

# ECONOMIC INTEGRATION: SAARC AND BEYOND

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I hereby declare that the data presented in this Dissertation report entitled, "**Economic Integration: SAARC and Beyond**" is based on the results of investigations carried out by me in the International Studies at the School of International and Area Studies, Goa University under the Supervision of Mr Yugank Naik and the same has not been submitted elsewhere for the award of a degree or diploma by me. Further, I understand that Goa University or its authorities will be not be responsible for the correctness of observations / experimental or other findings given the dissertation.

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This is to certify that the dissertation report “**Economic Integration: SAARC and Beyond**” is a bonafide work carried out by Ms Umesha Binari Thalagahawatta under my supervision in partial fulfilment of the requirements for the award of the degree of Masters in Arts in the Discipline International Studies at the School of International and Area Studies, Goa University.



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## **PREFACE**

Regional economic integration is extremely important in this fast-paced era of globalization. In the setting of South Asia, where diverse cultures and economies collide, pursuing economic cooperation is both a difficulty and an opportunity. In particular, the significance of the South Asian Association for Regional Cooperation (SAARC) is emphasized as this research attempts to investigate the complex terrain of economic integration within South Asia. This research attempts to clarify the difficulties of promoting economic cooperation in the face of geopolitical conflicts, infrastructure deficiencies, and bureaucratic barriers by carefully examining SAARC's initiatives, difficulties, and accomplishments.

Through an exploration of the complexities surrounding intra-regional trade, investment dynamics, and regulatory frameworks, this study seeks to provide significant insights and suggestions for enhancing SAARC's role in promoting fair and enduring progress throughout the region. This study will deepen the understanding of the advantages and disadvantages of economic integration in South Asia, ultimately paving the way to a more prosperous and connected future.

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**ABBREVIATIONS USED**

<b>Entity</b>	<b>Abbreviation</b>
ASEAN Currency Unit	ACU
ASEAN Economic Community	AEC
ASEAN Industrial Projects	AIP
ASEAN Trade in Goods Agreement	ATIGA
ASEAN–China Free Trade Area	ACFTA
Asian Development Bank	ADB
Asian Free Trade Area	AFTA
Asian Infrastructure Investment Bank	AIIB
Asia-Pacific Trade Agreement	APTA
Association of South East Asian Nations	ASEAN
Association of Southeast Asia	ASA
Bangladesh-Bhutan-India-Nepal Initiative	BBIN
Bangladesh-China-India-Myanmar Economic Corridor	BCIM-EC
Bay of Bengal	BoB
Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation	BIMSTEC
Belt and Road Initiative	BRI
China Communications Construction Company	CCCC
China Harbor Engineering Company	CHEC
China-Pakistan Economic Corridor	CPEC
Common Effective Preferential Tariff	CEPT
Economic Cooperation Organization	ECO
Electronic Data Interchange	EDI
Enterprises for ASEAN Initiative	EAI
European Economic Community	EEC
European Monetary System	EMS
European Union	EU
Export Processing Zone	EPZ
Federation of Indian Chambers of Commerce and Industry	FICCI
Financial Year	FY
Foreign Direct Investment	FDI
Free Trade Agreements	FTA
General Agreement on Tariffs and Trade	GATT
Gross Domestic Product	GDP
Group of Eminent Persons	GEP
Hanoi Plan of Action	HPA
Inter-Governmental Group	IGG
International Maritime Organization	IMO
International Monetary Fund	IMF
International Ship and Port Security Code	ISPS
Least Developed Countries	LDC
Liberation Tigers of Tamil Eelam	LTTE
Logistics Performance Index	LPI
Most Favoured Nation	MFN

Natural Economic Territories	NET
Non -Tariff Barriers	NTB
North American Free Trade Agreement	NAFTA
Pakistan occupied Kashmir	PoK
People's Republic of China	PRC
Preferential Trade Agreement	PTA
Quantitative Restrictions	QR
Regional Cooperation Arrangement	RCA
Regional Trade Agreement	RTA
Research and Information System	RIS
Residue Monitoring Plan	RMP
Rules of Origin	RoO
SAARC Agreement on Trade in Services	SATIS
SAARC Chamber of Commerce and Industry	SCCI
SAARC Development Fund	SDF
SAARC Preferential Trade Arrangement	SAPTA
SAARC Regional Multimodal Transport Study	SRMTS
SAFTA Ministerial Council	SMC
Sanitary and Phyto Sanitary	SPS
Singapore–Johor–Riau	SIJORI
Small and Medium-sized Enterprises	SME
South Asia Comprehensive Economic Partnership	SACEP
South Asia Subregional Economic Cooperation	SASEC
South Asian Association for Regional Cooperation	SAARC
South Asian Cooperation Fund	SACF
South Asian Currency Unit	SACU
South Asian Economic Union	SAEU
South Asian Free Trade Area	SAFTA
South Asian Monetary System	SAMS
South East Asia	SEA
Special Coordinating Committee of ASEAN Nations	SCCAN
Special Economic Zones	SEZ
State-Owned Enterprises	SOE
Sustainable Development Goals	SDG
Tariff Barriers	TB
Tariff Liberalization Programme	TLP
Technical Barriers to Trade	TBT
Trade Negotiating Committee	TNC
World Trade Organization	WTO

## **ABSTRACT**

The South Asian Association for Regional Cooperation (SAARC) facilitates economic integration within South Asia. The research explores the principles of this integration. It evaluates the effects of SAARC's developmental projects and trade agreements, including SAFTA and SAPTA, on regional economic cooperation. According to the study, the primary challenges to integration include uneven development, bureaucratic barriers, and political conflicts. It assesses SAARC's effectiveness in comparison to ASEAN through historical, statistical, and comparative analysis and suggests ways for further economic integration. Observation of this research support the significance of political collaboration by showing a relationship between lower political tensions and more intra-regional trade. The study also emphasizes the possible advantages of improved resource exchange and connectivity within a reconstituted SAARC framework. In order to realize South Asia's economic potential and promote economic integration, recommendations highlight the necessity of political will, institutional strengthening, and international cooperation.

***Keywords:*** SAARC, South Asia, Economic integration, India, Regional Organizations

## **CHAPTER 1**

# **INTRODUCTION TO ECONOMIC INTEGRATION & EXPANSE OF SOUTH ASIA**

### **1.1 INTRODUCTION**

Regional economic integration offers a comprehensive framework for tackling complex issues and releasing synergies that bilateral accords might only partially capture. It encourages a collaborative approach to economic growth, leading to a more robust and integrated South Asian economy.

There is significant potential for economic cooperation in South Asia in the commodities and services sectors to promote stability and growth in the region. This partnership spans multiple industries, such as manufacturing, natural resources, and agriculture. South Asian nations may increase production efficiency, lower trade barriers, and foster a more integrated economy by sharing common knowledge and resources. Effective regional partnerships and trade agreements are essential to fully realising the advantages of economic cooperation and ultimately contributing to the general development and prosperity of the region.

One of SAARC's main projects to promote economic integration is the South Asian Free Trade Area (SAFTA), established in 2006. SAFTA seeks to improve intraregional trade and economic cooperation by lowering tariffs and non-tariff trade obstacles among its member states. However, several challenges, including political

unrest, insufficient infrastructure, and bureaucratic red tape, have made it challenging to execute SAFTA.

SAARC has initiated several other programs and platforms besides SAFTA to advance regional economic integration. These consist of the South Asian Economic Union (SAEU), the SAARC Development Fund (SDF), and the SAARC Preferential Trade Arrangement (SAPTA). These programs seek to advance regional economic development, increase connectivity, and facilitate trade. However, the absence of institutional strength, political will, and member state's trust in each other has restricted the efficacy of these initiatives.

Additionally, SAARC has been instrumental in advancing infrastructure development and connectivity throughout South Asia. Initiatives like the SAARC Energy Ring and the SAARC Regional Multimodal Transport Study (SRMTS) aim to enhance member-state energy cooperation and transportation networks. However, development in these areas has been slow-paced due to financial limitations, technological difficulties, and geopolitical disparities needed to be faster-paced. SAARC continues to be an essential forum for advancing South Asian economic integration despite these obstacles. By offering a platform for communication, collaboration, and mutual comprehension among participating nations, SAARC can establish the groundwork for a more profound regional economic integration.

However, for SAARC to reach its full potential, it must overcome several significant obstacles, such as institutional weaknesses, security concerns, and political disputes. Increased political will, dedication, collaboration among participating nations, and backing from the global community are necessary to reach this goal.

Primarily, this study evaluates how SAARC promotes economic integration among its member nations by examining its administrative framework, decision-making procedures, and significant projects. Secondly, under the framework of SAARC, the study explores the many economic aspects of regional integration. It looks at initiatives like the South Asian Free Commerce Area (SAFTA) that promote intraregional commerce trade liberalisation and tariff reduction programs. The study also examines how SAARC promotes connectivity, investment, and infrastructure development initiatives to strengthen economic ties among its member nations.

The study also examines the difficulties and barriers to economic integration in South Asia, such as asymmetric development among member states, political unrest, and security worries. It assesses how well SAARC institutions can work to handle these issues and encourages reaching a consensus on common economic objectives. The study also examines SAARC's external economic integration initiatives, such as its interactions with international organisations, dialogue partners, and observer governments. It analyses the possible benefits and drawbacks of SAARC's interactions with international economic players and weighs the effects on stability and prosperity in the region.

In conclusion, this study offers insights about how SAARC supports South Asian economic integration. Through an analysis of the obstacles, possibilities, and factors influencing regional collaboration, it provides policy suggestions to improve SAARC's ability to act as a driving force behind equitable and sustainable progress in the region.

## 1.2 OBJECTIVES OF RESEARCH

In the context outlined above, this research aims to study the following objectives:

1. Analysing the existing economic integration strategies and mechanisms within SAARC member states and determining the significant challenges and barriers.
2. To evaluate the scale of intra-regional trade in the commodity market, investment, and economic interdependence among SAARC member states and provide recommendations for enhancing SAARC's role in South Asian economic integration.

### 1.3 RESEARCH QUESTIONS

The study aims to map out how SAARC can step in as an institution to propagate regional economic cooperation in South Asia and beyond. The study explores the following questions:

- To what extent has SAARC contributed to strengthening economic integration within South Asia?
- How do political and diplomatic relations among SAARC member states affect SAARC's ability to facilitate economic integration in South Asia as an institution?
- What is the correlation between increased intra-SAARC trade and South Asia's overall economic integration level?

### 1.4 HYPOTHESIS

- Reducing political tensions within SAARC members can lead to greater economic integration in South Asia.
- The volume of inter-state trade between SAARC member states and the region's economic integration level is correlated.

## 1.5 THEORETICAL APPROACH

This research refers to the neoliberal institutionalism theory to focus on how SAARC, as an international institution, shapes economic policies, trade agreements, and regional cooperation among member countries by creating a framework for economic integration. The research engages regional integration theories themed on functionalism and neo-functionalism. Such a theoretical framework facilitates understanding how functional needs drive economic integration within SAARC. It also considers whether they have resulted in more cooperation in areas other than economics, whether it leads to more extensive regional cooperation or specific economic integration measures within SAARC.

## 1.6 RESEARCH METHODOLOGY

- Through qualitative and quantitative data analysis, we can understand the nature of SAARC's role in economic integration in South Asia. The focus is on primary and secondary sources, consisting of textual analysis of government publications and archives, official SAARC documents, agreements, and reports on economic cooperation between 2012 and 2022.

The study has three primary analysis approaches as below:



- **Historical Analysis:** To assess the history of economic relations among SAARC countries between 2012-2022 and understand how historical events have shaped the current economic integration landscape.
- **Statistical Analysis:** Using economic indicators and statistics to evaluate the impact of SAARC on trade, investment, and economic growth in member states.
- **Comparative Analysis:** To compare SAARC's dynamics with those of other regional integration organisations such as ASEAN and their successful strategies and approaches.

## 1.7 CHAPTERISATION

The study is divided into six chapters as follows:

- The first chapter titled “Introduction to Economic Integration & Expanse of South Asia” discusses the study's rationale, research problems, objectives and significance.
- The second chapter titled “SAARC and Economic Integration” contains an overview of SAARC's objectives, followed by the role of SAARC in trade promotion and economic cooperation in South Asia, SAARC agreements, and initiatives for economic integration with SAFTA as the core focus.
- The third chapter titled “Challenges and Barriers” examine the barriers and challenges for SAARC regarding political tensions among member states,

regional economic disparities, bureaucratic and administrative challenges, and external actors affecting integration.

- The fourth chapter, “Contrasting SAARC and ASEAN Dynamics” delves into a comparison between SAARC and ASEAN regarding assessing ASEAN's approach to economic integration.
- The fifth chapter, “SAARC in New South Asia” deals with the timely topic of SAARC in new South Asia and how SAARC deals with other initiatives beyond the region, like BBIN, SASEC, BIMSTEC, and maritime SEA.
- The sixth chapter titled “Conclusion”, conclude the study with an analysis of the future potential of SAARC in rejuvenating economic integration in the region, followed by prospects and recommendations.

## 1.8 LITERATURE REVIEW

As part of this study, several journal articles along with some scholarly books on the given topic were reviewed as follows;

The significance of enhancing economic connectedness within South Asia is emphasised in the literature analysis in Saman Kelegama's article "**Towards Greater Economic Connectivity in South Asia**" (Kelegama, 2007). Kelegama draws attention to the necessity for South Asian states to rely less on the SAARC framework and other agreements, such as the South Asia Free Trade Area. The essay emphasises how

the business sector may help remove barriers to economic integration, especially by working with groups like the SAARC Chamber of Commerce and Industry. It also covers the obstacles to South Asia's economic integration: a need for progress and understanding within SAARC. There is still very little intra-regional trade in South Asia, despite initiatives like the South Asia Free Trade Area (SAFTA) and the South Asian Preferential Trade Agreement (SAPTA). The assessment also discusses trade hurdles in South Asia, the sluggish progress of regional integration, and the necessity for member states —mainly India—to take a more active role in advancing economic growth and regional cooperation within SAARC. The article also explains how the SAFTA framework will be less helpful if bilateral free trade agreements (FTAs) move quickly throughout the area. SAARC cannot draw in outside investment. It must, therefore, search for fresh opportunities and enact a SAARC agreement on investment promotion and protection. Regional politics also have a significant influence on the SAARC economic agenda. One cannot reasonably expect quick economic integration when the economic agenda weakens.

Muchkund Dubey's **"SAARC and South Asian Economic Integration"** (Dubey, 2007) paper examines the past and current challenges and prospects associated with economic integration in the South Asian region. Alongside this, the article mentions that the intra-regional trade in South Asia reached much higher levels in the past than today. However, while the current situation has recently started improving, intra-regional trade in South Asia is much less than in any other region except West Asia. The article claims that many more achievements could have been reached by now. However, the progress is limited primarily due to numerous "real impediments" to integration. To overcome these challenges, the article provides several policy-oriented recommendations and notes that India, with its scale, resources, and global ambitions,

must continue to determine the course of regional integration. Policy analysis also declares that more than India's unilateral policies are needed or suitable for regional integration. Countering governments should also show a positive intent towards India's initiatives for integration. Some key issues, such as regional trading, FDIs, and the general nature of economic development within the region, are also briefly discussed in the article. The article's conclusion briefly discusses the SAARC and the opportunity of South Asian economic integration based on the challenges and policy recommendations. This reveals the significance of regional cooperation and portrays India's duty, accompanied by an essential emphasis on the collective effort of India and all the neighbouring states, if economic integration in South Asia has to be successful. The article above argues that SAFTA is an inherently flawed agreement and contains no commitment to eliminating NTBs, no specific provisions for granting transit facilities, liberalisation of investment and trade in services, and no coordination of macroeconomic policies. Since the initiation of SAARC, the Member states have yet to agree on providing transit facilities through their countries for goods coming from neighbours. They have yet to express readiness to cooperate to get regional transport infrastructure working again.

The significance of regional economic integration in South Asia for promoting economic expansion and advancement is emphasised in the article **“Regional Economic Integration in South Asia: The Way Forward”** (Nasir, 2004) by Musleh-ud Din and Shahbaz Nasir. It discusses the obstacles to the region's successful economic integration while emphasising the benefits and chances that integration may present. The authors offer a conceptual study of regional economic cooperation that is region-specific to South Asia and focuses on a larger framework. The article likely offers frameworks, policies, and tactics to encourage regional economic integration

and remove obstacles to collaboration between South Asian states. The article also discusses standardisation and anti-dumping duties (Nasir, 2004). As potential avenues for growth in a region with more economic integration, anti-dumping duties shield domestic businesses and producers from unfair competition from overseas. While Bangladesh, India, and Pakistan each have their own Tariff Commissions to investigate related matters, Sri Lanka and the Maldives lack such a system to protect local producers. In conclusion, this article thoroughly analyses the challenges associated with regional economic integration and recommends improving cooperation between member states.

The difficulties and prospects associated with economic integration in South Asia are covered in the article **"Enhancing Economic Integration in South Asia: Issues and Prospects for Closer Monetary Cooperation"** (Maskay, 2010) by Sisira Jayasuriya & Nephil Matangi Maskay, with a particular emphasis on monetary cooperation. The writers stress how crucial it is for South Asia's subregional economies to integrate further to solve socioeconomic issues successfully. They stress the necessity of swift measures to quicken the region's economic integration process.

The article proposes the creation of the South Asia Comprehensive Economic Partnership (SACEP) to improve and unify current programs, including trade facilitation policies, trade in services liberalisation, and investment climate enhancement. It also highlights how crucial it is to create synergies with adjacent subregions like Southeast and Central Asia to deepen economic ties. The writers also emphasise the need for the institutional frameworks offered by regional organisations such as ECO, BIMSTEC, and SAARC to exploit synergies and establish a beneficial economic network. South Asian states can accomplish the 2030 Agenda for Sustainable Development by cooperating and utilising these institutional frameworks.

The article compares and contrasts the SAARC region's potential for economic and monetary union with Europe's in the late 1960s and early 1970s. It highlights how a dedication to integration might propel advancement, proposing a "single monetary system" as a first step toward a single currency. The idea of a South Asian Monetary System (SAMS) (Maskay, 2010) envisions summit-level political decision-making, similar to the European Monetary System (EMS). In light of political limitations, the article also examines the notion of a regional currency unit, maybe the "South Asian Currency Unit" (SACU). It also suggests creating the South Asian Cooperation Fund (SACF) to deal with balance of payments problems; it does this by taking cues from the Chiang Mai Initiative and possible connections with East Asian states. In conclusion, the article emphasises how urgently South Asian states must step up their efforts toward economic integration, primarily through monetary cooperation, to fully realise the region's economic potential and successfully manage everyday risks and vulnerabilities.

The South Asian Association for Regional Cooperation (SAARC) is the subject of Amita Batra's paper on **"SAARC and Economic Cooperation"** (Batra, 2014), which explores the evolving dynamics of regional economic integration in South Asia. The article focuses on how India's trade policy has changed and affected regional cooperation, highlighting the significance of economic growth, bilateral trade agreements, and the impact of a recovering Chinese economy on reshaping regional relationships. Other factors contributing to this positive trend include the evolving perception of SAARC in India due to China's growing regional influence and realising the advantages of collective regional initiatives. The article also covers the idea of sub-regionalism as a forerunner to regional economic integration. Member states can convene in more intimate regional groups with a targeted agenda involving cross-

border activities. As a result, member states would be more inclined to operate cooperatively. The essay also addresses the possibility of SAARC considering the establishment of a bilateral or regional fund for cross-border trade. In South Asia, border regions and villages are the poorest. As a result, trade financing may enable border regions to serve as conduits for the economic dynamics of their neighbouring nations.

As evidenced by the BBIN initiative (Bangladesh, Bhutan, India, Nepal), Dananjay Tripathi's "**Re-Imagining Border Studies in South Asia**" (Verma, 2021) chapter's discussion of new trends in cross-border trade and investment cooperation in South Asia reveals a shift towards subregional economic collaboration (Tripathi, 2021). This subregional strategy, which was first opposed, tries to address SAARC's problems. Subregional networks are prioritised above unilateral partnership in India's changing perspective on regional cooperation, as evidenced by the Gujral Doctrine.

The BBIN program aims to increase intraregional and international trade by converting transportation corridors into economic corridors. To improve regional connectivity, India, the country with the largest GDP, signed a Motor Vehicles Agreement and invested in infrastructure projects. The intention is to promote regional connectivity and value chains by converting transportation corridors into economic corridors. Additionally, this subregional cooperation presents South Asia as a gateway to the East by supporting more significant Pan-Asian connectivity initiatives and coinciding with the 'Act East' policy.

The book "**The Economy of South Asia**" by Tirthankar Roy talks about how the changes in political dynamics will impact South Asia's development trajectory in the next twenty years, especially as states cede control of economic reforms. The book

also discusses how the emergence of market forces, local interests, and new organisational structures will shape the region's future. The old elites, which included manufacturers, landlords, and bureaucrats, have given way to new economic forces as the distribution of wealth has changed. Political environments have changed due to the rise of regional corporate bureaucrats, local industries, and landlords. Politics have become more regionalised due to this decentralisation, which has created conflicts of interest between, for example, the development of urban infrastructure and agricultural subsidies (Roy, 2017). While economic growth has brought stability, poor institutional quality remains a concern. Despite the economic success driven by market forces, institutional weaknesses persist, often leading to reliance on political connections for business success. Improving institutional quality will be crucial for sustaining economic growth and ensuring the long-term viability of the South Asian economic miracle. Thus, future development hinges on interventions to enhance conditions for investment rather than relying solely on market-led growth.

The book **“Promoting Economic Cooperation in South Asia Beyond SAFTA”** by Sadiq Ahmed, Saman Kelegama and Ejaz Ghani emphasises how the South Asian Free Trade Agreement can remain relevant. A few recommendations are to reduce harmful listings with binding clauses, expedite the liberalisation of heavily traded products, eliminate non-tariff barriers with enforceable pledges, and improve trade facilitation measures while maintaining a realistic outlook. It also highlights the necessity of including trade in services more heavily and implementing creative strategies, such as ASEAN's common subsector strategy (S. Ahmed, 2010) to motivate member states to make commitments. Especially in the case of Sri Lanka, even though Sri Lanka already has substantial market access because of bilateral



agreements with Pakistan and India, there are still barriers preventing it from taking full advantage of this access. Entrepreneurs in Sri Lanka are urged to explore export opportunities in adjacent countries and diversify from traditional export markets. SAFTA needs to be significantly improved overall to influence regional trade.

## **CHAPTER 2**

### **SAARC & ECONOMIC INTEGRATION**

#### **2.1 INTRODUCTION**

Economists have highlighted over the years the crucial link between increased trade regime openness and the increased economic integration of developing states with the global economy. As countries get more competitive in terms of input consumption and output production at a reasonable cost, expanding intraregional is one of the most successful methods to integrate into the much bigger international economy. In addition to offering a bigger market and more complete use of manufacturing capacities, it also makes technology transfer, a more complete use of human capital, and entrepreneurial potential possible, all of which contribute to economies of scale. On the other hand, the most direct and significant type of regional economic cooperation is the growth of intraregional trade (Gharanna, 2000).

During the late 1980s, South Asian states have been gradually instituting wide-ranging economic liberalization and institutional reforms, inspired by the successful experience of trade liberalization and export-led growth in East Asian countries, as well as gains from intra-regional trade expansion. With the success of the European Union (EU), North American Free Trade Agreement (NAFTA), and Asian Free Trade Area (AFTA), SAARC has also made a significant stride toward intraregional economic cooperation with the South Asian Preferential Trading Arrangements (SAPTA). Members of SAARC are aware of the significant and wide-ranging effects trade liberalization has on the region. Through the best use of human and natural resources, collaboration among neighbors not only strengthens the financial and

economic sectors but also promotes stronger political stability and social and cultural cooperation among members.

