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CPEC and the Opportunity for Agriculture Sector

About the project

Funded by: IGC

Key Counterpart: Department of Agriculture, Punjab

Impact
The policy challenge this research targets is how to leverage CPEC investments for the agriculture sector. It provides recommendations for 4 subsectors, and a tool that the Department of Agriculture in Punjab can use to extend this analysis to other sub-sectors and understand the potential and key constraints. The work has been presented to high level policymakers (based at the State Bank of Pakistan and Planning & Development Department in Punjab) on multiple occasions. This work fed into Pakistan's Free Trade Agreement negotiations with China.

This policy note is written by Hasaan Khawar (CDPR Fellow) and is based on his articles published in The Express Tribune and on the research conducted by International Growth Centre on "Engagement with Punjab under CPEC: A Proposed Framework for Agriculture" by Hasaan Khawar, Nazish Afraz (LUMS) and Dr. Mushtaq Khan (LUMS).

In brief

- China is the world's largest importer of agricultural products but Pakistan's share is less than half percentage point in China's total food imports worth $160 billion.
- A shared border between Pakistan and China provides Pakistan the strategic edge to transport perishable goods without spoilage and incur lower transport costs.
- Though CPEC has reduced logistics cost, increasing exports will require examination of tariff and non-tariff
- arrangements, including quarantine inspections and fulfilling food safety standards.

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China is world's largest importer of agricultural products. In 2015 China imported $160 billion worth of agricultural products. However, Pakistan's share in these exports was miniscule - less than half a parentage point - despite having a large agrarian base and a shared border with China.

With a population of 1.3 billion people, China consumes almost $1 trillion worth of food every year. With increased urbanization and rising incomes, Chinese consumption patterns are also changing and demand for high quality imported food items is growing at a pace much faster than population growth. Therefore the domestic consumption is expected to grow by another $500 billion in the next 10 years. According to Bloomberg, it takes about 1 acre of arable land to feed an average U.S. consumer. With present population, China only has about 0.2 acres per citizen, which is going to be far short of future requirements, considering the evolving demand.

The world is therefore keenly focusing on China, with international conglomerates and food giants making long-term China plans. China, they expect, is going to be the biggest growth driver, in future.

China, world's largest importer of vegetables, gets 50% of these imports from USA and Brazil. In the world of international trade, shorter distances can provide a strategic advantage through lower transportation costs. But for perishable items like food, such proximity can translate into yet another edge. During transit over long distances, food items face higher risk of spoilage and contamination. Because of this, not only additional cost is incurred for preservation and packaging but often exporters have to make use of extra pesticides to increase shelf life of food.

Pakistan, being the next-door neighbor to China, therefore enjoys a unique advantage and China Pakistan Economic Corridor (CPEC) provides an unprecedented opportunity to capitalize on that. Agriculture development is one of the seven areas of cooperation under CPEC, whereas China is specifically interested to explore areas like cotton productivity, efficient irrigation and post-harvest infrastructure along the CPEC route.

However Pakistan's agriculture sector priorities vis-à-vis CPEC remain unclear. CPEC provides Pakistan a godsend to enhance its agriculture exports to China. This attractive opportunity is what should drive the CPEC agenda for agriculture from Pakistani side. So how can that happen, what should Pakistan negotiate for and how can it benefit from this huge opportunity? Recently, International Growth Centre sponsored a research project on this, which attempted to provide some of the answers in Punjab's context.

While CPEC is expected to lead to a reduction in logistics costs, this will not automatically translate into greater exports. Market access requires an examination of tariff and non-tariff barriers to trade too. The second phase of negotiations of the Pak-China Free Trade Agreement (PCFTA) are now under way. These negotiations were long overdue and considering Pakistan's inability to make use of the first phase signed in 2006, the domestic industry has a number of concerns.

Let's look at Pakistan's agriculture exports. Textile and clothing make for more than half of country's exports, followed by vegetables, accounting for 14%. Food products are the fourth important item in Pakistan's exports, constituting almost 4%. It is quite evident that not only bulk of Pakistan's exports is reliant on agriculture but also the top two food categories account for almost one-fifth of its exports.

Digging a bit deeper on Pakistan's agricultural and agro-processed exports, there is a well-diversified basket of $4.06 billion, excluding cotton and livestock. Now out of this $4 billion+, how much does Pakistan export to China? Only a third of a billion dollars, with rice taking more than half, followed by the 'beverage, spirits and vinegar' category, which takes another one-third. Although Pakistan's agricultural exports to China spread over 14 broad product categories, most of them are very small or negligible.

What is even more interesting is that China imports $76 billion worth of goods in these categories, with Pakistan claiming merely half a percent share. Since Pakistan is exporting these products elsewhere, it must be somewhat competitive and since China is importing them, there is an established market next door. So, what exactly is happening here?

Let's look at the example of rice. Pakistan is one of the top five world exporters of rice and rice exports of $1.9 billion in 2016 represented 5% of global rice exports. Rice exports to China, however, accounted for only 8% of this. On the other hand, China imported $1.4 billion worth of rice, with Pakistan getting only 11% share. From where did China get the rest? Mostly Vietnam and Thailand with 3-5 times more rice exports than Pakistan.

Despite the fact that the bulk of China's imports is in non-basmati rice, there is still significant room to increase Pakistan's exports. But the major impediment is non-favorable tariffs. China maintains a special low tariff of 1% on import of a quota of 5.3 million tonnes of rice, however, beyond this quota, rice imports are subject to a tariff of 65%. The ASEAN countries, which are the top exporters of rice to China, enjoy preferential tariffs as a part of ASEAN-China FTA — 20% on non-basmati and broken rice and 50% on tariff in basmati rice. In case of Pakistan, no preferential tariff is applicable on any rice category, making us non-competitive.

The story of rice is not the only one. Similar stories are there in other product categories such as citrus, fruit juices, vegetables, etc., where either tariff or non-tariff barriers are hindering Pakistan's exports to China that would otherwise be made.

Such insights should drive the ongoing PCFTA negotiations with China. Fortunately, Punjab has taken up many of these issues with the federal government but other provinces need to do the same. And this exercise should go beyond agricultural products. The state can pave the way by negotiating better terms of trade for Pakistani exporters, while businessmen should explore why they aren't exporting more.

Once Pakistan taps these opportunities, it could look for other high demand areas in China, where it can potentially develop production capabilities from the scratch.