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Regional Trade Barriers in South Asia: SAARC Lagging Behind ASEAN

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Abstract

Low levels of intra-regional trade in SAARC can be attributed to several factors, the primary ones being tariff barriers to trade, non-tariff barriers, trade facilitation barriers and other political factors like India Pakistan territorial dispute. The objective of this paper is to delve deeply into the current trade situation in the South Asia region vis-à-vis levels of informal trade, trade deficiencies – Tariff, Non-Tariff and Facilitation Barriers, and make an assessment as to how the huge untapped economic potential, marred by political impasse, be realized. A case study of the India Pakistan bilateral trade will be discussed to understand the gravity of the problem and a comparative analysis with ASEAN will be presented. Thereafter, a way forward will be suggested for increased intra-regional trade.

Keywords: ASEAN, India, Non-Tariff Barriers, Pakistan, SAARC, South Asia, Trade

1. Introduction

South Asia is home to the world's largest working age population. The region is brimming with opportunities but at the same time besieged by socio-economic challenges that plague the region's citizenry in its entirety. Regional cooperation in South Asia has been falling short of the mark, when compared to other regional blocks like Association of Southeast Asian Nations (ASEAN) and European Union (EU). While many in the region see economic engagement as a key driver of regional cooperation, it is worthwhile to note that intra-regional trade in South Asia stands at mere 5% compared to 25% in ASEAN. The question arises why South Asian Association for Regional Cooperation (SAARC) is lagging behind ASEAN. Academicians and scholars across South Asia cite India – Pakistan impasse as a major thorn to regional cooperation dialogue and initiatives. Others mention poor trade facilitation as a major limiting factor impeding economic cooperation in the region. If cooperation were to happen in South Asia, the region could realize the potential benefits of reaping economies of scale, infrastructure development, solving trans-boundary issues, developing transit linkages, and managing natural resources among many others. Regional cooperation in South Asia has not developed and the region waits with bated breath to see cooperation dialogue to be truly effective.

As stakeholders across region blame rift between the two neighbors – India and Pakistan, as an impediment to greater cooperation, the challenge lies in finding a feasible mechanism for increased engagement between the two countries. Since political diplomacy has failed to show results, arguments have been made on the potential of bilateral trade and commerce in normalizing relations, not just between the two neighbors, but also among countries in the entire region.

A quarter of the world's population lives in the South Asian region, yet South Asia accounts for less than 5% of the world Gross Domestic Product(GDP), and less

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than 2% of the world exports[3]. The abysmal state of intra-regional trade in South Asia calls for the need to do more research to understand what holds this intra-regional trade.

SAARC was established in 1985 to promote economic growth and development in the region. For active regional collaboration, SAARC Preferential Trade Arrangement (SAPTA) in 1995, and eventually South Asian Free Trade Area (SAFTA) in 2006, came into effect. The objective was to stimulate trade and foster deep economic engagement between the South Asian nations. Several initiatives were taken in this regard, and yet today, South Asia is the least integrated region in the world[3].

Low levels of intra-regional trade in SAARC can be attributed to several factors, the primary ones being tariff barriers to trade, non-tariff barriers, trade facilitation barriers and other political factors like India Pakistan territorial dispute.

The objective of this paper is to delve deeply into the current trade situation in the South Asia region vis-a-vis levels of informal trade, trade deficiencies – Tariff, Non-Tariff and Facilitation Barriers, and make an assessment as to how the huge untapped economic potential, marred by political impasse, be realized. A case study of the India Pakistan bilateral trade will be discussed to understand the gravity of the problem and a comparative analysis with ASEAN will be presented. Thereafter, a way forward will be suggested for increased intra-regional trade.

2. Economic Analysis of Trade Deficiencies

Tariff structures in South Asian economies compared with a few other Asian economies give an overview of the limited trade that can be attributed to high tariff rates. Based on the tariff rates seen in Table 1[8,18] argues that Sri Lanka maintains one of the lowest tariff rates – 8.2% in the region. This is followed by India at 10.3%. It needs to be noted that average trade-eighted tariff rate of India does not reflect the tariff peaks which are concentrated in agriculture and also higher tariffs levied on sectors like automobiles, garments and textiles, most of which are above 25%. As agricultural commodities form a major component of the exports from other South Asian economies, the distorting tariff rate hurts the intraregional trade with India. Same goes for Pakistan, which despite an average trade-weighted tariff rate of just 11.4%, has commodities subject to a slab as high as 25%.

