (GATS) visa was liberalized, many more technicians and engineers could augment their earnings through short professional visits abroad. Interviews with SMEs who had some awareness of WTO GATS Agreement showed that there was significant misunderstanding about this Mode as many felt that Mode 4 liberalization would also facilitate individuals seeking access to the employment markets of other countries or employment on a permanent

basis, which is not the case under GATS.

According to Shaiyyane Malik, a well-known designer based in Karachi, “we travel with groups to trade shows abroad. Many times new exporters or their staff don't get the relevant visas and at other times the visas arrive when the trade exhibition is over. This is a hindrance to business. At times some of my models have not been given visas and I have had to work with a foreign team who really don't know how to carry the look I want.”

Impact on the country's economy

Since Services constitute almost 60 per cent of Pakistan's GDP, any further liberalization or regulatory reform of this sector would have significant impact on the overall economic growth of the country.

Due to the possibility of providing online services (Mode 1), freelancing is now becoming a more acceptable way of life for many young people. According to Upwork, freelancing in Pakistan has enabled it to become among the top 10 earning countries. In major cities like Lahore, Karachi and Islamabad, there is now a growing culture of co-working spaces. A number of groups have emerged on social media focusing on various marketplaces and niches. Many information technology companies are establishing themselves in Pakistan providing new employment and skills.

A significant development is involvement of women in outsourcing work. One of the more well-known initiatives is the Women's Digital League or WDL which provides basic digital administrative services to clients around the world that range from content writing and transcription to graphic design and medical billing. Thanks to this initiative, many Pakistani women now have the opportunity to have full-time careers working from home. The company also trains rural Pakistani women to take on these tasks as well.

Full potential of Mode 2 is yet to be realized but already medical tourism is making an impact on the livelihoods of many border cities. As a result some state of the art hospitals have been set up, thus improving services to the locals as well.

Liberalization of Mode 3 including telecom and financial services has had the most beneficial overall economic impact on average Pakistanis during the last two decades. Major benefits include huge foreign direct investment, employment opportunities, increased revenue in the form of taxation and lower prices for the consumers. More efficient services sector not only increased productivity but also made the life of ordinary citizens easier. Through liberalization of the telecom industry, ordinary working class people have been able to use their time more productively and easily reach their clients and receive payments. For example, Easypaisa, a scheme launched by Telenor has made it very easy for ordinary Pakistanis to pay bills, transfer money and even open a mobile bank account without having to queue at the bank at inconvenient opening hours.

Pakistan's success in Mode 4 visa programs for temporary work abroad in developed countries such as the United States has been much less than its competitors like India. Nevertheless, during 2013 to 2014, about 4,000 Pakistanis were either awarded high-tech visas or had their existing H-1b visas renewed by the United States.

Impact on the business of SMEs

Efficient services sector brings countless benefits for SMEs. Since the share of agriculture sector in the economy is dwindling, it is the SMEs in the services sector that have been filling that gap. Having to compete in the international market improves quality, productivity and efficiency.

Seeking Solutions

Most professionals interviewed were of the view that thanks to the explosive growth of the Internet, SMEs have a tremendous potential to contribute to the growth of services. Unlike those exporting goods, SMEs do not have to normally face border issues such as import taxes, sanitary and phytosanitary measures. Of the various professionals interviewed, computer-services related experts were the most optimistic and quoted figures from international outsourcing firms such as Upwork to show that Pakistan has already emerged among the top exporting country for online services relating to software.

According to P@SHA (Pakistan Software Houses Association for IT), Pakistani firms are now providing most sophisticated software. The fact that recently NASA chose equipment management tool developed by a Lahore Based firm 7Vals shows the quality and reliability of software developed by Pakistani firms.

Interviews with many SMEs showed that solutions for improving market access for services were no different than those proposed in an earlier country note on SMEs and Trade Facilitation. For example, a number of suggestions related to the following:

- Organization of technical assistance and capacity building courses and workshops.
- Making information about rules and regulations for trade in services more easily accessible.
- Setting up Single Window offices where all SMEs needs can be met.