The European Union has served as an inspiration for regional economic organizations, which are becoming more and more important in achieving economic security within the multipolar framework of global interdependence. The most important international organization of this kind in South Asia is SAARC, which have helped the member states in growing closer to one another and becoming more powerful in the areas of trade, development cooperation, and financial policy in recent years. To maintain acceptable levels of welfare and political authority, economic security demands access to the markets, funds, and resources required. Many Western theories claim that economic warfare <sup>1</sup> is taking the place of military conflict in light of the end of the Cold War, the collapse of the Soviet Union, and the emergence of new economic giants like Japan that are directly competing with the United States. The situation is more unstable for developing nations, nevertheless, as their insecurity results from the current international economic system, which upholds the hegemony of the wealthy few while pushing everyone else to the periphery. These states are now prone to the global economic system because of their complicated interconnection and the growing politicization of economic matters. Human necessities in one state are now reliant on the actions and occurrences in another due to the globalization of production, consumption, and financial systems. Higher rates of overall economic growth result from regional economic collaboration in management issues and market expansion.

Even after gaining independence, South Asian states continued to follow the economic pattern established during the British colonial era, relying on industrialized nations for industrial and machinery products while contributing raw resources and agricultural

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<sup>1</sup> Economic warfare refers to the deliberate application of economic means against a country with the intent to weaken its economy and reduce its political and military power.

products.

Because of the lack of economic synergies that resulted, South Asian economies exclusively competed in the global market for tea, cotton products, and jute. In order to create economic advantages, the region's economies must be deliberately adjusted toward one another. By increasing the size of markets, lowering transportation costs, promoting products, and shifting trade from urban centers to the member countries of the area, regional cooperation can aid in the growth of intra-regional trade (Agarwal, 1987).

South Asia is a very dynamic, increasingly urbanized, resourceful region known for its rapid GDP growth since 1980s averaging roughly to a 6% per annum. On the other hand, South Asia is also a region lagging behind due to its high dependence on agriculture, being landlocked and constant political and regional tensions. However, a deep understanding of the present economic trends indicates that if the SAARC members manage to develop an integrated economy, South Asia could become the second largest economy in the world after China.

Established in 1985, The South Asian Association for Regional Cooperation (SAARC), aimed to integrate the economies of the eight South Asian states; India, Bangladesh, Nepal, Bhutan, Pakistan, Afghanistan, Sri Lanka and Maldives. As outlined in its mandate, SAARC aims to accelerate economic growth, foster mutual trust, understanding and collaboration among the member states by facilitating political interdependence, territorial integrity and non-interference in internal affairs. However, despite after almost four decades and close geographical, cultural and historical compatibility, South Asia remains as one of the least integrated regions in the world with intra-regional trade accounting for less than 5% of the total trade in the region (World Bank, 2016).

From its inception various ministerial and foreign secretary level meetings were held time to time to envision the institutionalisation of regional cooperation in South Asia. These discussions helped in initiating diplomatic activity on regional levels and creating an organizational framework. The Delhi Declaration of 1983 was considered as the basis of the SAARC Charter in which eleven non-controversial areas were identified to have cooperation among the member states:

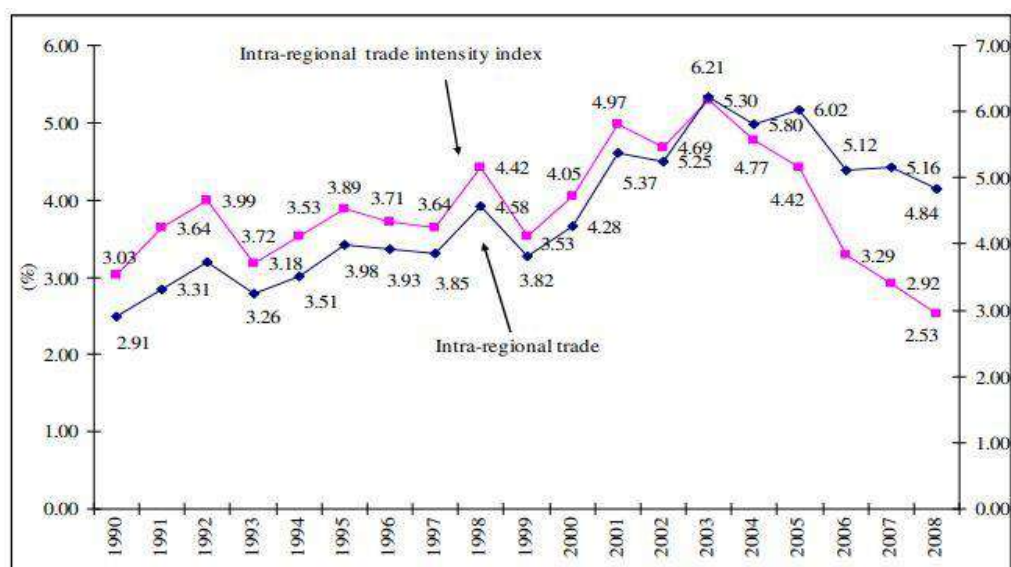
1. Telecommunication
2. Meteorology
3. Transport
4. Shipping
5. Tourism
6. Agricultural research
7. Joint ventures
8. Market promotion
9. Scientific and technological cooperation
10. Educational and technical cooperation
11. Cultural cooperation

SAARC's interest in promoting economic and development cooperation in South Asia lies in several key objectives such as trade liberalization, investment facilitation, industrial cooperation and financial cooperation. All in all, SAARC's economic objectives are aimed at building bilateral and multilateral economic relations among the member states through institutionalised regional economic cooperation.

## 2.2 PATTERN OF SOUTH ASIAN INTRA-REGIONAL TRADE

There has been gradual decline in intra-regional trade within SAARC. Prior to 1951, South Asia's intraregional trade accounted for double digits of the region's overall trade. However, by 1967, intraregional trade had dropped to just 2% of the region's overall trade as a result of South Asia becoming increasingly restricted to the global market, armed conflict and the political dispute between India and Pakistan becoming more intense. In the 1990s, the share started to rise again, and by 2002, it had reached 4.4% (T.Baysan, 2006). It dropped to 4.84 percent in 2008 after peaking at 6.21 percent in 2004. South Asia's larger trading with the outside world than within the region is the cause of this decline in intra-regional trade intensity. Although South Asia's increased exports are encouraging, the distribution of intra-regional trade within the area is significantly unequal, in contrast to the European Union (EU). However, in comparison to other regions like NAFTA, ASEAN, and the EU, South Asia's intra-regional trade share is typically dismal.

FIGURE 2.1: Intra-regional Trade in SAARC

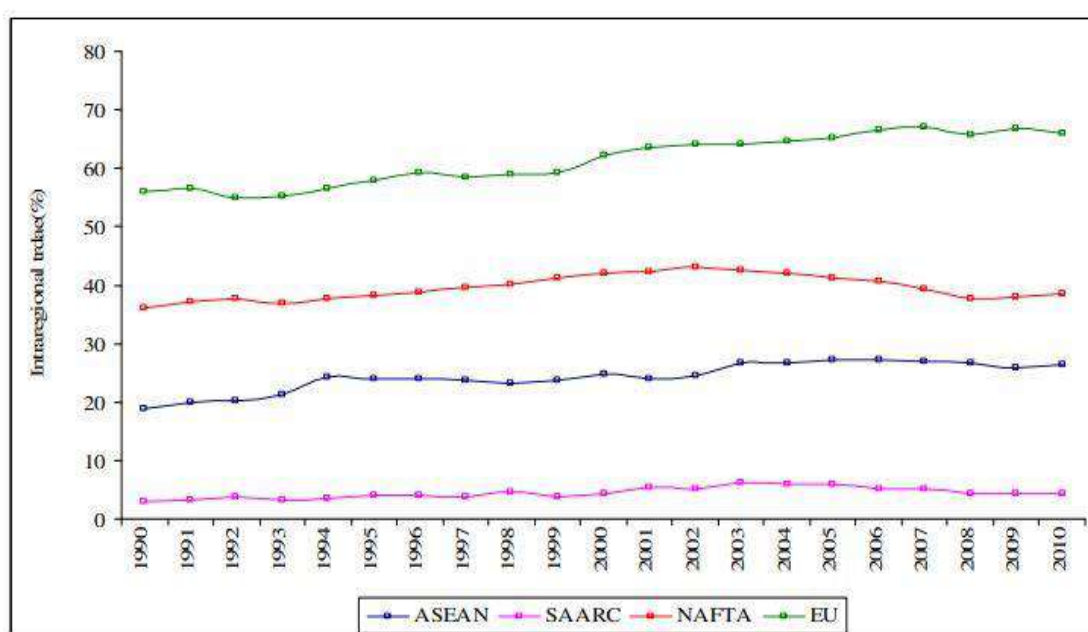


Source: World Bank Data

With the exception of Nepal and Bhutan, every South Asian states' primary export market lies outside its own region. India accounts for over 100% of Bhutan's total

exports, while 71% of Nepal's exports go to India because it is both states' primary export market. Additionally, it seems that trade is not divided fairly throughout the states of South Asia. Bangladesh has virtually little trade with Sri Lanka, Nepal, and Bhutan. India is Bangladesh's main import source. India is as well as the country that supplies the majority of resources to Bhutan, Nepal, and other countries. However, trade with India is mostly one-sided because there are very little exports from Bangladesh and Nepal to India and extremely huge quantities of imports from India to these two states.

FIGURE 2.2: Intra-regional Trade in SAARC and other regions



Source: Director of Trade Statistics Online Database, IMF.

One of the main causes of South Asia's low intraregional trade has long been identified as the high tariff rates among the member states. The average tariff rate in South Asia is greater than in any other region of the world. Therefore, one could argue that lowering tariff barriers across South Asian states will probably have a significant impact on the degree to which these states may access markets in their neighbors.

Informal cross-border trade is another significant component of intra-regional trade in South Asia and has long been believed to be very common. Research has been conducted on the unrecorded border trade across South Asian nations, highlighting the possibility that substantial amounts of documented trade may be accounted for by the irregular and informal trade that occurs between India and Bangladesh, Nepal, and Sri Lanka.

### 2.3 ROLE OF SAARC IN TRADE PROMOTION AND ECONOMIC COOPERATION.

Intra-regional trade improvement is a vital part of a growth strategy for a region like South Asia which has the largest middle class in the world along with a low wage labour force. SAARC focuses on promoting intra-regional trade through reducing trade barriers, promoting trade liberalization and enhancing trade facilitation. Additionally, SAARC as a regional organization promotes the execution of agreements pertaining to mutual administrative assistance, investment promotion and protection, trade in services, and avoiding double taxation. By increasing intraregional investments and operationalizing several economic and infrastructural windows, the organization seeks to close financing gaps for infrastructure.

A region achieves economic integration through 4 stages according to a study by Balassa (1961). Firstly, preferential trading agreements or free trade agreements are arranged in which trade barriers (tariffs and non-tariffs) are downsized. Then the member states establish a customs union with regular external tariffs. Following that the member states move onto create a common market alongside free movement of



goods, services, labor, and capital. Finally, they come together to create an economic union with the introduction of a common currency.

Small and Medium-sized Enterprises (SMEs) play a critical role in reducing poverty by generating job and income possibilities and by making a major contribution to the region's economic potential. Currently, however, central trade-related government and private sector organizations lack the necessary capacities and competences, which hinders the development of an appropriate framework for intraregional trade.

The SAARC agenda purposefully excluded economic related issues when it was created in 1985. When the goal of the SAARC was to engage in confidence-building to iron out the deeply ingrained interstate hostility in the region, it was believed that economic matters were too complex to be included in the agenda. It was believed that cooperation on non-economic matters was more desired because it was less contentious. In 1991, an independent commission was established to investigate the issue of poverty in the region, which may have been the only economic concern to make it onto the SAARC agenda in its early years. Aside from poverty, very little was done in the first ten years of SAARC's existence to advance economic cooperation in the area (Asian Development Bank, 2008).

Economic cooperation was added to SAARC's agenda at the beginning of its second decade (Batra, 2014). A crucial element of economic connection, or "trade," was added to the SAARC agenda on December 1995, with the establishment of the SAARC Preferential Trade Arrangement (SAPTA). The SAPTA was to give trade privileges for intraregional trade in goods. Prior to the formation of the SAPTA, South Asia's private sector chambers recognized the region's open economies, particularly in

the wake of India's 1991 reforms. In 1992, the SAARC Chamber of Commerce and Industry (SCCI) was established to advance regional trade and investment flows.

In addition to negotiating a sub-regional PTA under the SAARC framework, its member states pursued bilateral free trade agreements (FTAs) with other SAARC members. This led to the signing of the FTAs between Pakistan and Sri Lanka in 2002<sup>2</sup> and India and Sri Lanka in 1998<sup>3</sup>. Maybe a comparison could be made to the events that unfolded during the Uruguay Round of the WTO negotiations, in which certain GATT contracting parties engaged in side-by-side discussions for PTAs and the WTO. Perhaps the most similar aspect of both situations is the state parties' hesitancy regarding the scope of the agreements made in the larger forum—the WTO or SAFTA.

## 2.4 SAARC AGREEMENTS AND INITIATIVES FOR ECONOMIC INTEGRATION

Having open economies in the early post-independence years of the 1940s, South Asian states had emerged as some of the most severely protectionist economies worldwide by the 1970s. There were a lot of high tariffs and, more importantly, nontariff barriers, frequent state interventions in the economy, negative and frequently hostile attitudes toward foreign investment, and strict exchange controls. However, things began to alter in the late 1970s. Sri Lanka helmed a policy liberalization movement in 1977, and other states did the same in the 1980s. However, the liberalization process was not always smooth and varied greatly throughout member

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<sup>2</sup> Free Trade Agreement between the Islamic Republic of Pakistan and the Democratic Socialist Republic of Sri Lanka, signed on 1 Aug. 2002 (entered into force on 12 Jun. 2005)

<sup>3</sup> Free Trade Agreement between the Republic of India and the Democratic Socialist Republic of Sri Lanka, signed on 28 Dec. 1998 (entered into force on 1 Mar. 2000).

states. It dates back to the early 1990s, when India began a significant reform drive, that the entire region truly began to liberalize. Significant legislative challenges to trade and foreign investment persisted by the end of the decade, although the region had made tremendous strides in this regard.

Unilateral liberalization by individual states has been the main force behind changes to the trade policy framework in South Asia. However, since the SAARC was founded in 1985, there has also been a continuous process of preferential trade liberalization. It took South Asia almost ten years after SAARC's founding to focus on promoting trade through regional agreements, indicating that the area was relatively late in adopting the idea of regional economic cooperation. Nevertheless, SAARC was fast to establish an ambitious agenda after accepting the idea of regional economic cooperation.

## 2.5 SAPTA

The 1991 completion of a SAARC regional study on trade, manufacturing, and services resulted in a recommendation to strengthen regional cooperation in "core" economic areas. The creation of an Inter-Governmental Group (IGG) to seek cooperation on institutional frameworks to advance trade liberalization in South Asia was approved during the Sixth Summit, which was held in Colombo in December 1991. The SAARC Council of Ministers signed the South Asian Preferential Trading Arrangement (SAPTA), a draft agreement developed by the IGG, in 1993. After being ratified by every member, the agreement entered into force in 1995, bringing an end to SAARC's initial ten years and initiating cooperation in specialized sectors. SAPTA was created to foster mutual trade and economic cooperation within the SAARC region through tariff concessions. The objectives of SAPTA were to increase

intraregional trade by exchanging preferences for market access among SAARC states and to foster and promote technological and economic cooperation.

The establishment of SAPTA was influenced by a number of reasons. With the conclusion of the Cold War and the re-emergence of democracy in Bangladesh, Pakistan, and Nepal, a new political class emerged that was more cooperative. Furthermore, the SAARC member states had already started an economic liberalization program by that point. The spread of regional economic agreements around the globe also served as an accelerator on a global scale.

Over time, SAPTA's product coverage grew from its initial limitations. India had the longest list of items that member states traded for tariff benefits. To identify the origin of products, SAPTA had added rules of origin criteria. These requirements were essential to the preferential agreement's success. According to the introduction of SAPTA, member states recognize that increased trade has the potential to significantly boost their national economies by increasing investment and production. This, in turn, can lead to increased employment opportunities and help maintain higher living standards for citizens. Member states submitted offers for 226 items in the first round of talks. India offered over half of the products (106), indicating the poor nature of the concessions that were traded. The first wave of regional trade liberalization had a maximum value of \$72.5 million, which amounted to 6% of intra-regional trade in 1993.

The majority of the sectors in which member states provided duty reductions either had little or no transactions with one another. Of the 106 commodities India offered for concession in 1993–94, only 22 were imported, and of the 35 items provided by Pakistan, only 13. Bangladesh noted that only 18 of the 214 commodities on which

other members had provided concessional tariff rates were exported to the SAARC region between 1993 and 1995 (Bhattacharya, 2001). The IGG gathered four times to finalize the National Schedule of Concessions for the second round of trade preferences. Concessions were given out in this round by clearly stating which country they belonged to. The schedule indicated if the goods were subject to any non-tariff barriers (NTBs) and, if so, what concessions had been made. A greater number of concessions were made in the second round, with 2,013 goods being given up. Practically speaking, though, this round also produced very little trade news. The issue of product coverage seems to be of greater importance to members than trade coverage, despite trade liberalization depending on it. India obtained reductions on 474 tariff lines and offered concessions on 911 tariff units in this round. NTBs were only addressed in relation to 172 products during this round, and solely in the LDCs' best interests (Chibber, 2007). During its Nineteenth Session in Malé in 1997, the Council of Ministers pushed for the removal of NTBs and instructed the IGG to conduct third round discussions on a sectorial and overall basis.

The third round of discussions came to an end in November 1998, and the fourth round of SAPTA negotiations began in 1999. However, the Eleventh SAARC Summit was rescheduled to January 2002 because of Pakistan's conflict in Kargil. High tariffs and non-trade barriers (NTBs) in the form of quantitative restrictions (QRs) promoted cross-border informal trading and the poor performance of formal intra-SAARC trade. India unilaterally deleted the QR codes from 2000 import goods from SAARC states in August 1998, provided that the goods complied with the principles of rules of origin. Since India imports a lot of agricultural products from Sri Lanka and the removal of non-trafficking barriers (NTBs) is anticipated to cause informal trade to transfer to legal channels, Sri Lanka gained the most from this decision.

Key features of SAPTA included; a positive list of goods for which member states were required to grant partner states preferential market access (zero or reduced duties), more favorable treatment for SAARC's Least Developed Country (LDC) members, mainly through deeper duty reduction and flexible rules of origin and a gradual transition to a free trade area by liberalising intra-regional trade and removing non-tariff trade barriers. A product-by-product strategy, the exchange of goods for tariff reductions (zero or reduced tax), and direct trade measures were key tools in implementing the SAPTA. Additionally, SAPTA implemented protective measures against an increase in imports and an unfavorable balance of payments.

Nevertheless, SAPTA failed to make a substantial impact on increasing intraregional trade or strengthening trade cooperation among its member states. Some of the main takeaways from the SAPTA experience were;

- If the benefits of preferential trade were to be realized in practice, the non-tariff barriers that were in existence had to be removed quickly.
- It was challenging to accomplish the intended impact on regional trade without sufficiently deep tariff cuts
- The product-by-product exchange of privileged access under the positive list approach proved to be an ineffective strategy. A negative list strategy had to take its place because the previous one was too time-consuming, labor-intensive, and ineffective at promoting trade.
- Rules of Origin must be created in a way that minimizes trade diversion, supports market access opportunities, and is in line with member states' domestic capacities.

- More actions were required to draw in intra-regional capital and build supply-side capabilities that allowed export diversification

Limited trade volume, ineffective regional cooperation and reciprocity issues among the member states acted as main challenges for the success of the SAPTA even though SAPTA established the framework for South Asian regional economic cooperation.

## 2.6 SAFTA

The South Asian Free Trade Area (SAFTA) is the free trade arrangement affiliated to SAARC which came into action in 2006 succeeded by the 1993 SAARC Preferential Trading Agreement. All eight SAARC states were signatory members to the SAFTA while Myanmar, Iran, China and the European Union takes the role of observer states of SAFTA. Formation of free trade zone, tariff reduction, trade liberalization, inclusion of all products and special treatment for least developed countries (LDCs) were some of the salient features of SAFTA.<sup>4</sup>

A Group of Eminent Persons (GEP) was established during the Ninth SAARC Summit, which took place in Malé in 1997, to conduct an extensive evaluation of the association and suggest ways to improve its significance and operations. Three stages for the creation of an economic union in South Asia were suggested by the GEP in its study SAARC Vision Beyond the Year 2000. The goal was to negotiate the South Asian Free Trade Area (SAFTA) by 1999, with the goal of implementing it in 2000. For LDCs, it ought to be operational by 2008 and finished by 2010. By 2015, a customs union, or an integration of external tariffs, will constitute the second stage.

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<sup>4</sup> South Asian Free Trade Area Agreement. (2004).

By 2020, the third stage will result in the creation of the SAARC economic union and the integration of fiscal and monetary policy.

Expanding the export production capacity of LDCs through export-oriented joint ventures with funding from the South Asian Development Fund and the private sector of the more developed member states was one of the GEP's other ideas. Regional collaboration was desperately needed given the high level of tension and mistrust in the region, even though not much progress has been made on these issues. Positively, the percentage of intra-SAARC imports increased from 1.91 to 4.06 percent (1990–96), while the share of intra-SAARC exports in total SAARC exports increased from 3.16 to 4.8% (1990–2001) (Sami, 2002). The development of an integrated mega-sector of trade and services in the area is another crucial factor. The SAARC countries will not become powerful competitors in the economy unless they accomplish this. The benefits of trade liberalization and economic cooperation that SAARC members attain in their region will be degraded by competition in the exterior market.

A Committee of Experts was formed during the Tenth SAARC Summit in Colombo, 1998, with the special mandate to prepare a complete treaty regime for the creation of a free trade area. As previously mentioned, political difficulties among SAARC governments prevented things from progressing further, resulting in the indefinite postponement of the Eleventh SAARC Summit, which was eventually held in January 2002. February saw a two-day meeting of the SAFTA Committee of Experts in Kathmandu, which was followed by a meeting of the SAFTA Ministerial Council to discuss the state of the agreement's implementation, including the tariff liberalization program, NTBs, and QRs. During the Fourteenth SAARC Summit in New Delhi in April of 2007, Indian Prime Minister Manmohan Singh declared that the LDCs of



South Asia will have zero-duty entry to India by the end of the year, and that their sensitive list would also be further reduced. At the summit's conclusion, participants committed to advancing trade and economic cooperation, such as by accelerating the creation of an agreement that would promote and protect investments and bringing services under the scope of SAFTA.

However, over the time, the success of this Free Trade Agreement (FTA) was considered quite limited due to large Sensitive (negative) Lists maintained by the member states. Sensitive lists consist of items and goods by each country that are not offered concessional tariffs and are excluded from immediate tariff reductions. Usually, Sensitive Lists may only be kept for a limited time before being phased out to give the domestic import-competing sector time to adjust, in order for free trade agreements to be effective. Any sensitive list in a preferential trade agreement or free trade agreement is justified by the need to shield industries deemed unsuited for competition, according to socioeconomic and infant industry considerations and safeguard agriculture and small-scale farmers for the sake of food security.

Under SAFTA, the Tariff Liberalization Programme (TLP) excluded 53% of all intraregional import trade. Under the sensitive list category, India prohibited up to 52% of its total imports by value from SAFTA members. According to the SAFTA Ministerial Council (SMC) recommendations, member states are obliged to review their sensitive lists every four years or sooner, as per the tariff liberalization program. However, there is no official or legally enforceable obligation. Thus, each member state decides on a voluntary basis to reduce the number of sensitive listings. India should assume an asymmetrical role in liberalizing imports by reducing its own sensitive list in comparison to other South Asian nations, given that it has the largest economy among SAFTA members.