Table 1. Trade Weighted Average Tariff[8,18]

Country	Trade weighted Average Tariff Rate
South Asia	
Afghanistan	21.9%
Bangladesh	13%
India	10.3%
Maldives	20.4%
Nepal	12.8%
Pakistan	11.4%
Sri Lanka	8.2%
Other Asian	
People's Republic of China	13.9%
Malaysia	5.9%
Indonesia	6.1%

Note: Tariff rate applicable to most favored nations

Given such high tariff rates, academicians, traders and businessmen have, mostly unanimously, expressed interest in cutting down tariff rates and initiating a trade liberalization program. This was exactly the objective of SAFTA, an agreement that came into effect in 2006 to promote intra-regional trade. Under SAFTA, tariff rates levied on intra-regional trade should be less than 5%. But, there's an exception to this rule. Some domestic industries which need protection, goods of those industries fall under the Sensitive List/ Negative List, which are either not subject to tariff concessions of SAFTA or not allowed at all for intra-regional trade. Table 2 shows the percentage share of these sensitive list items in total imports in the South Asia region.

Table 2. Percentage Share of Sensitive List Items in SAARC[5,8]

Country	Share of SAFTA Sensitive List Imports in Total Imports from SAARC
Bangladesh	55.8%
India	47.8%
Maldives	67.2%
Nepal	29.4%
Pakistan	18.8%
Sri Lanka	26.9%

High percentage of sensitive list items in the total imports of SAARC countries raises an eyebrow on the effectiveness of a regional trade liberalization agreement like SAFTA. The question arises if a regional trade agreement like SAFTA is effective at all. In the South Asian case, as can be seen from Table 3, bilateral trade agreements like India – Sri Lanka Free Trade Agreement bypass regional SAFTA, where traders and businessmen prefer to trade under India-Sri Lanka FTA than under SAFTA.

Table 3. Comparison of Negative/ Sensitive Lists Between SAFTA and Bilateral FTAs[8,17]

Country	SAFTA	India Sri Lanka FTA	Pakistan Sri Lanka FTA
Bangladesh	1254		
Bhutan	137		
India	865	419	
Maldives	671		
Nepal	1335		
Pakistan	1183		540
Sri Lanka	1065	1180	697

Table 3[8] shows for instance that Pakistan maintains a Sensitive List of 1183 items but subjects Sri Lanka to only 540 items. Additionally, it is agreed[17] argues that time frame for reduction of duties to zero is 10 years in the case of SAFTA, while it is 8 years and 3 years in the case of India Sri Lanka FTA and Pakistan Sri Lanka FTA respectively. Therefore, numbers make it evident that bilateral agreements have proven to be more effective in reducing tariff barriers than a regional agreement like SAFTA. Experts have estimated the potential impact of a 100% tariff reduction. A complete reduction in tariffs can lead to creation of trade – gains in both exports and imports. Besides, a positive impact on national output and employment is estimated[8].

Traders and businessmen, mostly in the smaller countries are wary of the fact that trade creates both winners and losers. They are apprehensive of who will win and who will lose. Table 4 shows an example of impact on two countries – the biggest player India and one of the smaller countries Nepal, and it is clear that tariff reduction will lead to a win-win situation for all South Asian countries alike, though the degree of gain may vary depending on the size of the economy. Besides, the non-tariff barriers and trade facilitation barriers impose severe restrictions on smooth trade in the region. This will be discussed through the case study of India Pakistan bilateral trade.

Table 4. Prospective Gains from 100% Tariff Reduction[8, 2, 13, 14]

Country	Creation of Trade (USD billion)	Gains in Exports (USD million)	Gains in Imports (USD million)
India	0.4-0.7	942	477
Nepal	0.012	187	190

3. Case Study: India-Pakistan Bilateral Trade

Current trade volume between India and Pakistan, the two major players of the region, is less than $3 billion though it is believed that a considerable potential for more trade exists between the two. According to experts, a normalized trade regime has the potential to send the number soaring to $40 billion [10]. The question is how more Indian goods like tea, cotton, organic chemicals and petroleum products can go to Pakistan and how Pakistani goods like dates, jewelry, medical supplies and petroleum oils can find their way towards India.

