SOUTH ASIA

BANGLADESH

Key Economic Indicators

[Millions of U.S. Dollars unless otherwise indicated]

	1998 [1]	1999 [1]	2000 [1]
Income, Production and Employment:			
Real GDP Growth (% in constant prices) [2]	5.2	4.9	5.5
GDP Growth by Sector:			
Agriculture	3.2	4.8	6.4
Industry	8.3	4.9	5.6
Services	5.0	5.2	5.3
Per Capita GDP (Current US$)	348	357	373
Labor Force (000s)	N/A	N/A	N/A
Unemployment Rate	N/A	N/A	N/A
Money and Prices (annual percent change):			
Money Supply Growth (M2)	10.2	12.8	19.0
Consumer Price Inflation	7.0	9.0	4.5
Exchange Rate (Taka/US$, annual average)			
Official	45.4	47.9	49.7
Parallel	N/A	N/A	N/A
Balance of Payments and Trade:			
Total Exports FOB	5,161	5,313	5,752
Exports to United States [3]	1,846	2,273	N/A
Total Imports CIF	7,524	7,515	8,200
Imports from United States [3]	318	300	N/A
Trade Balance	–2,363	–2,202	–2,448
Balance with United States [3]	1,528	1,973	N/A
External Public Debt [4]	14,030	14,800	N/A
Fiscal Deficit/GDP (pct)	4.2	5.3	6.5
Current Account Balance/GDP (pct)	–1.1	–1.4	–1.1
External Debt Service/GDP (pct)	7.8	6.7	7.3
Gold and Foreign Exchange Reserves	1,800	1,500	1,500
Aid from United States [5]	77.0	153.0	92.8
Aid from all Sources [6]	1,419.0	1,502.0	1,575.0

[1] Figures are for Bangladesh's fiscal year (FY), July 1 to June 30.
[2] Based on 1995/1996 base year.
[3] Figures are for calendar year.
[4] Medium and long-term; Estimated by Ministry of Finance, Foreign Assistance Accounts.
[5] Figures are for the U.S. fiscal year (October 1–September 30).
[6] Disbursements; year 2000 number is provisional.

1. General Policy Framework

Bangladesh is one of the world's poorest, most densely populated, and least developed countries; its per capita income for fiscal year 2000 (July 1, 1999 to June 30, 2000) is estimated at $373. A large proportion of its population of roughly 130 million is tied directly or indirectly to agriculture, which accounts for 26 percent of GDP and about 70 percent of the labor force. Industrial output remains narrowly focused. Economic growth in fiscal year 2000 was 5.5 percent, up from 4.9 percent during the previous year, which was considered a recovery year from the massive 1998 floods. Bangladesh's average annual growth is 5 percent over the last ten years. Growth rates of 7–8 percent are required to begin to alleviate the nation's extreme poverty.

GDP growth continues to be weakened by a number of factors: low productivity, stagnant industrial growth, political instability, poor infrastructure, corruption, and low domestic savings and investment. High government borrowing and the widespread inflow of smuggled goods are the latest problems putting strains on the already weak economy. The state's presence in the economy continues to be large, and money-losing state enterprises have been a chronic drain on the treasury. During the 1990s Bangladesh took steps to liberalize its economy, and the private sector assumed a more prominent role as the climate improved for free markets and trade. The Awami League government, which came to power in June 1996, has largely continued the market-based policies of its predecessor, the Bangladesh Nationalist Party, and made some regulatory and policy changes toward that end. However, implementation of new policy directives by the bureaucracy has been slow and uneven among the sectors.

The World Bank and the International Monetary Fund (IMF) provided emergency balance of payment relief of about $320 million in fiscal year 1999, and over the past two years the IMF and Bangladesh have held follow-on Enhanced Structural Adjustment Facility discussions, though no agreement has been reached. Bangladesh's official foreign exchange reserves have recently edged down, and are currently (October 2000) at around $1.4 billion, roughly equivalent to two months of imports of goods and services. This level is at the lowest end of the range of reserves during recent years.

Inflation has continued to decline from the nine percent level reached in fiscal year 1999 following the 1998 flood. It fell to an annual rate of 4.5 percent for fiscal year 2000, and 2.2 percent for the last quarter of fiscal year 2000. A presumed record level of smuggled goods is credited by many for keeping the prices of consumable goods down. Food inflation is currently at 2.0 percent, while nonfood inflation is at 2.5 percent.

Responding to a continued overvaluation of the taka relative to the currencies of its main export competitors, Bangladesh devalued its currency by 3 percent in fiscal year 1999, an additional 2.1 percent in early fiscal 2000, and another 6 percent effective in mid-August 2000. The latest devaluation was a delayed response to declining external competitiveness, and is considered by many resident economists as inadequate.

Bangladesh's industrial output, heavily concentrated in garments, showed six percent growth in fiscal year 2000. Growth in the textile sector amounted to 9.1 percent. Elsewhere in the industrial sector, growth was either marginal or negative. Several factors have limited Bangladesh's exports over the past several years, including the relative overvaluation of the taka and the country's expensive and unreliable ports.

Monetary growth continued to accelerate during fiscal year 2000, reaching 20 percent in July 2000, largely as a result of central bank financing of the growing fiscal deficit. The fiscal year 2001 national budget projects a 5.9 percent deficit, a 12.4 percent increase over fiscal year 2000's deficit. Revenue collection has improved recently due largely to pre-shipment inspections (PSI), rising by about 20 percent during the last quarter. Budget projections for fiscal year 2001 call for a 13 percent increase in collections. Total receipts for fiscal year 1999 fell 7.3 percent from the year before, and by 7.7 percent in fiscal year 1998 from the year before. Government spending, including net lending, as a proportion of GDP increased to 15 percent in fiscal year 2000, up by over one percentage point from fiscal year 1999. As in prior years, about 60 percent of the fiscal deficit was financed through external sources (e.g., aid) while domestic sources (e.g., government borrowing) accounted for about 40 percent.

The government's primary monetary policy tools are the discount rate and the sale of Bangladesh Bank bills, though central bank influence over bank lending practices also plays an important role. Broad money growth (M2) increased to 19 percent in fiscal year 2000 from roughly 13 percent in fiscal year 1999, due largely to the government's continued high recourse to central bank financing of the deficit. Although the government has enacted some liberal investment policies to foster private sector involvement (mainly in energy and telecommunications), poor infrastructure, bureaucratic inertia, corruption, labor militancy, and a generally weak financial system discourage investment. Political unrest and a deteriorating law and order situation also discourage domestic and foreign investors.

