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- ARTICLES

Manufacturing: Greater competition key to export competiveness

Page No.38 ColNo.03

'Naya' can't do without 'purana'. At least that's what comes out of the new Cabinet. Good people all, let's root for the many who served Musharraf, some who belonged to PPP, and few who can be traced to PML-N, as they pad up for their second innings - especially Zubaida Jalal, the suave lady from Mand who swaps Education (under Musharraf)for Defence Production. Don't worry Zubaida - even we don't know what Defence Production is about.

It is Razak Dawood, the respected business leader and founder of the Big Business Club aka Pakistan Business Council (PBC), who faces the gravest of challenges. Asad can make the right kind of noises and beg or borrow his way out of trouble, but at the end of five years his balance sheet will be written by Razak (trade account, growth, investment, jobs).

Razak inherits exactly the same portfolio he had almost 19 years ago. The issues, too, are the same: stagnant exports, rising imports, sluggish manufacturing sector, plummeting Investments (especially FDI), and an inhospitable external environment (until daisy-cutting of Afghanistan turned a pariah into a partner).

Razak's strong suit is his willingness to listen. He is the kind of guy who will unapologetically wake you up in the middle of the night to seek advice. Once convinced he tears into the opposition, without a care for self-preservation(explains his being shown the door while his Q block colleague rose to greater heights).

Key word defining the Export challenge is 'competitiveness'. Government and entrepreneur have conspired together to dent competitiveness. Government found it easier to provide inordinate protection than carry out tough reforms. Business found little incentive to improve productivity when rent-seeking was for the asking.

There are things government needs to do to improve competitiveness - a consistent and predictable policy regime, improved social and physical infrastructure, greater ease of doing business. Most critically, it has to give the right signals - an unambiguous regime of carrot and stick.

There are things Business has to do - invest in competent management, train the work force that is rewarded for improved productivity, use technology to better leverage capital and labour, and innovate so it produces what the market wantsand not market what it produces.

All this is necessary but not sufficient.

Nothing works for competitiveness like competition. You take competition out and inefficiencies march in. Sadly, aspirations of self-sufficiency (legitimate) have often been employed as a ruse to check fair competition, as has been the spectre of 'deindustrialization'. Domestic competition has been compromised through a neutered Competition Commission and international competition negated through high tariff walls. High tariffs, especially when accompanied with dispersion and escalation, are inherently anti-manufacturing, anti-investment, anti-consumer, and anti-export -and they incentivize smuggling.

Manufacturing gets hurt because of the snowballing effect of high tariffs. Cost of production escalates. The 'tariff cocoon' also induces a lulling effect on production efficiencies. Over time, with the ever-increasing productivity of foreign suppliers, domestic producers need more and more protection to survive.

Investment decisions get distorted because flows are directed towards sectors with highest protection,

and not where you could develop a competitive edge. High import tariffs also introduce an element of uncertainty - you never know when the government brings them down, either autonomously or as a consequence of trade agreements or global developments.

Consumer is always at the receiving end. He pays higher than international prices, for poorer quality. Of course, consumers feel compensated if higher import duties mean more 'jobs', the flip side of the protection coin. This, however, has not been the case - large scale manufacturing, the principal beneficiary of protectionism, has not shown much buoyancy in job creation. Those who say manufacturing bears a disproportionate burden of taxes forget all the benefits it gets, mostly paid for by the consumers.

High tariffs spawn the well known 'anti-export bias': If the domestic market is more rewarding you have little incentive to export. Also, where the duty draw -back systems are convoluted the exporter's costs go up. Solutions like export processing zones and (duty free) import-for-export schemes haven't quite worked, nor have compensatory rebates.

Our Agricultural sector offers an instructive tutorial in costs of high protection. Largely insulated from foreign competition, its productivity levels show no signs of perking up. There is no compulsion to improve yields, produce new varieties, or cut costs - the hapless consumer is there to pay for your inefficiencies. We may be surplus in wheat and sugar but can't export because our prices are too high!

We are not pleading here for an across-the-board slashing of import duties. Lower import duties are an essential part of the solution but could blowback if unaccompanied by other pro-competitiveness reforms.

What we are pleading for is reasonable competition that ensures greater productivity, rational investment decisions, and helps exports. Three considerations should guide the tariff-rationalization exercise. First, when fixing nominal rates we should not be oblivious to effective rates of protection (ERP) - there are several instances in our current tariff code where ERP is several times the nominal rate.

Second, level of protection should be pegged to pre-determined 'dividend criteria': employment, exports, revenues, technological diffusion, total factor productivity, whatever. However, to sustain efficiency gains protection has to be on a diminishing scale, down to x percent over a period of time.

Third, intermediate goods used in industries with strong multiplier effects should have low protection levels. If, for example, construction is something that the government deems to give rich dividends, inputs like steel bars, paints, and glass will have to be less protected.

Improving export competitiveness is a tortuous road. Let's take the first step by initiating a tariff rationalization exercise. There is a lot more that needs to be done for export revival, from an Industrial policy that creates better linkages between large scale and SMEs, to a functioning EXIM bank, to taking a whip to TDAP to make it work for exporters and not travel agents.

Razak's success in his first innings was promoting 'export culture', not subsidizing exports (many subsidies were rolled back as a deliberate policy measure). The biggest impediment to export culture is the babus throwing the baby out with the bathwater. To check their excesses babus on his team would need to know better - and have clout. Sorry, Razak, for the earful. We wish you well.

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