According to research[16], a troubled trade track record

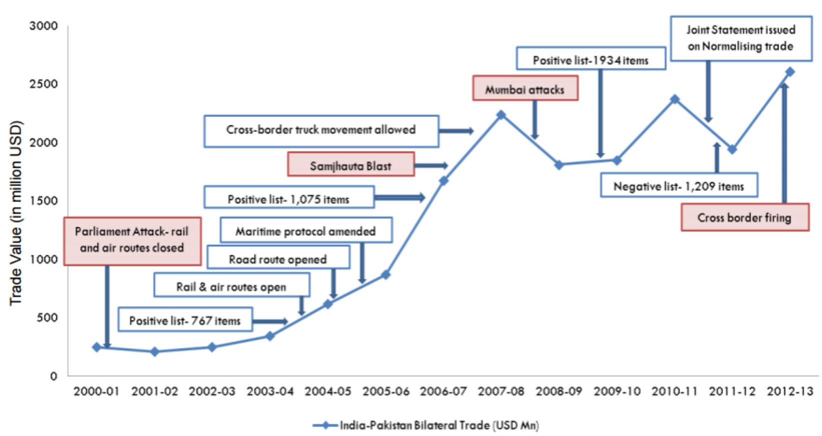

Figure 1. Bilateral Relationship between India and Pakistan.

exists between India and Pakistan, with trade getting suspended because of political and military conflicts. The Figure 1 below shows the bilateral relationship vis-a-vis the link between political events and economic engagements over the last decade.

Despite all the criticism, it is a fact worth stating that both India and Pakistan have taken a few phenomenal steps towards promoting bilateral trade and economic engagement. India's decision to grant Most Favored Nation (MFN) to Pakistan in 1996 followed by Pakistan establishing a positive list for Indian imports and signing of South Asian Free Trade Agreement (SAFTA) in 2004 stand testimony to the argument [11]. Later, in 2012, Pakistan replaced the positive list of nearly 2000 goods with a negative list of almost 1200 Indian goods, like automobiles, iron, and steel that could not be imported[10]. Launch of an integrated checkpoint between India and Pakistan at the Wagah-Attari land border drove the bilateral trade between India and Pakistan substantially - exports grew at 122 per cent and imports at 81 per cent from 2011-12 to 2012-13[15].

Though, Wagah-Attari border is the major land crossing between the two neighbors, research [9]states that infrastructural constraints vis-a-vis warehousing facilities, truck jams and parking, lack of financial institutions, and testing laboratories, along this border have led to the opening of informal trade routes like Mumbai-Dubai-Karachi and Mumbai-Dubai-Bandar Abbas-Afghanistan-Pakistan. It is explained that nearly 51 percent of informal trade taking place via Dubai does not reach Karachi directly[7]. Goods are transshipped from India to Dubai, to Bandar Abbas in Iran, to Afghanistan and finally Pakistan. Trade barriers and infrastructural constraints across borders make the longer indirect routes actually twice as trade efficient, when measured in terms of transaction costs incurred per container per kilometer.[7] Voicing their interest in formal trade researchers, [1]argue that higher volume of formal trade will increase economic dependence between India and Pakistan. This will result in high economic inter-dependence which will call for normalization of political relations as well. The share of global trade in India's GDP increased from 7 percent in 1970 to nearly 32 percent by 2010. And in the case of Pakistan, the share rose from 12 percent in 1970 to 34 percent in 2010[11]. But the question remains if the two neighbors are realizing the gains of each others' fast economic growth and geographic proximity.

4. Trade Potential between India and Pakistan: Revealed Comparative Advantage (RCA)

There have been several studies estimating the trade potential between India and Pakistan to examine how this potential can be realized. One study uses the Trade Possibility Approach for all items traded, followed by selecting only those items in which the countries have a Revealed Comparative Advantage (RCA) to export[7]. The study shows that the trade potential between India and Pakistan is estimated to lie between US$10.9 billion and US$19.8 billion.

