



# Cross-Line of Control Trade

Peacebuilding and economic potential

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with support from Conciliation Resources



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## Research team

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## Disclaimer

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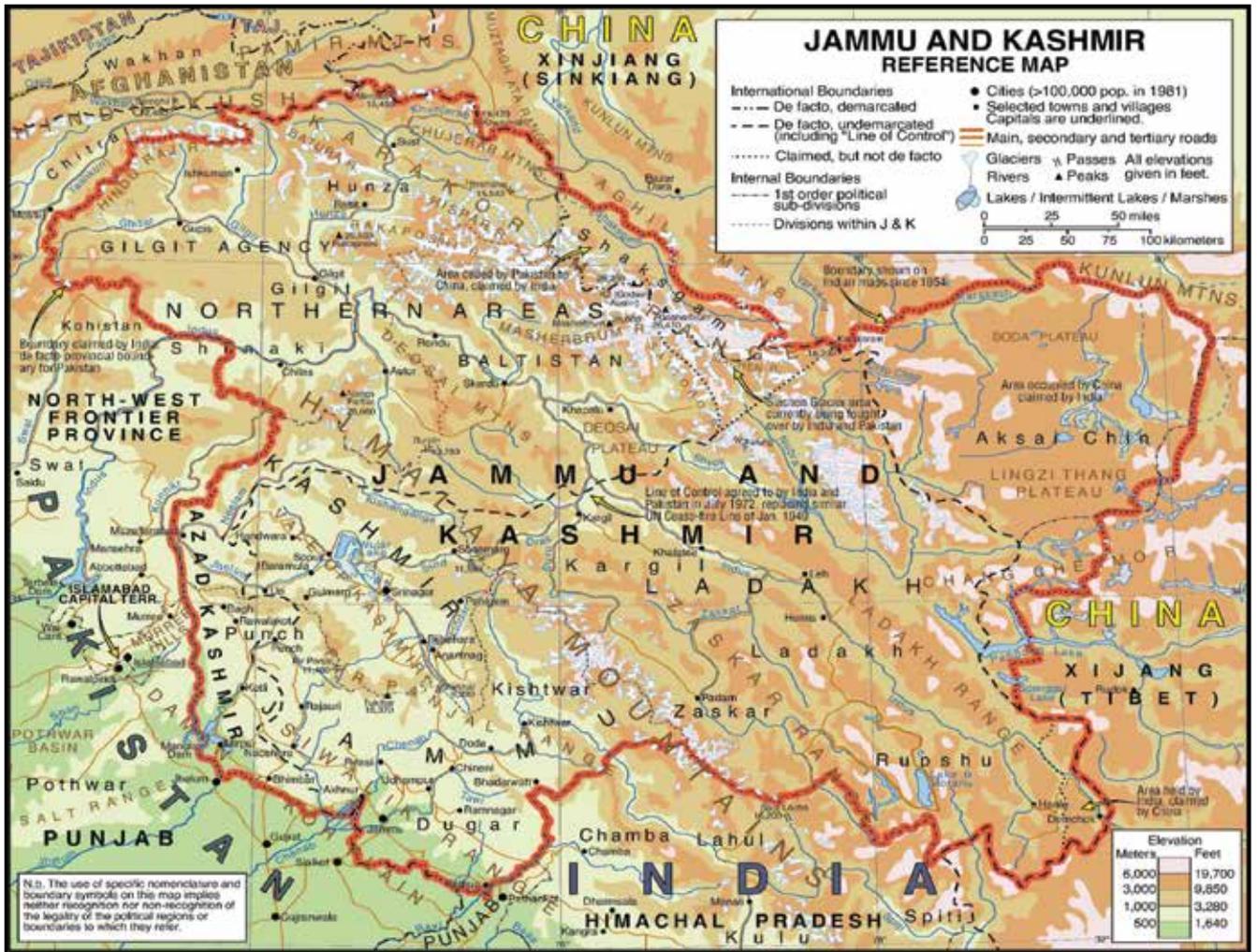
The Princely State of Jammu and Kashmir as it existed until 1947 lost its collective name along with the geographical unity. From the Indian official point of view the entire state is still known as Jammu and Kashmir but the areas on the west of the Line of Control (LoC) are referred to as Pakistan occupied Kashmir. From the official Pakistani point of view the former state is seen divided into three units: Azad Jammu Kashmir, Gilgit-Baltistan on the Pakistani side, and Indian occupied Kashmir on the Indian side. The United Nations refers to the two sides as Indian administered Kashmir and Pakistani administered Kashmir. Some independent accounts, even within India and Pakistan, make use of IaK and PaK.

For the purpose of this study we have mostly used the official names – Jammu and Kashmir (J&K), and Azad Jammu Kashmir (AJK) – unless specified otherwise. To make the frequent references more understandable, in some parts of this report we have also used terms 'LoC East' for Jammu and Kashmir and 'LoC West' to Azad Jammu Kashmir.

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**Map of Jammu and Kashmir region**

*Courtesy: Kashmir Study Group*

India and Pakistan agreed to launch trade, in 2008, across the Line of Control (LoC) between Jammu and Kashmir on Indian side and Azad Jammu and Kashmir on Pakistani side essentially as a measure of building peace and confidence but with some economic spin offs for the stakeholders. Business merely for the promotion of peace is no profitable stipulation and therefore not a sustainable process. But if cross-LoC trade in Kashmir does not contribute to the intended area of peace and stability then the confidence building measure is not worth further promotion.

Peace and profit have to be mutually complimentary to make the process sustainable. In this backdrop, the present study on *Peacebuilding and the economic potential of Cross-LoC Trade* was conceived and designed to address both the questions –peace and profit. Since the launch of trade in 2008 significant body of research and literature came out of Indian, Pakistani and Western sources but every study has addressed one question or the other but not both together in their entirety.

The present work is significant in its many aspects. One of the important steps of the study is the long term engagement with the stakeholders which contributed to the formation of Joint Chamber of Commerce and Industry<sup>1</sup> and of Joint Federation of Cross-LoC Traders<sup>2</sup>. After an agreement between the key stakeholders signed at Istanbul in November 2011, the Joint Chamber and Joint

Federation were formally constituted in 2012 in a unique democratic process after sustained consultations led by Ershad Mahmud and Zafar Iqbal Chaoudhary with stakeholders in Pakistani and Indian sides of Kashmir.

The research work makes simultaneous foray into the realm of peacebuilding and hard economics of cross-LoC trade. Another significant aspect of this work is the essential cross-LoC collaboration and teamwork between economists, political analysts, civil society actors and peace practitioners who looked at different questions from the strength of their expertise. With the assistance of second line of researchers, the team worked closely with the stakeholders, political actors and government officials to put their pieces together in the shape of this final report.

The report opens with a background to the Kashmir conflict and then goes on to delve deeply into the status of the line that divides the erstwhile princely state of Jammu Kashmir between India and Kashmir –first as ceasefire line and then as the Line of Control. Subsequent sections look at series of developments in Kashmir and discussion on the Composite Dialogue Process leading to softening of the Line of Control for limited travel in 2005 and trade in 2008. The next section is on the economics of cross-LoC trade, past trends and future possibilities. In-depth literature review, extensive interviews with cross-LoC traders, key political and civil society actors and peacebuilders have contributed to final thoughts in shaping up this study.

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1 For a note on background of JK Joint Chamber see <http://www.c-r.org/news/joint-chamber-strengthens-cooperation>

2 For background, process and membership see <http://www.kashmirtimes.com/newsdet.aspx?q=1059>

## Executive Summary

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The Cross-LoC trade and travel formally launched in 2008 and 2005, respectively, is the single biggest achievement of India-Pakistan dialogue in Kashmir. The other achievement worth mentioning is an unwritten agreement on ceasefire along LoC and international border which has been a success since 2003 despite occasional incidents of violation.

The softening of LoC for travel and trade is though by no means a lasting settlement of Kashmir issue, neither proposed as such India and Pakistan, but still it is seen as a matter of immense satisfaction and achievement for almost all segments of society, particularly the divided families along both sides of LoC in Jammu and Kashmir.

The fact that agreement on cross-LoC trade and travel came in barely few rounds of discussions and without any major hassles on technical issues is an indicator of the possibilities of India and Pakistan achieving greater cooperation on Kashmir.

With the change in political and security dynamics of the Kashmir conflict over decades some political sections as well as militant groups are opposed to the CBMs as it is seen as replacement of political dialogue. However, the growing stakes of the traders and rising hopes of the divided families softened these political sections and militant groups.

Except on two occasions when temporarily suspended due to situations arising out of violations of ceasefire along the Line of Control the trade has continued uninterrupted despite ups and downs security situation or diplomatic relations between India and Pakistan. This fact is a potential indicator of the possibilities of more cross-LoC collaborations in Kashmir.