Different criteria are used by member states to compile their sensitive lists. Protecting vulnerable groups, such as emerging industries (the infant industry argument), small-scale manufacturers (the socio-economic argument), and agricultural producers (the food security concerns), is one of these criteria. Nevertheless, it has been noted that industries with powerful domestic lobbies that are seeking protection frequently end up on the list as a result of stakeholder participation. Particularly in the case of India, these industries have grown to predominate on sensitive lists.

There are various factors that need to be taken into account in order to reduce the sensitive lists. Items that partner states are unable to provide are frequently included on sensitive lists; as a result, their inclusion on the list has no bearing. These items ought to be taken out. In keeping with India's current reform, the majority of the goods that medium enterprises were only allowed to produce have been dereserved to make businesses more competitive. Nonetheless, a number of the goods that were previously restricted to the small-scale industry are still included in India's sensitive lists under the SAFTA. These items have no justification for being on the sensitive list.

When an exporting state is competitive in the global market but India is not, the goods on the sensitive list are identified using the theory of revealed comparative advantage. These products may continue to be on the sensitive list and may be phased out over time.

Most member states maintain two separate sensitive lists under SAFTA; one for Least Developed Countries (LDCs) which is applicable to Bangladesh, Nepal, Maldives, Afghanistan and Bhutan and the other for non-LDCs applicable to India, Pakistan and

Sri Lanka. Additionally, states can maintain sensitive lists under bilateral FTAs they have with other states. A bilateral free trade agreement's main justification is that it ought to be more liberal than a regional one. Sensitive list negotiations would need to follow the terms of each individual agreement. Eliminating things that are included on the bilateral sensitive list but not the regional one is a crucial factor to take into consideration.

As the predominant economic power house of the region, India's bilateral agreements with SAARC members should have narrower sensitive lists than those upheld by SAFTA. India maintains several sensitive lists under its bilateral free trade agreements with Nepal, Bhutan, and Sri Lanka. Since India and Sri Lanka have a free trade agreement, Sri Lanka's operational sensitive list is also the bilateral sensitive list among the two non-LDCs in SAARC. India has free trade agreements (FTAs) with Nepal and Bhutan, two of the LDCs in SAARC, with virtually little on the former's sensitive list and none on the latter. Despite being on the LDC list, Afghanistan and the Maldives have extremely small economies and only export a small number of commodities.

However, current evidences suggest that SAFTA has already lost a great deal of momentum and is lagging behind in the dynamics of regionalism that are evolving in South Asia. SAFTA has been unsuccessful in its attempt to enact free trade in the SAARC region; it has already been surpassed by the bilateral process in numerous instances and looks like it may soon be overtaken completely by other regional and bilateral initiatives. The SAARC members clearly have different interests, including strategic ones.

Table 2.1 Sensitive Lists Under SAFTA

Member State	Number of Products in the Revised Sensitive Lists (2012 version)
Afghanistan	850
Bangladesh	987 (LDCs) / 993 (NLDCs)
Bhutan	156
India	25 (LDCs) / 614 (NLDCs)
Maldives	154
Nepal	998 (LDCs) / 1036 (NLDCs)
Pakistan	936
Sri Lanka	925 (LDCs) / 1058 (NLDCs)

*Source: Sri Lanka Department of Commerce*

The SAARC process as well as the future rate of regional economic cooperation under SAFTA are both internally challenged by these events. If SAFTA was keeping up with these advances, then a multitude of alternative bilateral and regional agreements among SAFTA members wouldn't be a significant barrier. SAFTA is, regrettably, now experiencing a lagging effect.

The two SAARC economies that are still the least integrated—Pakistan and India—must impose a more extensive trade liberalization agenda if SAFTA is to serve as the driving force behind the economic integration process. Sensitive lists will need to be loosened in addition to finding a way to resolve bilateral trade disputes between the two states. Moreover, other economies in South Asia will have to think about liberalizing their markets. Due to SAFTA sensitive lists, the majority of South Asian

economies currently limit between 55% and 65% of their imports from India. The fact that Pakistan only limits about 16.5% of Indian imports suggests that it has provided more lenient treatment, but this percentage must be considered in light of the ongoing economic restrictions between the two states. To encourage spillover effects, steps to include investment and trade in services within SAFTA must be promoted in addition to attempts to expand the TLP's purview.

The SAFTA treaty's lack of a clear commitment to address the problem of nontariff barriers (NTBs) is another area of concern. It is possible to distinguish between NTBs that need to be abolished and those that need to be harmonized when recognizing them. Examples of such measures include those pertaining to technical standards, plant and animal health, and environmental safety and protection. If there are any quantitative constraints, it will be easier to convert them to tariffs and then lower them. Quantitative restrictions (QRs) have been phased out in South Asia, but there are still nontariff barriers in place that can impede the free movement of commodities amongst SAARC nations. Although there are mechanisms in the SAFTA framework agreement to address NTBs and Para tariffs, countries are not required to make any explicit commitments. Specifically, the SAFTA framework agreement makes no commitment to address non-trade barriers (NTBs) on goods that are subject to tariff reductions.

Also, the fact that the SAFTA agreement is limited to goods trade is seen as a constraint. Global trends are driving the implementation of larger economic partnership agreements that cover investment, trade in services, and sectors of economic cooperation, as well as bilateral and regional trade efforts. By launching a collaborative study to look at the problems that need to be resolved, although SAARC

has taken the first steps toward integrating services and investment into the SAFTA framework agreement consequently, it is evident that SAFTA has some restrictions as it is.

## 2.7 WELFARE EFFECTS OF SAFTA

The South Asian corporate community, policy leaders, and researchers have all shown a great deal of interest in SAFTA. There is disagreement over whether SAFTA will benefit or negatively impact South Asian nations. This issue has been escalated because the results of several qualitative and quantitative investigations have been inconclusive in this regard. Nonetheless, the variations in the approaches taken in these investigations have had an impact on the findings.

Trade creation and trade diversion are two ideas used in trade theory to analyze the welfare impacts of any RTA (Raihan, 2012). Economic integration's overall welfare impacts are unclear and demand for case-by-case analysis. The rationale is that integration is a step toward free trade as well as a defensive policy. Trade diversion is the result of the defensive component of integration, and trade creation is the result of the trade liberalization component. Comparing the trade-creation and trade-diversion effects generates the overall welfare impact of an RTA on a member state. The development of an RTA will improve welfare of a member state if trade creation is the primary driver. On the other hand, the RTA will result in a welfare loss if the trade diversion effect outweighs the trade creation gain<sup>5</sup>.

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<sup>5</sup> if member countries are the low-cost producers of the traded good, there will be no trade diversion effect and integration will unambiguously increase welfare.

The research that suggests regional trade agreements (RTAs) primarily create trade serves as the foundation for regionalism's arguments. The majority of RTAs are probably going to result in very little welfare losses from trade diversion because the participating states are frequently neighbors and hence already have substantial trade. Additionally, it is asserted that governments can "lock-in" reform through RTAs, which is frequently politically impractical under multilateralism. Furthermore, trade liberalization can only occur through RTAs in the circumstance that international trade negotiations fail or come to a standstill. It is emphasized that states can advance regionalism and eventually move toward a more liberal trade policy overall. Nonetheless, there are several strong arguments opposing the creation of any RTA. Allegations have been made that the principle of multilateralism is compromised by RTA. It is suggested that protectionists may embrace free trade agreements (RTAs) in order to resist additional global liberalization and that the world may split into a few protectionist blocs. RTAs may therefore serve as obstacles to multilateralism rather than as pillars. RTAs discriminate against non-member nations as well, and they may even cause major discrimination against LDCs in developed and developing nations. An excellent illustration of this is NAFTA, which is said to have discriminated against LDCs like Bangladesh while favoring Mexico in the US market (Razzaque, 2005).

RTAs also imbalance the distribution of resources, favoring regional producers at the possible cost of local consumers (Delgado, 2007). The worldwide effects of several and overlapping RTAs in terms of the transaction costs they impose have also been the focus of RTA research (Feridhanusetyawan, 2005). It is also argued that trade ministries have a limited supply of resources. Thus, excessive participation in RTA talks could draw focus away from international liberalization.

Concerns have also been raised about the possibility that, even if member states reduce their tariffs, the home market may remain a "captive market" for their exporters, preventing a decline in the price of goods imported from those countries. For instance, critics of SAFTA frequently claim that Indian exporters may discover a "captive market" in Bangladesh as a result of this regional economic agreement. Because Indian exporters will have the "freedom" to raise prices to the point where goods from the rest of the world are sold, even if Bangladesh lowers its tariffs on Indian goods, the cost of those goods may not decrease in Bangladesh.

SAFTA's economic justification was not very strong (Baysan, Panagariya, & Pitigala, 2006). There are three key aspects of the economies of South Asia that could make an FTA between them undesirable economically. First, in terms of trade flows and GDP, the economies are tiny compared to the rest of the globe. Despite having a significant population, the region's per-capita income is very low, which keeps its economic size limited. And the ratio decreases dramatically if India is excluded. It was unlikely that the member nations' most productive suppliers were found in the area. As a result, there is a good chance that the FTA will significantly redirect trade. The second justification has to do with the SAARC economies' comparatively high levels of protection. Even in the case of a small trade diversion, a country taking part in a regional arrangement wouldn't be impacted if it were open itself. Nonetheless, it is clear that every state in the SAARC region continues to have high levels of protection. The political economy of the selection of excluded industries and Rules of Origin (RoO) is the third and final factor damaging the economic case for SAFTA. Domestic representatives ensure that the sectors that may not be able to survive competition from the union member are the ones that get left out when countries are permitted to



select which sectors can be excluded from tariff preferences in an FTA. Furthermore, the bureaucrat in charge of enforcing the rules of order may misuse them. If imports from the partner could pose a danger to a low-performing domestic competitor, administrative power could be used to prevent the imports from entering the country.

Nonetheless, the majority of South Asian policymakers have a positive outlook on SAFTA. They believe that SAFTA has a great deal of potential to increase trade among its member states. It is also expected that the member states will benefit greatly from increased market access in other South Asian states, particularly in India. Those in favor of SAFTA claim that although while there isn't much trade in South Asia through official channels, there is still a lot of trade there, with a significant amount of that trade occurring informally. While research indicates a lack of mutually beneficial relationships in the SAARC region, others believe that similar circumstances existed in ASEAN in the mid-1970s and that FDI <sup>6</sup> and intraregional investment might encourage previously inactive mutually beneficial relationships in the area. Additionally, they contend that the price of non-cooperation is very substantial. Thus, the issue is far from resolved. Whatever the outcome of the discussion, most people agree that regionalism has many positive effects outside of trade and that South Asian regional cooperation should not only be seen from a trade standpoint.

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<sup>6</sup> In the mid-1970s, intraregional trade in ASEAN was approximately 6%, but it is now up to approximately 25%. Similar to other regions, ASEAN initially had minimal mutually beneficial relationships, but preferential trade, foreign direct investment, and intraregional investment helped to change that.

## 2.8 INDIA'S ROLE IN FACILITATING TRADE UNDER SAFTA

Due to its central geographic location in the region, India is at the center of all regional trade facilitation and transit issues. As a result, the rate and course of economic integration in South Asia are largely determined by India's relationships with the other economies in the region. India is the largest economy in the region, accounting for more than 80% of South Asia's GDP. More than 90% of Bangladesh, Nepal, and Sri Lanka's regional trade as well as a significant percentage of their global trade is with India. Trading among the remaining South Asian states is far smaller than India's trade with most of its South Asian partners. India signed preferential trade deals with Afghanistan and free trade agreements with Nepal, Bhutan, and Sri Lanka to deepen its bilateral ties with its neighbors. India has implemented a number of bilateral and SAFTA-related initiatives in recent years to promote trade in the area. Numerous attempts have been put in place to reduce non-tariff barriers and transportation challenges, as well as to liberalize the tariff regimes that South Asian imports have to deal with. Less than 1% of India's total imports come from the rest of South Asia, despite the continued low level of intra-SAARC trade. This is mostly because transferring commodities across regional borders involves significant transaction costs. The two biggest economies in the area, Pakistan and India, have strained relations, which prevented the successful implementation of several trade-facilitating policies.

But in a significant development, Pakistan gave India the Most Favored Nation status in 2011, strengthening both the SAFTA process and trade ties between India and Pakistan. In this updated circumstance, greater effort by India would be advantageous to the path of regional trade integration than previously. Trade complementarities exist

in both trade in commodities and services, hence South Asian trade integration needs to be pushed with greater conviction.

India provided NLDCs and LDCs with different tariff reductions in accordance with SAFTA requirements. Additionally, India kept sensitive lists and different origin regulations for these two categories of states. Concessions granted to NLDCs, however, only apply to Pakistan because India has a free trade agreement with Sri Lanka; similarly, concessions granted to LDCs only apply to Bangladesh because it is the only LDC member of SAFTA with whom India does not have a free trade agreement. Therefore, all tariff liberalization initiatives with SAARC members are carried out bilaterally from India's perspective. The bilateral trade agreements with Afghanistan, Nepal, and Sri Lanka regulate discussions with those countries. The SAFTA for NLDCs regulates the tariff discussions with Pakistan, whereas the SAFTA for LDCs regulates the negotiations with Bangladesh.

India can accelerate the pace of South Asian regional economic integration in a number of ways. Since 2007, a number of trade integration measures have been implemented and it is crucial to maintain the pace by completing the remaining measures on schedule. India has reduced tariffs more quickly than it was anticipated under the terms of the SAFTA. In the future, India ought to provide NLDCs with more tariff breaks, up to the point where Pakistan receives the same concessions as Sri Lanka. Pakistan should also receive more duty-free advantages by reducing India's sensitive lists for NLDCs. Transparency in regulatory regimes is essential for addressing the different non-tariff obstacles. Notifying the WTO of non-tariff measures is one method by which this can be achieved by every member state. Another step that could lessen disparities in data is to make trade-related information

available via electronic media. India and Pakistan have come up with an original and easy way to inform Pakistani businesspeople and government officials about their respective regulatory frameworks (Nisha Taneja, 2013). To close information gaps on regulatory regimes, the two states have set up business-to-business and government-to-business exchanges. This has proven to be a successful strategy for promoting more trade as well as a strong means of creating confidence. Other states could also embrace a similar initiative.

Among all the South Asian states, customs is one area where the most development has been made. The efficiency of customs is still well below potential, though, so fixing this needs to be a top focus. With the implementation of the EDI system, India has experienced a reasonable degree of automation. Nonetheless, bilateral trade has not become more efficient as a result of automation in India and other neighbor states. Enhanced cooperation between customs officials on both sides of borders and the creation of one-stop, shared inspection facilities that would remove duplication of procedures would be important steps that could be taken to improve the effectiveness of customs inspection at land borders.

India has been actively involved in capacity building with Bangladesh and Nepal to address TBT and SPS measures. The actions include evaluating export testing laboratories, assisting authorities in creating certification programs, creating Residue Monitoring Plans (RMPs), and setting up a system of national licensing. It is essential that this capacity-building process be finished within the given period. In order to help down transaction costs, India should also further streamline its import processes. India should establish Equivalency Arrangements and Mutual Recognition Agreements with its trading partners to address the issue of non-acceptance of tests and certification.

## 2.9 CONCLUSION

The lengthy and sensitive list of specific engaging parties severely restricts the extent of tariff liberalization allowed by the SAFTA. Although it is understood that the SAFTA members may not be able to instantly waive all tariffs on goods included in their list of sensitive items, there should be a deadline for doing so. Decentralizing the SAFTA's dispute resolution mechanism is essential. It is alarming that the Agreement essentially does nothing to limit the extent to which trade dispute measures may be adopted for internal trade. The Agreement's general exclusion provision's limited scope is a good thing. However, protectionist measures may be implemented under that process to the extremely broad scope for establishing safeguards.

By actively engaging in the liberalization of its trade regimes, SAARC would be able to improve market access for its exports. It is important to remember that SAPTA only accounts for a tiny portion of regional trade. The desired shift to SAFTA would not be out of reach for the SAARC states if SAPTA implementation covering a significant portion of the regional trade with further tariff cuts and targeted tariff lines and products could be secured. In order to achieve their developmental objectives and completely integrate into the global commercial system, SAARC would benefit from rapid regional integration. In South Asia, the benefits of trade facilitation outweigh the benefits of just reducing goods tariffs. Trade liberalization is therefore a necessary but not sufficient requirement for SAFTA's effectiveness. The development of trade infrastructure (hardware) and trade facilitation (software) should be given the highest

priority. Furthermore, enhanced administrative and operational efficiency together with supporting policy reform in the Customs are necessary to enable trade liberalization. Without a doubt, a major factor in strengthening regional integration is intraregional investment movement. Both imports and exports will benefit from an increase in foreign investment. It would also lead to job creation. The energy sector is one that offers members a lot of trade and investment options, which is beneficial to them.

The main focus of the current SAFTA Treaty is "trade in goods." Beyond just facilitating "trade in goods," the SAFTA Treaty should include additional mechanisms for regional cooperation in the fields of investment, finance, trade in services, trade facilitation, and technology transfer. To encourage intra-regional investment, an enabling environment must be established. An intra-SAARC investment pact might establish an environment similar to this by establishing a SAARC Investment Area. The trade-investment nexus, for instance, is effectively operational in the bilateral free trade agreement between Sri Lanka and India, and the substantial trade deficits between these two nations have been balanced by the capital account through significant capital flows. South Asia's industries must integrate both horizontally and vertically in the context of investment flows in order to withstand the challenges of global competition.



## **CHAPTER 3**

### **CHALLENGES AND BARRIERS**

#### **3.1 INTRODUCTION**

Since the early 1990s, the number of Regional Cooperation Arrangements (RCAs)<sup>7</sup> has increased several times, and new ones are created frequently. However, despite their widespread appeal, RCAs have sometimes lived up to the hype. A few have achieved great success, a few have achieved less, and a few have failed or degraded into dysfunction soon after they were founded. Studies examining the comparative effectiveness of regional economic corridors typically assume that all RCAs are created equal, with the primary motivation being trade and economic opportunities among participating states. However, in actuality, there are several significant ways in which RCAs vary, including the non-economic goals they pursue, regional stability, and defence against external threats. Furthermore, the functioning of various RCAs is uniquely conditioned by the relative power balances among member states and their distinct political structures and practices. Any comprehensive RCA performance evaluation must consider each of these aspects.

Using the above approach, an evaluation of the SAARC's almost 40-year record demonstrates the importance of internal political dynamics and interstate power ties. A

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<sup>7</sup> All cooperation structures between two or more countries typically from the same geographic area are called "regional cooperation arrangements" (RCAs). However, the number of RCAs involving cross-regional countries is increasing. The formation of regional capital assemblies (RCAs) by nation-states serves a variety of purposes, both economic and non-economic. These purposes may include trade liberalization and economic integration, strengthening regional peace and stability, security cooperation, managing shared opportunities and challenges, and developing shared facilities, infrastructure, and resources.



notable feature of SAARC is the significant power disparity among its member states, with India having a GDP and demographic advantage over all other members and an essential military border. Several SAARC members, therefore, see India as a threat to their security and a potential source of economic dominance. Poor interstate relations and a lack of trust, particularly between Pakistan and India, intensify these views. As a result, several SAARC member states have expressed bilateral concerns with India and negotiated security arrangements with extra-regional actors. This has further strained relations with India and increased hostility throughout the region.

To minimise the threat of economic dominance, these regional dynamics have forced members to limit trade and economic exchanges with India and made the development of regional cooperation dependent on the status of relations among member states rather than on economic opportunities (Desai, 2010), thereby introducing uncertainty and unjustified variables into the cooperation process. These effects have hampered trade and cooperation. This has severely hindered SAARC's accomplishments in advancing trade and economic integration. However, by facilitating the region's leaders to engage in a cooperative framework through its summit meetings, SAARC has been successful in helping to moderate tensions among its member states. These gatherings have allowed the leaders to understand one another's perspectives and, in some instances, have even facilitated high-degree political choices.

Individual member states, primarily India and, to a lesser extent, Pakistan, have concluded preferential trade and cooperation arrangements with other states from inside and beyond the region due to uncertainty regarding future advancements in cooperation. Though in a scattered way that avoids the SAFTA and SAARC platforms, this tendency will likely bring about trade liberalisation and integration in

South Asia (Desai, 2010). Even in a compacted variation, trade liberalisation and integration in the area can provide significant advantages to SAARC participating countries. However, further development will depend on eliminating the current trust deficit and fostering better ties among member states, given the defining restrictions of interstate relations on cooperation in South Asia. Smaller SAARC member states will continue to be cautious about furthering their integration with the Indian economy if mistrust and scepticism endure and interstate relations stay unstable. As the leading member, India must lead the effort to improve relations in the region by easing the security worries and suspicions of dominance held by other members. In response, other members must accept India's leadership and realise that economic integration with India may enable them to overcome geographical and market-based barriers.

Better relations between states provide a favourable atmosphere for economic collaboration. Nonetheless, the trade account deficit and the institutional capacity disparity must also be successfully addressed in the region. Integration efforts have been delayed by the region's institutional incapacity to fund and carry out cooperation initiatives. The SAARC Secretariat must be given more authority and assistance to build this capacity quickly. This would enable it to monitor, support, and advertise SAARC activities and encourage cooperation among members in addressing the region's shared opportunities and challenges. With a robust and efficient Secretariat, proposals that hold significant importance for the region, like the development of its shared rivers, are likely to proceed.

### 3.2 THREAT OF INDIA'S DOMINANCE OVER THE REGION

India's pivotal role in the region and the apparent power imbalance among its member states define SAARC. While India accounts for almost 75% of SAARC 's population and nearly 80% of GDP, the most prominent SAARC member states account for roughly 11% (Asian Development Bank, 2012). India's military might also surpass that of all the other SAARC member states put together. Except for Afghanistan, Sri Lanka, and the Maldives, all other members of the SAARC have land borders with India. Nepal and Bhutan, two member states, are landlocked and rely on India as their transit route to the outside world. Bangladesh, another SAARC member, is encircled by India on all sides but has direct access to international waters on one side. Unresolved bilateral conflicts exist among members, primarily involving India. In other SAARC member states, the combination of these structural characteristics causes security worries and suspicions of dominance.

Due to its strong land lockup, Nepal depends on India for its vital imports and transit to the outside world. Due to this dependence, India has a significant influence over Nepal in many sectors of life, which disadvantages Nepal when interacting with its much larger neighbour. Bangladesh and Nepal will always depend somewhat on India due to their geographic location and underdeveloped economies. These conditions, meanwhile, also make them more fearful of India's potential dominance and reliance. Though maybe to a lesser extent, other smaller SAARC states have similar worries.

Even though South Asia was experiencing severe security worries and fear of Indian dominance at the time of SAARC's formation, both of these issues had to be removed from the organisation's mandate to gain support from Pakistan and India. Due to these omissions, SAARC was limited in its concentration on trade and economic cooperation, which was not its members' top priority and could not address urgent and significant issues for most member states. While security and Indian dominance were

no longer on SAARC's agenda, they remained relevant worldwide and even created circumstances that severely hindered regional cooperation. India's inability to convince its neighbours of its commitment to non-interference and the peaceful settlement of bilateral conflicts meant that security concerns about the country did not go away. Conversely, over time, several incidents intensified these worries, such as India's stance on the Liberation Tigers of Tamil Eelam (LTTE) movement in Sri Lanka, its alleged involvement in Nepal's internal affairs, and the continued standoff over several bilateral matters. As long as their security concerns remained unaddressed, member states had little reason to collaborate on other matters if they continued to view India as a threat and potential rival (Dash, 2008).