According to Trade Possibility Approach, the estimate of trade potential is the maximum possible trade that two countries can have if they sourced from each other all items which they sourced from the rest of the world. Though this can never be the case as relative prices would play an important role, these numbers give ballpark estimates of trade possibilities at a disaggregated level. The methodology for calculating trade potential is then extended by computing Revealed Comparative Advantage (RCA) for all items traded, such that India's export potential to Pakistan includes only those items in which India has a comparative advantage to export to the world. Similarly, for estimating India's import potential from Pakistan, the products for which Pakistan does not have a revealed comparative advantage vis-a-vis the world are eliminated. The RCA index is a ratio of the share of a given product in a country's exports relative to the product's share in world exports[7].

$RCA_{ij} = (X_{ij} / X_i) / (X_{wj} / X_w)$ where X_{ij} represents country's export of commodity j, X_{wj} represents world exports of commodity j, X_i represents the total exports of country i, and X_w represents total world exports. RCA index has been computed by averaging item-wise RCA for the years 2010 and 2011. An RCA index value of greater than unity implies that the country is competitive in exporting the product[7].

Table 5. India's Trade Potential with Pakistan in USD Million[7]

	Trade Possibility Approach	RCA Approach
Export Potential	25,358	16,936
Import Potential	5,136	4,308
Trade Potential	30,494	21,244

Comparison of trade potentials obtained using the two approaches above research; [7]finds that the difference is mainly due to lower estimates in India's export potential to Pakistan. India's export potential to Pakistan for products with comparative advantage is much lower, almost half of the total export potential obtained using the Trade Possibility Approach. This implies that India has a comparative advantage in about half of the commodities it can potentially export to Pakistan. On the other hand, the import potential does not differ much in the two approaches, indicating that Pakistan has a revealed comparative advantage in most of the products which can potentially be exported to India. India Pakistan trade is restricted due to the presence of trade facilitation barriers. Some of the country specific barriers to trade facilitation in South Asia are as follows.

It remarks that policy constraints, including regulatory impediments at borders and behind the border and poor infrastructural links appear to be consistent barriers across South Asian countries[8].

The next question is how the above parameters fare for ASEAN.

5. Comparative Analysis: SAARC and ASEAN

Research has shown that conflict management stands poles apart in ASEAN and SAARC. Though tensions between states in ASEAN continue to exist, which is evident in bilateral spats as those between Singapore and Malaysia in regards to their water treaties, Singapore and Thailand over Temasek Holdings investment, it is clear that the informal and quiet diplomacy encompassed in the 'ASEAN Way' has successfully managed conflict in Southeast Asia. ASEAN's relative success and SAARC's inability can be attributed to four main factors namely common threat perception, role of the key state, role of

Table 6. Country Specific Trade Facilitation Barriers in South Asia[5,8]

	South Asia
Bangladesh	Congested and inefficient major ports of entry
	No information technology infrastructure to support custom clearance at the border points
India	Certification requirements
	Inefficiently run border crossings
	Restrictions on rail movement of goods
	Complicated and restrictive visa requirements
	Long dwell times at ports and border points
	Several custom clearance requirements
	Transit restrictions
Nepal	Delays in customs clearance for cross border rail operations
	Lack of trained human resources and physical equipment to facilitate custom processes
	Lack of investment in creating new overland link
	Congestion at existing border points
Pakistan	Positive list approach to Indian imports
	Absence of land routes
	Sea travel restrictions
	Border restrictions and delays in customs clearances
	Visa restrictions
	Poorly managed and congested railway systems
	Transit Restrictions
Sri Lanka	Poor quality of roads connecting hinterland

extra-regional powers, all of which facilitate the creation of the fourth major factor, a common norm[12].