Despite unique topographical disadvantages and large distances from main markets the participation<sup>3</sup> of traders from parts of divided state, except Gilgit-Baltistan on Pakistani side and Leh district on Indian side is an indicator of economic as well as peacebuilding potential of the cross-LoC trade.

In the limited and controlled business environment on the basis of barter and in absence of proper infrastructural and communication facilities the cross-LoC trade has continuously grown to register monetary value worth \$ 340 million<sup>4</sup> in four years. The average annual trade of \$ 85 million

may be just a fraction of the India-Pakistan bilateral trade of \$ 1.9 billion<sup>5</sup> but this makes immense significance in the given non-traditional operational conditions.

To harness the full economic and peacebuilding potential of Cross-LoC Trade India and Pakistan should broaden the scope of cross-LoC travel to allow registered traders free, frequent and hassle free travel on either side.

Except few odd incidents the cross-LoC trade has not led to any security compromise. Based on this experience the governments should agree and expedite the process of communication and banking facilities for cross-LoC traders not only at the trade facilitations but also at other business centres like Srinagar, Jammu, Muzaffarabad and Mirpur.

In view of the limited production base on both sides of LoC trade should be opened to services and hospitality sectors.

The India-Pakistan Joint Working Group of cross-LoC CBMs should meet regularly to review progress on trade, revise list of trade items on basis of market assessment and address issues emerging in between intervals. The Joint Working Group should ideally co-opt non-official members the representatives of the cross-LoC Joint Chambers.

Based on the success of Cross-LoC trade, India and Pakistan should move to the next steps and look into other possible areas of collaboration like education, healthcare, environment, disaster management and tourism.

To achieve the intended purpose of cross-LoC trade it is important to have the political and civil society interactions going on alongside.

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3 For participation profile of Cross-LoC traders see an earlier report, released as part of this study, at [http://www.c-r.org/sites/c-r.org/files/perception\\_survey\\_peacebuilding\\_crossLoC\\_trade201204.pdf](http://www.c-r.org/sites/c-r.org/files/perception_survey_peacebuilding_crossLoC_trade201204.pdf)

4 PNR 1592.27 exports from AJK to J&K and INR 963.16 exports from J&K to AJK between November 2008 and November 2012. Sources: All Trade Facilitation Centres

5 During 2011-12. Source ASSOCHAM

Exhibiting courage to put the bitterness of previous years aside and make a fresh beginning, in July 2003, diplomatic relations and direct transport links were restored between India and Pakistan. In November a ceasefire along the Line of Control was initiated which emerged as biggest Confidence Building Measure on Kashmir until that date. The foundations of a revived and longest peace process, which eventually led to a slew CBMs on Kashmir including the softening of LoC, was laid in January 2004 when Prime Minister Vajpayee and President Musharraf met in Islamabad on the eve of SAARC summit. 'The Islamabad summit was a model of high-minded diplomacy. Divisive words were not spoken, substantive private sessions were held and common purpose was evident throughout. Musharraf and Vajpayee promised to fight terrorism, promote trade and work cooperatively on energy projects. Most strikingly, Musharraf pledged to prevent the use of territory under Pakistan's control to support terrorism in any manner<sup>6</sup>.

The Composite Dialogue Process was fully revived in June 2004 in pursuance of a decision taken by Vajpayee and Musharraf in January. The revived peace process, along the lines of Composite Dialogue, had a range of CBMs and risk reduction measures between the two countries but Kashmir assumed a central position and all Kashmir related negotiations mostly veered around the Line of Control. The period between 2003 and 2008 was of highest attention to Kashmir in any India-Pakistan dialogue. New Delhi and Islamabad were able to talk and do more about Kashmir only when they found out the Line of Control as a common ground for engagement with no challenge to their traditional positions. Years before full revival of the peace process Prime Minister Vajpayee had started talking about 'forward movement on Kashmir under the ambit of humanity'. President Pervez Musharraf would often talk about 'out of the box' solution. Hints from both sides indicated willingness for making the LoC porous. The smartly crafted peace process laid focus on the CBMs which had the people of Jammu and Kashmir and their humanitarian concerns, not the political positions, at the centre of engagements.

In summer of 2004 the Congress party returned to power in New Delhi and Dr Manmohan Singh

replaced Vajpayee as Prime Minister. The change in guard kept the continuity in peace process intact. The Foreign Ministers of India and Pakistan took a fresh look at the Composite Dialogue in New Delhi in September 2004 while Musharraf and Singh met in New York later in the month. Views were exchanged on all issues but what emerged most significant was to open the LoC in Kashmir for travel. The first major breakthrough on the technical issues related to bus service across LoC came about in December 2004 in a delegation level meeting between the officials of Indian ministry of Surface Transport and Pakistan's Foreign Affairs. The real moment of joy for millions of people across both sides of LoC in Kashmir came on February 16, 2005 with the formal announcement of bus service to run between Srinagar and Muzaffarabad. The joint statement issued from Islamabad said:

*"Both governments have agreed to allow travel across the LoC between Srinagar and Muzaffarabad by bus. Travel will be by an entry permit system, once identities are verified. Application forms for travel will be available with designated authorities in Srinagar and Muzaffarabad. The bus service is expected to commence from 7 April 2005."*

The formal launch of bus service on 7 April 2005 was a historic moment and first ever significant outcome of any India—Pakistan dialogue on Kashmir. While the mood was festive in all regions and among all communities on both sides of LoC in Jammu and Kashmir but a militant attack in Srinagar on the eve of launch was a noteworthy message that some sections wanted discussions on core political issues. The fortnightly run of the bus service, however, made significant contributions in changing the dynamics of conflict as people-to-people contacts enhanced trust and confidence. Barely ten days after launch of the Srinagar-Muzaffarabad bus service President Musharraf was in New Delhi on invitation of Prime Minister Manmohan Singh. In a way the meeting between the two leaders was the celebration of the success of peace process insofar as progress on Kashmir. A 17-point joint statement issued at the end of their deliberations stressed on further cooperation across the LoC as also range of fresh CBMs between mainland India and Pakistan. The Kashmir specific points of joint statement said:

*"In this spirit the two leaders addressed the issue of Jammu and Kashmir and agreed to continue these discussions in a sincere and purposeful and forward looking manner for a final settlement."*

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<sup>6</sup> Michael Krepon in 'Evaluating The Vajpayee-Musharraf Meeting In Islamabad, January 11, 2004; <http://www.stimson.org/essays/evaluating-the-vajpayee-musharraf-meeting-in-islamabad/>

*They were satisfied with the discussions and expressed their determination to work together to carry forward the process and to bring the benefit of peace to their people.*

*They also agreed to pursue further measures to enhance interaction and cooperation across the LoC including agreed meeting points for divided families, trade, pilgrimages and cultural interaction.*

*They condemned attempts to disrupt the Srinagar-Muzaffarabad bus service and welcomed its successful operationalisation. The two leaders pledged that they would not allow terrorism to impede the peace process.*

*They decided to increase the frequency of the bus service and also decided that trucks would be allowed to use this route to promote trade. They also agreed to operationalise additional routes including that between Poonch and Rawalakot.”*

The decision between Prime Minister Singh and President Musharraf to expand the LoC cooperation by opening one more link, increasing frequency of bus and allowing trade on the route came as massive opening for peacebuilding through people-to-people contacts. Another cross-LoC bus service rolled out in June 2006 between Poonch in Indian side and Rawalakot on Pakistani side.

Despite cumbersome permit regime the cross-LoC travel not only revived contacts between divided families but also contributed to a regional discourse for peace and stability. It was the India-Pakistan cooperation on Kashmir which eventually helped New Delhi to revive its internal peace process with Srinagar. In February 2006 Prime Minister Manmohan Singh convened a roundtable conference on Kashmir which was attended by representatives from different spectrums of society. The Hurriyat Conference boycotted the meeting but participation of some second rung of Kashmiri separatist leaders was conspicuous. Another roundtable conference chaired by Prime Minister Singh in Srinagar later in May led to constitution of five Working Groups. One of the Working Groups ‘named strengthening relations across LoC’ recommended, in April 2007, a range of measures for cooperation and collaborations between the divided parts of Jammu and Kashmir. While main recommendations greatly focused on making trade and trade easy and accessible for everyone on both sides of LoC there was a wide range of additional suggestions on collaborations in the areas of education, environment and disaster management. The Working Group also suggested formation of a contact group of legislator to discuss issues of mutual concern and cooperation.

## Cross-LoC trade begins

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In the summer of 2008 India faced serious problems in Kashmir Valley following street protests over a temple land controversy. Prolonged curfews in the trade hub of Jammu severely hit essential supplies in the Kashmir Valley. In August several thousands of Kashmiris took a march along Jhelum Valley Road<sup>7</sup>. The protest towards Line of Control symbolically meant that trade links with Muzaffarabad in Azad Kashmir be restored. Scores of protesters getting killed in clashes with security forces posed a serious political problem for India not only on domestic front but also its context of its international image. As restoration of peace in the Valley became a gigantic task the launch of cross-LoC trade appeared one potential possibility of soothing the bruised emotions in Kashmir through CBM.