The fiscal year 2001 national budget proposes to expand liquidity (in the form of interest free bonds) to Bangladesh's nationalized commercial banks that are burdened with bad loans. Reduced interest rates for lending to priority sectors like infrastructure, information technology, textiles, oil and gas, and agriculture-based industries are also proposed, as well as interest rebates (10 percent) to good performing credit recipients. The capital market received a number of incentives in the

budget for fiscal year 2001, including: a 10 percent tax rebate allowance to publicly listed companies that declare 25 percent dividend; a rise from $560 to $740 in the limit for deduction of tax-at-source from dividend income; the retraction of the increase in the requirement of deduction of tax-at-source on bonus shares, which was imposed in the last budget; a tax credit eligibility for investment in secondary market; and an increase in investment allowance from $3,700 to $4,200 for investments made in initial public offerings.

Information technology has been given significant incentives in the fiscal year 2001 budget in continuity with the 2000 budget. An equity development fund with an allocation of $18.5 million has been proposed for encouraging entrepreneurs to invest in software development. Ventures in these sectors will be eligible to receive up to 25 percent equity funding from the Bangladesh Bank. In the 2000 budget, the import of computers was made duty-free. In this year's budget, duties on other accessories, such as toner cartridges, CD–ROM drives, CDs, modems, magnetic tapes and disks, and ink jets and refill kits used in computer printers and software have also been made duty-free.

Leather, textile, agriculture-based food processing, ceramic and dishware, tea, poultry and fishery, plastic footwear, bicycles and newsprint industries have received significant duty concessions on the import of raw materials in the budget, also in continuity with last year's budget. The import of capital machinery by export-oriented industries will be made duty-free with indemnity bonds. The government has designated up to 16 sectors as "priority" areas and instructed state-owned banks to provide subsidized financing for their operations.

2. Exchange Rate Policies

At present, the central bank follows a semi-flexible exchange rate policy, revaluing the currency on the basis of the real effective exchange rate, vis-a-vis a basket of select currencies. Annual aid receipts and remittances from overseas workers have kept the exchange market somewhat stable. Increasing workers' remittances have been a bright spot for the economy. Official receipts rose by 16 percent in fiscal year 2000 from the previous year, to roughly $2 billion. An estimated $1 billion in remittances enter Bangladesh outside of official channels. The government's delayed decisions to devalue the local currency added unnecessary strain on the market. The current exchange rate is currently about taka 54 to $1.

Foreign firms supposedly have been able to repatriate profits, dividends, royalty payments and technical fees without difficulty, provided appropriate documentation is presented to the Bangladesh Bank. However, U.S. investors are starting to complain about the delays in getting the central bank's approval. Outbound foreign investment by Bangladeshi nationals requires government approval and must support export activities. Bangladeshi travelers are limited by law to taking no more than $3,000 out of the country per year.

3. Structural Policies

In 1993, Bangladesh successfully completed a three-year ESAF program, meeting all the IMF fiscal and monetary targets. During the flood-induced economic crisis in 1998, Bangladesh signaled a willingness to enter into another ESAF program; however, as the Bangladeshi economy recovered smartly from economic disruptions caused by the floods, Bangladesh's enthusiasm for a new ESAF program waned. Although there is little disagreement between the IMF and Bangladesh on the substance of needed economic reforms (i.e., tax reform with better administration and a broadening of the tax base; financial sector reform with stronger oversight and supervision by the central bank, improvement in the operation of state-owned commercial banks, improvement of loan portfolios; and public sector reforms with an acceleration of privatization of state-owned enterprises), progress in negotiations has not occurred.

Bangladesh has managed to maintain a laudable measure of macroeconomic stability since 1993, but its macroeconomic position remains vulnerable, with slowing export growth, a stagnant industrial sector, inadequate infrastructure, a banking sector in need of comprehensive reforms, and an inefficient public sector that continues to drain the treasury. Progress on important economic reforms has been slow, although the government has instituted reforms of the capital market and taken some market-friendly decisions to encourage foreign investment. Vested interest groups often successfully oppose reform efforts. The public sector still exercises a dominant influence on industry and the economy even though less than five percent of the labor force is employed by state-owned enterprise (SOEs). Non-financial SOEs are losing an estimated $290 million a year. Most public sector industries, including textiles, jute processing, and sugar refining, are chronic money losers. Their militant

unions have succeeded in setting relatively high wages which their private sector counterparts often feel compelled to meet out of fear of union action.

Private sector productivity is further stunted by the state's poor management of crucial infrastructure (power, railroads, ports, telecommunications). Recognizing these shortcomings, and in order to increase foreign investment in the power sector, the government formalized in October 1996 its private power policy, which grants tax holidays and the duty-free import of plant and equipment for private sector power producers. As of November 1999, the government was purchasing power from three international power producers, and was negotiating or had signed contracts with others. The difficulties and the high cost of doing business in Bangladesh have forced some companies to reconsider or limit their exposure in Bangladesh. Private investment is also allowed in the telecommunications sector for cellular communications, and in the hydrocarbons sector, where international companies initially expressed a high level of interest in a second round of bidding for remaining exploration rights. Bangladesh also witnessed a dramatic increase in the number of Internet service providers following the sharp reduction in the tax on Very Small Aperture Terminals in early 2000.

The government practically gave up trying to attract foreign portfolio investment in domestic capital markets after a stock market crash in late 1996 and turbulence in other financial markets around the world in 1997 and 1998. The banking sector is now dominated by four large nationalized commercial banks. However, entry of foreign and domestic private banks has been permitted; numerous new private domestic and foreign banks have established a foothold in the market since 1996. The banking sector continues to be in need of major reform.

4. Debt Management Policies

Assessed on the basis of disbursed outstanding principal, Bangladesh's external public debt was over $16 billion in fiscal year 2000, up slightly from fiscal year 1999. Because virtually all of the debt was provided on highly concessional terms by bilateral and multilateral donors, the net present value of the total outstanding debt is significantly lower than its face value. The external debt burden has eased during the 1990s with the external public debt as a percentage of GDP falling steadily from 46 percent in fiscal year 1994 to 37 percent in fiscal year 1998. Debt service as a percentage of current receipts has also declined sharply, from 20 percent in fiscal year 1991 to an estimated 8 percent in fiscal year 1998. Bangladesh maintains good relationships with the World Bank, Asian Development Bank, the IMF and the donor community.