The International Trade Centre (ITC) has done substantial work on the way forward for the services sector. In 2007, they published National Services Export Roadmap that listed concrete recommendations for facilitating

growth in Pakistan's services exports. The key strategic areas identified in this report included the strengthening of institutional support for service providers, streamlining of the regulatory environment by the government, strengthening of infrastructure and providing better information and support to stakeholders. Although there has been some progress on developing the services sector, most of the recommendations have not been acted upon. The Government of Pakistan needs to develop its own Roadmap to implement the proposed recommendations.

About three years ago, Services Trade Development Council was established in the Ministry of Commerce. Similarly there is an Export Development Cell at the Trade Development Authority of Pakistan. They occasionally hold meetings with the private sector to find ways and means for promoting export of services but no concrete measures have been adopted.

The best way for rapid development of services in Pakistan would be to undertake unilateral opening of its services sector. At the same time it needs to make bold proposals to open services bilaterally, regionally and multilaterally.

Although there has been good progress in providing private sector opportunities to compete in almost all sectors, nevertheless there are several sectors where the private sector and particularly the SMEs can bring more efficiency. For example, National Logistic Cell (NLC) run by the public sector enjoys many advantages over the SMEs in the transport sector. Such monopolies need to be broken.

Education and training policies should be reviewed and adapted to rapidly changing requirements for new skills. Education curriculum still promotes non-technical education. Similarly there are a large number of training institutes but their training is not

according to the job requirements.

The ICT sector could grow much faster if the impediments to its growth are lowered. At present there are multiple taxes on ICT hardware and software. These need to be rationalized so that the sector can grow rapidly.

Access to finance is a problem for the service exporters of Pakistan. The Roadmap provides a number of options and recommendations to the State Bank of Pakistan (SBP) and the local banks for improving services export lending facilities. One of the significant recommendations on which the Government of Pakistan has been working for a while but has not yet implemented is the establishment of an Export Import (Exim) Bank in Pakistan that can cater exclusively for the needs of the service exporters.

Conclusion

Services are the fastest rising sector of Pakistan's economy. If there is a concerted effort; it could provide a solution to many of the Pakistan's most pressing problems such as high unemployment, stagnant exports and relatively low economic growth. Opportunities provided by the Internet can be particularly helpful for small and medium enterprises to become a part of global networks and expand their exports. With its large pool of qualified experts, Pakistan can become a leader for providing outsourcings services. The government needs to provide enabling environment by making SMEs aware of opportunities and making it easier for accessing financial resources. It needs to see what steps other countries are taking to facilitate their services exporters and introduce similar measures in Pakistan. The government needs to create more awareness about the export potential of services and take bold steps at bilateral, regional and multilateral levels for further liberalization of services.

Annex A

Questionnaire on Trade in Services:

Main Issues Faced by SMEs and Their Solution

Services are an increasingly important in the global economy and a now constitute 59 percent of Pakistan's GDP. However, share of exports of Services in Pakistan's overall exports is about 18 per cent, which is much less than the potential.

The purpose of this questionnaire is to gather some initial information on the problems faced by small and medium enterprises (SMEs) in exporting/importing Services and, how the WTO Agreement on Trade in Services (GATS) could assist them. In addition, Pakistan is one of the 23 members of the World Trade Organization (WTO) who are negotiating a new Agreement known as the Trade in Services Agreement (TiSA) which aims at further opening up markets in Services.

This information will be used to prepare a report for our WTO delegation in Geneva to enable them bring up the problems faced by SMEs before the WTO Committee on Trade in Services and for negotiating further liberalization of Services in the context of TiSA.

1. Do you export/import any Services?
2. Are you aware of the WTO Agreement on Trade in and the status of its implementation in Pakistan?
3. Are you aware of the on-going negotiations on the WTO Trade in Services Agreement (TiSA) and Pakistan's participation?
4. Can you describe the main problems faced by you in exporting/importing Services?
5. What is its impact on your business/organisation? Please provide facts and figures.
6. How can the technical and capacity building assistance be used to overcome the problem?
7. What should be the national priorities for seeking further liberalization of Services?
8. What can the government do to facilitate export of Services from Pakistan?

Name, title and address of the exporting firm/association

Email and phone number



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GENEVA TRADE & BUSINESS CONNEXION FORUM

The Trade & Business Connexion project aims at bridging the gap between South and Southeast Asian WTO delegates and their national private sectors. Web: http://www.cuts-geneva.org/Geneva_Connexion_SNSEAsia.html



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