Furthermore, several SAARC member states established security agreements with extra-regional powers seeking to establish themselves in South Asia due to their ongoing concerns. Additionally, member states started to impart their bilateral problems with India. Members' mistrust and hostility toward one another grew because India believed such imparting would negatively impact its security. Involving foreign forces in regional conflicts rather than trying to resolve them inside the region undermined member states' commitment to SAARC. It prevented it from developing into an economically integrated regional organisation. There needed to be a focal state to enable members to coordinate policies and actions due to conflict and disagreements over India's leadership and dominance in the region (Bhutto, 1969). While having a focal state is thought to aid with coordination issues and give an RCA momentum, its absence can lead to coordination difficulty, foster disagreement among members, and ultimately result in the collapse of an RCA. The lack of resources needed to make up for poorer states that could not absorb the costs of trade

liberalisation was an unexpected consequence of SAARC's lack of a focal state. As a result, these states were reluctant to back SAARC's trade liberalisation program.

Inter-state ties between India and some SAARC states remained characterised by mistrust and suspicion due to the failure to address smaller states' regional security and dominance concerns. The prevailing atmosphere strengthened and intensified unfavourable public perceptions towards partner states in the area overall, specifically between India and other states (Dash, 2008). Unfavourable public impressions of a partner state or states might become an issue-blind barrier to cooperation, as is occasionally observed within SAARC. According to a recent survey, the public's opinion in SAARC member nations is generally hostile toward the RCA and other member states. This suggests that there needs to be more support for regional cooperation.

### 3.3 INFRASTRUCTURE DEFICITS IN SOUTH ASIA

The degree of growth in infrastructure in a region is one of the key factors influencing its economic performance. Infrastructure for transportation must be readily available to stimulate economic activity, especially international trade. Adopting a regional perspective to improve intraregional trade and development activities is necessary, as expanding transportation infrastructure frequently requires overcoming geographical barriers. Adopting a regional perspective to improve intraregional trade and development activities is necessary, as expanding transportation infrastructure frequently necessitates overcoming geographical barriers. Statistically speaking, the transport infrastructure has two main influences on intraregional trade, among other things. First, its creation is a way to facilitate trade between members of a regional organisation by facilitating the transportation of tradable goods. Second, developing

an affordable and effective transportation infrastructure could boost export competitiveness and promote regional trade. The success or failure of a region can be attributed to its infrastructure, which plays a crucial role in various aspects such as trade expansion, population growth management, poverty alleviation, and quality of life enhancement. These effects must be seen in the context of a two-way causal relationship between income and infrastructure on the one hand and trade and economic growth on the other <sup>8</sup>.

Even though South Asia received an integrated transportation system from the British, it was later fragmented and requires significant attention today. South Asian states have substandard ports, highways, waste management systems, and hospitals. South Asia lags behind all other regions except Sub-Saharan Africa in terms of access to all infrastructure services except internet users. South Asia lags behind even Sub-Saharan Africa despite having the second-highest average GDP growth rate globally at 6.7% <sup>9</sup>. This emphasises how much of an infrastructure deficit South Asia has compared to other regions and how urgently those gaps must be filled. The political and geographic context in South Asia has significantly impacted the region's transportation networks, particularly on rail travel in Bangladesh and Pakistan (Thapar, 2013). Furthermore, the region experiences limited access to land for the transportation of goods, even for those not on the negative list. In addition to having a bad reputation, Indian Railways, one of the most extensive rail networks in the world, is suffering enormous losses. Bangladesh, on the other hand, is considered to be a landlocked nation due to

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<sup>8</sup> Research and Information Systems for Developing Countries (RIS) (2004) South Asia development cooperation report. RIS, New Delhi

<sup>9</sup> SAARC Secretariat (2006) SAARC multimodal regional transport corporation. SAARC Secretariat, Kathmandu

Chittagong Port's inefficiency. For South Asian countries and regions that are landlocked or semi-locked, transportation network integration is essential.

Creating a robust regional transit system is essential to expanding the potential for using trade and development prospects. In order to increase intraregional trade, facilitate access to subregional markets, draw in more foreign direct investment, and become competitive with other parts of the world, South Asia needs a system of regional connectivity. In South Asia, there is now a bilateral transit system rather than a regional one. Limited trade relations exist between India and Bangladesh due to the expensive nature of trade logistics. A portion of northeastern India is also divided from the rest by Bangladesh, except for a tiny transit route known as the "chicken neck." The only way to reach the seaports from these divided states of Northeast India is to go via Kolkata, which requires crossing the chicken neck.

Furthermore, Bangladesh still needs to grant India transit access for trade with the North Eastern states. For example, a distance of approximately 1600 km separates Agartala (India) from Kolkata. However, less than 100 km separates Agartala from Chittagong, the closest seaport in Bangladesh, indicating substantial transportation expenses for these North Eastern states.

The relatively low rankings South Asian states received in the Global Competitiveness Index 2018's infrastructure rankings can be explained by the wide disparities in infrastructure. Regarding infrastructure, India came in at number 63 out of 140 countries, Sri Lanka came in at number 65, and Nepal came in at number 117<sup>10</sup>. The subregion pays a heavy price for its inadequate infrastructure. Inadequate electrical supply has reportedly affected one-third of enterprises in India and seventy-five per

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<sup>10</sup> (World Economic Forum 2018: 616-7).

cent % of those in Bangladesh, Nepal, and Pakistan. The subregion experiences 3-4% GDP losses <sup>11</sup> due to infrastructure deficiencies.

South Asia is considered one of the least integrated regions globally, with its underdeveloped surface transportation networks and insufficient steps to facilitate transportation.

As a result, trade within the region is significantly more expensive than trade with distant regions, such as North America, depriving local producers of the advantages of proximity. According to a UNESCAP study, South Asia's actual intraregional trade is less than one-third of its potential, which means that over US\$50 billion in trade opportunities are missed yearly, along with corresponding job losses and opportunities to reduce poverty. Therefore, developing cross-border transportation infrastructure and border facilitation is paramount to South Asian states.

At more than 3.5 million km, India's road network is the second longest globally, while its national highway network spans over 70,000 km. The quality of the roads, however, could be more satisfactory. Just 60% of the rural population has access to all-weather roads, and more than half of the state's highways have only two lanes. Due to delays and increased vehicle wear and tear, poor road quality raises transportation costs and harms local and international trade.

**TABLE 3.1. Infrastructure availability in Subregions in Asia and the Pacific and South Asian countries**

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<sup>11</sup> (UNESCAP 2018a).



	Telecom Access (per 100 people), 2013	Electricity Access (% of population), 2016	Access to improved water (% of population) 2015	Access to improved sanitation (% of population) 2015	Internet Users (per 100 people), 2017	Rail Density (km of railway per 1000 km <sup>2</sup> ) 2011	Road Density (km of road per 1000 km <sup>2</sup> ) 2011	Paved Roads (% of roads) 2012
East Asia	114	100	98	92	83	8	400	64
South-East Asia	125	88	89	77	54	4.7	276	55
South Asia	74	86	92	45	30	19.4	1123	52
Bangladesh	75	76	87	61	18	21.8	1838	10
India	73	85	94	40	34	21.7	1578	54
Nepal	80	91	92	46	21	...	139	54
Pakistan	74	99	91	64	16	10.1	341	73
Sri Lanka	108	96	96	95	34	23.3	1819	15
World	109	87	91	68	49	9.1	275	57

*Source: World Development Index online statistical database*

Excessive transportation expenses function as a non-tariff trade barrier; frequently, these costs represent a more significant percentage of import value than the tariff rates in place. The landlocked nation of Nepal has the highest trade transportation expenses relative to its import value. The number of goods traded across land in South Asia indicates the importance of roads and rail in aiding economic integration. Given that it shares borders with most of the countries in the region, it is not unexpected that over 60% of India's exports to South Asia are transported by road, with the remaining 13% being transported by rail. However, the World Bank Doing Business database reveals that South Asia's trade costs are significantly higher than those of high-income states and marginally better than those of Sub-Saharan Africa. The duration of exports and imports is notably extended, nearly matching that of Sub-Saharan African states, primarily because of delays at land-border crossings. As a result, a large percentage of trade between several South Asian countries has shifted to unofficial channels to avoid the complications and broader potential for corruption associated with conventional cross-border business procedures.

The SRMTS (2006) lists several obstacles to free trade, such as the absence of bilateral or multilateral agreements to enable the uninterrupted flow of vehicles and goods across borders, the lack of coordination for gauge conversion programs on various railway systems, the absence of facilities for storage and customs clearance at multiple border posts, and the absence of transparent customs procedures. Thus, in addition to offering adequate cross-border transportation connections that integrate the transport networks of various states, addressing these concerns at the top of the priority list is necessary to realise the full potential for intraregional trade. The World Bank International Trade and Transport Department's Logistics Performance Index (LPI), introduced in 2009, provides insight into the efficacy of border logistics. The LPI assigns scores between 1 and 5 based on several trade facilitation-related factors. Except for India, which has an LPI score of 3.12, which is relatively low compared to Japan or Singapore but near to the PRC, South Asian states score poorly when compared to other regions.

Due to their interdependence, the states in the region need connection infrastructure to access markets and take advantage of their natural resources assets. Reducing transportation costs can only be achieved by strengthening collaboration with adjacent coastal states. Suppose transit facilities are offered at a fair price for transporting commodities via pipelines carrying oil and gas and for trade in goods via roads and rail. In that case, there can be mutual benefit. Countries will be more inclined to work together and coordinate cross-border infrastructure construction as awareness of the potential benefits of trade and investment rises.

Some of the inefficiencies that South Asian states have to face due to infrastructure and connectivity issues are, (Srinivasan, 2012)

- Since foreign trucks are prohibited from entering Bangladesh, the shipment of perishables (fruit and items derived from it) from Nepal and Bhutan to Dhaka requires passing through four customs checkpoints at two border crossings and dividing the load between vehicles. Cargo damage can be severe even though the time and expense of the transfer make up a minor portion of the overall expenditures associated with transportation and logistics. Getting rid of these inefficiencies would mean that trucks could transport goods to Dhaka.
- The Wagah border is the only point where commodities can be transported by train or road between Pakistan and India. Only a specific range of goods can be exchanged, such as cement from Pakistan to India and vegetables and cattle from India to Pakistan. Cotton cannot be imported by rail into Pakistan; textile companies in the Lahore region import cotton from Mumbai via Karachi. Due to limited capacity, exporters from Kolkata are compelled to ship to Karachi via Singapore since they cannot reserve rail cars.
- Woolen carpets are transported from Kathmandu to the port of Kolkata, and from there, they are transported via Singapore to a port in Europe. Alternatively, they could be delivered straight to the European port, saving money and time on logistics, assuming transit is permitted via the Mumbai port.
- Shipping containers from Delhi to Dhaka travel via Tuglakabad, Mumbai port, Singapore, Chittagong port, and Dhaka. The entire process takes forty-five days. Rail travel between Delhi and Dhaka is estimated to take two to three days, covering a distance of 2,000 kilometres.

**Table 3.2. Trade Infrastructure in South Asia**

Country	LPI	Customs	Infrastructure	International shipments	Logistics competence	Tracking & tracing	Timeliness
Afghanistan	2.24	2.22	1.87	2.24	2.09	2.37	2.61
Bangladesh	2.74	2.33	2.49	2.99	2.44	2.64	3.46
Bhutan	2.38	2.14	1.83	2.44	2.24	2.54	2.99
PRC	3.49	3.16	3.54	3.31	3.49	3.55	3.91
India	3.12	2.7	2.91	3.13	3.16	3.14	3.61
Japan	3.97	3.79	4.19	3.55	4	4.13	4.26
Nepal	2.2	2.07	1.8	2.21	2.07	2.26	2.74
Pakistan	2.53	2.05	2.08	2.91	2.28	2.64	3.08
Singapore	4.09	4.02	4.22	3.86	4.12	4.15	4.23
Sri Lanka	2.29	1.96	1.88	2.48	2.09	2.23	2.98
United States	3.86	3.68	4.15	3.21	3.92	4.17	4.19

*Source: World Bank Data*

Almost 90% of global trade is carried by the oceans. Thus, Seaports and maritime routes are crucial in intra- and interregional trade. Likewise, this applies to South Asia. Seaports can be broadly divided into three groups: regional hub ports, trans-shipment hub ports, and regional ports. Larger shipping vessels often operate along or near the main maritime routes, utilising trans-shipment hubs, the initial class of seaports. The only transshipment hub in South Asia is Sri Lanka's Colombo port.

Additionally, the most developed is Colombo. However, because it must contend with competition from Chinese ports, its reputation among container ports could be improved. The largest port in India, Nhava Sheva Port, is classified as a regional hub port. Regional seaports manage the main transshipment hubs' connection services. The regional seaports of South Asia are Bangladesh's Chittagong and the Indian ports of Haldia and Calcutta. A variety of depressing realities at regional hub ports lead to a disturbance in trade flow. These consist of prolonged turnaround times, postponed shipments, cramped spaces, fluctuating weekly schedules, and postponements. The

cost of a traded item would increase by 40% if a trader chose the air route. Consequently, it is a drawback of the region's inadequate trade infrastructure. (Wilson, 2007)

Besides ports and related infrastructure, the regulatory framework and its adherence are other essential factors. The "International Ship and Port Security Code (ISPS)" was implemented by the "International Maritime Organization (IMO)." Approximately 102 states have approved this and put into effect the Code. Compared to the ports of East Asia, the regional airports and maritime ports seem less competitive. Shipping prices are closely correlated with port efficiency. Port entry tariffs are a component of shipping expenses, making them more significant in South Asia. South Asia cannot anticipate major gains at this time due to the region's shallow level of port efficiency. On the other hand, it can result in reduced transaction costs and promote trade with better port rules and performances. For increased trade and cooperation, newer frameworks for regional economic cooperation and better regional security mechanisms are still essential.

One of the main obstacles to expanding regional economic integration in the South Asian region is the absence of trans-frontier transit stations and road networks. For example, Afghanistan needs more facilities for transporting cargo and transportation infrastructure. A developed inland waterway connects Bangladesh and India for shipping. When discussing India and Pakistan, a third party typically takes a path other than the Wagah border. The absence of regional transportation connections is why shipping costs are still rising. This issue is critical in states like Afghanistan, Bhutan, and Nepal that do not have a seaport. Moreover, protests in the industry also have a significant role in trade delays and bottlenecks at land connections. Thus, when

it comes to trade shipments, companies carefully consider two critical factors: time and cost.

The main routes for transporting commodities in South Asia are mostly made up of inland road networks. Negligent maintenance, outdated bridges, a network growth system, and constrained capacity are all in a regional setting.

As a result, it raises the price of commodities, transportation, vehicle maintenance, and licensing requirements. As a result, restrictions are placed on the cargo's weight and cargo-carrying vehicles. As a result, shipping efficiency could be improved and carried out at a more significant expense. Improving the potential for regional and supraregional trade and commerce is severely hampered by the region's poor road connection.

### 3.4 POLITICAL TENSIONS IN THE REGION

Multiple intraregional and intrastate disputes, motivated by restricted ideas on religion, caste, language, or ethnicity or by geographical borders, are a persistent problem in South Asia. Economic development has nearly always been a secondary goal in SAARC member states due to the disputes that have dominated public and political life for decades. The region, full of ongoing conflicts, has never offered the right conditions to enable attempts to integrate the economies. Because of historical baggage in their relationships, the countries have been unable to put their differences behind them and move forward. For example, India and Nepal have disagreed despite their generally friendly ties. The governments of Nepal and India were required by the terms of the 1950 Treaty of Peace and Friendship to hold discussions with one another

in order to develop effective responses to address security risks arising from external aggression.

Additionally, it mandated that the two governments notify one another of any significant disagreements with any neighbouring nation that would hurt India-Nepal relations. Due to its restriction on Nepal's autonomy and the greater likelihood of Indian dominance, this provision was disliked in that country. Another tactic Nepal made to distance itself from India was its closeness to China. Following the 1962 India-China war, Nepal permitted China to construct the Lhasa–Kathmandu route. India saw this action as a significant threat to India's security interests and Nepal's acceptance of China's influence and presence in South Asia. The declaration of Nepal as a zone of peace, which China backed but which India saw as a step to separate itself from India and the obligations under the Treaty of Peace, was another conflict between the two states.<sup>12</sup>

With most SAARC states, Sri Lanka has no significant disagreements. The primary points of conflict with India were the denial of citizenship to a sizable number of Tamils, their return to India, and India's intervention in the Tamil ethnic conflict in Sri Lanka since 1983. Sri Lanka said that India had given Tamil terrorists weapons and training. However, as India has backed the Sri Lankan government's efforts to bring peace, relations between the two states have improved. The United Nations Human Rights Council voted <sup>13</sup> India against Sri Lanka on accountability and crimes during

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<sup>12</sup> Apart from these issues, being bordering states, India and Nepal have issues regarding migration, border security and allegations of smuggling Indian goods across the borders, thus negatively affecting the Nepalese economy (Gurung Commission report of 1983).

<sup>13</sup> The Indian government had to make this decision to retain its domestic allies' support. See "India votes against Sri Lanka" UN Human Rights Council Resolution adopted, March 22, 2012. Available at <http://www.ndtv.com/article/world/unlike-china-india-likely-to-vote-against-sri-lanka-for-alleged-warcrimes-188871>.

the civil war that resulted in the defeat of the Tamil Tigers, which had impacted relations between the two states.

The sharing of waters, boundary demarcation, and illegal migration from the Chittagong Hill Tracts are unsolved issues between India and Bangladesh. The link between eastern and western Bengal prior to separation is still deeply remembered in Bangladesh. Over time, Such a conflict-ridden environment reinforced and intensified negative public perceptions of other nations in the area, especially India. Reluctant dedication to regional integration has resulted from a persistently unfavourable view of one another. (Dash, 2008)

The two-nation idea <sup>14</sup> led to the division of India and Pakistan, which has resulted in tense relations throughout history, characterised by fears on both sides. There are still several unsolved bilateral conflicts, the largest of which is the territorial dispute over Kashmir, despite multiple attempts to defuse the situation, which failed miserably. Pakistan was afraid that if Kashmir, a territory with a majority of Muslims, remained a part of India, Pakistan's basic foundation would crumble.

On the other hand, India was afraid that losing Kashmir would undermine its secular structure and encourage separatist sentiments. Three wars have been fought between the two states over Kashmir in the last 60 years, and there has always been low-level insurgency and tense relations between them. Trade was substantial in the late 1940s when both countries were part of British India, a single political entity. Even after India and Pakistan gained independence in 1947 when, Pakistan (which at the time

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<sup>14</sup> According to the two-nation theory, Indian Muslims and Hindus are two different nationalities, independent of ethnicity or other similarities. Muslims in the Indian subcontinent get their central identity from their religion rather than from their language or ethnicity.



also included Bangladesh) accounted for over half of its imports and nearly two-thirds of its exports. However, trade between them decreased as tensions over territory and security grew. The connection between these two countries, the largest in South Asia, affects the entire region, specifically towards economic integration.

Based on the idea that nation-states are reluctant to deal with current or potential opponents, India and Pakistan need more incentives to engage in trade since they see each other as enemies. Research on the potential for trade and commerce obstacles between the two states demonstrates that trade between India and Pakistan is restricted. Pakistan supposedly keeps a sizable negative list exclusive to Indian goods in addition to refusing to grant India's most-favoured-nation (MFN) designation, effectively prohibiting or severely impairing possible trade between the two states. In 2005, the State Bank of Pakistan conducted a study which revealed that although the unit price of Pakistani products was lower than that of the competing imports to India, 32% of the product categories supplied by Pakistan were imported by India from other states. Similarly, even though Indian exports were more expensive, Pakistan imported roughly half of India's exports from other states. According to a 2005 research study, Pakistan lost between US\$400 million and US\$900 million a year due to importing these goods from other countries. According to a similar analysis conducted in India (Taneja, 2007), 45 of the top 50 exports from Pakistan were purchased by India from other countries but not Pakistan. Comparably, an analysis of India's top 50 exports revealed that almost two-thirds of these goods were not included on Pakistan's "positive" list of goods that India was permitted to import, blocking their entry. Despite being a tiny list, it also revealed that many textile products of great export importance to Pakistan were included on India's "sensitive" products list, which hindered their entry into India.

Political and military disputes among the region's nations are a significant obstacle to regional integration. Mutual anxieties, hatred, and bitterness characterise interstate political interactions. The nuclear-armed states of India and Pakistan have tense relations because of terrorism and Kashmir. These nations shell out enormous sums of money to purchase weapons and other military assets. The amount that can be conserved for socioeconomic areas is directly reduced by unnecessary military spending. The emergence of risks like cyberwarfare and cybercrime has also led to mistrust amongst the regional states (Kumar, Saurabh, & Sharma, 2015). Tensions between India and Pakistan have increased as a result of new types of conflict, such as the fourth and fifth generations of warfare, non-state actors like armed networks or warriors, etc. This ultimately hurt their complete economic integration.

Regarding trade and collaboration, the circumstances between India and Bangladesh and India and Nepal are comparatively similar. Bangladesh maintains a restrictive trading system with India despite having an MFN agreement between the two countries. In contradiction of trade logic, Bangladesh has occasionally refused to trade with India, even in goods with a comparative advantage. Bangladesh is most likely opposed to permitting more trade with India because doing so will make the country more dependent on India.

Similarly, Nepal has hesitated to welcome Indian investments despite the Free Trade Agreement and Investment Agreement and the mutual need for foreign direct investment. Nepal's central resource is hydropower (potential capacity > 70,000 MW), and its development could result in significant export revenue.

Moreover, India has an energy shortage, which would be a ready market for Nepal's energy output. Nonetheless, the two states have worked together throughout the

previous few decades to produce a capacity of less than 700 MW, or 1% of its total capacity.

India benefits significantly from a large trade balance generated by Bangladesh's trade with India. Research and Information System for Developing Countries (RIS) studies from 2008 demonstrated that Bangladesh's export sectors' supply constraints cause these trade imbalances. However, Bangladesh hesitates to accept value-adding investments from India in sectors of the Indian economy. Indian corporations have been discussing investment proposals for developing gas-based businesses in Bangladesh since 1975, but no agreement has been achieved.

Constant miscommunications and conflicts within the region mean that imports from extra-regional providers hinder efforts to expand investments and trade with India, even at higher costs. Pakistan also imposes trade restrictions on India to control the flow of Indian goods into its market and prevent mutuality and interdependence from increasing. Furthermore, the aim of disconnecting Pakistan's historical ties to the Indian economy has influenced the country's economic structure entirely since independence. A portion of the population, investors, and businesses involved in the impacted sectors are sure to oppose the development of extensive trade and investment with India, which would necessitate an economic reorientation, at least in some areas. The deficient level of intra-regional trade, which accounts for only 5% of members' total trade, reflects the underlying unwillingness of SAARC member states to permit the free trade flow among themselves due to these regional conflicts. Studies show that intraregional trade has enormous growth potential, but the member states have yet to do much to pursue this potential. The facilities for trade and exchange within the region and the business environment present significant barriers to expanding intraregional trade. Participants from the private sector have cited several

significant barriers, including stringent business visa regulations, broken land customs stations, an absence of regional vehicle agreements, and ambiguous and imprecise NTBs.

On the other hand, nearly every state in South Asia is struggling with significant security issues, including extremism, insurgencies, separatist movements, civil unrest, and disputes arising from ethnic or religious differences. The largest state in the region, India, is dealing with similar problems in Nagaland, Kashmir, Punjab, and the eastern provinces of Mizoram and Assam. The annexation of Indian-occupied Kashmir and the recent Indian Citizenship Enactment have increased India's security concerns. Given Indian politics, federalism, and its secular proclamation in comparison to the Hindutva doctrine being adhered to, as well as the religious extremism that is still evident today, the state is expected to face increasingly significant obstacles. Speaking about Pakistan, despite past military operations, inefficient governance, and global geopolitical concerns, the country is dealing with economic crises, federal-provincial divisions, and extremism.