A decision on Cross-LoC trade had already been taken but dates for launch and other technical issues were still under discussion. The Foreign Ministers of India and Pakistan met on May 21, 2008 to discuss new and existing Jammu and

Kashmir-specific CBMs, and allowed intra-Jammu Kashmir trade and truck services. On July 18, 2008, the India-Pakistan Joint Working Group on cross-LoC CBMs met in Islamabad to discuss the list of items to be allowed for trade through the truck service.

Getting an immediate launch date from Pakistan was a challenge for India as Islamabad was going through political change. After general elections of earlier that year ousted Pervez Musharraf regime, Asif Ali Zardari of Pakistan Peoples’ Party took over as President on September 6, 2008. New Delhi greeted the new leadership in Islamabad but a formal contact at high level was yet to take place while crisis was deepening in Kashmir. The backchannel was activated to make progress on cross-LoC trade. On September 22, 2008, the modalities regarding the movement of trucks, code of conduct for the drivers, permits, security, timings and list of items to be traded were agreed upon between Pakistan and India to conduct cross-LoC trade.

Prime Minister Singh and President Zardari met in New York on September 25 on the sidelines of UN

<sup>7</sup> The Srinagar-Muzaffarabad road the Valley’s only trade route before 1947

General Assembly meeting. Besides establishing first contact on Zardari's election as President and reviewing with him the Composite Dialogue, the biggest thing on Prime Minister Singh's agenda was obviously getting Pakistan to agree on a date for the launch of cross-LoC trade. This was a crucial test for India-Pakistan peace process and depth of its trust. President Zardari responded positively. Both leaders issued a joint statement<sup>8</sup> declaring October

8 <http://indiatoday.intoday.in/story/Joint+press+statement+after+Manmohan-Zardari+meeting/1/16072.html>

21 as the date for the launch of cross-LoC trade. The joint statement also reiterated commitment to the ceasefire and mutual desire for resolving their outstanding issues. Following this, cross-LoC trade on the Srinagar-Muzaffarabad and Poonch-Rawalakot routes commenced from October 21, 2008. Twenty-one items were identified for duty free passage from each side. The basis of selection of items, however, still remains unclear.

## Softening LoC: The stakeholder perspective

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The recent India-Pakistan Confidence Building Measures on Kashmir have mainly bordered around the Line of Control. Opening the Line of Control at two points has been the one and only substantive outcome of India-Pakistan dialogue on Kashmir. In terms of understanding the peacebuilding potential of cross-LoC trade, or any cooperation across the LoC, it is important to understand long term goals of the key stakeholders – India, Pakistan and different segments of society across the divides in Jammu and Kashmir.

As we have seen in earlier sections in this report and many other developments over the last decade, which have not been discussed here, would suggest that India, Pakistan and the people of Kashmir have reached the Mutually Hurting Stalemate Stage<sup>9</sup> on Kashmir. Some critical statements from militant groups and their ideologues notwithstanding there is a general consensus that there is no other way of lasting peace and stability in Kashmir than reaching an understanding at the political level. It is clear, that none of the parties involved in the conflict can alter the status quo through military means. It is perhaps this realisation which brings India and Pakistan closer on cross-LoC cooperation in Kashmir. It is absolutely important to remember that Kashmir is no more the only issue of contention between India and Pakistan at present as it was in 1948.

The two countries are nuclear powers, terrorism is a common threat to both and serious issue between them, their economies are exceptionally sluggish because of obstacles in economic cooperation. An overwhelming majority in both countries is of the view that enhanced economic cooperation and closer ties in other areas of interest like culture,

education and sports could help India and Pakistan tide over their historical bitterness and help them fight the common challenges together. However, for being in a position of mainland cooperation it is important for both countries to achieve stability in Kashmir. The fact that India and Pakistan were able to enhance mainland cooperation –new trade regime, new visa regime, cultural exchanges and sporting ties –only after significant progress in Kashmir with LoC openings as the centre of engagements. It is a recognised fact that the issue of Kashmir is very complicated and it goes beyond a porous LoC but the journey of LoC from being a line of conflict and military hostilities to a line of commerce and cooperation is significant to the success of peace process as it goes on.

The people of Jammu and Kashmir, belonging to all regions and communities, have always seen the division of their State as unnatural and the drawing of the LoC as against their wishes. Whatever nationalist outlooks they may have assumed on Indian and Pakistani side there has always remained a broad consensus among the people on organic unity of Jammu and Kashmir. In this context when the LoC is opened for travel and trade it comes as most significant moment in the life of the people who have spent decades in waiting for opportunities to cross the historic divides. The intensity of emotions with which people look at the opportunity of movement across the LoC depends on the pain and circumstances they have gone through after separating from their dear ones or the celebrated cultures of oneness.

It is important not to forget that trade and travel through traditional routes –Srinagar-Muzaffarabad and Poonch-Rawalakot –was not just launched but actually restored some six decades after these links got severed due to division of Jammu and Kashmir. But in these six decades the dynamics of conflict have changed so much that restoration

9 Once conflicts escalate for a while, they often reach a stalemate: a situation in which neither side can win, but neither side wants to back down or accept loss either. For more on MHS see <http://www.beyondintractability.org/bi-essay/stalemate>

of links appears incremental gain for all principal stakeholders not really a lasting settlement. In that context all segments of society across both sides

of LoC believe in this trade and travel as essential measure of building confidence for a lasting settlement which is acceptable to all.

## Kashmiri dissidents and militant groups

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In Kashmir Valley the All Parties Hurriyat Conference, the main political force symbolising dissent, is cautiously optimistic about LoC trade and travel. "We have always supported cross-LoC trade to promote confidence building for resolving Kashmir issue", says Mirwaiz Umar Farooq, the chairperson of All Parties Hurriyat Conference (APHC). Contrary to the assertion of fringe elements who dub LoC trade as a tactic to divert attention from the core political issues, Mirwaiz looks at this CBM as an essential support to the peace process. Syed Ali Gilani who heads the hardliner faction of APHC and has also not averse to promotion of cross-LoC cooperation but he wants follow up on the political issues. "After initiation of these steps, dialogue should be held with pro-freedom leadership to resolve the Kashmir issue in its historical perspective", says Gilani. The militant leadership is, however, much critical though not completely opposed. Syed Salahuddin, the chief of United Jihad Council who hails from the Valley but lives in Pakistan, says that the 'cross-LoC trade is a deliberate attempt to weaken the freedom movement in Kashmir'. "Lakhs of Kashmiris had not scarified their lives for the trade", questions Salahuddin. "We are not against trade but the intensity and the clamour about the trade is aimed at diverting the attention of the people from the core issue of Kashmir", he says. It may be mentioned here that barely few months after the launch of cross-LoC travel in 2005 Mirwaiz headed a delegation of APHC to travel to Muzaffarabad and Islamabad through Jehlum Valley road. The visit drew flak from the United Jihad Council and the hardliners in Srinagar, with an unfazed Mirwaiz criticizing the hardliners on

both sides saying: "For fear of being labeled as treacherous should we sit at home and repeat the song of UN resolutions. One lakh people have already lost their lives. Should we wait for the sacrifices of another lakh people before we begin to look at the other possible ways to resolve the issue?"

While all political parties in Azad Kashmir are foremost supporters of the Cross-LoC trade and travel, in Jammu and Kashmir the mainstream<sup>10</sup> political parties compete against each other in claiming credit for getting the LoC softened. Notable among the AJK parties is the Muslim Conference which has long been stressing on swipe card based LoC crossing open to every resident of Jammu and Kashmir on both sides of the divide. In Jammu and Kashmir, the Peoples Democratic Party, which ruled the state when LoC travel was initiated, has the Jhelum Valley Road dotted with billboards on eve of elections to drive home a point that it got Srinagar connected with Muzaffarabad. In its proposal for lasting settlement of Kashmir the People's Democratic Party lists cross-LoC institutional cooperation and common use of Indian and Pakistan currency tenders as way of addressing external dimension of the issue. The National Conference, Jammu and Kashmir's oldest political party, is equally enthusiastic. The competitions of these parties in claiming credits for LoC trade and travel are not the expressions in isolation. These campaigns are in response to the emotional expressions of the people which the parties are eager to take along.

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<sup>10</sup> In context of Jammu and Kashmir the mainstream political parties are those which contest elections and seek to enter offices of power.