5. Development Aid

During U.S. fiscal year 2000, USAID provided roughly $93 million to Bangladesh for economic development in the following sectors: population, health, and nutrition ($34 million); agribusiness, small and medium sized ($7 million), energy sector support ($4 million), food security and disaster preparedness ($1.3 million), democracy and human rights ($5.4 million), and Title II food aid ($41 million).

Security Assistance from the United States to the Bangladesh military during U.S. fiscal year 2000 totaled roughly $450,000 for International Military Education Training (IMET). In addition to IMET, Enhanced International Peacekeeping Cooperation grants were provided to the Bangladesh military in the amount of $275,000 for training and $1.8 million for purchasing training equipment. These grants are to be expended over a five-year period.

6. Significant Barriers to U.S. Exports

Since 1991, the Government has made significant progress in liberalizing what had been one of the most restrictive trade regimes in Asia. Even so, Bangladesh continues to raise a relatively high share of its government revenues from import-based taxes, custom duties, the value added tax (VAT), and supplementary duties on imports. Tariff reform, which began in 1994, has continued to date. Last year's budget accelerated Bangladesh's efforts to shift from a tariff-based revenue system to an income-based one. Some of the budget's changes to the tariff regime included: reduction in customs duty brackets from five to four, lowering of the top duty rate from 40 percent to 37.5 percent, and a unification of duty rates for different products within the broad HS code or product category, and a targeted reduction of duties to benefit certain sectors. The budget reduced the average tariff for capital goods from 12.6 percent in fiscal year 1999 to 8.9 percent in fiscal year 2000, for intermediate goods from 19.1 percent to 15.5 percent, and for consumer goods from 31.8 percent to 29.2 percent. Other reforms included: the broadening of VAT; introduction of measures designed to increase transparency, reduce corruption, and limit the discretion of the bureaucracy in adjudicating tax/tariff cases; introduction of a mandatory pre-shipment inspection (PSI) system of customs valuation; and reduc-

tion in the number of personal income tax brackets and simplification of tax administration procedures. The import of information technology products is also completely duty free.

Bangladesh, a founding member of the World Trade Organization (WTO), is subject to all the disciplines of the WTO. Some barriers to U.S. exports or direct investment exist. Policy instability, when policies are altered at the behest of special interests, creates difficulties for foreign companies. A government monopoly controls basic services and long-distance service in the telecommunications market, although the government has allowed private companies to enter the wireless communication market. Non-tariff barriers also exist in the pharmaceutical sector, where manufacturing and import controls imposed by the national drug policy and the Drugs (Control) Ordinance of 1982 discriminate against foreign drug companies. Bangladesh is not a signatory to the WTO agreements on government procurement or civil aircraft. Government procurement generally takes place through a tendering process, which is not always transparent, meaning U.S. businesses are not always guaranteed a level field for competing. Customs procedures are lengthy and burdensome, and sometimes complicated by corruption. Introduction of the PSI system of customs valuation is expected to simplify customs procedures, make valuation less arbitrary, and reduce corruption.

Other drawbacks to investment in Bangladesh include low labor productivity, poor infrastructure, excessive regulations, a slow and risk-averse bureaucracy, and unpredictable law and order. The lack of effective commercial laws makes enforcement of business contracts difficult. Officially, private industrial investment, whether domestic or foreign, is fully deregulated, and the government has significantly streamlined the investment registration process. Although the government has simplified the registration processes for investors, domestic and foreign investors typically must obtain a series of approvals from various government agencies to implement their projects. Bureaucratic red tape, compounded by corruption, slows and distorts decision-making and procurement. Existing export processing zones (EPZs) have successfully facilitated investment and export growth. The EPZs are exempt from some Bangladeshi labor laws, and workers there are denied basic labor rights, such as freedom of association. Bangladesh's access to benefits under Generalized System of Preferences (GSP) could be jeopardized if the government does not take steps to provide these workers their labor rights.

Agreements between Bangladesh and U.S. companies in gas exploration and production and energy production prompted the rise in total U.S. foreign direct investment (FDI) from $25 million before 1995 to over $750 million in 2000. Other opportunities for significant investment in gas exploration and production, power generation and private port construction/operation could further swell U.S. investment and trade, if needed economic policy changes and gas export decisions are made. Total FDI in Bangladesh during fiscal year 2000 fell by 50 percent from the previous year, from over $300 million to about $150 million. The fall-off in large investment expenditures by international oil companies in 1999 accounts for much of this decline.

Inadequate infrastructure (especially power supplies, port and transportation) is undermining Bangladesh's industrial base and any effort to attract FDI to Bangladesh. In addition, slow bureaucratic decision-making, corruption, occasional general strikes (hartals), and a largely unskilled labor force are sending a mixed message about prospects for investing in Bangladesh.

7. Export Subsidies Policies

The government encourages export growth through measures such as duty-free status for some imported inputs, including capital machinery and cotton, and easy access to financing for exporters. Ready-made garment producers are assisted by bonded warehousing and back-to-back letter of credit facilities for imported cloth and accessories. The central bank offers a 25 percent rebate to domestic manufacturers of fabric for ready-made garment exports. Exporters are allowed to exchange 100 percent of their foreign currency earnings through any authorized dealer. Government-financed interest rate subsidies to exporters have been reduced in stages over five years. EPZs are located in Chittagong and Dhaka, and others are opening elsewhere in Bangladesh. East Asian countries have been the largest investors in EPZs.

8. Protection of U.S. Intellectual Property

Bangladesh is a signatory of the Uruguay Round agreements, including the WTO's Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), and is obligated to bring its laws and enforcement efforts into TRIPS compliance by January 1, 2006. Bangladesh has also been a member of the World Intellectual Property Organization (WIPO) in Geneva since 1985. Bangladesh has never

been cited in the U.S. Trade Representative's "Special 301" Watch List, which identifies countries that deny adequate and effective protection for intellectual property rights or deny fair and equitable market access for persons that rely on intellectual property protection. Even though Bangladesh has not been placed on the "Special 301" Watch List, it has outdated Intellectual Property Rights (IPR) laws, an unwieldy system of registering intellectual property rights, and a weak enforcement mechanism. Intellectual property infringement is common, particularly of computer software, motion pictures, pharmaceutical products and audio- and videocassettes. Despite the difficulties, U.S. firms have successfully pursued their IPR rights in Bangladeshi courts. Bangladesh enacted a Copyright Law in July 2000, updating its copyright system and bringing the country into compliance with TRIPS; the Government of Bangladesh has been urged to move quickly on getting the law implemented.