Afghanistan is at a crossroads where it must deal with political unrest, prolonged hostilities, ethnic and political splits, the overwhelming presence of foreign soldiers, terrorism, and socioeconomic collapse. Smaller states with weaker economies and monetary systems, like Nepal and Sri Lanka, also deal with internal conflicts. Although these tensions make integration more difficult, increasing economic cooperation can benefit all states by assisting them in addressing their respective internal problems and reducing their political disputes between states.

### 3.5 CONCLUSION

In its efforts to achieve economic integration in South Asia, SAARC encounters many obstacles. First, collaboration and the advancement of economic integration are hindered by geopolitical conflicts among member states, especially those between India and Pakistan. Second, insufficient energy supplies and inadequate transportation networks make it difficult for goods and services to be moved throughout the region effectively. Trade and investment restrictions are also brought about by member states' diverse economic policies and regulatory frameworks. Moreover, achieving equal economic integration is hampered by regional socioeconomic differences and uneven development levels. Institutional limitations and bureaucracy need to be improved within SAARC to hamper the implementation of agreed-upon initiatives. To solve these issues, promote deeper economic integration, and realise the region's full potential, persistent political will, regional cooperation, and institutional reform initiatives are needed.

Restrictive non-tariff barriers (NTBs) like price controls, pre-shipment inspection, non-automatic licensing requirements, sanitary and phytosanitary (SPS) standards, and technical trade barriers are some main obstacles to South Asia's economic integration. These NTBs make it impossible for states to gain from regional integration by severely discouraging trade and restricting business competitiveness. Furthermore, the ineffective customs procedures, high documentation requirements, lengthy delays, and expensive trading processes further impede economic integration among South Asian states. Another major obstacle to South Asia's economic integration is trade barriers for services. Trade in services is hampered by significant barriers, with additional equivalents to tariff rates for goods consistently exceeding 10% and reaching up to

70% in specific industries. In order to encourage regional integration and accelerate economic progress in the region, these obstacles must be removed.

In conclusion, although South Asia's economic integration faces many obstacles, there are also chances to get beyond them through regional cooperation and policy changes. South Asian states may enhance economic growth in the region and realise the full potential of regional integration by tackling these obstacles.

## **CHAPTER 4**

### **CONTRASTING SAARC AND ASEAN DYNAMICS**

#### **4.1 INTRODUCTION**

The primary goal of the SAARC, which was founded in December 1985, was to start the process of regional cooperation in the face of mistrust and conflicts. The idea was that this would create a dynamism all its own, allowing for the development of confidence, the resolution of disputes or at least their proper management, which would lessen their adverse effects and ultimately lead to regional economic cooperation. However, because of ingrained mistrust, varying security perspectives, and ongoing bilateral conflicts among the member states, the hopes that long-torn South Asia might finally be moving towards a cooperative framework are giving way to a growing sense of despair with the emergence of SAARC. Despite intense pressure from within the region and the ongoing changes in the global economy and international relations, SAARC still needs to establish a successful mechanism for handling intraregional issues. Additionally, the organization is plagued by ongoing issues that occasionally cause its operations to be paralysed. Many attempts to achieve the desired breakthrough still need to be realised.

The Association of South East Asian Nations (ASEAN), founded in the neighbourhood of South Asia in 1967, continues to be efficient in making headway in cooperative and economic endeavours, in contrast to the appalling performance of SAARC. Deep-seated mistrust and disagreements among the member states existed

when the ASEAN was founded. Furthermore, in the preceding years, the region had seen the collapse of conflict management and cooperation due to several factors, including the Indonesian policy of *Konfrontasi*<sup>15</sup> towards Malaysia (1963–1966), the Philippines' claim to Sabah, and Singapore's separation from Malaysia and its aftermath.

At one point, the disputes between the SAARC states and these other ASEAN states seemed equally unsolvable. However, through effective conflict management strategies, ASEAN countries have demonstrated remarkable effectiveness over the years in resolving intragroup conflicts and minimising their adverse effects on regional economic cooperation. More importantly, ASEAN has created a system of procedures and mechanisms for handling intragroup disputes over time. In the end, ASEAN decisively moved from hostilities to cooperative efforts that benefited both parties (Sabur & Kakir, 2000).

While SAARC took a functional approach to cooperation, prioritising areas where political concerns were least involved, ASEAN member states chose to collaborate in economic matters and the challenges in the field to be dealt with initially. Although the Charter listed economic growth and collective autonomy as goals, member states effectively began to cooperate in the economic sphere much later. However, regarding their operational characteristics, the first ten years of each group's economic cooperation are very similar. Before the Bali Summit 1976, ASEAN and other states had minimal economic cooperation. Similarly, until the South Asian Preferential Trade Arrangement (SAPTA) was adopted in 1993, SAARC made little progress

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<sup>15</sup> *Konfrontasi* (or Confrontation, 1963–1966) was Indonesia's response to the formation of the Federation of Malaysia, arising from the British decolonisation process in Southeast Asia. *Konfrontasi* involved armed incursions, bomb attacks and other subversive acts aimed at destabilising the states that were to be included in the Federation, namely, Singapore, Malaya, Sarawak, Brunei and North Borneo (now known as Sabah).



toward regional economic security. That is not meant to imply that in the early years, they did nothing at all. These associations first took initial moves in the direction of economic collaboration. The Association of Southeast Asia (A.S.A.) resolved to review all of its cooperation initiatives during its Second Standing Committee Meeting in 1968. Since critical facts were ignored, its executed programs had yet to be successful.

With economies as varied as those of Indonesia and Singapore, ASEAN had a population three times larger than A.S.A's. Due to its position and absence of natural resources, Singapore was compelled to pursue international investment actively. Like Indonesia, Singapore was worried about the impact of outside economic factors, but it also had faith in its ability to handle them. 1968, trade and industry accounted for about half of Singapore's G.D.P., compared to only roughly 30% in Indonesia. Indonesia prioritised import substitution as part of its economic development plan, while Singapore favoured export-oriented industrial development. With Singapore being the most industrialised state and Indonesia being the least, this tendency caused problems within the ASEAN (Kawai & Naknoi, 2015).

Economic cooperation grew slowly due to the disparities in member states' economic progress, which was made more difficult by political disputes and divisions. Other members of the 1968 Meeting on Commerce and Industry opposed the Philippines' proposal to create a common market and free trade area. The continuing conflict between Malaysia and the Philippines over Sabah made the situation tense. For nearly a year, this disagreement delayed all ASEAN meetings.

On the other hand, several economic problems were pointed out in the government of Bangladesh's inaugural proposal for regional cooperation in South Asia. This region controls a substantial portion of the global market for various goods, including cotton,

jute, and tea. Collaborative efforts lower advertising expenses and are more effective in export markets. Even in the early years, economic issues were discussed at yearly meetings, but these were not included in the final SAARC Charter. The First SAARC Summit Meeting resulted in the Dhaka Declaration, which called for an immediate restart of the North-South dialogue and highlighted the significant global setbacks to the economic development of developing countries. These included sharply declining prices for commodities, declining terms of trade, intensifying protectionist policies, soaring debt burdens, and declining flows of external resources, mainly subsidised assistance. The need for communal self-reliance as the foundation of development was again highlighted in 1987 during the Third Summit Conference in Kathmandu. Additionally, Bangladesh presented a motion to collaborate with international and regional financial institutions to grow and draw foreign funding. Nevertheless, members disagreed with this as some claimed it would have political consequences. Given that SAARC is in the same state, it would be essential to look into how ASEAN managed conflicts and took a leap of faith in adopting a successful process towards economic cooperation. To assess their applicability to SAARC, this chapter will delve into ASEAN's experiences managing and resolving disputes and obstacles in pursuing sustainable economic cooperation.

## 4.2 CONFLICT RESOLUTION

Launched in the middle of a great deal of mistrust and multiple interconnected domestic and interstate tensions among member states, both SAARC and ASEAN were influenced by the region's post-colonial socioeconomic and political-cultural growth dynamics and the legacy of colonialism. The interstate relations between or

among the member states of SAARC and ASEAN have been plagued by several specific factors, which are essentially the same: historical hostility, unresolved land and maritime boundaries, conflicting economic interests, sharing of common natural resources, and a turbulent process of nation-building that has resulted in numerous intra-state conflicts and their multilateral consequences. However, these variables' relative strengths, how they interact, and how they contribute to forming and maintaining particular disputes among these two groups have sometimes been different. While disagreements over marine boundaries plague ASEAN countries, disputes among SAARC countries over maritime boundaries remain dormant. Conversely, disagreements about the distribution of shared river flows are highly prevalent in SAARC, whereas they are nonexistent in ASEAN. However, there are many similarities between SAARC and ASEAN intra-group conflicts.

There were too many divisive topics within both SAARC and ASEAN, and member-state disagreements were excessive. Due to the perception that these issues were too delicate to discuss in the early stages of cooperative forums, conflict management was left off of the agendas of both organisations. Although exercising such caution was wise, the member states of both organisations could handle the fallout with a different level of caution.

Since no ASEAN mechanism was in place to resolve conflicts between member states, the Association was intentionally ignored, and disagreements were resolved unofficially. The member states frequently used bilateral negotiations to resolve disagreements. The disputing parties may specifically request and, outside of the ASEAN framework, involve a third party in the dispute as a mediator. An informal method like this could handle intragroup conflicts so well that ASEAN formally took on the role of conflict management and developed a formal structure for it during the

First Summit, which took place in Bali on February 23 and 24, 1976 (Alagappa, 1994). In an attempt to resolve controversial issues, SAARC leaders also made steps to initiate discussions and negotiations during the SAARC conferences. However, this may have minimal, if any, impact on the situation.

The question of why ASEAN was more inclined towards conflict management than SAARC is intriguing in this context. As a result of domestic political unrest and the threat of communism from across the border, ASEAN served as a focal point for its members. Poverty and economic deprivation were the primary causes of political instability, and this finding confirmed that the governments of ASEAN member states could more effectively and directly address social and political unrest if regional tensions were reduced through regional cooperation. The primary goal of this approach was to concentrate on achieving ambitious socioeconomic development programs that created a stake on the part of ASEAN members. Alternatively, the SAARC countries chose to channel mass complaints by creating chauvinism directed toward their neighbours, as they lacked socioeconomic development programs capable of addressing economic distress and the ensuing sociopolitical turbulence. This is still the most significant element influencing how the SAARC nations handle intragroup disputes.

Since the Association's founding, the member nations of ASEAN have gradually enhanced their cooperation and interaction. As a result, their security perceptions and the nature of their relationships have drastically changed, with a clear shift from conflict to collaboration. The factors that encouraged distrust and hostility between them have mostly faded. The apprehensions and conflicting security agendas carried over from the past are likely to continue the momentum that the regional cooperation process within the ASEAN framework has created. While some of the previous

security-related concerns still impact the relationship between them in the updated politico-security matrix, the political expression of these concerns and conflicting priorities is still adequately restrained within the bounds of widely recognised regional norms and restrictions.

The experiences of the ASEAN member states make it clear that the domestic environment was a significant factor in the dramatic change these nations' foreign policies underwent. The emergence of ASEAN was synchronised with the progressive initiation of extremely ambitious socioeconomic development initiatives by its member nations. They implemented ambitious programs in the late 1960s and early 1970s in response to socio-political unrest intensified by the communist threat from over the border and issues of underdevelopment, poverty, inequality, and deprivation. As nation-building progressed, increasing amounts of effort were needed to ensure this process was as successful as possible. Over time, this led to growing stakes in a friendly community. This was the primary cause of the ASEAN countries' self-control and willingness to handle bilateral disputes.

South Asia performed worse than South East Asia regarding socioeconomic underdevelopment, high concentrations of poverty, inequality, deprivation, and subsequent political unrest. Except for India at the moment, no SAARC state has ever demonstrated the vision to launch a socioeconomic development program of the same magnitude as those launched by ASEAN states. South Asian states thus started to lag behind more and more other nations in terms of socioeconomic development and standard of living. The procedure, which began in the 1960s, continues today. South Asia has presently lagged behind all of the world's major regions (Sabur, 2001).

### 4.3 COMPARISON OF ECONOMIES

Regarding per capita income, South Asia falls under the second poorest region of the world. With 25 per cent of the world's population, nearly 40 per cent of the world's absolute poor live in the region. More than any other emerging country or region globally, South Asia is predicted to grow by 5.8 per cent this year; this growth rate needs to be increased to satisfy the region's development objectives. Growth prospects are vulnerable to adverse factors, such as weak financial circumstances. The average government debt in South Asian nations was 86% of G.D.P. in 2022, which raised borrowing rates, increased default risks, and shifted credit away from the private sector. A further slowdown in China's economic growth and increasingly frequent and severe natural disasters due to climate change could impact the region's economy. In FY23/24, growth in India is predicted to stay strong at 6.3 per cent. Due to the robust recovery in tourism in both Nepal and the Maldives, the output is expected to increase by 3.9 per cent in FY23/24. The effects of recent currency crises are still felt in several of the region's states. In FY23/24, Bangladesh's growth is expected to decrease to 5.6% (Asian Development Bank, 2023). Pakistan's growth is expected to be less than the population growth rate in FY23/24, at about 1.7%. Following a sharp recession, Sri Lanka's economy is starting to show signs of recovery. In 2024, growth is predicted to reach 1.7%, following a 3.8 per cent contraction in 2023 (World Bank, 2024).

In South Asia, the level of human deprivation is enormous. Roughly 260 million people do not have access to health care; 337 million do not have access to clean

drinking water; and 830 million do not have access to even the most basic sanitary comforts (Haq, 1997). The list might be expanded infinitely, revealing the staggering incapacity of the South Asian governing class to confront the growth obstacles that have relegated the region to the bottom of the development league according to most development metrics.

Furthermore, to date, no South Asian state has demonstrated the vision to implement any development plan that could address issues such as misgovernance, poverty, inequality, deprivation, environmental degradation, globalisation, and, most importantly, the ensuing socio-political unrest, which poses a far greater threat to the future of the region than traditional security threats. This has complicated the process of economic integration and affected conflict and cooperation in South Asian regional politics. The socioeconomic downturn in South Asia and the ensuing socio-political unrest have pressured the ruling class to refocus widespread complaints. The most convenient ploy for the ruling elites in South Asia has emerged, as experiences indicate, in the form of public displays of indifference on issues of bilateral conflicts with neighbours and, on occasion, artificial escalation of such disputes to the point of reaching a crisis or even drifting towards war.

**TABLE 4.1: Real G.D.P. growth at constant market prices (per cent)**

Country fiscal year		Real GDP growth at constant market prices (percent)				Revision to forecast from April 2023 (percentage point)	
Calendar year basis		2022	2023(f)	2024(f)	2025(f)	2023(f)	2024(f)
South Asia region (excluding Afghanistan)		8.2	5.8	5.6	5.6	0.2	-0.3
Maldives	January to December	13.9	6.5	5.2	5.5	-0.1	-0.1
Sri Lanka	January to December	-7.8	-3.8	1.7	2.4	0.4	0.7
Fiscal year basis		21/22	22/23(e)	23/24(f)	24/25(f)	22/23(e)	23/24(f)
Bangladesh	July to June	7.1	6.0	5.6	5.8	0.8	-0.6
Bhutan	July to June	4.8	4.6	4.0	4.6	0.1	0.9
India	April to March	9.1	7.2	6.3	6.4	0.3	0.0
Nepal	mid-July to mid-July	5.6	1.9	3.9	5.0	-2.2	-1.0
Pakistan	July to June	6.1	-0.6	1.7	2.4	-1.0	-0.3

**Source:** World Bank Macro Poverty Outlook and World Bank staff calculations<sup>16</sup>

Therefore, the SAARC countries must implement radical economic development programs capable of reorienting national attention from politics to economics to set up a decisive shift away from conflict and toward a path of economic cooperation.

This would establish a substantial stake in a welcoming neighbourhood. Even with success in regional economic cooperation, as the ASEAN experience indicates, such a transition at the national level enables a regional grouping to handle intra-group tensions and create a peaceful regional order effectively.

<sup>16</sup> (e)= estimate (f)=forecast. G.D.P. is measured in 2015 prices and market exchange rates. Pakistan is reported at factor cost. National account statistics for Afghanistan are not available. To estimate regional aggregates in the calendar year, fiscal year data are converted to calendar year data by taking the average of two consecutive fiscal years for Bangladesh, Bhutan, Nepal, and Pakistan, as quarterly G.D.P. data are unavailable.



On the other hand, home to about 8.5% of the world's population, Southeast Asia's economy has historically and predictably grown at rates far higher than global and advanced economies. Southeast Asia's GDP per capita is US\$4,685 according to 2020 International Monetary Fund estimates, comparable to South Africa, Iraq, and Georgia<sup>17</sup>. Southeast Asian economies performed admirably in the years following ASEAN's inception. All economies saw G.D.P. growth during this time, while Malaysia and the Philippines saw slower development. Indonesia, Singapore, Thailand, and Vietnam saw the fastest increase. Early indications of improving export demand supported growth, a continuing recovery of the services sector, particularly tourism, and strong domestic demand, underpinned by stable employment prospects and falling prices. Southeast Asia's economy would rank fifth in the world if it were considered a single economic region, and given its predicted rapid expansion, its importance to the international economy can only rise. Southeast Asia, which accounts for 3.4% of the world's G.D.P., offers a fascinating region ranging from Singapore's highly developed society to Vietnam's fast-evolving middle class. It is only reasonable to assume that the region's strategic significance on the international scene will only rise given its sizable and youthful population and some of the fastest developing economies in the world.

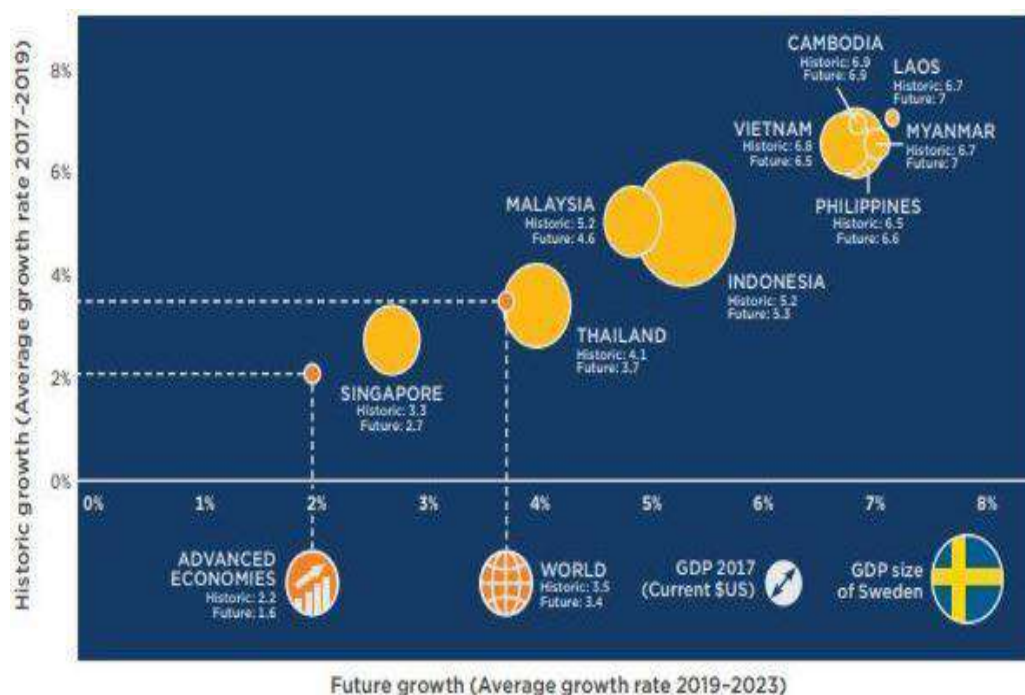
In 1967, ASEAN was established by Singapore, Malaysia, Thailand, Indonesia, and the Philippines and later joined by Vietnam, Myanmar, Laos, and Cambodia. Its objectives were to foster regional peace, cooperation, and mutual aid on issues of shared interest and to expedite economic growth, social advancement, and cultural development. As a result, ASEAN shares the same vision as the E.U. but has a

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<sup>17</sup> International Monetary Fund Data, 2023

different degree of integration—at least compared to what has been achieved thus far. Nonetheless, advancements are being made gradually, with the ASEAN Economic Community (A.E.C.) catalysing economic unification. ASEAN has negotiated free trade agreements (F.T.A.s) with major economies like China, India, Japan, Korea, and Australia in addition to its own internal F.T.A., known as the ASEAN Trade in Goods Agreement (ATIGA) (Business Sweden, 2024). Southeast Asia has prospered via trade with other areas and nations for ages due to its advantageous geographic location. The Strait of Malacca, which connects Indonesia, Malaysia, and Singapore, has been a major global trading route for centuries. While the reliance of each Southeast Asian nation on foreign trade varies, they all claim a similar commitment to further openness and integration both within the region and with global value chains. As a reference to the "Asian tigers"—Hong Kong, South Korea, Taiwan, and Singapore—which all attained high levels of economic development in the latter half of the 20th century through export-led growth with a high technology content, Indonesia, Malaysia, the Philippines, Thailand, and Vietnam have been dubbed the "tiger cub economies."

**Figure 4.1: Historic VS Forecasted G.D.P. Growth Rates; South East Asia, World and Advanced Economies**



Sources: I.M.F., World Bank, OECO

Despite Southeast Asia's aspirations to become more integrated regionally through ASEAN, it is essential to recognise its great variety. It may be challenging to envision ten states that are more diverse from one another from several angles. Regarding income, Singapore's G.D.P. per person exceeds Myanmar's by more than 40 times. The political systems that exist are autocratic and democratic. Economic structures vary from capitalism to socialism. Despite this variety, the ASEAN leaders are nevertheless dedicated to fortifying the alliance to advance the degree of financial integration. The advantages of greater integration and utilising one another's advantages exceed the dangers and drawbacks of protectionism and more intense rivalry.

#### 4.4 ASEAN'S APPROACH TO ECONOMIC INTEGRATION

The main political motives behind establishing the ASEAN process in 1967 were these nations' perceptions that regional cooperation was essential for security purposes, specifically to protect themselves from the perceived communist threat. Integration of the economy was not a top priority. The process of economic cooperation only began "modestly and selectively in ASEAN with the introduction of the P.T.A. (preferential trading arrangement) in 1977 and followed more ambitiously with the decision to form an Asian Free Trade Agreement (AFTA) in 1992." (Soesastro, 2005) The term "economic integration" was not even mentioned during the first ten years of its existence. Leaders of ASEAN initially decided in 1992 to finish AFTA in 15 years. However, later plans were changed to speed up the process to create an Asian Economic Community (A.E.C.) with a single market and a single production base.

Even though ASEAN has made great strides in promoting regional economic integration, agreements have not been implemented, and trade obstacles within the area have not been removed as quickly as anticipated. Even though the degree of integration attained in ASEAN has occasionally been referred to as "shallow integration," it has unquestionably advanced far more than SAARC. As a result of ASEAN's growth to include once-hostile neighbours like Vietnam and the apparent absence of political conflicts among its members, there has been a modest but steady shift towards greater collaboration across all levels, including monetary cooperation. After several member states were affected by the financial crisis of 1997–1998, the topic of monetary integration only started to receive significant attention. ASEAN

released the "Vision 2020" declaration in December 1997, outlining steps towards increased economic integration and regional cooperation in response to the crisis. The ASEAN summit in Hanoi the following year concluded an action plan that called for intensifying cooperation on money, tax, and other financial-related concerns, as well as strengthening the financial system in the region to sustain macroeconomic and financial stability. Rather than pursuing further monetary integration within, ASEAN has focused on monetary cooperation within a broader regional framework. The ASEAN member states have also advanced by focusing their commercial and financial cooperation on a larger territory. They worked together in the Chiang Mai Initiative 2000 to create a network of bilateral swap agreements among the ASEAN countries and a regional financing arrangement within the larger framework of ASEAN+3 (ASEAN member countries plus China, Japan, and the Republic of Korea). Since reaching this agreement, ASEAN+3 has looked into the possibilities of more extensive financial cooperation between its members, including creating an ASEAN Currency Unit (A.C.U.) and the potential for an ASEAN exchange rate system.