## Peace sentiment: What do traders think?

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Even in face of strict security monitoring, cumbersome trade regime and absence of essential infrastructural facilities the traders are more optimistic about cross-LoC trade than one would have imagined. As a part of this study an

opinion poll<sup>11</sup> was conducted with the traders in February 2012 and formally launched in Jammu and Muzaffarabad later in April. A sample of 10 per cent of all the traders engaged in four

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<sup>11</sup> See full report on first ever perception survey with Cross-LoC traders on both sides of LoC in Jammu and Kashmir at [http://www.c-r.org/sites/c-r.org/files/perception\\_survey\\_peacebuilding\\_crossLoC\\_trade201204.pdf](http://www.c-r.org/sites/c-r.org/files/perception_survey_peacebuilding_crossLoC_trade201204.pdf)

trading points on both sides of Line of Control was selected and they were presented with open ended questions. Despite absence of options to chose there was a large similarity of answers which reflected a common approach of traders irrespective of their location and the political atmosphere they live in.

There are 472 traders belonging to ten districts of Kashmir province and two districts of Jammu province registered for trade through Salamabad-Chakhoti sector (also known as Srinagar–Muzaffarabad route) and 165 traders belonging to only three districts of Jammu province and two districts of Kashmir province registered for trade through Chakan-da-Bagh–Tetrinote sector (also known as Poonch–Rawalakot road). On the Pakistani side of Line of Control there are around 2,200 traders but only 600 of them have reported active. Therefore, equal number of sample was selected from both sides<sup>12</sup>.

The survey reveals that at least 6 out of the 10 traders have relatives on the other side of LoC. As many as 62 per cent of the respondents confirmed that they have relatives on the other side and most of them said that their status of being the members of divided families was major basic reason for joining the cross-LoC trade.

Looking at the basic purpose of launching cross-LoC trade, a significant majority of 60 per cent traders think that Confidence Building Measures involving people to people contacts across the Line of Control –travel, trade and tourism etc –can actually help in paving way for the resolution of Kashmir issue. While the traders on Indian side of LoC are still little cautious about the end result of

<sup>12</sup> The number of traders mentioned here was at the time of survey in early 2012

such initiatives but those on the Pakistani side have more overwhelming response.

Even as the infrastructural facilities towards the trade facilitation centres on both sides of LoC have considerably improved over the past three years but the key requirements for any business –access to markets, free travel, communication and banking – are still missing. Despite these critical lacunae and other procedural difficulties, a good number of traders have sustained their interest and many new are joining. Of all the respondents for this survey, 49 per cent have stayed on in the trade despite all difficulties right from inception. Twenty-seven per cent are into it for the last two years while 24 per cent were relatively new to the trade as they joined at different points during last one year.

In a true reflection of diversity of stakeholders in Jammu and Kashmir there is no single factor which became first reason for the traders to come into Cross-LoC trade. However, analysis of individual responses brings about the much obvious results. Unemployment seems to be a major reason for coming to cross-LoC trade but there is also a significant number of traders who claim that supporting the Confidence Building Measures was also major motivation for them. Of all respondents, 36 per cent have said that they saw in cross-LoC trade an avenue of addressing their problem of unemployment. Twenty-five per cent of respondents claim to have made a careful decision in supporting the peace process while for another 19 per cent the cross-LoC trade came to them as an additional source of earning money. Again, these reasons vary across both sides of LoC. An overwhelming 40 per cent of respondents on Pakistani side have listed support to peace process as their first reason while only 10 per cent on the Indian side said so.

## Cross-LoC Trade: Analysis and recommendations

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Ever since India and Pakistan agreed to convert the Line of Control into the Line of Commerce in effect making the LoC meaningless in a “adversarial strategic” sense, efforts, often sporadic and often seemingly directionless, have been made to give effect to this vision. Commerce between the parts of the erstwhile Jammu and Kashmir that are today administered by India and Pakistan, it is hoped will be the precursor to a state of affairs when the Line of Control that divides the state will become “irrelevant.”

For that to occur, the peace dividend that accrues from commerce must be such that cooperation

rather than conflict and confrontation, becomes the preferred option to bring peace to this region. Thus when trade is allowed to occur between India administered JK and Pakistan administered JK, or the terms that are used in this report, LoC East and LoC West, the gains from this trade and the spread of these gains must be such that conflict is not longer an attractive option. As this report argues, the cause and effect of this trade is by no means only economic in nature.

Like negotiations between Indian and Pakistan whose trajectory is often non-linear, the trading arrangements that have been put in place for LoC

East and West do not on the surface seem logical. If integration between the two parts of the erstwhile State of Jammu and Kashmir was indeed the goal of the two negotiating governments, then a number of arrangements could have been considered.

The simplest of these arrangements (and arguably the most logical one) would have been to allow free trade of goods (and possibly services) between LoC East and West provided they are according to a pre-decided Rules of Origin deemed to have been produced in the erstwhile State of Jammu and Kashmir with goods from the rest of India and Pakistan also circulating free of customs duty both in LoC East and LoC West or after the imposition of a common tariff or a tariff set by their respective national governments and levied as Indian goods enter LoC West or Pakistani goods enter LoC East.

Third Party goods to also circulate free of customs duty both in LoC East and LoC West or after the imposition of a common tariff or a tariff set by their respective national governments and levied as Third Party goods imported by India enter LoC West

or Third Party Goods imported by Pakistan enter LoC East.

But for a long time recently this was not how trade between LoC East and West has been structured. The cross-LoC trade as has been practiced till very recently come about, at least in part, because of deep emotional feelings and an inexplicable leap of faith between a set of individuals who made enormously risky investments in spite of the absence of the normal safeguards and institutions that govern trade between nations, and the unreasonably restricted space afforded to traders by a selection of tradable commodities that do not seem to take into account the structures of production and demand on both sides of the LoC.

This has given rise to a structure of trade and traders that will prove to be problematic in the medium run as the coming evolution of the structure of trade and beneficiaries will in all probably exclude the pioneers who invested so much in the face of immeasurable risk and often unhelpful governments.

## The basis of trade: What do LoC East and West have?

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Paul Krugman once remarked “regions trade to take advantage of their differences.” Thus, following this Krugmanian definition LoC East and West would import items that are unavailable or in short supply in their respective regions and export those goods that the other region requires and they produce. Thus an analysis of demand as well as production both in LoC East and West is crucial if one is to make any prediction about the composition and volume of trade that would occur.

### LoC East

If one looks at the sectoral composition of LoC East's economy, it is clear that services today dominate the economy (45.9 per cent) followed by Industry (27.2 per cent) and Agriculture (26.9 per cent) as of 2007-8 where the Gross State Domestic Product of the State stood at Rs 23,000 crores. Growth in the same year was led by Banking and Insurance (9.1 per cent), Construction (12.6 per cent), Manufacturing (11.7 per cent) and Transport, storage and Communication (15.7 per cent) (CII-2009<sup>13</sup>).

Where agriculture is concerned, the state is not self-sufficient in food crops and per hectare yields of crops like rice, wheat and maize are not significantly above the (already low) national average. The same is true for items like, milk, meat and eggs. However,

for a host of horticultural items like apples, walnuts, almonds etc. the state is a net exporter.

Where industry is concerned, a historical legacy of the centre and state governments trying to promote industrial growth as a part of national industrialization strategy or as a means to promote decentralized growth has ensured the existence of an industrial base in the state. This base, which while not as extensive as its southern neighbours i.e. Punjab and Haryana, is not negligible either and is spread across industrial estates in Samba, Kathua, Bari Brahmana (in Jammu Division) and Khanmoh, Shalteng, Rangreth and Lathipora in Kashmir Division. Items varying from cement, construction steel, paints, pharmaceuticals, plastics are manufactured in these estates. Registered data as in the Annual Survey of Industry reveals that 649 factories in the state added net value of over Rs 3,200 crores and employed 45,000 workers.

The numbers with regard to Micro, Small and Medium Enterprises (MSMEs) are more impressive. The number of registered small-scale industries (SSIs) in 2010 was 53,157 employing over 247,000 people. These units include handicrafts such as shawl making, papier-mâche etc. the demand for which in the national and international market is immense.

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<sup>13</sup> Investment Climate- A Study of North Indian States of India, Confederation of Indian Industry, 2009

However, if we concentrate on those units that are listed in the Annual Survey of Industry, it is clear that these were set up in Jammu and Kashmir to take advantage of the subsidies that were on offer on account of the various schemes implemented by the central and the state governments and were meant to serve a larger market. Thus there exists excess capacity that can cater to demand generated by LoC West should such demand make itself felt.

Regarding the pattern of demand generated by LoC East, the demand is largely for food items and fruits where primary goods are concerned and fast moving consumer goods. By and large these are met by the rest of the national economy. A noticeable demand that is generated by the state is the demand for financial instruments which includes participation in the stock market in particular and the financial market in general.

### LoC West

In contrast, the industrial base of LoC West is more modest. Officially, the cumulative investment in industry in LoC West is Pakistani Rs 1,740 crores and employs 10,000 people. However the classification of industry in LoC West is flexible enough to include poultry farms and hotels while other items like bakeries, flour mills and stone crushing units clearly cater to domestic use.