9. Worker Rights

a. *The Right of Association:* Bangladesh's Constitution guarantees freedom of association, the right to join unions, and, with government approval, the right to form a union. With the exception of workers in the railway, postal, telegraph, and telephone sectors, government civil servants are forbidden to join unions. However, some workers covered by this ban have formed unregistered unions. The ban also applies to security-related government employees, such as those in the military and police. Civil servants, such as teachers and nurses, are forbidden to join unions, but they often join associations that perform functions similar to labor unions.

b. *The Right to Organize and Bargain Collectively:* Many unions in Bangladesh are highly politicized. Virtually all the National Trade Union centers are affiliated with political parties, including one with the ruling party. Pitched battles between members of rival labor unions occur regularly. Some unions are militant and allegedly engage in intimidation and extortion. Unions occasionally do use their right to call labor strikes.

The Essential Services Ordinance permits the government to bar strikes for three months in any sector deemed "essential." Mechanisms for conciliation, arbitration and labor court dispute resolution were established under the Industrial Relations Ordinance of 1969. There have been numerous complaints of garment workers being harassed and fired in some factories for trying to organize workers. Workers in Bangladesh's EPZs are prohibited from forming unions, and the government has not fulfilled promises that restrictions on freedom of association and formation of unions in the EPZs would be lifted in stages between 1995 and 2000. The outcome of the AFL–CIO petition to the U.S. Trade Representative to revoke GSP benefits for Bangladesh because of its failure to keep its commitment to restore full labor rights in the EPZs is yet to be decided.

c. *Prohibition of Forced or Compulsory Labor:* The constitution prohibits forced or compulsory labor. The Factories Act and the Shops and Establishments Act, both passed in 1965, set up inspection mechanisms to guard against forced labor, but resources for enforcement are scarce. There is no evidence of widespread forced labor, though conditions for some domestic servants resemble servitude, and some trafficked women and children are forced to work as prostitutes.

d. *Minimum Age for Employment of Children:* Bangladesh has laws that prohibit labor by children. The Factories Act bars children under the age of 14 from working in factories. In reality, enforcement of these rules is inadequate. According to United Nations estimates, about one third of Bangladesh's population under the age of 18 is working. In a society as poor as Bangladesh's, the extra income obtained by children, however meager, is sought by many families. In July 1995, Bangladesh garment exporters signed a Memorandum of Understanding that has largely eliminated child labor in the garment export sector. Under the MOU, schools and a stipend program were established for displaced child workers. A monitoring system managed by the ILO enforces the MOU. As a result of the MOU, child labor has been dramatically reduced, though not completely eliminated from the garment export sector. In June 2000, the MOU was extended for one year.

e. *Acceptable Conditions of Work:* Regulations regarding minimum wages, hours of work, and occupational safety and health are not strictly enforced. The legal minimum wage varies depending on occupation and industry. It is generally not enforced. For example, the minimum monthly wage for garment workers is 930 taka ($17), but some do not receive even that amount. The law sets a standard 48-hour workweek with one mandated day off. A 60-hour workweek, inclusive of a maximum 12 hours of overtime, is allowed. Relative to the average standard of living in Bangladesh, the average monthly wage could be described as sufficient for minimal, basic needs. The Factories Act of 1965 nominally sets occupational health and safety

standards. The law is comprehensive, but is largely ignored by many Bangladeshi employers and not enforced by the government.

f. *Rights in Sectors with U.S. Investment:* As far as can be determined, firms with U.S. capital investment abide by the labor laws. Similarly, these firms respect the minimum age for the employment of children. According to both the government and representatives of the firms, workers in firms with U.S. capital investment generally earn a much higher salary than the minimum wage set for each specific industry, and enjoy better working conditions.

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

[Millions of U.S. Dollars]

Category	Amount	
Petroleum		([1])
Total Manufacturing		0
Food and Kindred Products	0	
Chemicals and Allied Products	0	
Primary and Fabricated Metals	0	
Industrial Machinery and Equipment	0	
Electric and Electronic Equipment	0	
Transportation Equipment	0	
Other Manufacturing	0	
Wholesale Trade		–14
Banking		([1])
Finance/Insurance/Real Estate		–4
Services		0
Other Industries		4
TOTAL ALL INDUSTRIES		143

([1]) Suppressed to avoid disclosing data of individual companies.

Source: U.S. Department of Commerce, Bureau of Economic Analysis.

INDIA

Key Economic Indicators

[Billions of U.S. Dollars unless otherwise indicated]

	1998 [1]	1999 [1]	2000 [2]
Income, Production and Employment:			
Nominal GDP [3]	420.0	448.0	480.0
Real GDP Growth (pct) [4]	6.8	6.4	5.8
GDP by Sector (pct estimated):			
Agriculture	26.7	26.6	26.0
Manufacturing	25.3	24.5	22.8
Services	48.0	49.0	51.2
Government	N/A	N/A	N/A
Per Capita GDP (US$)	425.0	452.0	486.0
Labor Force (millions)	410.0	420.0	436.0
Unemployment Rate (pct)	22.5	22.5	22.5
Money and Prices (annual percentage growth):			
Money Supply Growth (M3)	19.2	13.6	15.0
Consumer Price Inflation [5]	13.1	3.4	6.0
Exchange Rate (Rupee/US$ annual average)			
Official	42.08	43.5	45.3
Parallel	42.08	43.3	45.6
Balance of Payments and Trade:			
Total Exports FOB [6]	33.2	37.6	42.5
Exports to United States [7]	7.3	8.5	9.3
Total Imports CIF [4]	42.4	47.3	52.0
Imports from United States [7]	3.6	3.6	3.6
Trade Balance [6]	–9.2	–9.6	–10.5

Key Economic Indicators—Continued

[Billions of U.S. Dollars unless otherwise indicated]

	1998 [1]	1999 [1]	2000 [2]
Balance with United States [7]	3.7	4.9	5.5
External Public Debt [8]	97.7	98.4	98.0
Central Government Fiscal Deficit/GDP (pct)	4.5	5.6	5.1
Current Account Deficit/GDP (pct)	1.0	0.9	1.2
Debt Service Payments/GDP (pct)	2.6	2.5	2.2
Gold and Foreign Exchange Reserves	29.4	32.5	38.1
Aid from United States (US$ million)	121.8	142.9	142.5
Aid from All Other Sources	2.7	N/A	N/A

[1] Data for 1998 and 1999 differ from data contained in previous reports inasmuch as previous figures provided by the Government of India were provisional.
[2] Data are for the Indian fiscal year (IFY), April 1 to March 31, unless otherwise noted. Figures for 2000 are either Embassy or Center for Monitoring the Indian Economy (CMIE, a private research agency) estimates based on data available in September 2000.
[3] GDP at factor cost.
[4] Percentage changes calculated in local currency.
[5] Wholesale price index is benchmark for inflation.
[6] Merchandise trade.
[7] Source: Directorate General of Commercial Intelligence Service, Department of Commerce, on a fiscal year basis. Figures for 2000 are estimates based on data available through September 2000.
[8] Includes a rupee debt of $3.4 billion to the former Soviet Union.