An agreement was reached in principle to create a self-managed reserve pooling mechanism governed by a single contractual agreement and follow a step-by-step procedure at the 10th ASEAN+3 Finance Ministers' Meeting in May 2007 to alleviate the region's immediate cash shortages and support the current global financial arrangements. Since the start of the global financial crisis, more work has been done to operationalise this reserve pool and reach an agreement among participating nations over their payments to the pool. Nevertheless, despite occasional discussions on creating an ASEAN or even more expansive East Asian monetary unit, no significant efforts will be made shortly to achieve this degree of monetary integration (Ramayandi, 2005).

Given the length of time and slow pace of ASEAN's economic integration, it is evident that SAARC is not yet prepared for a shared currency or an economic union. Instead, SAARC may benefit from ASEAN's experience guiding the organisation toward interim measures that eventually lead to deeper regional economic integration. There is no convincing economic justification for SAARC to consider a single currency now, according to the low levels of intraregional trade and total factor mobility, particularly labour mobility. Of course, it is often known that political commitments rather than merely economic considerations are the main forces behind initiatives towards currency unions or other forms of monetary cooperation. SAARC and ASEAN are similar in openness, notwithstanding the latter's higher intraregional trade. However, the main distinction is that SAARC needs a political commitment to substantial integration.

The only practical action in this situation is to investigate whether SAARC has an institutional framework supporting transitional measures towards more extensive monetary cooperation. The SAARCFINANCE network, an association of SAARC Finance Secretaries and Central Bank Governors, is already considered a similar institution for financial cooperation. In order "to identify, analyse and help SAARC face up to current global, financial and economic developments affecting the region," the network was established after the 1998 SAARC Summit in Colombo (Colombo Declaration, 1998, para. 21). At the subsequent summit in Kathmandu, the SAARCFINANCE network was acknowledged as an official body within the SAARC process (SAARC Council of Ministers, 2002, para.9). The SAARCFINANCE network has organised high-level meetings and information exchanges since its establishment. It currently meets with top officials from the finance ministries and central bank

governors to examine global economic, fiscal, and monetary trends that could affect the area on the outskirts of the annual meetings of the World Bank and the I.M.F. An extra meeting could occur once a year in a SAARC member state if necessary. Additionally, the network has established SAARCFINANCE units in each central bank to conduct research, conduct staff exchanges, and offer training on various topics.

When analysing the possibilities for increased financial cooperation, SAARCFINANCE's potential benefits must be considered. Studies conducted several years ago pointed to ASEAN's lack of institutions as a barrier to the region's consideration of a single currency. In this sense, SAARC is more developed than ASEAN since SAARCFINANCE's presence offers a foundational structure for deeper regional financial integration. In reality, SAARC might progress if the variations in political commitment are ignored and only the ASEAN experience is considered from the standpoint of structured monetary cooperation.

ASEAN Leaders decided to create an ASEAN Economic Community (A.E.C.) by 2020 during the Bali ASEAN Summit 2003, taking the region's economic cooperation one step further. With unrestricted access to capital, skilled labour, investments, services, and goods, the A.E.C. will function as a single market and industrial base. ASEAN members decided to make their common market more appealing to foreign investors in response to fierce competition, particularly from the developing Chinese market economy. They did this hoping that a unified ASEAN market with over 500 million people would maintain the region's appeal as a destination for foreign direct investment.

FDI into ASEAN hit US\$ 38 billion in 2005, above levels seen before the Asian financial crisis of 1997–1998. Moreover, Southeast Asian Trade Ministers decided in August 2006 to implement incentives to establish a single market similar to Europe by 2015. By 2015, the political unrest in Myanmar and its members' unwillingness to open markets for goods, including agricultural products, were no longer considered obstacles to the envisioned A.E.C. The Trade Ministers also decided that by 2012, all N.T.B.s, including license requirements, Q.R. codes, technical controls, and inspection procedures, will be eliminated. The revised Charter was accepted by ASEAN leaders in January 2007, establishing the group as a rule-based organisation.

#### 4.5 THE SOUTH EAST ASIAN ECONOMIC CRISIS

When the Southeast Asian economic crisis struck in 1997, things quickly changed. The sharp decline in the Thai baht's value against the U.S. dollar in the middle of the year caused a domino effect that mainly affected Indonesia, Malaysia, the Philippines, and Vietnam. In 1995, the average growth rate of Southeast Asian economies was 6.71 per cent, compared with a global average of 2.8%. Even the economies of Vietnam (8.8% growth), Laos (8.4%), Cambodia (5.2%), and Myanmar (4.2%) showed growth. Many ASEAN states had been impacted by the crisis during the ASEAN Ministerial Meeting in Kuala Lumpur in July 1997 since their economies had experienced devaluation. Despite its issues, ASEAN remained an effective political and economic force in the region. The financial crisis of 1997 made it obvious how interdependent these nations are and how urgently they must strengthen their cooperation efforts.

Following the economic crisis, the Second ASEAN Informal Summit convened in Kuala Lumpur in December 1997, wherein the ASEAN Vision 2020 was approved,



and action plans for its implementation were formulated. The first of several programs, the Hanoi Plan of Action (H.P.A.) 1998, was designed to last six years and had progress reviews every three years (Dent, 2003). The H.P.A. recommended strengthening ASEAN financial systems and surveillance procedures to preserve regional macroeconomic and financial stability. It encouraged more cooperation on financial, tax, and insurance problems and the liberalisation of the financial services industry under the ASEAN Framework Agreement on Services. It investigated the possibility of creating an exchange rate and currency system for ASEAN. Additionally, it was agreed to improve trade facilitation in customs by simplifying the process, extending the Green Lane to include all ASEAN goods, and putting in place an ASEAN Harmonized Tariff Nomenclature by 2000. It also demanded that the ASEAN Investment Area framework agreement be implemented.

Southeast Asian states continued to be economically fragile in 1999, even with their robust recoveries, and more needed to be done to prevent any future crises, according to a report by ASEAN's "surveillance" group. The report acknowledged that the region had recovered due to a robust global economy and the U.S.'s continued demand for Asian goods. However, it also issued a warning, noting that bank and business restructurings in ASEAN states had been poor and that there had been inadequate investment recovery. Member states moved up the deadline for eliminating tariffs from 2015 to 2010 at the 1999 Summit. One crucial step was the acceleration of free trade within Southeast Asia. In 1999, the ASEAN economy had a growth of 4.6%, following a decrease of 4.4% in the previous year.

Exports from the Asia-Pacific region rose as well, rising 6.4% from US\$ 322.8 billion in 1998 to US\$ 343.4 billion in 1999. Southeast Asian states expressed concern in

2001 due to the declining demand for goods from the U.S. and the declining value of the Japanese yen, indicating the global economy's interdependence. The ASEAN-6 states realised that enlarging the organisation to include the Southeast region would have political and economic advantages. This would boost the Association's market size, legitimacy, and efficacy in addressing local concerns and its political and economic standing in the global world. ASEAN's leaders were concerned that a two-tier regional forum may emerge simultaneously as the organisation expanded during the second part of the 1990s. The original ASEAN members believed there could not be a "development gap" between new and old members to preserve ASEAN's influence in the international venue. New members would, therefore, need extra care. In order to ease newcomers to the CEPT scheme by adapting their requirements and allowing them an entire decade to complete the tariff reduction process, the founding members of ASEAN allowed Laos and Myanmar until 2008, Cambodia until 2010, and Vietnam until 2006 to join the AFTA. By 2003, the initial AFTA signatories had reduced their tariffs to 0–5% on 99.6% of the items. Trade among ASEAN nations has improved over the past 20 years of industrialisation. AFTA's delayed implementation was caused mainly by member states' demands and doubts about lowering tariffs on specific goods. When Malaysia asked for the trade liberalisation of automobile products to be postponed until 2005, Thailand threatened to request a similar postponement for palm oil. As planned, the Philippines declined to reduce petrochemical tariffs. Textile makers in Indonesia also requested government protection.

#### 4.5 ECONOMIC INTEGRATION PROJECTS UNDER ASEAN

An expert panel was established at the Economic Ministers Meeting in March 1976 to investigate the possibility of developing large-scale industrial plants under ASEAN's administration. These initiatives included the manufacturing of phosphate in the Philippines, soda ash in Thailand, diesel engines in Singapore, and urea in Indonesia and Malaysia. The massive ASEAN Industrial Projects (A.I.P.) required US\$ 300 million in investments. The host state subscribed 60% of the stock, with the remaining 40% being split among the other states. Even with this, the A.I.P. program was deemed excessively ambitious and could have provided more success. Even after the agreement had been reached, there were still many issues with project implementation. One needed more funding and technical assistance. Japan gave one million dollars, but no additional loans were forthcoming. Only the area projects were carried out of the five original projects. Other factors included the low level of private sector participation and the unwillingness of several ASEAN governments to work on the projects they were assigned.

Another program, ASEAN Industrial Complementation, focused on privately owned small businesses that were already well-established. Its primary goal was to encourage and facilitate trade and links within industries. However, this idea did not work out like A.I.P., primarily because of the tedious approval and selection procedure.

The establishment of ASEAN Industrial Joint Ventures in 1981 was another project by ASEAN that focused on economic integration in the region, which required the involvement of a minimum of two member states. This initiative involved active participation from the private sector. Combining financial and technological resources promoted the formation of industrial joint ventures. It was anticipated that multinational companies would also take part in this plan.

In February 1977, a deal on ASEAN Preferential Trade Arrangements (P.T.A.) was agreed upon in Manila. The Philippines and Singapore supported a general decrease in pricing. Differences also emerged here, with Indonesia resisting the proposal until an item-by-item method was adopted. An Indonesian proposal was agreed upon at the next Economic Ministers Meeting, requesting each member to provide fifty products for preferential trading and quarterly Committee on Trade and Tourism sessions. Two thousand three hundred twenty-seven products were agreed upon for preference exchange in the first round, with 71 products agreed upon by 1979 (Chhibber, 2007). The P.T.A. began with voluntary offerings from members and gradually transitioned to an inclusive strategy wherein automatic preferences were granted based on specific import value limits. The P.T.A., however, was also a failure because the participating products were not exchanged between the ASEAN member states. The Philippines suggested an external single tariff or customs union and gradually lowering intra-ASEAN tariffs at the 1986 ASEAN Manila Economic Ministers Meeting. Indonesia rejected this because they desired no deadlines. Because it did not wish to increase its external tariffs, Singapore was also against a customs union. A customs union is not desirable for ASEAN members due to low volumes of intra-ASEAN commerce (about 20%) and a firm reliance on external markets.

The ASEAN Free Trade Area (AFTA) was signed in 1992 in Singapore during the Fourth ASEAN Summit Meeting (MacLean, 1996). The goals behind the formation of AFTA were the following:

- The desire of ASEAN to maintain its status as a significant organisation in the face of emerging new regional organisations.

- Changes in the global political economy during the 1980s and the growing influence of business interests all through the ASEAN region.

High tariffs and taxes on traded goods were eliminated as part of AFTA, and Q.R.s and other N.T.B.s were phased out. The deadline for finishing the process of transferring to a Common Effective Preferential Tariff (CEPT), harmonising standards across ASEAN member states, removing obstacles to international investment, and conducting macroeconomic consultations was advanced by the ASEAN Economic Ministers in 1994.

By 2003, members of CEPT reduced tariffs on goods originating in the region to a range of 0% to 5%. For a product eligible for these special tariffs, at least 40% of its value must come from the ASEAN region. CEPT offers two types of tariff reductions: standard and fast track. 92% of items were part of the CEPT program by the end of 1994. The procedure was facilitated by the ASEAN Economic Ministers Meeting that took place in September 1994 in Thailand. The Twenty-ninth ASEAN Ministerial Meeting, which took place in Jakarta in 1996, reported that intra-ASEAN CEPT product exports increased by 21% in 1995, from US\$ 49.1 billion to US\$ 59.3 billion. At this meeting, the private sector was asked to provide trade facilitation measures, such as industry-specific projects and development programs for small and medium-sized economies. The ASEAN Foreign Ministers also received the ratification of the Basic Agreement on ASEAN Industrial Cooperation, which expanded the parameters of the region's economic integration.

In the early 1980s, Thailand, Malaysia, Indonesia, and the Philippines had import substitution programs. The issue with the P.T.A. was that each state protected its internal market for its industry, despite its appeal since it provided a bigger market to help local industries. The economic downturn of the early 1980s, the global debt crisis, the U.S. government's adherence to protectionist policies, and the recession that followed the short security period of 1982–1983 were significant problems for the ASEAN member states. Furthermore, ASEAN needed to increase exports and sustain foreign exchange profits since international financial institutions were growing more robust and had more influence over the internal affairs of borrowing governments. Moreover, manufactured commodities accounted for 61.3% of intra-ASEAN trade in 1990 compared to 28.2% in 1980. Multinational companies were a significant factor in this transformation. After adopting a growth strategy driven by exports and supported by foreign direct investment (FDI), ASEAN sought to maintain its competitiveness (Bowles, 1997).

#### 4.6 LESSONS FROM ASEAN

The enduring significant power-small power dynamic is among the specific problems that continue to be the primary causes of mistrust and the ensuing differences in the economic integration of SAARC member states. India's inherent supremacy in the region and New Delhi's occasional attempts to convert that dominance into an enforced one remain at the issue's core. The asymmetry of power in the area is an unchangeable objective reality. The way that India views its neighbours and vice versa can be altered. ASEAN's experience in handling a similar phenomenon can be used as guidance.

At times, Indonesia's policies toward its neighbours have been even harsher than India's. However, ASEAN may find a middle ground where Indonesia's regional aspirations and ensuing security issues could be considered. Indonesia's contribution to this area was crucial, especially regarding the political wisdom and vision its leaders showed. Indonesia deliberately pursued a policy of becoming a constructive partner instead of its previous status as a regional troublemaker. In particular, Indonesia showed great caution while handling economic disputes to ease its ASEAN members' long-standing worries regarding Jakarta's hegemonic intentions. Political self-denial on Indonesia's side provided ASEAN with an incredible political base and substantially contributed to normalising the region's economic integration.

In the SAARC framework, India playing a comparable role will probably have the same outcomes. Positive signals in this area included the policy adjustments made by India, its attempts to replace the India Doctrine with the Gujral Doctrine, and its attempts to take a more diplomatic approach to disputes with its neighbours. The establishment of India's new policy towards Southeast Asia is still in its early stages. Meanwhile, it is still being determined how far the administration would or could go to resolve the disputes with the neighbours. The forces and variables that support such a policy continue to have varying effects. Developing elite cooperation that supports the existing strategy is essential to making it long-lasting. The natural desire of India to be in charge of regional issues would make this a challenging endeavour for the future. Therefore, it is still being determined whether it will force India to adopt the same political self-denial stance as Indonesia does across the ASEAN. Nevertheless,

this activity is necessary to break through the current distrust and hostility in the SAARC region.

Similarly, the smaller South Asian states must reevaluate their approaches to India. The realities of South Asia and the ASEAN experience indicate that significant sacrifices must be made by all parties involved to manage interstate disputes and their eventual settlement. Smaller South Asian states must figure out how to accommodate some of India's regional ambitions while also applying pressure on India for concessions. That does not require giving up the states' strongly upheld national sovereignty. Even ASEAN's smaller neighbours have willingly given in to some of its regional ambitions without compromising their main issues. Given this situation, the smaller, more alert South Asian states must deal with India more innovatively.

Both groupings have carefully maintained their respective organisations above regional concerns concerning intra-group and economic conflicts without giving them any official responsibility in conflict management. Although ASEAN officially took on these responsibilities in 1976 (Sabur, 2003), dispute resolution within the organisation is still primarily done on an informal basis today. In reality, though, there were significant differences in how these two groups handled intragroup conflicts regarding matter and style. ASEAN member states frequently used forums to speak out and resolve their disputes. Such innovation has yet to be observed in the SAARC context. Such innovative solutions from its members are essential to the grouping's successful operation, where the management of intragroup conflicts and the cooperative process are kept tightly apart.



In contrast to ASEAN, bilateral talks within SAARC are relatively formal and widely discussed. The leadership is under great tension just by the process itself since it must constantly consider its audience. The sides are highly attentive to one another throughout the entire negotiating process. This frequently limits the leadership's capacity to reach even small compromises on problems about trade and bilateral conflicts, which may be justified in light of the country's long-standing interests. However, the SAARC member states might benefit from the ASEAN's approach to informal and, when necessary, behind-the-scenes conversations at many levels. It is feasible to establish multiple communication channels among the SAARC members to carry out informal or semi-official negotiations, notwithstanding some of the previously noted challenges. These discussions provide a channel for more openly expressing one's opinion and improving mutual understanding of perspectives. These conversations, conducted over time and through various possibilities, would increase understanding of one another's condition and eventually help reduce disagreements on the bilateral dispute issues. These procedures may also significantly increase the effectiveness of formal meetings and discussions by reducing some of the pressure on them. To enhance the current negotiation culture, the too-cautious and watchful approach of most SAARC states must be more inventive and progressive.

In contrast to ASEAN, South Asia has more intra-group conflicts and apparent disparities between the opposing sides on most of these topics. As such, they will last longer than the ASEAN ones. Under the current circumstances, understanding how to resolve disputes through practical conflict management techniques is more critical for SAARC states than ASEAN states. However, some bilateral disputes in the SAARC area affect some countries' survival imperatives or critical issues, which call for prompt resolution. The disagreement between Bangladesh and India around the

distribution of Ganges water is one example of such a problem. Under the current conditions, SAARC, like ASEAN, must also institutionalise its intragroup disputes in line with its own goals. Some problems can wait until later, while more urgent ones could be brought forward immediately for an early resolution. This would lessen a significant load on the conflict management process and help systematise disputes for their priority-based settlement, which would pave the way for the region's economic integration.

Like the conflict process, economic cooperation develops a unique dynamic at some point that is challenging to cease. This is true because both processes provide the emotional and psychological foundation and the required dynamics for their survival. As a result of the foundations that ASEAN has laid during its transition from conflict to cooperation, the process of regional cooperation operating under its banner has become sustainable. SAARC cannot accept anything less. However, ASEAN's accomplishments result from constant labour during a challenging and occasionally even violent phase of change. Given the existing challenges and the forces and circumstances that are maintaining them, South Asia's shift from conflict to economic cooperation is likely even more challenging than that of ASEAN. Thus, South Asia will need to work tirelessly and develop extreme patience over an extended period to accomplish its goals.

Regarding managing economic integration among member states, SAARC can draw inspiration and knowledge from ASEAN's extensive experience handling the same. This includes ASEAN's highly skilled and discrete diplomatic practices and its effective conflict management mechanism. This must be considered, though, because, despite specific shared historical experiences, socioeconomic experiences, and

political and cultural ties, there are also significant political, diplomatic, and economic disparities between the two regions. Thus, while the ASEAN's experiences are certainly worth considering, the SAARC states will need to develop a practical system of their own for managing economic integration and come up with suitable diplomatic strategies through collaborative efforts, keeping in mind the current geostrategic, socioeconomic, and political constraints in the region. This is still a very challenging task. It would take continuous effort and perseverance from the member states, a great deal of creativity and innovation, and strategic planning and trade expertise to succeed. In this sense, the region's leadership will play a critical role in helping South Asia transform from a region ravaged by aggression to an economically integrated one. In particular, success will be measured by the SAARC's capacity to project a long-term vision for the future and exhibit wisdom and ability.

#### 4.7 NATURAL ECONOMIC TERRITORIES (N.E.T.s)

The phenomena of N.E.T.s (Jordan & Khanna, 1995). It is especially well-suited to the Asian setting, where there is a strong preference for informal agreements over legally binding treaties and instrumental changes rather than radical systemic changes (Amos A Jordan, 1995). States can also experiment with working together through N.E.T.s, although they proceed cautiously given the region's diverse socio-political systems, complicated security dynamics, and varying levels of economic growth.

- Indonesia–Malaysia–Singapore Growth Triangle: Southeast Asia's oldest and most advanced N.E.T. This economic triangle, also referred to as SIJORI (Singapore–Johor–Riau), features the transfer of trade from Singapore to Johor

and Batam. These sectors, including tourism, span from low-tech to high-tech and use Singapore's infrastructure and administrative knowledge.

- **Indonesia–Malaysia–Thailand Growth Triangle:** The three nations in question requested that the Asian Development Bank (A.D.B.) conduct a feasibility analysis of the region's economic possibilities. The three central governments, who seek to connect the more industrialised region surrounding Penang in northern Malaysia with the surplus labour and agriculture-based economies in Sumatra and southern Thailand, view the development of each sub-region as critically important.
- **The Golden Quadrangle:** This includes the border region that links western China, Myanmar, Thailand, Laos, and Cambodia. Here, local business owners with similar ethnic, cultural, and historical connections are engaged in successful trade.

Singapore has bilateral free trade agreements (F.T.A.s) with the U.S., Japan, Australia, New Zealand, and the European Free Trade Association. It had already signed a similar contract with Mexico. Many ASEAN members are concerned that these free trade agreements could weaken the AFTA and make it more difficult for ASEAN to negotiate with other important allies like China and Japan in the future. Nonetheless, the Singaporean government insists that its free trade agreements are meant to enhance rather than replace regional processes. Singapore's innovative free trade agreement (F.T.A.) served as a model for other Asian nations and established the nation's position as the policy leader for most of East Asia and ASEAN.

Furthermore, the benefits of free trade agreements (F.T.A.s) and their global expansion pressured other ASEAN members to adopt a more positive outlook on the state of affairs. In December 2002, Malaysia's former prime minister, Mahathir bin Mohamad, declared the country would open free trade relations with Japan. The same year, President Gloria Arroyo of the Philippines suggested an F.T.A. with Japan.

On the other hand, Nepalese officials proposed an agreement that called for sub-regional cooperation during the 1996 SAARC Ministerial Meeting in Kathmandu. The World Bank launched the South Asia Development Triangle with a program for transboundary development cooperation, encompassing most of the Ganga-Brahmaputra-Meghna basin and covering the eastern and northeastern parts of India, Bangladesh, Nepal, and Bhutan. The World Bank was eager to support ASEAN-style cooperative ventures in South Asia. The Asian Development Bank (A.D.B.) has extended an offer of assistance and resources based on its conviction that productive collaboration within this sub-region can provide substantial benefits, namely in terms of joint ventures for hydropower and other forms of infrastructure development. The four foreign secretaries of SAARC met in 1997, renaming the program the "South Asia Growth Quadrangle" and agreeing not to include it under SAARC. While Sri Lanka, Pakistan, and the Maldives thought that forming sub-regional groupings could negatively impact SAARC, Bangladesh has long held this opinion. At the Malé SAARC meeting, it was decided to consider sub-regional cooperation exclusively in line with Article 7 of the Charter, which permits cooperation between two or more states but not necessarily between all SAARC members, in light of these concerns. In order to get around the unanimity condition and prevent any one-member state from imposing a veto on all regional cooperation, SAARC permits several less-than-total regional groupings.

#### 4.8 RELATIONS WITH EXTRA-REGIONAL ASSOCIATIONS AND STATES

The most intriguing part of ASEAN collaboration in economic integration is how they handle other governments or groups equally despite different points of view. Even if these disagreements occasionally surface, members often display self-control in favour of a consensus reached through consultations. In order to establish shared policies and engage in trade and tariff-related negotiations with the European Economic Community (E.E.C.), the Special Coordinating Committee of ASEAN Nations (SCCAN) was established in 1972. SCCAN received assistance from the ASEAN Brussels Committee, which is comprised of authorised ASEAN ambassadors to the E.E.C.