Thus the industrial base of LoC West seems to preclude significant export potential to LoC East or for that matter be able to generate a market for LoC East's products. This is, however, deceptive and cognizance has to be taken of the fact that large

number of people from LoC West have emigrated abroad, viz the UK and the Gulf to better their lives. Their remittances play a very important role in the economy of LoC West.

The importance of remittances can be gauged from the fact that while the population of LoC West is less than 2 per cent of the population of Pakistan, 6.25 per cent of remittances remitted by Non-Resident Pakistanis go to LoC West. Remittances sent by official channels to Pakistan were \$7.8 billion in 2008 which means approximately \$ 500 million was the share of LoC West (Nenova *et al* 2009<sup>14</sup>).

Research on how remittance money is spent in LoC West is revealing. It shows not only have remittances contributed significantly to increase income (25 per cent by some estimates), but also receivers of such remittances spend this money to buy plots, start construction/renovation activities, purchase vehicles and household appliances as well as meet daily expenses, medical bills, school fees and social ceremonies (Khan *et al* 2011<sup>15</sup>).

This means that as market LoC West would be in demand for construction material like cement, construction steel, paint, household appliances etc. LoC East would be ready at least to supply part of the items demanded if such trade was allowed.

14 Nenova, T. C. Niang and A. Ahmad, Bringing Finance to Pakistan's Poor: A Study on Access to Finance for the Underserved and Small Enterprises, World Bank 2009

15 Khan, H.M.Israr, M.Summar, S.N.Shaukat, M.Khan, Abdulmanan, N. Ahmad and R. Karim, Impact Of Remittances on the Socio-Economic Conditions of Rural Families in District Poonch of Azad Jammu and Kashmir, Sarhad Journal of Agriculture Vol.27, No.4, 2011

## The potential consequences of a single market

What would happen if the State of Jammu and Kashmir were to be a single market in the sense that goods produced in LoC East and West could be freely exchanged?

It is clear that in such a scenario, given the structures of production and demand, the balance of trade would largely be in favour of LoC East. This is because as already stated, given the sustained support to industry via the various industrial promotion policies financed and administered by both the state and central governments, there are several industrial hubs both in Jammu and Kashmir. In comparison, LoC West's industrial presence is far more modest. But LoC West is an impressive market because of a large expatriate population that is divided between the UK and the Gulf States. The remittances sent by these expatriates are considerable given the population of

LoC West and manifests itself in the construction of often palatial homes.

Thus there would be considerable demand for construction material e.g. cement, construction steel, paint etc. which are produced in LoC East. In contrast there are few items that would be made in LoC West that would be demanded in LoC East.

This asymmetry does not mean that LoC West will lose because the items that would be imported are not made in that region. They are either imported from "mainland" Pakistan or from abroad. Similarly consumption items like plastic items are manufactured in LoC East. These too could be exported to LoC West.

The consequence of this trade would be to benefit the consumer in LoC West and industrialists in LoC East. It is likely that industrialists would directly take

charge of their marketing rather than use locals who reside near the LoC or deal directly with established traders located in the urban areas of LoC West.

However, the consequences of a more open trade regime in particular and a more open market regime are often unpredictable in favourable ways. Entrepreneurial ingenuity in ferreting out unstated human desires can have unexpected consequences and may result in new products and services that may have either a local or a more universal appeal.

This, however, cannot be calculated *a priori*. It is likely that the MSMEs would play a larger role in this trade given their small size and flexibility.

What can be calculated is likely to reveal that the “metropolitan areas” of the region will gain more than those who live near the LoC. This may not be a “fair” outcome to those who commenced this trade at no small risk to the huge sums of money they invested, but it is an outcome that cannot be ruled out.

## Analysing volume of trade and goods traded

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The Reality of Cross-LoC Trade as it commenced and progressed until very recently was of course substantially different. While India and Pakistan did single out that out of the 72 Confidence Building Measures (CBM), Trade and Travel across the LoC as a key element of the Confidence Building Measures between India and Pakistan, the manner in which this would be operationalised was unconventional.

The Volume of cross LoC trade (the sum of trade in the sectors) has generally been on the upward trend growing from approximately 138 crores Indian in 2009–10 to 315 crores in 2011–12 (one way trade). If calculated in terms of per annual percentage growth, such growth would look spectacular but it must be remembered that the original base trade itself was low to nonexistent. The choice of goods traded, however, reveals the real premise of this trade. For LoC East, the main items exported are items like onions and various kinds of spices and coconuts none of which is produced in LoC East. Similarly, amongs the items imported, dry fruits and carpets dominate which again are produced in other parts of Pakistan. Another item which had a significant presence before authorities banned its trade was *mungi* (a local popular kind of pulse) which again must have been brought in for trade from outside LoC West. Given below are two tables that show the volume of cross-LoC Trade through both crossing points, i.e. Salamabad-Uri as well as the Chakkan-da-Bagh-Poonch.

In addition the volume of trade, given the narrow local market, also indicates that cross-LoC trade is actually India-Pakistan trade through Jammu and Kashmir.

Clearly, while borders are being rendered “meaningless,” the economies of LoC East and LoC West are not being integrated, which was the main motive behind promoting cross-LoC trade. The beneficiaries clearly apart from local businessmen who handle this trade are clearly producers of these products who are residents of either LoC East

or LoC West. There is, however, one silver lining in this entire process and that is the creation of a new class of businessmen who have come to their own as a result of this trade and this has much to do with the process of cross-LoC trade itself. However, there are signs that this cross-LoC trade has now reached a plateau. This on account the governments of India and Pakistan cracking down of the items that were being traded but were not on the list. At the same time list has not yet expanded to include all the items that are produced in the erstwhile princely State of Jammu and Kashmir. This is hardly surprising and is a development that would have occurred either as a result of administrative action or through natural processes when traders would seek out more “rational” routes to export their wares to the main Indian and Pakistani markets which are and would remain the final destination of goods that today are traded across the LoC Cross-LoC and trade: The process<sup>16</sup>

The process of trade that prevailed till July 2012, as described in detail by Kira (2011), was a complicated and a time-consuming one (see Appendix III) and can be understood with the help of the flow chart below: While total trade is a more simplified process (See Appendix IV), the initial conditions that existed it can be argued is largely instrumental in deciding which of the traders are still in business today.

### The consequence of opaqueness

The initial complicated nature of trade served to make trade opaque and is restrictive in nature. The consequence of this opaqueness and restrictive nature of trade was that it kept out the more established business of Jammu and Srinagar from this trade. After all seen in a rational manner (in the classical profit maximizing businessman’s viewpoint), venturing into cross-LoC trade was not an attractive proposition given other alternatives.

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<sup>16</sup> Kira, A.H. *Cross LoC Trade in Kashmir: From Line of Control to Line of Commerce*, Working Paper Number 2011/020, Indira Gandhi Institute of Development Research, Mumbai

This space was thus given to other smaller businessmen for whom the trouble such a trade

regime would entail would be worth it given their potential alternatives.

Year	Export to AJK			Import from AJK		
	No. of trucks	Quantity in qtls.	Value in crores (Ind. Rs)	No. of trucks	Quantity in qtls.	Value in crores (Pak. Rs)
2008-09	180	3987.31	1.3625	219	7293.39	-
2009-10	1830	119004.75	71.8046	2662	193221.06	92.4149
2010-11	3650	247235.20	156.4756	2413	159907.58	260.4339
2011-12	4406	350079.81	244.3543	2960	201376.71	407.7228
2012-13 (Ending 01/2013)	6070	498081.77	275.5556	2880	200186.43	456.3789
<b>Total</b>	<b>16136</b>	<b>1218388</b>	<b>749.55</b>	<b>11134</b>	<b>761985</b>	<b>1216.95</b>

TABLE 1: Trade Facilitation Centre, Salamabad, Uri

Year	Export to AJK			Import from AJK		
	No. of trucks	Quantity in qtls	Value in crores (Indian currency)	No. of trucks	Quantity in qtls	Value in crores (Pakistan currency)
2008-09	42	1534.76	0.39	23	185.50	0.6066
2009-10	1492	142921.76	67.17	1560	59196.53	127.0719
2010-11	1836	133443.72	88.76	1626	113377.36	171.3454
2011-12	2020	115192.60	75.83	1255	167158.46	123.5179
2012-13 ending 11/2012	969	94011.52	33.7282	591	462979.65	58.4878
<b>Total</b>	<b>6359</b>	<b>487104</b>	<b>265.9</b>	<b>5055</b>	<b>802897</b>	<b>481</b>

TABLE 2: Trade Facilitation Centre, Chakkan-da-Bagh oonch

In addition, emotional attachment to the other part of the LoC also played a major role. It is not easy to justify the risks taken in the absence of a proper dispute settlement mechanism if the business partner on the other side of the LoC decided to renege on a deal. Thus businessmen located close to the LoC became pioneers not because they were the best suited, but because they were the most eager. However as enquiries reveal, the proportion of first-timers is also significant which meant that for some this virgin area offered an opportunity to join the ranks of businessmen in the state.

