

Book Launch on Trade and Connectivity

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Perspectives on the Trade's Impact on Economic Transformation and People's Wellbeing

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Good morning everyone. Thank you very much to the Economic Advisory Group, PRIME, and the Friedrich Naumann Foundation, for the opportunity to be part of today's launch of the report on *Trade and Connectivity*. I am very honored to participate in this panel with the Honorable Minister for Commerce, your Excellency the Ambassador of the Republic of Indonesia, Chairperson Economic Advisory Group, and Dr. Aadil Nakhoda from IBA Karachi.

Today's theme greatly appeals to me as I have seen, in my life experience and as a professional, how trade can really make a difference for people's wellbeing.

Let me start with some family memories around trade that go back to my great-grandfather, who at the turn of 20th century, lost in a wolf attack his most valuable asset, a horse carriage he used to provide essential goods to isolated villages scattered around a remote valley in Spain. Deprived of his livelihood, he migrated to Bilbao, which was at the time one the most the prosperous and export-oriented cities in Spain. So, after many years of hard work, he managed to set up a company to export tiles, on a small scale, to the rest of Spain, Portugal and France.

I thought this family story somehow mirrors Spain's aspirations later in the 1960s and 1970s to overcome a self-imposed regime of autarchy that, through tariff and non-tariff barriers to trade and multiple currency practices, imposed severe constraints on Spain's ability to grow sustainably, as evidenced by the frequent episodes of external distress during the 1960s and 1970s. Spanish economists have termed this period as the *stop and go* years, with a constant recalibration of policies to prevent balance of payment crises.

The catalytic force for change for Spain came from the country's integration with the European Union and the global economy more broadly during the 1980s and 1990s. While this was primarily a *political aspiration* for the country, it brought about a massive economic transformation. Let me say a few words on that:

- As custom and regulatory duties with Europe were eliminated, and as a reduced common external tariff on imports from the rest of the world was adopted, trade openness (measured as combined exports and imports as a percentage GDP) increased from 33 percent in 1985 to nearly 50 percent in 2000, with inter- and intra-industry trade increasing roughly equally.
- Growth in FDI accelerated from 4 percent on average during the first half of the 1980s to a phenomenal 24 percent during the second half of the 1980s.
- Trade openness and exposure to foreign competition allowed productivity to increase, and the composition of exports gradually shifted from sectors intensive in primary resources and

labor, towards industries with a greater technological component (such as cars or medicaments). Spain moved up the value chain.

- As a result, the average growth over 1985-2000 overperformed the growth seen during the *stop and go* years by half a percentage point, which, while not massive was sustained, and so allowed Spain to overcome external sector vulnerabilities and income per capita levels to gradually converge to the European Union average.

What did this all mean for a middle-class family like mine? Within a decade, from 1970s to the late 1980s, the quantity goods available to us increased, and the quality that we could afford improved. The budget of 10,000 pesetas, equivalent to €60, went a lot further for a lot better. As children we witnessed a real-life transformation in our standards of living within a relatively short period as trade with Europe and the rest of the world increased.

These developments are as staggering as *expected* according to the predictions of mainstream endogenous growth models. For example, in a model contributed by Romer and Rivera-Batiz in the early 1990s, economic integration lifts growth *permanently* because open trade encourages the exploitation of economies of scale and more efficient allocation of resources, technology given.

Alongside trade, two other major developments unfolded in parallel in Spain, which reduced our external vulnerability, fast growing tourism and remittances. Those two developments signaled the country's quest for economic modernization, and are behind the *social transformation* Spain went through while preserving our culture and core set of values.

Turning to Pakistan, Pakistan is yet to embrace integration, and, as a matter of fact, it has turned more inwards since the turn of the century. Exports as a share of GDP fell from 14 ½ percent in 1999 to less than 10 ½ percent in 2021. More integration with regional and global markets is important to improve technological transfer and competition, reverse the productivity decline, reduce external vulnerabilities, and increase Pakistan's modest per capita GDP growth. To realize the country's export potential, it will be important to reduce the anti-export bias of tariff policy (by reducing import duties which are amongst the highest in the world) and modernizing export promotion schemes. In parallel, the authorities should ensure, though *active policy efforts*, that the benefits from an export-oriented growth model are distributed to the low-skilled and vulnerable segments of the population.

Thank you very much again for the opportunity to share these impressions on trade. The IMF is engaged with Pakistan because we believe in Pakistan's potential for economic transformation, for the benefit of all of its citizens. We certainly welcome the initiative of the Economic Advisory Group and other think tanks promoting free trade and market based economic policies, to elicit debate on trade, connectivity, and other topics that are important for Pakistan's development. The IMF would count it as a success to see a Pakistan that has transformed itself to be far more regionally and globally integrated than it presently is, and to see the real-lives of Pakistanis on upward trajectory of improvement.