Sources: Government of India economic survey, Government of India budgets, Reserve Bank of India bulletins, World Bank, IMF, USAID, and private research agencies.

1. General Policy Framework

Economic reforms since 1991 have helped India achieve a large measure of macroeconomic stability and a moderate degree of liberalization of its trade, investment and financial sectors. These reforms boosted annual economic growth to around seven percent in the 1994–1997 period. In the Indian Fiscal Year (IFY) 1997–98, growth slowed to 5 percent on the heels of the Asian financial crisis but increased to 6.8 percent in 1998–99 and then 6.4 percent in 1999–00. For IFY 2000–01, the Center for Monitoring the Indian Economy (CMIE) projects GDP growth of about 5.8 percent and industrial growth of about 7 percent. The United States continues to be the largest investor in India and its biggest trading partner. The Indian economy has the potential to perform well, and the long-term prospects remain encouraging.

There are continuing concerns, though, over inadequate infrastructure and chronic large budget deficits. Inefficiencies and shortfalls in capacity are reflected in congested roads and ports, power failures, and drinking water shortages. Infrastructure investments have diminished, largely because of the inefficient pricing structure of power and other services. In IFY 1999–2000, the central government's gross fiscal deficit rose to 5.6 percent of GDP with the consolidated public sector deficit (including states) over 10 percent. The high fiscal deficit/GDP rate continues to be a significant drag on economic growth.

During the first five months of IFY 2000–01, the money supply (M3) rose by an estimated 14 percent, almost reaching the Reserve Bank of India's (RBI) target of 15 percent for the year. Credit policies announced in April 2000 have focused on structural and financial sector reforms while emphasizing the need to guard against emerging inflationary pressures (e.g., a higher oil import bill that will affect foreign exchange levels and overall inflation). Government and private sources predict an average inflation rate (as measured by the Consumer Price Index) of 7.5 to 8 percent during IFY 2000–01, compared to 3.4 percent the previous year.

2. Exchange Rate Policy

On March 1, 1993 the exchange rate was unified and the rupee was made fully convertible on the trade account that year and on the current account in the following year. Controls remain on capital account transactions, with the exception of Non-Resident Indians (NRIs) and foreign institutional investors, but the gradual removal of these controls is expected as foreign exchange reserves increase and India makes progress in merging its capital markets with international financial markets. In June 1997 the Tarapore Committee on Capital Account Convertibility recommended a three year (1998–2000) period for complete capital account convertibility of the rupee. The government has defended its position in that India is in no hurry to complete full convertibility, especially given the crisis in East Asian economies and the need to strengthen the banking sector further.

The RBI intervenes in the foreign exchange market to maintain a stable rupee. The rupee is tied to a basket of currencies with the dollar playing a predominant role. In IFY 1999–00 the average exchange rate was rupees 43.28 per dollar. From April to August 2000, the rupee depreciated substantially (6.4 percent) against the dollar and is, as of October 2000, trading in the range of 45.50–46.38 per dollar. India was shielded from the East Asian currency crisis due to a staged approach to liberalization and its relatively low degree of exposure to global financial markets. In addition, India's short term foreign borrowing is relatively low and Indian banks and financial institutions have very little exposure to the real estate sector.

3. Structural Policies

Pricing Policies: Central and state governments still regulate the prices of many essential products (e.g., food-grains, sugar, edible oils, basic medicines, energy, fertilizers, and water), while many basic foods are under a dual pricing system. Some output is supplied at fixed prices through government distribution outlets ("fair price shops"), with the remainder sold by producers on the free market. Prices in government outlets usually are regulated according to a cost-plus formula. Regulation of basic drug prices has been a particular problem for U.S. pharmaceutical firms operating in India, although changes in national drug policy have sharply reduced the number of price-controlled formulations from 142 in 1994 to 72 at present. Agricultural commodity procurement prices have risen substantially during the past eight years, while prices for nitrogenous fertilizer, rural electricity, and irrigation are subsidized. Acute power shortages are forcing several states to arrest the financial decline of the state electricity boards by moving to market pricing. The federal government has also begun to scrutinize more carefully the cost of its subsidies, especially in the power sector.

Tax Policies: Public finances remain highly dependent on indirect taxes, particularly import tariffs. Between 1991 and 1999, indirect taxes accounted for about 69 percent of central government tax revenue. India's direct tax base is slight: only 23 million taxpayers out of a possible 200 million households. Marginal corporate rates are high by international standards, although the corporate income tax rate for foreign companies has been lowered from 55 percent to 48 percent. Tax evasion is rampant. The government has stated that future rate cuts will depend on the success of efforts to improve tax compliance. Over the last eight years, the government streamlined the nation's tax regime, increased the revenue share from direct taxes, introduced a Value-Added Tax (VAT), and worked to simplify India's complex tax code. In the 2000–2001 budget, the excise and custom duty structure was rationalized by reducing three tiers of excise duties to one, and five tiers of custom duties to four. The government also provides certain tax incentives, such as a 10-year tax holiday for infrastructure projects, research and development projects, and software technology park projects.

Regulatory Policies: The "new industrial policy" announced in July 1991 considerably relaxed the government's regulatory hold on investment and production decisions. Industrial licenses now are only required for six "strategic" areas. Some restrictions remain for manufacturing in the public and small-scale industrial sectors. Most plant location strictures have been removed. The Indian government recently established a Telecommunications Dispute Settlement and Appellate Tribunal to adjudicate disputes between licensors and licensees. Nevertheless, Indian industry remains highly regulated by a powerful bureaucracy armed with excessive rules and broad discretion. As economic reforms take root at the federal level, the focus of liberalization is gradually shifting to state governments, which, under India's federal system of government, enjoy extensive regulatory powers. The speed and quality of regulatory decisions governing important issues such as zoning, land-use and the environment can vary dramatically from one state to another. Political opposition has slowed or halted important regulatory reforms governing areas like labor and bankruptcy law that would enhance the efficiency and levels of domestic and foreign investment.

