CAN DOMESTIC TRADE BE THE ENGINE OF PAKISTAN'S GROWTH?

Omer Siddique

[1]In Pakistan, when trade is mentioned, people invariably think of international trade. How to increase exports and decrease import dependence is discussed ad nauseam. Sadly, domestic trade has been neglected in Pakistan as a vehicle for growth. The bias against domestic commerce has been because of the Haq/HAG model of the 1960s, which focuses on increasing exports and reducing imports through an import substitution policy. Consequently, a lopsided policy focus on increasing exports and achieving import substitution has stifled domestic trade and market development.[2]

MAKING A CASE FOR A GROWTH PARADIGM LED BY DOMESTIC COMMERCE

There is a strong case for shifting the focus to a domestic commerce led growth paradigm. In this paradigm, the development of domestic markets is considered the primary driver of growth and production.[3] The conducive business environment in the domestic market facilitates entrepreneurs to grow, thrive, develop new products, and create brand names. In such markets innovations and entrepreneurship thrive through risk-taking and understanding of consumers' tastes and markets. Innovation and entrepreneurship taking place in the domestic market later move out and lead to higher exports and foreign exchange earnings. More importantly, in this model not only goods are exported but there is a greater likelihood of businesses being exported leading to the birth of the Pakistani multinational.[4]

Several examples from around the world show that this strategy has brought phenomenal growth in the case of large domestic markets and provides an effective way to breed entrepreneurship, risk-taking, innovation, product and brand development, and competitive markets. Multinationals like Coke, McDonald's, and Ford all started as domestic industries. Their testing ground was the domestic consumer market.

DOMESTIC COMMERCE IN PAKISTAN: AN OVERVIEW

Second Largest Employer

Despite the neglect, Pakistan's domestic commerce sector has been resilient and making important contributions to the economy. Domestic commerce's share in total employment is 36.02%[5] making it the second largest employment-generating sector after agriculture.

Largest Contributor to Output

Domestic commerce also contributes substantially to Pakistan's output: its share in the output was 52.55% in 2022-23 – the highest among all the sectors

Wholesale & Retail

The wholesale and retail trade (WRT) is the largest sector and the mainstay of domestic trade. The WRT has a share of 14.37% in total employment. The sector, which is considered mainly informal, also employs a bulk of informal sector workers: 34.19% of the total informal workers are employed in the WRT sector. In terms of output, the WRT's share in GDP, at 18%, is the highest among the domestic commerce activities.

In 2002, there were 1.57 million WRT establishments in Pakistan compared to 1.0028 million establishments in 1988.[6] According to PIDE's estimates, there are currently 2.66 million WRT establishments in Pakistan.[7] This is evidence of the dynamism of the domestic commerce in Pakistan. Back-of-the-envelope estimates – based on the sector's output growth, growth in the number of establishments, and employment figures – signal the sector's efficiency and productivity.

WHAT STIFLES DOMESTIC COMMERCE IN PAKISTAN?

Urban Zoning, Commercial Space, and Rent

An important factor that has stifled domestic commerce in Pakistan is the severely limited space for domestic commerce, especially the WRT.[8] The current zoning regulations and urban planning have encumbered domestic commerce in Pakistan.[9] In twin cities, especially in Islamabad, commercial spaces are limited and mixed-use construction is almost non-existent. The new projects allocate very little space for commercial activities compared to the space for residential construction. All these facts stifle domestic commerce.

Domestic businesses often complain about high rents. In the case of Islamabad, the Supreme Court's 2016 ruling to disallow commercial activity in residential units/areas has contributed to high rent. Moreover, according to the Islamabad Rent Restriction (Amendment) Act 2021, owners of residential and commercial properties are allowed to increase the rent by 10% every year. In some cases, landlords increase the rent by more than 10%, but tenants do not go for mediation or litigation because of high time and pecuniary costs.

Local Administration, Tax Administration, and Bureaucracy

The attitude of the bureaucracy and other authorities does not support domestic commerce activities. The high degree of informality in domestic commerce, especially in the WRT sector, emanates from the attitude of administration, tax authorities, and bureaucracy. Government departments, such as the FBR and the EOBI, create unnecessary problems for traders, which wastes time and resources. Officials from different departments and authorities visit the businesses routinely. Moreover, domestic traders do not engage with formal financial institutions because of documentation requirements and the fear of being approached by the tax authorities

Cumbersome Registration Process

In Pakistan, the process of opening and registering a new business is very difficult and cumbersome, which is well-documented by various PIDE studies.[10] Similarly, the process of filing a tax return is very difficult. While opening a business, entrepreneurs have to deal with various departments, such as the labour department, EOBI, and WWF, among others, making it very confusing for a businessman, especially for local traders who are less educated. Sometimes even a literate person is unable to digest processes and formalities.

