





**South Asia:
The Quest For Regional Cooperation**

**Editor
Ashok K Behuria**

**Institute for Defence Studies and Analyses
New Delhi**





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Preface

Need for Greater Cooperation

South Asia is home to 22 per cent of the of the total population of the world and accounts for 5.9 per cent of global GDP. In terms of human development index (HDI), the countries of the region are ranked quite low, i.e., in the overall list of 182 countries, Maldives occupies the best rank of 95 while Afghanistan is ranked 181.

In the post cold war years, the countries of the region have taken measures, at unilateral, bilateral and multi-lateral levels, to liberalize their economies and bring prosperity to their peoples. However, this has hardly altered the pattern of intra-regional economic interaction among the countries in the region. In fact, it is one of the least integrated regions of the world. Its share in the world economy is also quite unimpressive. As a region, it contributes only 1.7 to the global trade and intra-regional trade accounts for mere 6 percent the total trade for the countries in the region. In comparison, the percentage of intra-regional trade in the case of NAFTA, EU and ASEAN is quite high, i.e., 62, 58 and 26 respectively.

The reasons for such low level of intra-regional trade are several: tariff, non-tariff/para tariff barriers (customs surcharges, additional charges, rules of origin, internal taxes levied on imports etc.), lack of complementarities in production, lack of initiative to develop adequate trade facilitation measures (clearly defined border procedures, establish transport and communication networks, reduction of tariff etc.) and political differences amongst major regional countries.

This is why, South Asian Association for Regional Countries (SAARC) has failed make any substantial progress during the last twenty four years of its existence. In fact, the history of the region shows that the primary reason for slow integration has been lack of mutual trust and zero-sum approach towards bilateral relationship. Lack of economic cooperation has stifled cooperation in other areas like fighting poverty, illiteracy, crisis in governance and terrorism, improving agriculture, communication links, intra-regional tourism, people-to people-contact. Even if SAARC member countries have



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pledged to get together “to work together in a spirit of friendship, trust and understanding” and aim “to accelerate the process of economic and social development in Member States”, in reality the organisation’s activities have been hamstrung by political differences among them. This problem has also affected the performance of other regional initiatives like Bay of Bengal Initiative for MultiSectoral Technical and Economic Cooperation (BIMSTEC) and Mekong-Ganga Cooperation (MGC).

India, the largest economy in the region, has established itself as a stable democracy with a consistent rate of economic growth. In the post-cold war period, India liberalised its economy and sought to integrate with the wider world. It has adopted a more nuanced and balanced foreign policy towards its neighbours. Given the constraints within SAARC, it has sought to engage its neighbours both politically and economically at bilateral levels. It has entered into free trade agreements with Sri Lanka, Nepal and Bhutan. The new government in Bangladesh is also contemplating FTA with India at the moment. Analysts believe that these FTAs have gone beyond SAFTA- the free trade initiative under SAARC. While SAFTA could evolve as a meaningful initiative in the region and accelerate the process of regional economic integration, Pakistan’s insistence on resolution of political issues as a precondition to trade and economic cooperation has affected the functioning of SAARC as a regional organisation.

In recent years, the business communities as well as civil society groups in Pakistan have shown interest in trade and commerce between India and Pakistan in spite of political differences. They have argued that such cooperation along with cultural exchanges and people to people contact will create an atmosphere of trust and provide the context for meaningful political dialogue. However, this has not so far affected the policy of the Pakistan government vis-à-vis India.

Against this backdrop, the year 2008 witnessed significant political developments in South Asia. In February Pakistan reverted to civilian rule. In March Bhutan became a democracy. In April, elections were held successfully in Nepal for the constituent Assembly after years of political turmoil. Maldives ushered in multi-party democracy in

October and Bangladesh reverted to democratic rule in December. Such emphatic shift towards democratic and popular governments in South Asia, it was believed, would build on the reservoir of good-will (as is emphasised by many in the region) amongst people of South Asia, and lead the region towards peace and prosperity in the coming days. Against this backdrop, Institute for Defence Studies and Analyses (IDSA) had invited a group of strategic experts, scholars, academicians and civil society representatives from the neighbourhood to discuss the changing political context in South Asia and its impact on regional cooperation and security in the region. This was the second annual conference on India's neighbourhood titled- *Changing Political Context In India's Neighbourhood And Prospects Of Security And Regional Cooperation*. It sought to debate the prospects of security and regional cooperation in the region.

The presentations by distinguished participants outlined the common challenges that the countries faced and reaffirmed the need for the states in the region to shed their differences and engage with each other in meaningful ways. The participants held that most of the countries in the region had a chequered experience with the system of popular and representative governance. In some cases unelected institutions within the state have tried to retain their hold on the structures of power and sought to shift attention away from real issues affecting the people. It was critical therefore to focus attention on the common challenges, some of which are identified below.