4. Debt Management Policies

External Debt Structure and Management: India's total external debt reached $98.4 billion in March 2000. Debt service payments were estimated at $4.5 billion in IFY 1998–99. Roughly two-thirds of the country's foreign currency debt is composed of multilateral and bilateral debt, with much of it (approximately 38.5 percent) on highly concessional terms. The addition of new debt has slowed substantially, as the government has maintained a tight rein on foreign commercial borrowing and defense-related debt and has encouraged foreign equity investment rather than debt financing. As a result, the ratio of total external debt to GDP fell from 39.8 percent in IFY 1992–93 to 22 percent in IFY 1999–00. By October 2000, India's

reform program had succeeded in boosting foreign exchange reserves to $32.7 billion (excluding gold and SDRs). Forex reserves had grown to $35.1 billion by March 2000 but have declined as the RBI has spent dollars defending the rupee.

Relationship with Creditors: India has an excellent debt servicing record. Citing its growing foreign exchange reserves and ample food stocks, India chose not to negotiate an extended financing facility with the IMF when its standby arrangement expired in May 1993. In October 1998 Standard and Poor's (S&P) downgraded India's foreign currency rating from BB+ to BB. In October 1999 Moody's upgraded India's foreign currency rating outlook from stable to positive while maintaining an unchanged speculative grade rating of Ba2. In October 2000 S&P downgraded its outlook on India from positive to stable, due to slow structural reforms and burgeoning fiscal deficits.

5. Significant Barriers to U.S. Exports

Import Licenses: U.S. exports have benefited from significant reductions in India's import-licensing requirements. Since 1992, the government has eliminated the licensing system for imports of intermediates and capital goods. India's import-weighted tariff has fallen from 87 percent in 1992 to 25.4 percent at present. U.S. exports to India increased from $2.0 billion in 1991 to $3.6 billion in IFY 1999–00. India historically maintained quantitative restrictions (QRs) on imports on balance of payments grounds. Pointing to an improved foreign exchange situation, the United States sought removal of the restrictions. In November 1997 the United States moved within the WTO to resolve the issue. In April 1999 a dispute settlement panel favored the United States, a decision that was affirmed on appeal in August 1999. India and the United States subsequently reached agreement on a two-stage phase out of the QRs. The first stage, which went into effect April 1, 2000, lifted restrictions on half of the QRs (715 items), including consumer products and processed food items. The second stage, which will go into effect April 1, 2001, will eliminate the remaining QRs and affect (among other items) fertilizers, food grains, automobiles, tobacco, and crude petroleum products.

Some commodity imports must be channeled ("canalized") through public enterprises, although many "canalized" items are now decontrolled. The main canalized items currently are petroleum products and some pharmaceutical products. Pursuant to the report of the above-mentioned WTO panel, India must eliminate the canalization requirement by April 1, 2001. Import licenses are still required for pesticides and insecticides, some fruits and vegetables, breeding stock, most pharmaceuticals and chemicals, and products reserved in India for small-scale industry. This licensing requirement serves in many cases as an effective ban on importation.

Services Barriers: The Indian government runs many major service industries either partially or entirely, but private sector participants are increasingly being allowed to compete in the market. Entry of foreign banks remains highly regulated, but approval has so far been granted for the operation of 25 new foreign banks or bank branches since June 1993, when the RBI issued guidelines under which new private banks may be established. As of July 2000, 45 foreign banks were operating approximately 180 branches in India. Furthermore, financial authorities have permitted sweeping changes in non-bank financial services since then. India does not allow foreign nationals to practice law in its courts, but some foreign law firms maintain liaison offices in India. India recently opened the general insurance and domestic long distance telephony sectors to private and foreign investment. Foreign investors, however, are limited to a 26 percent share of insurance companies and a 49 percent stake in domestic long distance firms. Foreign and domestic joint ventures participate in telecommunications, advertising, accounting, and a wide range of financial and corporate consulting services. There is a growing awareness of India's potential as a major exporter of services, particularly in the information technology field, and of the increasing demand for a more open services market.

Standards, Testing, Labeling and Certification: Indian standards generally follow international norms and do not constitute a significant barrier to trade. However, India's food safety laws are often outdated or more stringent than international norms. Where differences exist, India is seeking to harmonize national standards with international norms. Labeling of genetically modified organisms (GMOs) is not yet an issue in India and imports of GMOs are negligible.

Investment Barriers: The industrial policy introduced in July 1991 achieved a dramatic overhaul of regulations restricting foreign direct investment (FDI). The requirement for government approval for equity investments of up to 51 percent in 48 industries covering the bulk of manufacturing activities has been entirely eliminated, although the government reserves the right to deny requests for increased equity stakes. Automatic approval up to 74 percent of FDI is permitted in eight categories including drugs/pharmaceuticals, mining, storage, warehousing, and trans-

port. In addition 100 percent of FDI is automatically approved in a few sectors—electricity generation and transmission, construction/maintenance of roads, venture capital funds, and business e-commerce. However, government approval of foreign infrastructure projects that are not subject to the automatic approval process frequently is held up for lengthy periods of time.

Most sectors of the Indian economy are now open to foreign investors, except those linked to national security such as defense, railways and atomic energy. The United States and India have not negotiated a Bilateral Investment Treaty, although an agreement covering the operations of the Overseas Private Investment Corporation (OPIC) was updated in 1997. OPIC operations resumed in December 1998, following the partial lifting of sanctions imposed on India after its nuclear tests in May 1998. In 1994 India became a member of the Multilateral Investment Guarantee Agency, an agency of the World Bank. The Indian government ratified the Uruguay Round GATT Agreement on January 1, 1995 and is a member of the WTO. With regard to Trade-Related Investment Measures (TRIMs), the United States is challenging in WTO the local content and trade balancing measures that India applies to foreign joint ventures in the motor vehicle manufacturing sector.

Government Procurement Practices: Indian government procurement practices are not transparent and occasionally discriminate against foreign suppliers, but they are improving under the influence of fiscal stringency. Price and quality preferences for local suppliers were largely abolished in June 1992. Recipients of preferential treatment are now concentrated in the small-scale industrial and handicrafts sectors, which represent a very small share of total government procurement. According to a recently renewed rule, public sector units receive preferential treatment inasmuch as they may undercut the lowest bid on a government contract by 10 percent. Defense procurement through agents is not permitted, forcing U.S. firms to maintain resident representation. When foreign financing is involved, procurement agencies generally comply with multilateral development bank requirements for international tenders. India is not a signatory of the WTO Government Procurement Agreement.