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[1]This essay is based on the forthcoming report by PIDE and RASTA: "The State of Commerce in Pakistan: International and Domestic."
[2]Haque, N.U. (2006a). Beyond Planning and Mercantilism: An Evaluation of Pakistan's Growth Strategy. Pakistan Development Review 45(1): 3–48.
[3]Haque, N.U. (2006b). Awake the Sleeper Within: Releasing the Energy of Stifled Domestic Commerce! PIDE Working Papers No. 2006:11. Islamabad: Pakistan Institute of Development Economics.
[4]Haque, N.U. (2006b)
[5]Labor Force Survey (2020-21). It is important to note that the LFS, or any other official statistics, does not categorize domestic commerce separately. Domestic commerce sectors are selected based on the nature of activities. These include wholesale & retail trade, transport & storage, education, accommodation & food, professional, finance & insurance, and real estate.

[6]Pakistan Bureau of Statistics (2005). Economic Census 2005. Islamabad: Paikstan Bureau of Statistics. The economic census was carried out from 2001 to 2003 and the results were published in 2005.
[7]PIDE/RASTA (forthcoming). The State of Commerce in Pakistan: International and Domestic. Islamabad: Pakistan Institute of Development Economics. The projections are based on data collected for the State of Commerce report and have used the estimates of the average number of employees per establishment to estimate the total number of WRT establishments in Pakistan.
[8]Haque, N.U. & Nayab, D. (eds.) (2020). Cities – Engines of Growth (2nd ed.). Islamabad: Pakistan Institute of Development Economics; Haque, N.U. (2015). Flawed Urban Development Policies in Pakistan. PIDE Working Paper No. 119. Islamabad: Pakistan Institute of Development Economics;
[9]Haque, N.U. & Waqaar, I. (eds.) (2006). Domestic Commerce – The Missing Link. Islamabad: UNDP/Ministry of Commerce.
[10]Haque, N.U., Qasim, A.W., & Khan, F.J (2023). PIDE Sludge Audit Volume II. Islamabad: Pakistan Institute of Development Economics.
Haque, N.U., & Qasim, A.W. (2022). Regulatory Bodies: Hurting Growth and Investment. PIDE Monograph Series 2022:4. Islamabad: Pakistan Institute of Development Economics
Haque, N.U., Qasim, A.W., & Khawaja, I (2022). PIDE Sludge Audit Volume I. Islamabad: Pakistan Institute of Development Economics.

Finance and Credit

Banks do not facilitate and entertain smaller domestic traders. Banks require them to open and maintain an account for at least six months and maintain a certain average balance. If traders fail to meet these conditions, banks do not provide them with the facility. The irony is that if the businessman had enough credit, they would not need a loan. Moreover, banks do not develop retail and trade-specific products despite instructions from the State Bank because they do not have any incentive to lend at lower interest rates. They find it more profitable to invest in government paper.

DOES THE BUCK STOP WITH THE GOVERNMENT?

Conventional Methods of Procurement and Supply Management

In Pakistan, entrepreneurs in the domestic trade sector, rely on conventional methods for procurement and replenishment. They struggle with a lack of supply predictability and slow replenishment cycles resulting in regular stockouts. An average retailer spends a considerable time per week on procurement alone. This traditional mode of procurement means greater effort and time spent in the process. Moreover, traditional retailers in Pakistan cannot get competitive prices because of reliance on one supplier. They do not search for alternate suppliers or products.

Geographical Limitations and Broken Value Chain

As far as wholesalers and distributors are concerned, they do not grow because of a limited customer base which is a result of geographical and logistical limitations. Furthermore, rail logistics need to be improved in Pakistan but due to a variety of reasons, very few businesses use the railway system to transport goods via the rail network across Pakistan.

Inventory Management, Market Intelligence, and Demand Forecasting

Even chain stores, big retailers, and supermarkets rely on outdated and conventional methods for procurement, inventory management, market intelligence, and demand forecasts. They do not grow and build international brands because they do not use modern methods, such as market data, for forecasting and market intelligence. A majority of industry players still manually use Excel to analyse sales trends and forecast future sales. In short, Pakistani big retail players and brands do not use market intelligence to the extent that the rest of the world uses such tools.

Chasing Incentives and Subsidies

Globally, business conglomerates add value, innovate, and diversify investment, but in Pakistan, conglomerates prioritise maximising returns without emphasising innovation, product diversification, or R&D. In Pakistan, business conglomerates own a large number of companies, but their net worth, by international standards, is unimpressive – the highest-valued conglomerate's worth is USD 6 billion. In comparison, India's second-largest business group is worth more than USD 300 billion. One of the reasons Pakistan has not been able to build global brands is that Pakistan's businessmen prefer to invest in conventional sectors, such as textiles, real estate, financial services, and power/energy. This risk-averse approach indicates reliance on government support, subsidies, and preferential treatment. Rent-seeking behaviour further reinforces this risk aversion and a focus on maintaining maximum ownership stakes. A recent example is that of mobile manufacturing. Seeking incentives offered in the Mobile Manufacturing Policy 2020, established business houses set up mobile assembly plants. They have not thus far achieved any localisation of parts, R&D, employment generation, and exports as outlined in the policy.

The author is a Senior Research Economist at the Pakistan Institute of Development Economics (PIDE), Islamabad.