Particular attention should be paid to the ASEAN Dialogue Partner meetings with the US, Canada, Australia, New Zealand, the E.E.C., and Japan. The foundation of ASEAN's economy is its links with the U.S. and Japan. ASEAN nations have expressed concern over the US-Japanese bilateral trade imbalance and the resulting trade policy disputes since the late 1980s. If the U.S. imposed protectionist obstacles on Japanese exports that originate from offshore plants like those in ASEAN states, this conflict may have harmed them. Without neutralising flows from other countries, especially the U.S., ASEAN worries that it will increasingly rely on Japan and have less negotiating strength regarding foreign investments, trade, and technology transfers. Several issues have arisen between the U.S. and ASEAN due to U.S. trade policy toward developing nations. The ASEAN member states view the U.S.

Association of Market Access with human and labour rights, democracy, the environment, and intellectual property rights as unjustified and politicised meddling in internal affairs. They see it as just another example of industrialised states engaging in protectionism.

In addition, tensions between the U.S. and ASEAN arose during the financial crisis in Southeast Asia. Members of ASEAN felt deceived since the U.S. blocked aid from Thailand despite pressuring ASEAN nations to open their capital markets. Japan participated in the Miyazawa initiative by offering Thailand and Indonesia I.M.F. packages and bilateral support to the impacted economies. It also suggested creating the Asian Monetary Fund, which was expected to be funded with \$10 billion.

China was a helpful and accountable ally during the South East Asian financial crisis. It did not devalue the yuan throughout the crisis and promised US\$1 billion to assist Thailand. However, China's admission into the W.T.O. simultaneously increased the ASEAN states' concerns about economic competition from China. On the other hand, China proposed the ASEAN–China Free Trade Area (ACFTA) to assure ASEAN about its long-term friendliness and interest in Southeast Asia. China benefited politically and economically from this. China started expanding quickly as a market for ASEAN food and raw material exports and as an exporter to ASEAN member states. ASEAN and China increased their investment ties as well. China and ASEAN agreed to establish a free trade area in ten years at Brunei in 2002. November 4, 2002, in Phnom Penh, saw the signed Framework Agreement on Comprehensive Economic Cooperation between ASEAN and China.

China and ASEAN decided to eliminate tariffs on early harvest goods, primarily agricultural commodities, for three years beginning in January 2004. Within days after this agreement, the U.S. offered the Enterprises for ASEAN Initiative (E.A.I.) to oppose the Chinese, granting ASEAN governments broad access to U.S. markets. Similarly, in November 2002, Japan and ASEAN signed the ASEAN-Japan Comprehensive Economic Partnership. Additionally, India offered to discuss the completion of an ASEAN–India Free Trade Area in ten years. The financial crisis that shook Southeast Asia brought attention to the interdependence of the region's states. Meetings were regularly agreed upon by the heads of state and government of ASEAN, China, Japan, and South Korea in Hanoi in December 1998. The foundation for collaboration in liquidity surveillance, self-help and support systems, and global financial reforms was developed during the May 2000 conference of the ASEAN Plus Three Financial Ministers in Chiang Mai, Thailand. The extension of the currency exchange agreement, named the "Chiang Mai Initiative," summed up South East Asia's commitment to advancing regional cooperation. Through this agreement, Southeast Asian states experiencing a crisis now had access to short-term foreign exchange support (Nabers, 2003).

Members of SAARC should similarly benefit from the dynamics of globalisation. 1986 Islamabad hosted the First SAARC Ministerial Meeting on International Economic Issues. In order to improve the operation of the SAARC Secretariat and its regional centres on agriculture and meteorology (Dhaka), the European Commission and the SAARC Secretariat have signed a Memorandum of Understanding (Area of Cooperation) that includes information sharing, staff training, and technical assistance, including funding for specific programs. The Japanese government has provided funds to form the SAARC-Japan Special Fund. In 1995–1996, US\$ 200,000 and US\$



300,000 were allotted for Component I, which dealt with cultural events, and Component II, which dealt with technical research, meetings, and seminars connected to promoting economic relationships with SAARC countries. Additionally, the U.S., China, Japan, Korea, and the European Union (E.U.) were all present as observers at the Fourteenth SAARC Summit, along with Afghanistan, a new member.

#### 4.9 CONCLUSION

Similar issues existed initially as intraregional trade expanded in the ASEAN and SAARC regions. The economies of the ASEAN region, except Singapore, which exports primary goods to developed nations, were incompatible and had varying degrees of growth. Nonetheless, ASEAN states have succeeded in developing complementary industries and are now exporters of industrialised goods. The least developed states in the SAARC region continue to believe that more intraregional trade would not be as advantageous as other developed states due to differences in the individual states' economic development, with India being the most developed.

Furthermore, non-tariff obstacles like import quotas and licensing are an integral part of initiatives to protect domestic sectors in both the SAARC and ASEAN regions. These are the primary barriers preventing intraregional trade from growing. Initiatives like AFTA have gradually removed these obstacles. Another barrier to intraregional cooperation in South Asia is inadequate communication and transportation infrastructure. However, political issues are the primary barrier to regional economic cooperation in South Asia. Setting SAARC members apart from the ASEAN region results from political disagreement and a need for more political resolve to enhance

economic cooperation. Members of ASEAN do voice their disagreements, but they do not go so far as to undermine the organisation itself since they value the international recognition that ASEAN has granted them. SAARC member states can follow ASEAN's lead if they take note of the cooperative outcomes and stay clear of its flaws. Interaction between SAARC states will increase through cooperation in the service sector, just as it did with ASEAN states. In contrast to SAARC, where 85% of external funding still comes from official channels, 83% of external funding in Southeast Asia comes from private capital (Chibber, 2007). In order to deal with the area as a whole, SAARC should also be open to possible investors. SAARC countries can no longer afford to be marginalised in the current era of globalisation.

## **CHAPTER 5**

### **SAARC AND NEW SOUTH ASIA**

#### **5.1 INTRODUCTION**

The Maldivian government selected "SAARC Summit 17: Building Bridges" as the theme for the 17th SAARC Summit, which took place in the Maldives in November 2011. The theme was chosen as an innovative idea to connect SAARC's past, present, and future without dismissing its accomplishments during the previous 26 years (Shifau, 2012). The solid base upon which SAARC was founded today must create connections with fresh perspectives, overcome the region's obstacles, and transcend its customary setting. To connect SAARC to more prominent Asia and the rest of the globe, new bridges must be constructed, and internal borders and barriers must be removed. In addition to establishing connections with observers and other actors outside the region, SAARC must accelerate its economic integration. Creating adequate transportation and communication networks is essential to enable rapid population mobility and promote trade throughout Asia and beyond. Expanding networking with other regional blocs and connecting to global emerging economies will help the region thrive. However, the region's economy will thrive.

Building a bridge to the Far East and South East Asia and expanding regional trade beyond South Asia would benefit both South-South cooperation and regional trade. Expanding SAFTA to include China and Myanmar will allow trade to increase significantly in the region, benefiting South Asia on a large scale. (Islam, 2018) As a

result, even while supporting and fostering intraregional trade is critical, SAARC may also need to give interregional trade and involve observers in trade ties a significant thought. Research should also be done by SAARC on the growth of industries that might be created jointly and have the potential to compete globally as a more assertive regional economic bloc.

The future direction of SAARC's interaction will still depend on economic cooperation. Nonetheless, it would be more beneficial for SAARC to broaden and deepen economic cooperation outside of SAARC. SAARC must discard its closed-door policy <sup>18</sup> and instead develop open relations with international organizations and players outside the South Asian region to expand its prospects. In addition, the interest expressed by Observers and cooperating organizations in joining forces with SAARC in all economic and developmental initiatives ought to be transformed into worthwhile projects. While the SAARC agenda is massive, it is essential to the development of South Asia. To accomplish economic integration goals, SAARC must broaden its horizons, reassess its strategy, and move effectively with the flow of the world economy.

## 5.2 CHINA'S MEMBERSHIP IN SAARC AND BRI

Applying the logic of regional institutionalism, SAARC still needs to create a robust regional network in South Asia, with the strategic rivals India and Pakistan being comparable as the primary destabilizing factor in establishing the regional institutional

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<sup>18</sup> closed-door policy within SAARC could lead to a more transparent, accountable, and effective organization that is better equipped to address the diverse challenges facing the South Asian region.

nexus. China's entry into SAARC represents a turning point in the regional model of South Asia, and this has been a significant source of concern for India, which views China's entry as a gateway to South Asia and, more importantly, as an opposing threat to India's regional supremacy.

Granting China full membership status is one of the significant concerns that SAARC is dealing with and has been a frequently debated item on the agenda at SAARC summits. At the 2005 Dhaka Summit, China joined SAARC as an observer member through the efforts of Bangladesh, Pakistan, and Nepal (Jash, 2016) while Afghanistan, Bhutan, India, and the Maldives strongly rejected the proposal. China has since made compelling arguments for full membership, pointing to the region's physical proximity, trade connections, political exchanges, and historical and civilisational ties. China's aggressive campaign for membership has heightened India's strategic concerns. India is concerned about how China uses its cooperative relationship with other South Asian nations to play the political card. This was evident at the 18th SAARC Summit in 2014, which took place in Kathmandu, where China's pursuit of full membership overshadowed the primary regional discussions. Nepali diplomats and media led China's vigorous pursuit of full membership, and was further supported by Pakistan's policy declaration supporting the promotion of observers' status within SAARC. In expressing its strong opposition, India prevented China's aspirations by requesting observers to back regional economic initiatives in exchange for dialogue partners. Thus, by introducing the quotient of "dialogue partners," India challenged Pakistan's logic of elevation by referring to observers as "peripheral." India worries that China's entrance may undermine SAARC's operational structure's consensus-driven methodology and hamper its future goals (Kumar, 2015).

Notably, China and India are fighting each other in the SAARC, and this push-pull force impacts the institutional status quo. It is evident that even with solid opposition, India's fear of China does not hold the ability to prevent China's ambitions. China entered the region through active diplomacy with other SAARC member states, even facing fierce opposition from India. China has been able to strengthen its position through the use of proxies, first with Pakistan and then with other states in the area like Bangladesh, Sri Lanka, and Nepal. China is a better option than India because of the economic pattern, which shows that China is leading South Asia's economy while India's protectionist inclinations have given way.

In light of these political realities, it's interesting to observe that, in contrast to India's opposition to China's SAARC membership, other South Asian states enthusiastically support China's pursuit of full membership. In this parallel, the question remains: "How long can India tolerate the resistance to China's full SAARC membership?" Given the growing Chinese influence in the region, India's resistance is brief because trade relations are crucial to China's engagement in South Asia. China is the region's top trading partner with Bangladesh, Pakistan, and India, and it is the second largest to Nepal and Sri Lanka. With its "all-weather" partner Pakistan, it has a free trade agreement; it is now negotiating one with Sri Lanka and the Maldives. Additionally, under the Asia-Pacific Trade Agreement (APTA), it has enjoyed advantageous regional trade arrangements for several goods with Bangladesh, Sri Lanka, and India since 2001. China's imports from South Asia climbed from \$1.9 billion in 2000 to \$22.6 billion in 2012, while the country's trade with the region rose significantly from \$5.7 billion in 2000 to \$93 billion in 2012.

It is significant that from the mid-2000s, China has increased its financial flows to the region through loans and grants. China has surpassed other traditional donors to South

Asian states, including Pakistan, Sri Lanka, and Bangladesh. China is mainly linked with significant infrastructure projects like ports, highways, bridges, and power plants. It has also overtaken India as the primary source of funding for projects in the majority of the smaller South Asian states. India now faces a challenge due to these variables' substantial contributions to the emergence of the Chinese economic order in South Asia. From this perspective, South Asia's regional matrix gains a new dimension due to the competitive presence of China and India in SAARC. First, a determined Pakistan will disregard India's interests and work harder to include its greatest friend, China, in the regional framework. India, meanwhile, is apprehensive about joining other South Asian states given the escalating hostilities, like the recent political rift between Nepal and India. Thus, the question of how long India can obstruct China remains unresolved.

China may play a different card while dealing with India in South Asia. Here, diplomacy must have its proper place. China could assist by acting as a trustworthy intermediary in mending the divide between Bangladesh, Nepal, and India, as well as between India and Pakistan. China might be more outspoken in expressing its desire to solve economic and trade conflicts. For India to further integrate itself with the South Asian economic integration process, it might be encouraged to make amends with its neighbours. Perhaps the guiding principle of all SAARC member states' foreign policy is "prosper thy neighbour," particularly for South Asia. The dynamics between India, Pakistan and Afghanistan are crucial since geopolitics always seems to raise its ugly head and undermine the peace in the region. In the Bay of Bengal and South Asian areas, China might be wise to cooperate with the US and India. Conversely, India might be able to accept China. The pie may be split in a relaxed atmosphere on a win-win basis.

China is using the Belt and Road Initiative (BRI) as a significant tactic to improve cooperation and communication with neighbouring countries, particularly South Asian countries. Being a massive infrastructure, trade, and connectivity initiative, the BRI has spread beyond Eurasia and Southeast Asia to countries including South Asia, the Middle East, and numerous regions of Africa (Chatterjee, 2022). Following its implementation, the BRI has improved the trade balances of Pakistan, Afghanistan, and the Maldives and stabilised the foreign direct investment landscape. However, the influence of the BRI in South Asia is not limited to China's geopolitical standing or economic gains; it also depends on how recipient states view China and how they respond to the program.

South Asia regards the BRI as a constructive Chinese endeavour that offers substantial economic advantages. It can also enhance favourable perceptions of China, enabling recipient states to cooperate more with China. Recipient states must, however, manage the BRI to further their internal agendas. They are likely to continue to embrace increased Chinese investment if they believe the BRI will help them achieve their declared economic objectives. On the other hand, it may cause recipient states to hesitate and ultimately hinder future collaboration with China and the BRI if they believe it will not deliver on its promises of economic benefits or that it will have significant political side consequences.

China has exerted influence in South Asia by proposing to assist nations with the backend of a transaction, which has led to private loans with government guarantees or agreements detrimental to the borrowing country. Before and after they accept Chinese loans, the US can offer support to South Asian states, managing and



restructuring their total foreign debt and enhancing their ability to avert future setbacks (Brattberg & Feigenbaum, 2021).

BRI was not intended to be a regional organisation; instead, it was designed to be a network of economic corridors. Instead, to support Chinese growth in the future, the emphasis has been on opening up markets and enhancing infrastructure. The Asian Infrastructure Investment Bank (AIIB)<sup>19</sup> and the Silk Road Fund, among other Chinese state lenders, are the primary sources of finance for the system. The Chinese government has made it clear that participation in this venture will help them expand, and partner states will also gain from it.

China first entered South Asia by facilitating trade, and in 2006, it signed a free trade agreement (FTA) with Pakistan. (Kazmi, 2007) The decision to pursue an FTA was applauded since Pakistan is one of China's most important defence partners and most devoted allies. Pakistan signed the FTA to draw in long-term Chinese investment opportunities, even though it was unfairly biased in China's favour (Shabir, 2007). Despite pressure from India, the Maldives signed a free trade agreement (FTA) with China in 2017 <sup>20</sup>, and similar discussions are underway with Nepal and Sri Lanka. China has made approximately 2 billion US dollars (USD) in investments in Sri Lanka, including a mega port project, an international airport, and a new industrial zone constructed on an artificial island one mile from Colombo. These investments are funded by several loans to the government of Sri Lanka and in-kind donations to State-Owned Enterprises (SOEs), including China Communications Construction

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<sup>19</sup> There are number of estimates and the most reliable ones are between US \$1–2 trillion. <https://www.csis.org/analysis/how-big-chinas-belt-and-road>.

<sup>20</sup> China has been actively adding smaller countries to the BRI. In this case, the Maldives signed a free trade agreement with an eye toward possibly investing in the modernization of the port infrastructure in Male, the nation's capital. Like with other nations, China cannot include its nation in the BRI framework unless it first signs a free trade agreement.

Company (CCCC) and China Harbor Engineering Company (CHEC) <sup>21</sup>. Unlike conventional free trade agreements, these investments have already been made before the FTA is signed. Furthermore, despite political fallout on the home front from these agreements—namely, allegations that Sri Lanka is becoming trapped in a debt trap—successive administrations have insisted that the process continue.

As part of the BRI, China has even more extensive and deeper ties to Pakistan than Sri Lanka. One of the six primary parts of the BRI project is the CPEC. With a projected investment of over 62 billion US dollars spread over ten years (Hussain, 2017). CPEC is a long-term project. Like China's investment in Sri Lanka, Chinese state and SOE lenders finance the CPEC through loans. However, in Pakistan's case, the China-Pakistan Economic Corridor (CPEC) is more than just a collection of investments; it is integrated into the country's development strategy in addition to several bilateral investment agreements spanning multiple industries, including telecommunications, energy, and transportation.

With its 2013 launch, the China-Pakistan Economic Corridor (CPEC) gave Pakistan's economy the much-needed boost of investment required to recover from five years of economic instability following the 2008 financial crisis and the ongoing electricity crisis. Pakistan was presented with a stable investment and growth prospect by CPEC, which the government enthusiastically embraced. CPEC was and still is a perfect fit for Pakistan. 2013 saw Pakistan in a challenging position due to growing tensions with India and pressure from the US and EU partners on Afghanistan. Given China's tense

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<sup>21</sup> The projects are designed to create brand new infrastructure in Sri Lanka that can facilitate the expected growth through foreign direct investment that BRI can attract in the long run. <https://www.scmp.com/news/china/diplomacy-defence/article/2126606/china-invest-further-us1-billion-sri-lankan-harbour> and <https://www.scmp.com/news/china/diplomacy-defence/article/2149766/sri-lanka-pushes-forward-plans-chinese-investment-zone>

relations with India, Pakistan saw China's intervention as an opportunity to relax foreign policy restrictions and gain a ready ally in its opposition to India. China entered the picture with the prospect of investments and a more prominent role in Pakistan's economic future. Since then, Pakistan's economic growth and development aspirations have been built around the CPEC. In addition, Pakistan granted China a 99-year lease to develop and run the port city of Gwadar as an indication of its commitment to the China-Pakistan Economic Corridor (CPEC). China's long-term strategy to avoid any unrest that would affect its trading routes over the Strait of Malacca depends on the port (Markey, 2016). The port also established a pipeline as a substitute for maritime routes to import oil from the Middle East into China.

The Belt and Road Initiative (BRI) has impacted Pakistan and Sri Lanka by giving local authorities the necessary economic gains. The Belt and Road Initiative (BRI) has reorganised South Asia into an Indian sphere of influence and a Chinese crescent of influence, given the significance of SAARC and regionalism. An organisation like SAARC, which was already battling with member indifference, is experiencing stagnation in such a situation.

### 5.3 BANGLADESH-CHINA-INDIA-MYANMAR ECONOMIC CORRIDOR (BCIM-EC)

The Bangladesh-China-India-Myanmar (BCIM) Forum for the Regional Cooperation project, formerly known as the "Kunming Initiative," was founded in 1999. It was primarily designed as a Track II dialogue to establish a sub-regional "cooperation zone" that would connect the relatively underdeveloped regions that stretch from land-

locked areas of Southwest China to Eastern India, as well as the neighbouring least developed countries (LDCs), Bangladesh, Myanmar, and the northeastern region of India (Uberoi, 2013). The BCIM was established with the understanding that the project would be activated at the intergovernmental level, known as Track I, to boost trade and connectivity from Kunming to Kolkata. Bangladesh and Myanmar proposed several proposals to strengthen regional collaboration in this project, which was gaining ground for constructing infrastructure linking Bangladesh and Myanmar with the Western Region of China. Major problems, such as the Indian government's reluctance to participate in multilateral, regional forums with China, given the historical sensitivity of India's insurgency-prone northeast area (Uberoi, 2008) were still highly debated nevertheless.

As a first step toward revitalising the Belt and Road architecture, China wanted to integrate the China–Pakistan Economic Corridor (CPEC) infrastructure with the regional economic corridor of the BCIM. The CPEC would cover the Pakistani-owned Kashmir–BCIM corridor (PoK) portions. The development of the border regions and the economic integration of the sub-region, which would facilitate the integration of Asia, has been the project's two main goals since the BCIM initiative's inception. The original three Ts—Trade, Transport, and Tourism—were given priority by the BCIM, but with time, TTE (Trade, Transport, and Energy) emerged. Considering that the connection route is rich in natural resources and Encompasses an area of 165,000 square kilometres with a population of 440 million people (Sajjanhar, 2023), it has the potential to yield enormous economic benefits in trade, investment, and communication linkage. Reviving the ancient Southern Silk Road trade route, the corridor intends to make travelling from China to India more accessible. The goal was to highlight digital connectivity, facilitate trade, lower obstacles that promote the

smoother movement of goods and services, and not simply concentrate on the physical connectivity that connects roads, railroads, canals, and the air.

Figure 5.1. Map of BCIM–EC in South and Southeast Asia.



*Source: Daily Star Newspaper, Bangladesh.*

Each of the BCIM member states has a unique area of expertise that could stimulate economic growth inside each state. For example, Myanmar offers cheap labour in plenty and has positioned itself as a significant product exporter. India is among the top Asian states in terms of service exports. China enjoys a competitive edge due to its status as the world's largest exporter of manufactured goods. Bangladesh exports both low-quality manufactured goods and services. The region is also abundant in both

conventional and renewable energy sources. When it comes to connectivity, Bangladesh's Chittagong Port has the potential to serve as a hub for services to Northeast India, Southeast China, Burma, Nepal, and Bangladesh. The Bay of Bengal (BoB) occupies a strategic geographic position and is vital to the BCIM project, which aims to link China and South Asia. In keeping with the importance of Cox's Bazaar's geographic location, Japan and Bangladesh have launched the BoB industrial growth belt (Big-B) plan to accelerate the industrial growth of Cox's Bazaar, Chittagong, and Dhaka, which will ultimately have an impact on South Asian regional economic integration. China is attempting to establish maritime and land-based connections with South Asia. China can advance toward Bangladesh because it already has connections with Myanmar.

Using Bangladesh as an example, increased trade and investment activities between Bangladesh and China can help the country's export capability to China. China can assist Bangladesh by moving its declining businesses there because Bangladesh has an abundance of cheap labour. Bangladesh may lower the cost of importing garment inputs from China by strengthening its value chain, which would help the country's textile and apparel industry. This can be accomplished in two ways: first, by increasing the port's capacity and shortening the clearance time at Chittagong, and second, by building the necessary factories in Bangladesh, China may expand its production base for non-cotton RMG inputs. Furthermore, Chinese participation in Bangladesh's two Special Economic Zones (SEZs) and the creation of an Export Processing Zone (EPZ) specifically for China will help expand bilateral trade and increase Bangladesh's exports to international markets (Khatun, 2016). It should be emphasised that the Chinese port in Guangzhou is farther away from the landlocked

southern part of China than from Chittagong port. China is currently investing heavily in the Chittagong port to increase its capacity. Bangladesh can also increase its exports by utilising the roughly 5,000 goods that China has granted duty-free access to, resulting in the formation of trade creation (Kabir, 2016).

Furthermore, Bangladesh may link to the Northeastern part of India, which is technically the whole of India, with which it has a significant amount of trade. Bangladesh and India share three-fourths of their border. Expanded access to the sizable markets in China and India has the potential to make Bangladesh a desirable location for foreign direct investment. Furthermore, Bangladesh could develop into a central commercial hub for South and Southeast Asia by connecting with China via Myanmar. In light of this, the Bay of Bengal is strategically located on the geographical map.