At the time of ASEAN's founding research, [12] states that conditions provided Indonesia, Malaysia, the Philippines, Singapore and Thailand with the impetus to set aside bilateral tensions and create a regional organization that could stabilize the region. Hence, these states were able to formulate an informal conflict management norm in the ASEAN Way. While this conflict management norm has thus far been geared more towards conflict prevention in the most basic sense, that is, the prevention of an armed inter-state conflict in the region, it is clear that at this basic level ASEAN (and its 'ASEAN Way') has been successful in managing conflict in the region, as there has been no armed conflict between states in Southeast Asia since 1967[12].

Table 7. Document and Time for Trade[8]

Documents to export (number)	8.5	6.7
Documents to import (number)	9.0	7.8
Time to export (days)	31.5	22.0
Time to import (days)	31.1	21.7

Trading across borders, besides the tariff and non-tariff barriers, also depends on other trade facilitation measures in place. As shown in Table 7, an assessment of the procedures and time taken to trade between countries, gives an overview of trade facilitation across specific borders.

Fewer documents are needed to trade in South East Asian countries like Singapore, Thailand, and Indonesia compared to those of South Asia. This can be attributed to the automated trading systems in place in the South East Asian countries[8].

A similar comparative picture of customs clearance shows that it takes much longer for South Asian countries to undertake the same custom clearance processes than other Asian countries.

Table 8. Number of Days for Custom Clearance[8,18]

Country	Number of Days
Pakistan	6.75
Bangladesh	4.47
India	3.45
Sri Lanka	1.59
Nepal	1.41
China	1.20
Average (for Middle Income Countries)	2.20

Critical review and analysis of trade facilitation measures under South Asian Free Trade Area is required to identify the gaps, followed by actual implementation of the measures on how to bridge the identified gaps.

6. Charting the Course

The big question remains how South Asia will catch up with other Asian economies, like those of East Asia and South-East Asia.Some of the underlying factors for successful integration of South-East Asian economies have been the ASEAN Economic Community (AEC) Blueprint with the development of a Single Window system, harmonization and standardization of customs and procedures among many other favourable trade and investment policies. South Asian nations have witnessed minimal implementation of regional initiatives, thus necessitating greater impetus on sub-regional and bilateral engagements. Sub-regional cooperation, wherein two or three countries address issues of common interest, can be highly feasible and could be a building block for greater cooperation. While academicians and traders are looking to intensify trade diplomacy between the two biggest countries – India and Pakistan, a few traders are apprehensive of the fact that trade will create both winners and losers, and Indian goods may flood Pakistani markets. Researchers[10] express the need to protect potential losers, if any, from increased normalization by using the increased revenue from expansion of formal trade to compensate those who may not benefit from the trade liberalization[10]. It is said that though Pakistani businessmen are wary of opening the door to large competitors from India, they are open to doing trade and business with India after the mutual benefit is made clear[4]. Common language and a shared culture make it easier for businessmen across border to engage. Trade transit needs to be prioritized as well.

In this context, is stated[8] how the proposed Afghanistan-Pakistan-India-Bangladesh–Myanmar (APIBM) Transport Corridor deserves high priority. "It can make Pakistan and Afghanistan hubs for India's trade with Central Asia, Iran, and the Middle East and Central Asia if accompanied by upgrading of infrastructure and land customs stations at the Afghan border with the Central Asian countries (Tajikistan, Turkmenistan, and