Customs Procedures: Liberalization of India's trade regime has reduced tariff and nontariff barriers, but it has not eased some of the worst aspects of customs procedures. Documentation requirements are extensive and delays are frequent. In 1996, the Indian government switched to the harmonized system of commodity classification, removing ambiguities and providing more transparency to its export-import policy.

6. Export Subsidies Policies

The 1991 budget phased out most direct export subsidies, but a web of indirect subsidies remains. Export promotion measures include exemptions or concessional tariffs on raw materials and capital inputs, and access to Special Import Licenses (SILs) for restricted inputs. The SIL requirement must be eliminated by April 1, 2001, pursuant to the WTO panel report on balance of payments-based QRs. Concessional income tax provisions traditionally applied to exports (export earnings were tax-exempt), although the Indian government is eliminating this provision over five years in equal stages. In IFY 1999–2000 80 percent of export earnings are exempt from taxes. Commercial banks provide export financing on concessional terms.

7. Protection of U.S. Intellectual Property

In India, various statutes for the protection of intellectual property rights exist although enforcement is poor and piracy is rife. Copyright enforcement, particularly with the proliferation of the Internet and cable television, is generating increased attention from the Indian judiciary. Still, there have been only four criminal convictions for piracy in India since a new copyright law went into effect in 1995. In April 1998 the United States and India reached an agreement to resolve a long-running dispute over India's failure to implement its obligations under the WTO TRIPS Agreement. In April 1999 the Indian Parliament passed a patent bill establishing a "mailbox" system for the filing of pharmaceutical and agricultural chemical product patent applications and allowing exclusive marketing rights. India failed, however, to meet the WTO deadline to bring its intellectual property laws and enforcement efforts into TRIPS compliance by January 1, 2000. A draft Patents Bill, amending the Patents Act of 1970, was introduced in the Indian Parliament in December 1999 and currently is pending with a joint parliamentary committee. Passage of the bill is not expected until 2001. The Indian government has announced its intention to take full advantage of the 2005 transition period allowed for developing countries under TRIPS before implementing full patent protection. India is a member of the Bern Convention for the Protection of Literary and Artistic Works. In August 1998 it became a member of the Paris Convention, and in December 1998 it became a signatory to the Patent Cooperation Treaty.

Over the past decade, the USTR has targeted India as a Priority Foreign Country in the "Special 301" process, and despite some improvements, India is still included in the "Special 301" Priority Watch List. India was identified in April 1991 as a "Priority Foreign Country" under the "Special 301" provision of the 1988 Trade Act, and a Section 301 investigation was initiated in May 1991. In February 1992 the USTR determined that India's denial of adequate and effective intellectual property protection was unreasonable and burdens or restricts U.S. commerce, especially in the area of patent protection. In April 1992 the United States suspended duty-free privileges under the Generalized System of Preferences (GSP) for $60 million in trade from India. In June 1992 additional GSP benefits were withdrawn, increasing the total affected trade to approximately $80 million.

India's patent protection is weak and has especially adverse effects on U.S. pharmaceutical and chemical firms. Estimated annual losses to the pharmaceutical industry due to piracy are about $500 million. India's Patent Act prohibits patents for any invention intended for use or capable of being used as a food, medicine, or drug or relating to substances prepared or produced by chemical processes. Many U.S.-invented drugs are widely reproduced since product patent protection is not available. Processes for making drugs may be patented, but the patent term is limited to the shorter of five years from the grant of patent or seven years from the filing date of the patent application. Product patents in other areas are granted for 14 years from the date of filing.

Trademark protection is considered good and was raised to international standards with the passage in December 1999 of a new Trademark Bill that codifies existing court decisions on the use and protection of foreign trademarks, including service marks. Enforcement of trademark owner rights has been indifferent in the past, but is steadily improving as the courts and police respond to domestic concerns about the high cost of piracy to Indian rights' holders.

India continues to have high piracy rates for all types of copyrighted works. Strong criminal penalties are available on paper, and the classification of copyright infringements as "cognizable offenses" theoretically expands police search and seizure authority. Still, severely backlogged Indian courts coupled with the excessive requirements of Indian criminal procedure have led to infrequent and lax enforcement. The recently passed Information Technology Act provides a legal framework for the prevention of piracy and protection of intellectual property rights, to include penalties for the unauthorized copying of computer software.

The proliferation of unregulated cable television operators (estimated at over 40,000) has led to pervasive cable piracy. A strong anti-piracy effort in the business applications software field, where India ranks third in the world with $5 billion in sales in 1999, has produced a drop in the business software piracy rate from 78 percent in 1995 to 61 percent in 1999. According to a recent industry report, trade losses due to the piracy of U.S. motion pictures, sound recordings and musical compositions, computer programs, and books totaled $310 million in 1999.

8. Worker Rights

a. *The Right of Association:* India's constitution gives workers the right of association. Workers may form and join trade unions of their choice and work actions are protected by law. Unions represent roughly 2 percent of the total workforce, and about 25 percent of industrial and service workers in the organized sector.

b. *The Right to Organize and Bargain Collectively:* Indian law recognizes the right to organize and bargain collectively. Procedural mechanisms exist to adjudicate labor disputes that cannot be resolved through collective bargaining. State and local authorities occasionally use their power to declare strikes "illegal" and force adjudication.

c. *Prohibition of Forced or Compulsory Labor:* Forced labor is prohibited by the constitution; a 1976 law specifically prohibits the formerly common practice of "bonded labor." Despite implementation of the 1976 law, bonded labor continues in many rural areas. Efforts to eradicate the practice are complicated by extreme poverty and jurisdictional disputes between the central and state governments; legislation is a central government function, while enforcement is the responsibility of the states.

d. *Minimum Age for Employment of Children:* Poor social and economic conditions and lack of compulsory education make child labor a major problem in India. The government's 1991 census estimated that 11.3 million Indian children from ages 5 to 15 are working. Non-governmental organizations estimate that there may be more than 55 million child laborers. A 1986 law bans employment of children under age 14 in hazardous occupations and strictly regulates child employment in other fields. Nevertheless, hundreds of thousands of children are employed in the glass, pottery, carpet and fireworks industries, among others. Resource constraints and

the sheer magnitude of the problem limit states' ability to enforce child-labor legislation. The U.S. Department of Labor has initiated cooperative programs with the Indian government to address child labor.

e. *Acceptable Conditions of Work:* India has a maximum eight-hour workday and 48-hour workweek. This maximum is generally observed by employers in the formal sector. Occupational safety and health measures vary widely from state to state and among industries, as does the minimum wage.

f. *Rights in Sectors with U.S. Investment:* U.S. investment exists largely in manufacturing and service sectors where organized labor is predominant and working conditions are well above the average for India. U.S. investors generally offer better than prevailing wages, benefits and work conditions. Intense government and press scrutiny of all foreign activities ensures that any violation of acceptable standards under the five worker-rights criteria mentioned above would receive immediate attention.