By operating in conditions that were opaque and restrictive they were able to gauge demand conditions on the other side and over time started to fulfill that demand. Interestingly, the structure of demand did not always conform to the list of allowable items and yet these were supplied, an act involving great risk and courage, given that the consequences could have left to seizure of goods without compensation. Thus some local businessmen prospered from this trade. The ones who survived, it appears are the ones who were able to find a market on the other side of the LoC. This given the fact that most participants had

relatives on the other side was not surprising. The condition of barter which meant an artificial balancing of trade ensured that this benefit was prematurely capped. Its effect on the rest of both sides of LoC must have been strictly limited as the bulk of these goods outside Jammu and Kashmir, on both sides of the divide. Thus it is not surprising that participants have asked for the liberalization of this trade to include banking facilities and consider barter trade to be a hindrance. It is also not surprising that most traders want the inclusion of items that are produced anywhere in India and the Indian side or more precisely the state government of Jammu and Kashmir has proposed certain measures in this regard. From their perspective, this is understandable as trade across the LoC as controlled by them implies that an increase in item coverage will lead to rise in volumes traded and thus profits. Indeed, for those who have persevered have witnessed that this trade has grown steadily and continuously. It is now known among traders that issues of trusting their partners depend on the choice of partners and using their relatives across the LoC they have tackled this problem. Therefore, most traders have made money from cross-LoC trade notwithstanding the inconvenience

of barter trade with the added task of converting goods received in lieu of payment into cash. Additionally, the fact that traders divided by the

LoC and deprived of the most rudimentary forms of communication have managed to evolve a dispute settlement mechanism is remarkable.

## Business sentiment: What do traders think?

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A survey of the traders dealing in the cross-LoC trade carried out jointly by Indus Research Foundation (IRF) and Centre for Peace, Development and Reforms (CPDR) for the present study reveal how they look at cross-LoC trade in its entirety. It is interesting to note that more than 50 per cent of the trade taking place in these areas is between the relatives but hardly surprising as this is the only way to create an atmosphere of certainty in a very uncertain market.

Traders on the Indian side admitted that several traders on the other side are seeing the opening of cross-LoC trade as an opportunity to have a comfortable life as nearly 65 per cent have said that the future of the trade is bright and are in favor of it to be continued. It is important to note here that since this trade is based on a system of barter, traders have more reasons to feel comfortable trading with their relatives rather than with a faceless trader whom they have not met, as it involves risk.

It is also seen that the traders have generally earned profits from the barter system (85 per cent of the respondents) but they do admit that the process of barter trade is a long, lengthy and a hectic process to convert goods into cash and therefore demand a proper banking system to realize cash from the trade as soon as possible because barter trade actually diminishes their working capital or the cash that they have for the business process as according to the traders the conversion takes anywhere from 20 days to few months. In other words realisation of cash is the need of the hour for the traders. There are several difficulties in the process of conducting this duty-free trade. The TFO pointed to the need for better infrastructure at the TFC for storing of goods as these are not insured. Also, the process of offloading and reloading for screening causes damage especially to fresh fruits whose value depreciates greatly.

The traders felt there should be a bigger scanning machine that can scan the entire truck without offloading, as reflected by the 57 per cent responses about the facilities provided at the TFC being unsatisfactory.

Since this is mainly barter trade, the value of commodities exchanged is hard to determine and businessmen on both sides have difficulties in

settling their accounts as already mentioned the quality of goods delivered from the LoC West mainly depend upon the trading party and if its relatives the element of risk is diminished with 38 per cent respondents voicing this concern although 44 per cent were satisfied with the goods that they receive.

Also, limiting the trade to 21 items is seen as stifling the potential for trade in other items. It is interesting to see that all the respondents are in favour of redrafting the list of the item for trade and they also want that the list should not be limited to the state of Jammu and Kashmir but the trade items so included should be from the other parts of the country. As it was seen that the goods that were traded also included items like coconut, cardamom, banana, pineapple among others items.

Although the trade with its own issues and teething problems has provided the traders from the both sides an opportunity to grow and expand business in to new markets as mentioned by the traders in their responses that they were able to find new markets with this trade (92 per cent) and are able to project profits due to this trade (82 per cent) and 85 per cent of the traders are able to realize the money that they have invested in the trade.

Another good sign was that 62 per cent of the traders are those who are associated with the trade since the beginning meaning that the trade has actually provided them with the sufficient returns to remain associated with this trade.

The profits made by traders may actually be quantified. Presently, the average value of goods being exchanged over the LoC (or two way trade) in the Poonch-Rawalakot sector alone varies from Indian 6- 8 crores *per week* or roughly Rs 350 crores *per annum*. If this is assumed to be equally shared by the registered traders in this sector, it translates to a turnover over Rs 2 crores *per annum per trader*. For any reasonable rate of return, the profits earned would be considerable. Even if we now do away with the unrealistic assumption of cross-LoC trade being shared equally by all traders, the fact remains and which is confirmed by the traders surveyed that this trade is a lucrative one.

The traders are now looking at the various improvements that can be brought into the existing structure so that the ending result of the

trade is beneficial for everyone involved. The few suggestions that were given by the traders are:

- The holding of Trade Awareness Programs
- Increase in Items List (Traded items)
- Good Indo-Pak Relationship
- Ease of Access in LoC (Especially for Traders)
- Common Banking / Sale - purchase system

But the future of cross LoC trade may not be as they think.

### The possible consequences of trade 'regularisation'

As cross-LoC trade becomes "regularised" in the sense that banking facilities, the removal of barter, the inclusion of more items that are produced anywhere on either side of the divide in Jammu and Kashmir becomes part of the list of tradable items become part of the process of going forward coupled with exclusion of those items that are not produced in Jammu and Kashmir (East and West), it is clear that more people from the state will benefit

from this trade but they will be located in the main commercial sectors in Jammu and Kashmir.

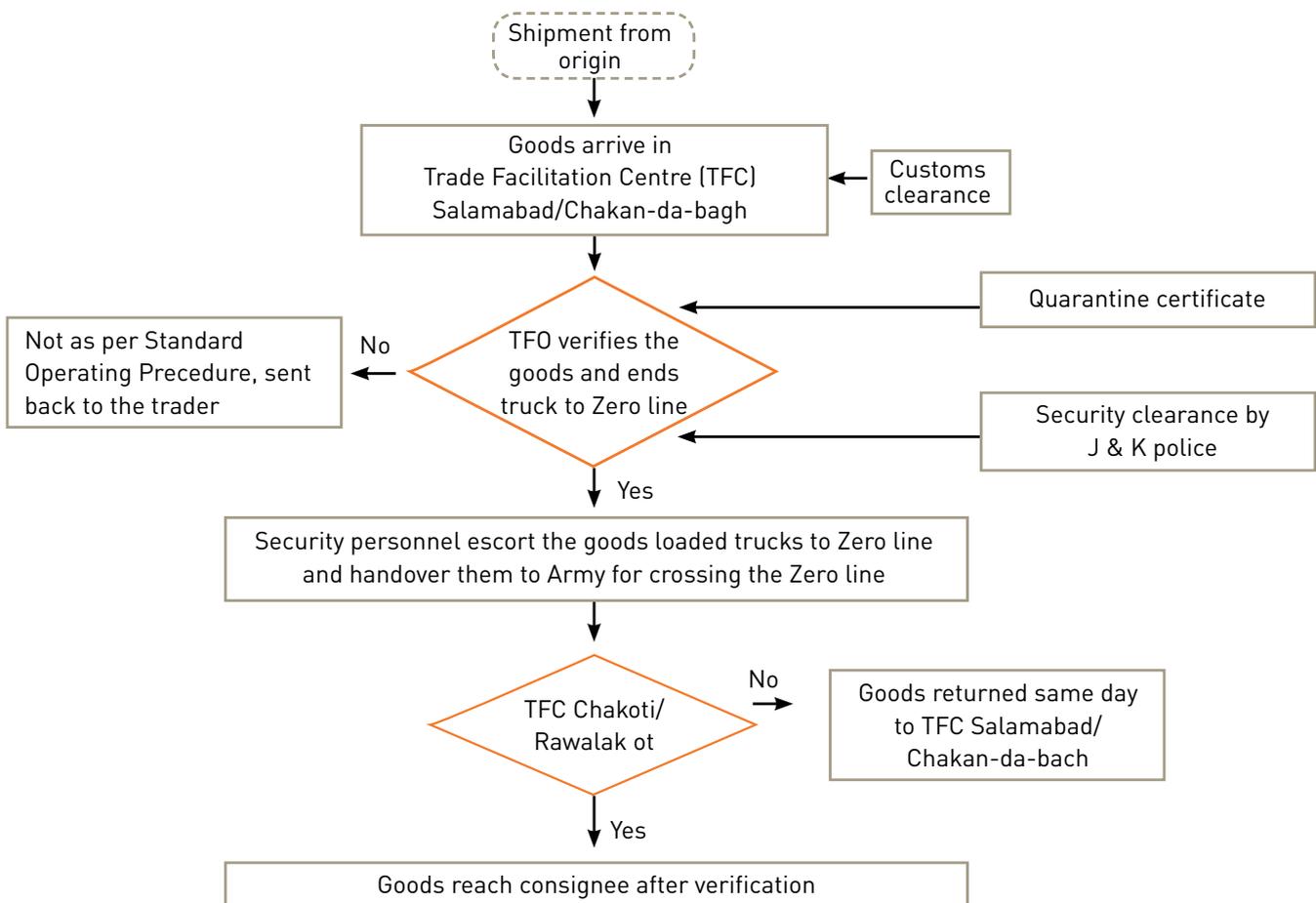
There is no reason to argue that the pioneers will lose out, but a change in strategy will be necessary for them to take advantage of the increasing and perhaps inevitable liberalization of cross-LoC Trade.

