Indian Council for Research on International Economic Relations

ICRIER-Wadhwani Chair in India – US Policy Studies

ISSUE BRIEF

"Advancing the Strategic Potential of India-US Relations, Accelerating India's Economic Development"

Vol. 2, Issue 9

August 08, 2012

Investing in Peace

by Rohit Viswanath

In a move which came as a surprise to pessimists among observers of India-Pakistan relations, India has imparted further momentum to economic exchanges by deciding to allow foreign direct investment (FDI) from Pakistan. The official announcement, made on August 1, read: "The Government of India has reviewed the policy and decided to permit a citizen of Pakistan or an entity incorporated in Pakistan to make investments in India, under the government route, in sectors/activities other than defense, space and atomic energy." In order to address security concerns which may arise, FDI proposals from Pakistan would be routed through the Foreign Investment Promotion Board (FIPB) and not through the automatic route.

Pakistan has welcomed India's decision, saying the move will create goodwill and boost efforts to normalize bilateral relations. Consequently, the State Bank of Pakistan has already given the green signal to the National Bank of Pakistan and the United Bank to operate in India. Pakistan enjoys comparative advantage in sectors like cement, textiles and sporting goods and could well explore these avenues to start with.

This unilateral decision to allow Pakistani investment in India is a significant indicator of India's determination to normalize the economic discourse between the two nations. The move will provide a further incentive for Pakistan to actually extend MFN status to India. Although Pakistan had notified its intent in March this year, it is yet to implement this measure amidst reports of continuing resistance from hardliners.

It is also clear that this step by India is more political than based on any economic calculation of substantive investments flowing in. Facilitating Pakistani FDI into India represents a huge psychological blow to elements hostile to improved ties between the two countries. It will help bolster the marginalized peace constituency in Pakistan. Trade and investment activities can be an effective antidote to entrenched hostility and suspicion, even though these elements will remain a drawback factor in the foreseeable future.

Links of Interest

ICRIER - Wadhwani Chair

India – US Insight
Vol. 2, Issue 7
"***Prospects for India-Japan Civil Nuclear Cooperation***"
by Dr. Rajaram Panda
July 24, 2012

Issue Brief is produced by the Indian Council for Research on International Economic Relations (ICRIER), an autonomous, policy-oriented, not-for-profit economic policy think tank. ICRIER's main focus is to enhance the knowledge content of policy making through research targeted at improving India's interface with the global economy.

ICRIER does not take specific policy positions; accordingly, all views, positions, and conclusions expressed in this publication should be understood to be solely those of the author(s)

ICRIER - Wadhwani Chair in India – US Policy Studies

Amb. Hemant Krishan Singh
Chair Professor

ICRIER - Wadhwani Chair in India – US Policy Studies

Indian Council for Research on International Economic Relations

Core 6A, 4th Floor

India Habitat Centre

Lodhi Road

New Delhi-110 003

Phone:

91 11 43112400 X 402 /435

Fax:

91 11 24620180

Website:

WWW.ICRIER.ORG/ICRIER_WADHWANI

E-Mail:
uschair@icrier.res.in

ISSUE BRIEF
Vol.2, Issue 9
August 2012

In the past, the Pakistan Army has been the staunchest opponent of greater economic ties between the two nations. Recent events have rendered it vulnerable, opening a small window of opportunity for strengthening the relative role and power of democratic institutions. India must leverage this conjuncture by offering economic inducements for Pakistan's domestic and external realignment, even if the chances of this transpiring are considered remote. As economic imperatives supersede security concerns in the visa policies of India and Pakistan, liberalization of travel should also become possible. This can lead not only to business-to-business contacts but also burgeoning people-to-people contacts.

Earlier this year, Pakistan had scrapped the positive list of imports that allowed less than 2,000 goods to be imported from India. It has since moved to a negative list that disallows import of just 1,123 items, allowing more than 7,000 products to be imported. However, Pakistan allows only 137 items to be imported through the Wagah-Attari land route. The rest have to go via the sea route to Karachi through Mumbai and Dubai, increasing transportation and transaction costs manifold. According to a study released by the Associated Chambers of Commerce and Industry of India (Assocham), bilateral trade could increase to $8 billion a year in the next two years from the current level of $2.6 billion.

The integrated check post (ICP) at the Wagah-Attari border, inaugurated on April 13, 2012 has started showing promising results. According to Indian Customs' data*, India's imports during the first quarter of the current financial year, i.e. April 2012 - June 2012, were $344.42 million as compared to just $167.65 million during the corresponding period of the last financial year. Similarly, India's exports touched $645.99 million during the first quarter, well above the $465.96 million registered during the corresponding period of the previous financial year. India mainly imports cement, gypsum, dry fruits and rock salt from Pakistan, while it exports meat, vegetables, soya meal, raw cotton and yarn to Pakistan.

India can utilize the next meeting of Commerce Secretaries due in September, 2012, to remove existing limitations on tradable items across the land border. This will provide a further boost to bilateral trade.

Pakistan has the potential to become the pivot of South Asian trade and energy flows as it is the natural transit point for overland exchanges with Afghanistan and Central Asia. However, to derive this benefit it must first create an open and secure environment for enhanced economic interaction within the region.

Given their problematic historical relations, India and Pakistan have a long way to go to build confidence in prospects for trade and economic relations. While the gradual build-up of stakeholders in their respective business establishments will help, ultimately both sides will need to sustain a strong political will to make the most of the opportunities presented by the mutual economic benefits of enhanced trade and investment.

……………………

❖ **Rohit Viswanath is a research associate at ICRIER.**

References

*Customs data converted @ Rs.55 to the dollar.