#### 5.4 BAY OF BENGAL INITIATIVE FOR MULTI-SECTORAL TECHNICAL AND ECONOMIC COOPERATION (BIMSTEC)

Unlike SAARC, countries were driven to join BIMSTEC in 1997 due to two factors: first, the demands of globalisation, which led them to search for new markets and economic areas, and second, to take advantage of the opportunity presented by the end of the Cold War, which introduced new geopolitical considerations. India's Look East Policy and Thailand's Look West Policy directly led to the creation of BIMSTEC. It is also known as sub-regional cooperation because it connects South and Southeast Asian states and, unlike SAARC, has a definite economic purpose. With 1.3 billion people, 21% of the global population, a combined GDP of US\$750 billion, a great deal of mutual benefit, and a combined GDP of US\$750 billion, BIMSTEC offers a

singular connection between South and Southeast Asia. Based on a study, the BIMSTEC - FTA has the potential to generate trade worth US\$43–59 billion. Four countries made up BIMSTEC at its formation: Bangladesh, India, Thailand, and Sri Lanka. Following Myanmar's 1998 entry, Nepal and Bhutan joined in 2003. It becomes a valuable tool for further strengthening India's and other BIMSTEC members' strategic economic ties to Southeast Asia. For Bangladesh, Sri Lanka, Nepal, Bhutan, and Bhutan, it's also a platform where Thailand's presence can lessen India's dominant role (Murthy, 2008).

BIMSTEC decided to cooperate in six areas in 1997, adopting the subregional cooperation model. Each member state is organised and carries out programs in their respective areas. The six areas were trade and investment, technology, energy, tourism, transportation and communication, and fisheries. These sectors were further broken down into subsectors, each with a chair state that reported to the lead country and was in charge of co-coordinating the subsector's operations. Along with other topics, the members indicated they wanted to discuss how to encourage intra-regional cooperation on removing non-tariff barriers NTBs, market access challenges, services, and PTAs. The need for more institutionalised financial arrangements, trade facilitation measures, and a customs expert group to facilitate intra-regional trade was also demanded by the BIMSTEC member states. To promote trade and investment among member nations and draw outside parties to trade with and invest in BIMSTEC, member nations of the organisation decided to create the BIMSTEC Framework Agreement. It was agreed that the Trade Negotiating Committee (TNC) would move on to negotiations on trade in services and investment after concluding talks on trade in products. The BIMSTEC-FTA was supposed to go into effect by July



2006, but it never did. A BIMSTEC free trade agreement would benefit India, according to several research. Talks are still ongoing, nevertheless, to resolve some of the more subtle concerns about product coverage of the negative list, the reciprocity principle, rules of origin (RoO), and product distribution over the usual track reduction and elimination.

India's active and compelling hegemonic position within BIMSTEC and its foreign policy orientation towards its member states are essential to its success. India is aware that regional organisations provide economic incorporation, a necessary component for creating inclusive regional identities (Beeson & Lee-Brown, 2021). In addition to giving India a unique identity, BIMSTEC offers several strategic alternatives for rebalancing power, seizing the lead, and opposing China's dominating and destabilising influence on South and Southeast Asian economies. On the other hand, SAARC is headed toward collapse due to India's growing lack of interest in continuing the organisation. Encouraging regionalism through SAARC would make it possible for Pakistan, India's bitterest rival, to have an equal share of the organisation's benefits, which runs counter to India's goal of establishing and demonstrating its economic dominance. India encounters various challenges when pursuing initiatives under the SAARC banner, as Pakistan, its primary opponent, opposes India's leading position.

Smaller states are also uneasy due to the economic disparity between India and other members (Bhattacharjee, 2018). As a result, SAARC has performed mediocrely and has yet to be able to contribute significantly to the development of regional economic cooperation. In contrast, BIMSTEC aligns with India's policy of Act East and places a high priority on "Neighborhood First." As such, BIMSTEC's success largely depends

on India's involvement in promoting regional economic cooperation under the BIMSTEC umbrella.

Table 5.1. Socio-economic conditions of BIMSTEC and SAARC member countries

2021

Name of the country	Annual GDP (US\$)	GDP per capita (US\$)	Human development index (HDI)
Afghanistan	\$20,116 m	\$517	0.511
Bangladesh	\$323,057 m	\$1962	0.632
Bhutan	\$2503 m	\$3244	0.654
India	\$266,0240 m	\$1928	0.645
Maldives	\$3738 m	\$6915	0.740
Myanmar	\$81,257 m	\$1493	0.583
Nepal	\$33,983 m	\$1166	0.602
Pakistan	\$261,726 m	\$1255	0.557
Sri Lanka	\$80,677 m	\$3681	0.782
Thailand	\$501,712 m	\$7188	0.777

*Source: World Bank Data 2021*

Small states around the Bay of Bengal and the Indian Ocean prefer regional blocs like BIMSTEC because they can assist member states in achieving better economic results

than they would through the fragmented multilateralism and platforms the World Trade Organization (WTO) promotes. Encouraging shared prosperity is possible because STEC prances for smaller regional states. This is because India is committed to sharing the spotlight with smaller states and desires to take the lead. However, smaller members know that India's unclear position may make it impossible to advance regional economic cooperation under the SAARC umbrella.

India is a critical player in developing successful regionalism due to its vast potential for effectively promoting regionalism. BIMSTEC is outperforming SAARC in boosting intraregional trade and fostering regional cooperation across various industries. As a result, it encourages member-state trust, which is essential for achieving a shared objective through regional platforms. On the other hand, SAARC's efforts to further its regional economic objectives have suffered. Numerous summits postponed because of bilateral conflicts indicate the fundamental lack of confidence among its member states when working toward shared goals. As a result, most of SAARC's initiatives and projects to advance regionalism need to be more active.

Notwithstanding India's dominant position in the region, these states are prepared to assist India in advancing regionalism through BIMSTEC as their goals align with support for India. Smaller states can only negotiate with larger governments if they possess the required military might and resources, primarily economic resources. In reality, though, none of the common member states of the two organisations have the means to challenge India's hegemonic position. They must, therefore, comply with India's diplomatic strategy. India needs to take significant steps to address South

Asia's uneven and asymmetric power structure to promote multisectoral advancements through regionalism under the SAARC umbrella.

India has shown greater interest in BIMSTEC's active participation since its inception, especially as compared to its approach to SAARC. BIMSTEC took a while to establish itself. However, in 2019, Prime Minister Modi showed that India had finally solidified BIMSTEC as its favoured forum for regional cooperation when he invited six other BIMSTEC member states to his oath-taking ceremony. According to India's Minister of External Affairs, BIMSTEC perfectly fits the country's "Neighborhood First" and "Act East" policies. This declaration illustrates how much India values BIMSTEC (Rahman, 2016). It also demonstrates the widely held belief that India is motivated by goals that will advance its ambition to become the economic powerhouse and dominant force in South and Southeast Asia.

India has placed a great deal of economic weight on BIMSTEC. The member states of the BIMSTEC have exhibited remarkable resilience in maintaining economic growth rates nearing 7.5% over the past five years despite financial constraints (Bhattacharjee, 2018). According to the ratio of the Indian Chambers of Commerce and Industry (FICCI)'s data on imports and exports, BIMSTEC is the world's most active trade-driven regional grouping. This is hardly unexpected given that 25% of all trade occurs along the Bay of Bengal route (Dutta, 2019). India has an apparent goal: through BIMSTEC, it wants to become the only powerful state and achieve control over 25% of world trade. India has to investigate new overseas markets in this globalised world. By establishing new markets, this platform will enable BIMSTEC member nations to increase the amount of trade commodities they

produce while also improving the economic circumstances of many people. Building trust and regional economic cooperation requires intergovernmental trade. Member states are encouraged to reduce tariff barriers and increase the harmonisation of their trade policies employing trust.

Investigating untapped natural resources in its rural eastern provinces, such as east Uttar Pradesh, eastern Madhya Pradesh, Bihar, Orissa, and West Bengal, India's proximity to BIMSTEC would further stimulate economic activity. India would be assisted by a multinational platform to use the water resources in these developing states to produce hydroelectric electricity (Yahya, 2005). Another excellent illustration of India's sincere desire for BIMSTEC as the ideal forum for advancing economic cooperation is the country's marine security initiative. In addition to fostering the Blue Economy—which aims to improve economic growth and standard of living via the sustainable use of ocean resources—India's expanding relations with other BIMSTEC members will also offer an overall response for the country's maritime security (Cai, 2017).

Considering everything, it is not surprising that SAARC is failing since its members lack confidence in one another because of the bilateral disagreement between India and Pakistan. Even with this, it is clear that SAARC's ability to serve as a robust platform for regional cooperation is consistently hampered by India's aim to achieve geopolitical domination in the area and to play a significant role in global affairs. India must confront China and Pakistan, two countries that prevent SAARC from realizing its full potential if it is to achieve its ambitious objectives. India continuously refuses Pakistan's central role in advancing economic integration through SAARC. India's goal of achieving economic domination is at odds with Pakistan's desire to

receive equal benefits from SAARC, which is why India is acting in this manner. Therefore, because of India's lack of cooperation, any program launched under the SAARC flag cannot bring about significant change. In addition, by entirely using ocean resources, BIMSTEC is better suited to advance India's goals of creating economic domination and solidarity. India achieves two key goals through BIMSTEC: it separates Pakistan from the rest of the world in the growth process. It hinders China's ability to benefit from the Blue Economy fully.

### 5.5 BANGLADESH, BHUTAN, INDIA AND NEPAL (BBIN)

Another logical result of SAARC's disability is the BBIN, a subregional alliance of India, Bangladesh, Bhutan, and Nepal, all SAARC members. Given the increasing trade, economic, and infrastructure connection between these states, the BBIN can operate as a cohesive organization even though it is not a breakaway group and is based on numerous prior studies on sub-regional cooperation. With the aid of sub-regionalism, India's regionalism set-up is now expected to pick up momentum. Moving past the old concept of "consensus," SAARC states are leading the way in embracing sub-regionalism within the region. One tool designed to revolutionize and ease trade is the BBIN Motor Vehicles Agreement. Bhutan's concerns about the agreement's potential effects on security and the environment have prevented it from being entirely successful thus far.

BBIN has committed to investigating the regional power trade, inter-grid connectivity, transit facilities, and multimodal transportation modes. Although Bangladesh and India are two countries that are severely energy-poor, Nepal and Bhutan have a large amount of untapped hydropower potential that might create a sizable market for the

electricity produced in these two countries. About 1500 MW of hydropower have been made in Bhutan thus far, which is only 5% of the 30,000 MW estimated potential. About 16% of the estimated 4300 MW of practical potential has been successfully exploited by Nepal, with a little over 700 MW remaining. Even though the governments of Bhutan and Nepal are working together to develop the necessary cross-border transmission infrastructure and generate hydropower, the SAARC countries have yet to establish proper coordination at the regional or sub-regional levels despite signing a Framework of Agreement on Energy Cooperation during the 18th SAARC Summit in Kathmandu.

To improve sustainable transportation, broaden trade prospects, and establish connections with global value chains, the BBIN member states are also investigating cross-border trade and streamlining international transit routes. In order to eliminate geographical and economic isolation, accelerate the sub-region's progress toward the Sustainable Development Goals (SDGs), and promote shared economic prosperity, BBIN focuses on regional cooperation. These initiatives are in line with more comprehensive regional plans like the World Bank's #OneSouthAsia framework, which attempts to strengthen South Asia by promoting inclusive growth, resilience, and increased economic integration.

Prime Minister Narendra Modi's aim to integrate the economy of South Asia is evident in the BBIN efforts. The message is clear: India will not think twice to support sub-regionalism in the area if obstacles are raised and the SAARC route becomes congested. In addition to BBIN, New Delhi is hoping to establish comparable sub-regional groups with Sri Lanka and the Maldives. In spite of Pakistan's obstructive stance, India is also eager to engage Afghanistan and Pakistan on the western sub-

regional front. Any other sub-regional grouping in the region, including the BBIN proposals, will not succeed without a more focused agenda and increased political will. Additionally, BBIN must coordinate and establish a feasible agenda with some of the other sub-regional organizations that currently exist in the region, like the BIMSTEC and BCIM-EC whose membership spans beyond South Asia.

## 5.6 CONCLUSION

The existence of various sub-regional organizations and China's supremacy in South Asia have had an impact on SAARC as a whole but at the same time have given more economic gains to individual member states. India is concerned about China's increasing involvement and influence in South Asia because of the Belt and Road Initiative (BRI), which has put states like Sri Lanka and the Maldives in debt. India has been attempting to counterbalance China's influence by promising more aid and financial support to smaller states, but doubts have been raised regarding India's commitment to the prosperity of the region due to its dispute with Pakistan and its narrow-minded approach to SAARC.

Only 5% of trade occurs inside the SAARC region, and member states' mistrust and bilateralism are the outcome of the rivalry between Pakistan and India, which has bound the organization. Further impeding the effectiveness of SAARC has been India's disinterest in using the organization to promote intra-regional trade and close the trade deficit with other members. Regional groupings like BBIN and BIMSTEC, to which India gives greater emphasis than SAARC, are progressively gaining momentum. The formation of sub-regional organizations has caused SAARC to refocus its efforts and focus on these new alliances. For example, India's increased



participation in BBIN and BIMSTEC has sparked concerns about its commitment to SAARC. This is because, in light of SAARC's stagnation as a result of member-state mistrust and bilateral conflicts, India believes these sub-regional organizations to be more successful in fostering economic cooperation and integration.

In order to get over SAARC's restrictions, member states now have an alternate venue for economic cooperation and integration: sub-regional organizations. For instance, the BBIN effort has made it easier to collaborate on energy and transportation infrastructure, which has been a major obstacle for SAARC. Likewise, with room to develop, BIMSTEC has done a better job of fostering investment and trade among its member states. Aside from the conventional regionalism led by SAARC, new kinds of regionalism have also emerged in South Asia as a result of sub-regional organizations. Although trans-regional projects like the BCIM-EC have the potential to strengthen economic ties between member states, these new forms of regionalism also raise concerns about how they may affect SAARC-centric regionalism.

In conclusion, SAARC has been impacted by other sub-regional organizations in South Asia and external actors like China, because they offer substitute venues for economic integration and cooperation, divert attention from SAARC, and encourage the creation of new regional identities in the region. But these sub-regional groups' capacity to overcome the obstacles and constraints that have hampered SAARC's development, like the lack of confidence amongst member states and bilateral disputes, is also critical to their success.

## **CHAPTER 6**

### **CONCLUSION**

This research was based on three main research questions, and these questions have been answered in the chapters as follows:

The first research question, “To what extent has SAARC promoted economic integration within South Asia? - has been answered in the 2<sup>nd</sup> chapter, which provides a detailed study of all the initiatives and follow-ups such as SAPTA, SAFTA, trade liberalization, trade facilitation, etc, taken by SAARC in promoting the region's economic integration.

The South Asian trade liberalization regime began with SAPTA. The ultimate objective was the creation of the Customs Union, which would mean total economic integration throughout South Asia, and it was believed that it would open the door for free trade areas. However, because of its list-based approach to trade, which leaves little room for trade liberalisation, the SAPTA could not positively affect economic growth. A positive list strategy involves countries compiling a list of particular goods for which they lower non-tariff barriers or grant tariff concessions. Within the context of SAPTA, only goods included in the positive list provided by each member state were eligible for intra-regional free trade (Alam, 2006). Despite having limited room for free trade, SAPTA cleared the door for additional trade liberalization. SAARC took the lead in creating the SAARC Free Trade Area (SAFTA), the first phase of economic integration.

In 2006, SAPTA was replaced by SAFTA. To achieve "free" trade—a tariff system with all rates below 5%—between the three NLDC members—India, Pakistan, and Sri

Lanka—by 2015 and among all NLDC members by 2018—Article 7 of the SAFTA calls for a two-stage tariff reduction program. Little progress has been made thus far in putting the suggested tariff reduction plans into action. It is unlikely to bring about "free trade" in the region even if it is fully implemented, as all participating countries have chosen to keep a long list of "sensitive" products to shield specific economic sectors from SAFTA duty exemption, 53% of intra-SAARC imports (Dubey, 2010) are restricted due to the sensitive list. India has more than three times as much on its sensitive list as it did during the previous round of talks for a free trade agreement with ASEAN. A range of non tariff barriers (NTBs) persist in restricting trade. Pakistan has chosen not to apply the agreement's provisions to its trade with India, therefore keeping out of the SAFTA process, which may be the most significant portion of regional trade. (Dubey, 2010)

Thus, it is evident that SAARC has advanced South Asia's economic integration to some extent. Trade within the region has been promoted, and tariffs have been reduced due to initiatives like SAFTA. However, its effectiveness has been hampered by implementation issues and bilateral disagreements, particularly political tensions amongst the member states. SAARC has generally established the fundamental framework for economic cooperation; nevertheless, complete integration is still a work in progress.

This gives the flow to the 2<sup>nd</sup> research question - How do political and diplomatic relations among SAARC member states affect the organization's ability to facilitate economic integration in South Asia? - which is answered in the 3<sup>rd</sup> chapter. The chapter discusses political tensions in the region, infrastructure deficits in South Asia, and how smaller member states perceive India's dominance over the area as a threat,

which are primary issues that have limited SAARC's role in economic integration in South Asia.

Trade struggles and business competitiveness are discouraged by non-tariff trade barriers such as price restrictions, pre-shipment inspections, manual licensing requirements, sanitary and phytosanitary (SPS) standards, and technological trade barriers, inefficient customs procedures, heavy documentation requirements, lengthy delays, and costly trading procedures further hamper economic integrations. Trade barriers for services also provide a hurdle. These include enormous obstacles with added value equivalents that are regularly higher than 10% of tariff rates for commodities and, in some cases, as high as 70% in specific industries. Policy adjustments and regional cooperation are required to increase economic growth and realize the full potential of regional integration to overcome these obstacles and promote regional economic integration.

The 2<sup>nd</sup> chapter also covers the following: What is the correlation between increased intra-SAARC trade and the level of economic integration in South Asia? - the 3<sup>rd</sup> research question. Due to growing global market integration and political unrest, intraregional trade in South Asia has historically been low, making up double digits of the region's total trade before 1951 but only 2% by 1967. In the 1990s, the share increased again, peaking at 4.4% in 2002 before falling to 3.84% in 2008. Even though exports have increased, South Asia's intra regional trade share remains low compared to other regions like the EU, ASEAN, and NAFTA. The region's intraregional trade distribution is also uneven. In contrast, the intra-regional trade ratios for East Asia and Europe are 35% and 60%, respectively, and less than 5% for South Asia. India's substantial worldwide trade share—of which only a small portion is with other South Asian states—is the primary cause of the low intra-regional trade

ratio. The correlation between intra-regional trade and economic growth in South Asia is noteworthy, indicating that more regional integration might hinder growth.

The World Bank has highlighted the potential advantages of intraregional trade for South Asia; moreover, there needs to be more data to draw firm conclusions on the correlation between economic growth and the intra-trade ratio of regional trade agreements (RTAs) as a credible measure of regional integration. The benefits of intra-regional trade are supported by the theory of comparative advantage and later analytical developments; however, any deviation from the member countries' world trade share is indicative of distortions brought about by shared borders, culture, history, political aspirations, security concerns, and domestic policies that either lower or increase the profitability of intra-trade (Wignaraja,2022).

The 4th chapter of this research provides a comparative case study of SAARC and ASEAN approach to economic integration in their regions. Though political and security issues have hindered SAARC's progress, ASEAN has been more successful in creating complementary businesses. Both SAARC and ASEAN have had difficulties in attaining regional economic integration. The SAFTA and the SAARC Study on Regional Economic Integration are measures that SAARC is using to solve the issues both areas have in addressing the various levels of economic development among member states.

While they have pursued regional economic union, SAARC and ASEAN have faced different obstacles and levels of success. Due to political and security concerns among its members, especially the hatred between two essential member states, SAARC must catch up. Other members' attempts, like those of Afghanistan and Sri Lanka, to

gradually move closer to regional economic integration have been hampered by this. On the other hand, ASEAN has had tremendous success growing supplementary industries and exporting manufactured goods.

Nonetheless, resolving the disparities in economic development between respective states presents difficulties for both regions (Rahman, 2011). As intraregional trade increased, some initial problems emerged in the ASEAN and SAARC regions. The SAARC region has challenges because of the disparities in economic development among its member states. In contrast, ASEAN states have succeeded in creating complementary sectors and becoming exporters of manufactured goods. The SAARC governments, which are the least developed, are skeptical about the advantages of intraregional trade because they think it might not be as beneficial as trading with more developed countries. With India being the most developed state in the region, this difference is more noticeable (Sinha, 2010). Even with attempts, the SAARC region's potential benefits of intraregional trade still need to be fully realized due to disparities in economic growth. In the current globalization setting, SAARC members should learn from ASEAN's cooperative outcomes and investor-friendly stance to prevent alienation from the world stage.

Chapter 5 of this research focuses on the timely topic of SAARC's unbound role in New South Asia. Deepening economic integration and exchanging resources and information can benefit South Asian states greatly, both within the subregion and beyond. By doing this, they could take full advantage of their strategic location at the meeting point of Southeast Asia and Central Asia on the Eurasian continent. Using enhanced interconnectivity within and between adjacent subregions, South Asia has the potential to become a major hub for trade between Europe and Central Asia, as well as Southeast and East Asia. This development will also support the broader

concept of regionalism in Asia and the Pacific. With the easing of sanctions on the Islamic Republic of Iran and the democratic transition in Myanmar, among other changes, the geopolitical environment is now more favorable for utilizing the potential for greater economic cooperation.

The research was also based on two hypotheses as follows;

- Reducing political tensions among SAARC members leads to greater economic integration in South Asia.
- The relationship between the trade volume among SAARC members and the level of economic integration should be correlated.

The first hypothesis is proven to be accurate according to the analysis of the 3<sup>rd</sup> chapter. As the chapter highlights, Since SAARC's inception, there has been an apparent lack of political will among its members to transform the organization into a vibrant one, hindering regional economic integration and collaboration. Thus, to achieve deeper financial integration in South Asia, efforts to promote political cooperation, the business environment, and regional stability should go hand in hand with measures to reduce political tensions.

The 2<sup>nd</sup> hypothesis is also proven, as discussed above and in - detail in the 2<sup>nd</sup> chapter. By examining the current state of intra-regional trade, the influence of trade agreements, the possibility of increased trade, the role of non-tariff barriers, the impact of economic integration, the effect of exchange rate volatility, and the shared border, the correlation between the volume of trade among SAARC members and the degree of financial integration can be established (Asian Development Bank, 2009). The SAARC states can boost intraregional trade and achieve greater economic

integration by tackling these issues. Furthermore, by increasing trade between SAARC states, the creation of regional trade agreements

like SAFTA has sought to promote deeper integration and economic cooperation. The potential for more intraregional trade within South Asia has been acknowledged despite obstacles such as trade barriers and historical conflicts. Studies show that intra-regional trade has grown significantly more than inter-regional trade.

Furthermore, although with minor magnitudes of values, the Extended Gravity Model analysis on SAARC members from 1991 to 2010 revealed that GDP, GDP per capita, exchange rate volatility, and common border substantially impact intra-regional trade among SAARC countries. This implies that trade activity is anticipated to increase as political disagreements among SAARC members decrease, underscoring the relationship between trade volume and regional economic integration.

In conclusion, SAARC significantly contributes to South Asia's economic integration, offering a forum for trade liberalization and regional cooperation. These initiatives can open up new markets, allow for the complete use of production capacities and transfer technology, and unleash the potential of abundant human, financial, and entrepreneurial resources in the region. The most effective and direct form of regional economic cooperation is the expansion of intraregional trade. Since the late 1980s, South Asian states have been implementing extensive institutional reforms and economic liberalization due to East Asian states' successful export-led growth and trade liberalization experiences. SAARC adopted an economic cooperation program in 1991 and established SAPTA in 1993 as part of its continuous attempts to transform into a preferential trading bloc and eventually a free trade area and SAFTA in 2004 to



abolish tariffs on traded goods between 2006 and 2016 and build a borderless economic zone. Adopted in 2010, the \$300 million SAARC Development Fund was established with social, economic, and infrastructure windows, along with the SATIS. All these initiatives can deepen economic integration in the region by providing suitable legal frameworks and policies. Nevertheless, the area still needs help realizing the potential advantages of economic integration, and more work is required to improve market integration and intraregional trade.

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