The advantages that traders near the LoC possess are flexibility (due to relatively smaller size) and better knowledge of local demand conditions. Thus local traders will have to trade in a spectrum of items that will find takers across the LoC but where no single item has that critical size where the producer finds it economic to deal with a distributor in LoC West.

### Jammu and Kashmir: A Common Market for Trade and Investment

It may be argued that the drive to make borders porous and to convert the Line of Control into a Line of Commerce has largely been pushed by India. As the two countries near this goal, consistency demands that the next logical step,

### Cross-LoC Flow



Source: Kira, *Cross-LoC trade in Kashmir: From Line of Control to Line of Commerce*. 2011

the free flow of investment between LoC East and LoC West, should follow. This will be a more evenly contested affair, if trade and investment flows be called as such. In contrast to non-resident Indians the bulk of whom are professionals, the emigrants who trace their origins from LoC West boast of quite a few businessmen who have made their fortunes in hospitality and tourism. This complements the needs of Jammu and Kashmir, where tourism is important but where the sector is need of investment and a good degree of professionalism.

Such a step would bring in an important and vocal stakeholder, that is the emigrant from LoC West and integrate him with the peace process. By giving him stakes in cross-LoC commerce a very

important constituency would be brought on to the path of peace.

From this to a freer flow of natural persons between LoC East and LoC West for tourism, education, business and personal persons is the next logical step. It is only then that borders would be rendered meaningless.

However, sequencing of steps is important as is follow-up action. Flows of investment build an obvious bond- the recipient witnesses an increase in output due to this investment while the investor has a vested interest to see that the location of his investment is free of turmoil. This mutual interdependence if spread sufficiently wide and with sufficient stakeholders builds up a considerable constituency for peace.

## Summary and conclusion

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The economics of trade has its own logic and dynamic: it cannot be ordered to benefit whoever policy makers should think should be benefitted. However, traders who have risked fortunes to be trail blazers in a trade regime filled with opacity and obstacles can also be expected to discover new avenues and opportunities for profit. Given their proximity to the other market and the cultural and linguistic affinity that they possess the process of discovery and even the creation of new markets is a likely outcome of the process forward. Eventually as the transformation of the Line of Control to the Line of Commerce starts to include investment as

well as the movement of permanent residents of JK State, these gains will increase even more.

But the aim of cross-LoC Trade is more than to benefit people who live on the LoC; it is to cement the two sides of what was once a single administrative entity and in the case of Jammu region what was once a single socio-economic-cultural unit into one unit again. In the run up to that goal, violence to resolve the case of Jammu and Kashmir remains no longer an acceptable or viable option.

## Appendix I

### Agreed Outcomes of the Meeting of India-Pakistan Working Group on Cross LoC CBMs, held on 18 July 2008 in Islamabad

- Triple entry permits will be introduced with effect from 1 October 2008. A separate form for this purpose has been agreed upon. All three entries are to be made from the same crossing point. This facility will be automatically available to senior citizens and accompanying spouses.
- Regional Passport Officer, Jammu and Deputy Commissioner Rawalakot would be the respective designated authorities for the Poonch–Rawalakot bus service with effect from 1 October 2008.
- Monthly coordination meetings between the designated authorities will be held, with the provision to convene urgent meetings whenever required.
- Crossings will stand enhanced to 60 persons per crossing.
- Steps to be taken to reduce processing time for applications on both sides.
- The operation of the Tithwal–Chiliana crossing point will be effective from May to November of every year, in view of the accessibility problems in the winter.
- Crossing on Uri–Hajipir will be facilitated.
- The Designated Authorities will start exchanging application forms by e-mail from 1<sup>st</sup> October 2008. E-mail transfer will be backed up by hard copies.
- In cases of emergencies (death of close relatives across LoC), clearances to be processed within a week. Stay in such cases will be for up to 7 days. This will be effective from 1<sup>st</sup> October 2008.
- Frequency of Srinagar–Muzaffarabad and Poonch–Rawalakot bus services will be increased from fortnightly to weekly with effect from 21 August 2008 and 25 August 2008 respectively.
- Designated Authorities will reconcile data regarding crossings regularly.

### Cross-LoC Trade

- List of commodities to be traded with zero tariff regime were exchanged. To begin implementation, each side will indicate the items that they are willing to receive.
- The visit of Chambers of Commerce from both sides of LoC will take place as early as possible to make recommendations on modalities of trade.

Source: Ministry of External Affairs, India

## Appendix II

### Standard Operating Procedures for Cross LoC Trade, current July 2012

Trade across the LoC is restricted to 21 items. These are the products produced on both sides of the LoC. Trucks with valid papers are allowed to enter. The process is computerized and single-entry permits known as Truck Entry Permits are issued in triplicate by the respective Trade Facilitation Officers (TFOs). The drivers are given entry permission after a thorough checking of their background. The permits contain a photo ID of the driver, his name, address, license number and details of the vehicle. It also specifies that there is no contraband or dangerous material in the vehicle or in the consignment. For the purposes of ready indentifiability, the drivers of these trucks are made to wear bright yellow and pink jackets/ vests with “Driver-Chakoti/Rawalakot” and “Driver Salamabad/Chakandabagh” respectively inscribed on the back. They are permitted till the designated points where they offload their trucks. The same drivers are not allowed frequently. Once the trucks enter, they have to return the same day after offloading.

The trucks are allowed to carry a capacity of 1 to 1.5 tonnes. The cargoes are sealed by the TFO. The signatures and seals of the TFOs are exchanged by both sides. The cargo has to clearly indicate the items being carried, the particulars of the consignor(s) and the consignee(s) and the packing list with marks and numbers, which has to accompany the consignment. A copy of the invoice raised by the exporter has to be carried and both these documents are to be attested and sealed by the TFO. The two countries have taken appropriate security steps to facilitate cross-LoC trade. Keeping the security concerns in mind, the truck movements are allowed on four days a week, both on the Srinagar-Muzaffarabad and the Poonch-Rawalakot routes, between 0900 hrs and 1600 hrs. As per the modalities finalized by the two countries, there would be a regular review of the flow of trade, a list of items and the modalities on a quarterly basis by the TFOs. However, the first review is to be carried on by the Working Group on Cross-LoC CBMs, and on an annual basis thereafter.

To ensure that there is no breach in security during the process of trading, the registered drivers from both the sides are verified at the time of departure and arrival. The drivers are only allowed entry up to the respective Trade Facilitation Centres (TFCs) – on the Indian side and on the Pakistani side – where the goods are loaded and offloaded. Once the

goods are received, they are screened electronically at the TFC warehouse. The Custodian who is the overall in-charge of the TFC is responsible for the registration of traders who are sending their goods and ensures that the items traded are part of the list.

The documents that are submitted to the Pakistani side and vice-versa, are:

1. Cargo manifests duly certified
2. Truck entry permits of the vehicles
3. Plant health certification
4. Security certificates
5. Invoices

As per the agreed modalities (SOP), the cargo passes the Line of Control at Kaman Post (Uri) and Chakan-da-Bagh (Poonch) after being cleared by TFC, Salamabad or Chakan-da-bagh respectively. The movement of vehicles carrying goods on the two routes is allowed on Tuesday and Wednesday between 0900 hours and 1600 hours every week. The two days have now been extended to four days a week as per the agreement between Pakistan and India in July 2011.

