

Prospects and Challenges for South Asian Regional Integration

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Prospects

- South Asia has shown impressive growth in the last decade
- This growth is reflected in the growth of trade and investment in the region
- India has been star performer among all South Asian countries
- More global integration and South Asia's proximity to the growing Asian region (China, ASEAN) are explanatory factors of this growth

Prospects

- Large human capital base combined with competition through open economies is playing a crucial role in the growth process
- Increased remittances and growing middle class with high purchasing power
- Youth bulge and a possible demographic dividend
- High growth in services with modern technology

Regional Frameworks

- SAARC has functioned for three decades
- Two decades of preferential trade under SAPTA (1995-2005) and SAFTA (2006-2016) for trade in goods
- Plans to move towards a South Asian Economic Community and then a South Asian Economic Union by 2022 (or 2025 ?)
- SATIS put into operation in 2010 for trade in services
- SAARC Investment Treaty ready for signing

Progress

- SAARC is the least integrated region in the world
- Intra-regional trade at 6% is one of the lowest in the world compared to 66% in EU, 48% in NAFTA, and 27% in ASEAN
- Intra-regional services trade also at a very low level
- For example, there is little spill overs from the growing IT industry in India to its neighbours

Progress

- Intra-regional investment is at 1% and smaller countries have failed to attract larger chunk of growing outward investment from India
- Efficiency-seeking industrial restructuring in the region is at a very low level and this is seen from IIT (Intra-Industry Trade) indices estimated in various studies
- Joint ventures with buy-back arrangements and subcontracting activities at a low level in the region

Impediments for Trade in Goods

- Low preferential margins, large negative list with actively traded goods kept out of liberalization
- NTBs, procedural delays, and poor connectivity – according to the WB, cost of trading across borders in the region is highest in the world
- Lack of supply capacity in most small countries to exploit the growing larger markets in India and Pakistan
- “trust deficit” and the vulnerability of SAARC progress to political issues

Impediments for Trade in Services

- SATIS which works under GATS-Plus is progressing slowly due to “offer” and “request” lists of all members not been completed
- Afghanistan and Bhutan not being WTO members (Afghan received membership in December 2015) was a delaying factor
- Outdated regulatory systems taking a long time to modernize
- Bulk of the services transfers have happened through Mode 3 (Commercial Presence in smaller countries) and Mode 3 liberalization has been a slow process

Impediments for Intra-Regional Investment Flows

- High transaction cost -- presence of non-transparent procedures and bureaucratic delays.
- Poor infrastructure, etc.
- Lack of a SAARC Investment Area on the lines of ASEAN
- Lack of an Investment Treaty with clearly rules-based system

Emerging Issues

- With Global Value Chains increasingly determining trade, reducing tariffs in the region has become vital for South Asian integration process both to the world and in the region
- With increasing “servicification” of the manufacturing sector (services value added accounts for 26% of manufacturing in developing countries), services liberalization is important for South Asian competitiveness
- Vertical and horizontal integration of industries is important for investment to drive trade and the trade-investment nexus to drive intra-regional trade

Challenges

- Addressing the impediments to trade in goods, services, and investment
- Binding commitments are required in Trade Facilitation and NTB removal
- Bilateral FTAs moving ahead of the South Asian trade integrating process – the possible integration
- LDCs need Special and Differential Treatment– more support to go through the process -- Given its economic power, India will have to take on a disproportionately larger responsibility for promoting regional cooperation in SA

Challenges

- Focus SAARC Development Fund to develop the supply capacity of the smaller countries; utilize AIIB and ADB for the process
- SAARC Secretariat should be empowered to drive the SAARC economic agenda
- None of these issues are new issues and South Asia's Track 2 has done research in most of these areas and readily available for Track 1 but an effective interaction mechanism between the two Tracks need to be formed

Concluding Remarks

- If the highlighted issues are addressed, Intra-regional trade can easily be boosted to about 20% in the region
- The benefits of more economic integration in the region will dilute the political differences and lead to deeper integration in the region
- A deeper integrated SAARC could be an important building bloc of a future Asian Economic Community

- Thank you