* *Problem of governance*: It is said that good governance boosts economic growth while better governance inhibits conflict. Crisis of governance is at the “core of all problems in South Asia”, said noted Pakistani economist Mahbub ul Haq in 1998. This remains true even today. Much of the socio-economic problems that affect South Asian societies owe their origin to mis-governance or mal-governance at grassroots levels. Governance, in all its dimensions— civic, political and economic— provides the context for democratic politics and misgovernance retards the growth of democracy and development. This also generates popular disaffection and creates conditions for conflict and violence

* *Economic underdevelopment and disparity*: South Asia is one of the poorest regions in the world that houses 40 per cent of world's



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poor. Over 500 million live below poverty line (poverty line defined differently by different states). It is home to world's half of all illiterates. This is the region where more children are out of school than the rest of the world, and two-thirds of these are female. 260 million inhabitants lack basic health facilities; 337 million lack safe drinking water; 830 million are without rudimentary sanitation and 400 million go hungry every day. There is a link between poor governance, underdevelopment, disparity and social conflict. Taken together, they affect the growth of democracy.

* *Crisis of political leadership:* The political leadership in different countries in South Asia has not been able to provide the right direction to political processes. Rather than promoting democratic values that revolve around concepts of liberty, equality and inclusive growth, they tend to promote existing socio-cultural faultlines for narrow political gains. They have reduced democracy to electocracy where winning elections has become more important than building democratic traditions.

* *Ethnic, Social and Cultural Divisions:* South Asia is regarded as an ethnic boiling pot. Most of the countries in South Asia are multicultural, multi-ethnic and multilingual. It is natural therefore that there is a persisting competition for resources among different groups. Due to lack of transparency and accountability in governance, many groups have felt alienated from the political system and sought to adopt non-democratic means to achieve their goals. In some cases also, such divisions have led to deep and abiding political divisions along the lines of caste, class, community and ethnicity. In some cases this has led to disintegrationist pressures on the states. This has posed serious challenges to functioning of democracy.

* *Challenge of Non-state actors:* In the post-cold war period, the world has seen the rise of non-state actors as a serious threat to the smooth functioning of the state system. South Asia is no exception to this. Due to multiple reasons, historical, political and economic, almost all the states have witnessed varying degrees of insurgency over a long period of time. In recent years these insurgencies have assumed critical proportions due to proliferation of small arms and cross-border networks amongst militant groups. This has created serious internal security problems and hampered the growth of normal political activity

in many states. The Mumbai attacks of November 2008, has demonstrated how non-state actors can vitiate the security atmosphere and retard the process of peace and mutual understanding.

* Security and development: Security and development are interdependent categories. Advocates of human security emphasise that it does not merely mean the absence of violent conflict. It encompasses principles of liberty, equality, human rights, good governance and physical security which contribute to individual well being. The vicious cycle of lack of development leading to conflict leading to lack of development is well known. The challenge therefore is how to turn it into a virtuous cycle of development leading to security leading to development. In South Asian societies internal insecurities often grow out of uneven and unequal development. Hence more inclusive and egalitarian development between regions and cultural groups is essential to lead to greater security. This calls for efficient political systems, based on the principle of democracy and human rights, which emphasise on peace and development.

The participants in the conference agreed that regional cooperation held the key to economic prosperity and eradication of mass poverty. They argued that if the countries of the region came together to build economic prosperity for the people of South Asia, this would have tremendous effect on their internal politics and strengthen democracy, development and security in the long run. In view of the fact that economies of different countries in the region are growing at a decent pace, there is an opportunity for the countries in the region to link up with one another and address the common problems confronting them. The South Asian leaderships should seize the opportunity and work towards meeting the common problems collectively to bring peace and prosperity to the people of the region.

The papers presented in the conference are being brought together in this volume for wider dissemination of the ideas and perspectives contained therein. The book is divided into two sections. The first section deals with the issue of regional cooperation and the second focuses on country-specific studies.

In the first section, Hamid Ansari dwells on the need to knit the South Asian region in a network of mutually beneficial economic



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partnerships contributing to long-term political and social stability. He argues that despite movement towards popular and democratically elected governments, the possibility of regional cooperation remains marginal. He identifies a host of reasons ranging from crisis in governance, poverty, terrorism to mutual distrust. He seeks to allay the fears of the other states of the region by saying that India is seriously committed to the idea of having closer ties with all the states in the neighbourhood and it has taken the lead in building infrastructure for intra-regional trade in the full knowledge that the economic importance of intra-regional trade is considerable for the smaller regional economies. He is hopeful that there may be a scope for better relationship between India and other states because there is due recognition of the importance of good relations with India and an advocacy for closer economic and political relations.

Ataur Rahman, in his paper, outlines the common challenges and argues that costs of the existing approaches towards one another have been enormous. Therefore, it urges the countries of the region to develop a shared political approach to solve the common problems they encounter. In his paper, Susil Sirivardana focuses on the issue of poverty and has harped on the need to develop a pro-poor strategy through a clean, transparent and responsible system of governance accountable to the people and sensitive to their genuine needs. He has even raised the issue of ‘rethinking democracy’ by quoting exhaustively from the works of Rajni Kothari, the noted Indian political scientist.