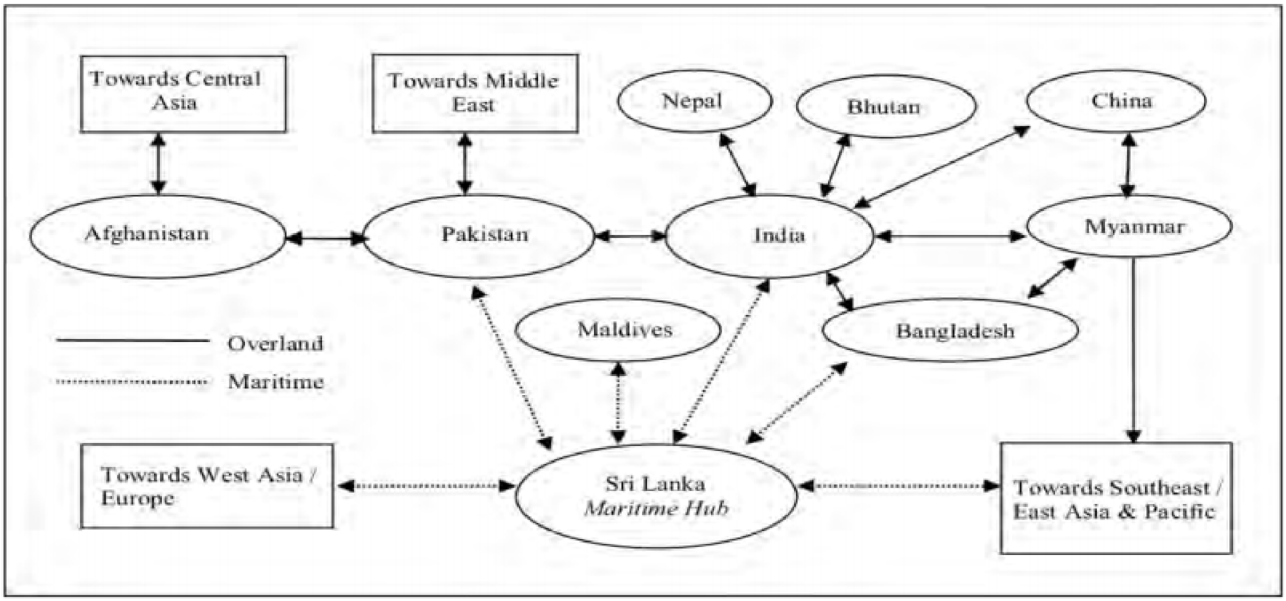

Figure 2. Intra and Inter Regional Connectivity.

Uzbekistan). Similarly, Bangladesh could become a hub for India's trade with Myanmar and other Southeast Asian countries, besides serving as a transit route for India's northeastern region. Myanmar itself will become a transit hub for India's trade with other ASEAN countries. Sri Lanka is already well placed to be a maritime hub in South Asia, with a lot of India's trade transshipped through the port of Colombo. Apart from transit revenues, there are huge gains associated with energy conservation from efficient use of resources. This APIBM corridor could be Asia's new silk route, linking Central Asia and East Asia, with South Asia as the land bridge playing the role of a vital transport corridor for expanded trade and transportation"[8].

India, Pakistan and Afghanistan need to formalize land trade routes giving India access to trade with Central Asia and Afghanistan access to rest of South Asia. For greater trade, Pakistan needs access to Nepal, Bhutan and Bangladesh through India and India needs access to Afghanistan through Pakistan. Full implementation of agreements and initiatives, including Afghan Pakistan Transit and Trade Agreement, Central Asia-South Asia Electricity Transmission Project (CASA-1000), Turkmenistan, Afghanistan, Pakistan and India gas pipeline initiative, is required to realize the benefits of regional trade, not only in the region, but also from China to Iran. Researchers[6] advocate for complete removal of trade tariffs under South Asian Free Trade Area (SAFTA), which could increase intra-regional trade by 1.6 times over and above the existing level[6]. It is suggested to focus on infrastructure development and improving the efficiency of existing trade routes[10]. For example, for smooth trade across Wagah-Attari border, there is need for testing laboratories, scanning machines, increased warehousing capacity, mutual recognition of standards, and easing the visa restrictions.

In the south, India, Maldives and Sri Lanka could work together to ensure maritime security and, promote the fishing industry and coastal tourism, as well as trade of edible oils and tea.

"The peace dividend of a more economically integrated and rapidly developing region, as exemplified by the European experience, could be a major additional benefit for the countries in South Asia, extended trade relationships would reduce the potential for conflict by creating strong constituencies for peace. Peace and stability in the region would spur the 'neighborhood effect' in FDI. The perception of South Asia as a stable region for investment would substantially increase FDI, especially with growing acceptance of India as a regional, if not, a global leader. Moreover, as the experience of EU and ASEAN suggest, the true benefits of regional trade are only realized through the investment channel"[8].

South-East Asian countries have let go of their sovereignty issues in favor of a common trade policy and it is time South Asia lets bilateral disputes take a backseat to economic cooperation. Good fences will not make good neighbors, definitely not in South Asia. It is time for trade and peace in South Asia.

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