The process is also comprised of the following formalities to be done for the purpose of import and export:

#### **The Trading-Out of goods (Outward Clearance of Cargo):**

The exporter of goods applies to the Custodian, whose function is presently being handled by General Manager District Industries Centre Baramulla/Poonch for issuance of 'Truck Entry Permit' (TEP). The custodian forwards the application to the designated officer of Jammu and Kashmir Police to verify the antecedents of the exporter, which then issues TEP to the applicant in triplicate. On receiving the TEP, the goods are shipped to TFC Salamabad or Chakkan-da-Bagh as applicable one day prior to the trade day. The exporter hands over TEP along with the invoice copies to the respective Custodian. The transport operator or his authorized representative presents himself before the Trade Facilitation Officer (TFO) at TFC along with the empty truck and after getting security clearance on the day of dispatch of goods undertakes rummaging. The Custodian then presents the cargo for inspection and examination of TFO who verifies that the goods contained in the truck are as per the approved list of items. The TFO subjects the cargo to X-Ray scanning or physical examination to ascertain that the shipment contains the permitted goods. Any goods not found

under the approved list of items are not allowed to be loaded in the vehicle. The consignments of plant/plant products are issued a plant health certificate by the designated quarantine officer, which is attached with the cargo manifest. The stuffing of cargo is done in presence of TFO and on completion of the stuffing the trucks are sealed by the TFO with a onetime tamper-proof bottle seal or lead seal. The transporter or his authorized representative submits cargo manifest (in duplicate) to the TFO. The manifest is certified by TFO in the manner specified in the manifest after cross verifying with the invoice copies and based on the physical examination already conducted. The TFO mentions the bottle seal/lead seal number on the manifest. After conducting the verification checks, the Jammu and Kashmir police certify that no contraband or dangerous material is in the vehicle or consignment. The certificate is attached with the cargo manifest on being shipped to the crossing point for shipment. The truck or the vehicle carrying the goods then commences movement under escort of the security agency to Chakoti or Rawalakot on the other PaK side of Line of Control.

#### **The Trading-In process (Inward Clearance of Cargo):**

Each vehicle driver who crosses the Line of Control points from PAJK carries a 'Truck Entry Permit' in triplicate that contains the picture identity, name, address, license number, details of the vehicle and a certification that there is no contraband or dangerous material in the vehicle or consignment. A Cargo Manifest (CM) is also carried by the driver entering the Line of Control. The immigration officers at Kaman Post and Chakan-da-bagh check the TEP and keep record of the entry and exit of the driver. At the time of entry, the driver hands over one copy of TEP to the immigration officer, the second copy to the Trade Facilitation Officer and the third copy is stamped 'Exit', when the driver leaves the LoC. The plant and plant products consignments are accompanied by a 'plant health certificate', which are inspected for pests, weeds and disease by the quarantine officials on arrival.

#### **Security clearance:**

The preliminary screening of documents of the cargo and inspection of trucks is done at the crossing points of Kaman Post and Chakan-da-bagh. The officials of Jammu and Kashmir police inspect the seal of the incoming vehicles and after carrying visual inspection escort the vehicles in a convoy to TFCs Salamabad in Uri and Chakkan-da-bagh in Poonch.

## The Processes at the Trade Facilitation Centre:

On reaching TFC, the custodian arranges for unloading of the goods after verification of the seal and cargo manifest. The TFO verifies the cargo manifest along with related invoice copies and checks as to whether the goods declared in cargo manifest are under the permitted list of items. The goods are then examined by J&K police officials from security angle before being sent to the warehouses for rummaging. The copy of cargo manifest and invoices covering the cargo are retained by the TFO and after unloading the trucks are allowed to return on the same day. The consignment of plants/plant products is issued a 'plant health certificate' after inspection by the designated plant quarantine officer and on finding it free from pests, the consignment is released. However, if any live infestation is found, the consignment is rejected and sent back. The consignments are subjected to x-ray scanning and physical verification and if goods are found to be outside the list of 21 items, the same are returned in the vehicle that brought them.

## Appendix III

### Cross-LoC Trade: Banking Mechanism proposed by Jammu and Kashmir Government and unveiled on October 4, 2012

"It is envisaged that the commercial banks in J&K and PoK would provide a facility to their respective exporters to realize their dues by opening a Trade Facilitation Account at their end. The Initial debit and final credit by the exporters' bank would be through the facilitation account. The exporter would be paid only after the Importer has paid his bank treating the transaction akin to payment of bills on collection basis.

Fifteen days have been provided for the settlement cycle. Ten days has been set aside for the transaction to be completed by the importer. However, an extra five days have been included on the understanding that banks would periodically settle amongst each other through the respective NOSTRO accounts. The exporter could also be given immediate credit on day one based on their banker's level of comfort with the party subject to the terms and conditions prescribed by the bank. Flow charts showing the mechanism, process flows and accounting process to be followed on collection/credit basis for exports from PoK / exports from J&K are enclosed in Annex I.

i) The outstanding entry in the Trade Facilitation Account would be reversed once the amount is received from the bank of the importer.

ii) The cross rate of INR/PKR would be arrived by using market determined US\$/INR and US\$/PKR rates. This rate would be applied for sale/purchase of INR against PKR and would be a pure commercial decision taken by the banks.

iii) Both the Reserve Bank of India and the State Bank of Pakistan would not be involved in the process of trade settlement and would not bear the exchange rate risk in part or in entirety. Both the central banks with the explicit permission from their respective governments would however need to grant permission to their commercial banks to undertake transactions under the, proposed scheme.

iv) The invoice will be denominated In Indian Rupees (INR) irrespective of the direction of trade.

v) The final settlement of trade between the commercial banks would be in a mutually accepted international currency, say US Dollar.

vi) Since the exchange risk is arising out of a commercial transaction, the exchange risk would necessarily be borne by the importer. This would be collected as a "Facilitation Fees". Such fee would also cover the exchange risk (up to final settlement), transaction costs, handling costs, etc. The fee could be a percentage of the cost of goods and should be added to the invoice i.e. invoice = cost of goods + facilitation fee.

vii) The model does not envisage any form of subsidy from either J&K Govt. /Bank or the Government of India.

#### 2. Requirements for operational sing the model

a) J&K Bank needs to be given permission by GOI/ RBI to establish banking arrangements with banks in PoK.

b) J & K Bank should scrupulously adhere to the KYC guidelines issued by RBI for its exporters, importers, and the correspondent banks it would deal with in PoK. This would be verified by the RBI during its usual inspection/periodic scrutinies.

c) Any markup on exchange rate in the form of facilitation fee, processing charges, exchange risk, etc is a matter of negotiation between two commercial banks to cover their operational cost and offering protection to their customers. Facilitation fee as a percentage of cost of goods, as suggested in the mechanism, is by way of an example only. The credit extended by J&K Bank Ltd should be subject to the extant interest rate guidelines including that of base rate (in case immediate credit is afforded to the exporter/delay in settlement).

d) Eligibility of goods for trade would be as per the list issued by the GOI.

e) At the border, an effective mechanism for clearing goods and transmitting the information to respective commercial banks is a must. Both the banks can visit LoC/clearing points for familiarization with the mechanism in consultation with the respective authorities manning those points.

f) Net settlement by banks in both the sides need to be decided as to its periodicity and the currency of settlement. Since the final trade settlement is with a bank or Pakistan, under normal circumstances, adherence to existing provisions of ACU mechanism would have to be ensured.

Since these transactions are denominated in local currency, they would fall outside the ACU mechanism. Therefore, it would require special permission to route such settlement outside the ACU mechanism with banks of Pakistan. Such a special arrangement would tantamount to trade with Pakistan though it is in effect with PoK which is deemed to be an Indian territory.

However, keeping in view the decision taken by the Government /MHA for a special arrangement independent of the sovereignty related issue, the above proposal is being made.

In this connection, a reference is invited to para (e) of page 7 of 21 of F No 17/5/2009-BOA; MOF (Dept of Financial Services), GOI letter dated January 18 2010. MHA have vide their letter 6 October, 2010 to the MoF, DFS with a copy to RBI have advised that once a bankable proposition is finalized the formalities of getting approval is best left to the MEA and have requested the DFS to submit their proposal/plan for financial mechanism for conduct of cross LoC trade to MHA for taking up further with the Government of Pakistan through MEA.”

## Glossary

<b>AJK</b>	Azad Jammu Kashmir
<b>APHC</b>	All Parties Hurriyat Conference
<b>CBM</b>	Confidence Building Measures
<b>CPDR</b>	Centre for Peace, Development and Reforms
<b>IaK</b>	India administered Pakistan
<b>IRF</b>	Indus Research Foundation
<b>J&amp;K</b>	Jammu & Kashmir
<b>LoC</b>	Line of Control
<b>MSME</b>	Micro, Small and Medium Enterprises
<b>PaK</b>	Pakistan administered Kashmir
<b>SSI</b>	Small-scale industries
<b>TEP</b>	Truck Entry Permit
<b>TFC</b>	Trade Facilitation Centres
<b>TFO</b>	Trade Facilitation Officers



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