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

[Millions of U.S. Dollars]

Category	Amount	
Petroleum		–386
Total Manufacturing		466
Food and Kindred Products	–65	
Chemicals and Allied Products	92	
Primary and Fabricated Metals	–31	
Industrial Machinery and Equipment	355	
Electric and Electronic Equipment	131	
Transportation Equipment	–123	
Other Manufacturing	108	
Wholesale Trade		128
Banking		420
Finance/Insurance/Real Estate		263
Services		50
Other Industries		247
TOTAL ALL INDUSTRIES		1,189

Source: U.S. Department of Commerce, Bureau of Economic Analysis.

PAKISTAN

Key Economic Indicators

[Billions of U.S. Dollars unless otherwise indicated]

	1998	1999	2000 [1]
Income, Production and Employment:			
Nominal GDP [2]	57.4	54.0	56.5
Real GDP Growth (pct)	4.3	3.1	4.8
GDP by sector (pct):			
Agriculture	25.2	24.5	25.9
Manufacturing	18.3	18.6	16.8
Services	9.7	8.9	9.3
Government	6.1	6.1	6.3
Per Capita GDP (US$)	441	406	415
Labor Force (millions)	37.7	38.6	39.4
Unemployment Rate (pct)	6.1	6.1	6.1
Money and Prices (annual percentage growth):			
Money Supply Growth (M2)	14.2	3.5	3.2
Consumer Price Inflation	7.8	6.1	3.4
Exchange Rate (Rupees/US$)			
Official	43.2	50.2	51.7
Parallel	52.2	54.2	54.2

Key Economic Indicators—Continued

[Billions of U.S. Dollars unless otherwise indicated]

	1998	1999	2000 [1]
Balance of Payments and Trade:			
Total Exports FOB [3]	8.4	7.7	8.56
Exports to United States	1.7	1.7	2.1
Total Imports CIF [3]	10.3	9.3	10.3
Imports from United States	1.1	0.7	0.647
Trade Balance [3]	–1.9	–1.6	–1.75
Balance with United States	0.6	1.0	1.4
External Public Debt	29.7	28.6	31.04
Fiscal Deficit/GDP (pct)	7.7	6.0	6.5
Current Account Deficit/GDP (pct)	3.2	4.1	2.4
External Debt Service Payments/GDP (pct)	5.0	6.3	5.1
Gold & Foreign Exchange Reserves	1.54	2.3	1.9
Aid from United States (U.S.$ millions)	307	42	50
Aid from All Other Sources [4]	2.8	2.3	1.5

[1] Data are for the corresponding Fiscal Years ending June 30. Rupee exchange rates used to convert to dollars are 43.2 for 1998, 50.2 for 1999 and 51.7 for 2000.
[2] GDP at factor cost.
[3] Merchandise trade.
[4] No military aid is believed to be included in these figures. Figures are for loans and grants contracted.

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

1. General Policy Framework

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

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

Monetary Policy: The Government of Pakistan has followed a liberal monetary policy during 1999–2000 in order to provide cheap credit to the sagging industrial sector by reducing interest rates on Treasury bills that act as a benchmark for the lending rates of banks. Although domestic credit expansion was higher in 1999–2000 due to large borrowing by the government sector, conversion of non-resident foreign currency accounts into rupees and an increase in liquid reserves, actual growth in money supply has remained stagnant at just 3.2 percent against the target of 9.4 percent, due to low credit demand from the private sector. There has been a recent tightening of monetary policy to stem the slide of the rupee. The govern-

ment and the State Bank of Pakistan (SBP) are attempting structural reforms in an effort to move toward more indirect, market-based methods of monetary control along with greater autonomy for the SBP. Other government monetary reforms include efforts to rationalize staff, enhance competition in the banking sector, and improve prudential regulation and supervision. Prior to the coup, however, state-owned development finance institutions had continued to make politically influenced lending decisions and, partly as a result, have weak balance sheets. In December 1999 the Supreme Court ruled that interest (riba) is prohibited under Islam and struck down a number of laws and ordered that Pakistan is to implement an interest-free financial system by June 30, 2001. The Government of Pakistan has created two commissions, one at the State Bank of Pakistan and other at the Ministry of Finance, to study the implementation of this decision.

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

2. Exchange Rate Policy

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

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

3. Structural Policies

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

Pricing and Tax Policies: Pakistani government agencies and public sector companies allow only exclusive agents to submit bids for tenders as an assurance that they receive only one quotation from each supplier. In the market, pricing is often

complicated by the country's complex tax structure, which often includes a number of taxes and customs duties that marketers must build into their final sales prices. These include landing charges, customs duty, bank charges, insurance, and the recently introduced GST. The government has recently done away with the "octroi" tax (a municipal toll tax). Exemptions or relief from import duties have been allowed on imported machinery. Tax relief has also been provided for expansion and balancing, modernization and replacement in existing industries.

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

4. Debt Management Policies

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

5. Significant Barriers to U.S. Exports

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

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

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

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

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

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

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

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

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

6. Export Subsidies Policies

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

7. Protection of U.S. Intellectual Property

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

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

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

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

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

8. Worker Rights

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

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

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

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

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

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

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

[Millions of U.S. Dollars]

Category	Amount	
Petroleum		229
Total Manufacturing		13
Food and Kindred Products	27	
Chemicals and Allied Products	(1)	
Primary and Fabricated Metals	(1)	
Industrial Machinery and Equipment	0	
Electric and Electronic Equipment	0	
Transportation Equipment	0	
Other Manufacturing	0	
Wholesale Trade		41
Banking		139
Finance/Insurance/Real Estate		65
Services		2
Other Industries		–2
TOTAL ALL INDUSTRIES		488

(1) Suppressed to avoid disclosing data of individual companies.

Source: U.S. Department of Commerce, Bureau of Economic Analysis.