Sadiq Ahmed has dealt with the issue of food security in his paper and argued that “regional cooperation can be an effective way to manage the farm productivity challenge and ought to be a key element in the design of future food security strategies in South Asia”. Saman Kelegama analyses the Colombo declaration of the 15th SAARC summit and emphasises on the need for effective implementation of all SAARC programmes and mechanisms by rationalization and performance evaluation on a regular basis.

In his paper assessing the economic effects of closer integration, Ganesh Wignaraja has urged South Asian countries to look east and draw lessons from the South East Asian experience. The lessons

that he has isolated in his paper are: (i) integrate with a large neighbouring economy; (ii) emphasize market orientation in regional strategy; (iii) Tailor policy mix to national circumstances; and (iv) involve the private sector in developing regional strategy.

The paper by S.D. Muni dwells on India's role in promoting regional security and cooperation. It argues that "Indian diplomacy is promising to be more accommodative of the neighbours' legitimate concerns", but its "neighbours need to learn to be able to appreciate the complexities of the problems India has had to face". He affirms that at times, "they have taken steps consciously and launched initiatives to vitiate India's security and stability", however, a "change of perspective on both sides of the diplomatic equation would lay the foundation of a new partnership at the regional level".

The papers in the second section take a critical look at the political situations in some of the individual countries in the region plagued by conflict. The papers underline the need to understand the changing political dynamics in individual countries in a dispassionate manner. For example, Babar Sattar in his paper focusses on regional security cooperation asserts that there is a need to rethink "the traditional security doctrines of Pakistan, India and Iran and the strategies deployed to pursue the perceived strategic interests" to bring about meaningful security cooperation amongst the states in the region. In their papers on Afghanistan and regional security, Haroun Mir and Walliullah Rehmani have pointed to the problems inherent in Afghan society and polity and argued that regional and international actors have contributed to the worsening of Afghan situation over the last three decades. They hope that a real democracy in Afghanistan together with a constructive regional initiative to bring peace could secure peace for Afghan people. The paper by Aditya Adhikari lays out the dynamics of Nepalese politics passing through a critical transition today.

The papers, as mentioned above, are based on the presentations and discussions in the IDSA Annual Conference 2008 on 'India and its Neighbours'. It is important to note here that during the course of the discussions many innovative ideas were put forward by the participants which provide food for thought for scholars and analysts.



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For example, it was suggested by Mahfuz Anam, a senior Bangladeshi journalist, that leading scholars and experts should conduct research on the costs of non-cooperation by quantifying the economic losses that accrue to the states because of their unwillingness to cooperate with each other. Similarly, there was a suggestion that in the wake of the global economic downturn the finance ministers of different states should meet informally within or outside the forum of SAARC to discuss issues of mutual concern. There were also references to taking collective measures to develop a WTO type regional dispute settlement mechanism and coordinate approaches on foreign and security policies. There was also a bold suggestion for a defence ministers' forum outside the framework of SAARC by Prof. S.D.Muni to discuss common security issues in an informal manner. It was commonly held that rather than waiting for the resolution of their political and security problems, South Asian states should use economic cooperation as a tool to create a conducive atmosphere for meaningful discussion on complex and intractable issues, failing which 'regional cooperation' will remain a pipe dream.

Above all, the papers in this volume reiterate that people of South Asia have natural affinities based on shared history, geography, and culture. There is a natural bonding amongst the people which transcends the relationship between countries and governments. One expects that in the coming days, the states of South Asia will take these facts into account while refashioning their policies towards each other and towards the region, and take initiative to deal with common challenges facing them collectively. This will lay the foundation for a better tomorrow for the people of South Asia.

We would like express our sincere thanks to Shri N. S. Sisodia, Director General, IDSA, for his guidance, encouragement and support. We also gratefully acknowledge the active involvement of Sreeradha Datta, Smruti Pattanaik, Sumita Kumar, Alok Bansal, Nihar R Nayak, Vishal Chandra and Anand Kumar— members of the South Asia Cluster at IDSA— in the deliberations of the conference and in planning this volume. We hope this volume will be of use to policy-makers, strategic analysts and students of international relations.

New Delhi
October 2009

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Part One

Perspectives on Regional Cooperation







Changing Political Context in South Asia and Prospects of Security and Regional Cooperation*

Hamid Ansari

The logic of geography is compelling. For India, the neighbourhood radiates in concentric circles, buttressed by history, cultural affinities and economic necessities.

Our political commitment to closer ties with our neighbours in South Asia is serious. India's security interests are better served if our neighbours evolve as viable states with moderate and stable political and social environments and vibrant economies. We wish to see South Asia at peace with itself, leading to ever widening circles of security, peace and prosperity in the region.

The theme of this seminar is twofold: security and regional cooperation. Both need to be understood in themselves as also in their mutual relationship. Their logical manifestations could be (1) security exclusively in national terms (2) regional security cooperation (3) regional economic cooperation and (4) a mix of all these resulting in comprehensive security. In terms of linkages, it would be valid to ask if the perceived regional economic cooperation is to be the first step in our quest for regional security cooperation, or vice versa.

Perceptions, as this audience is well aware, have changed overtime. At one point security in the conventional sense offered a menu of choices in regard to security cooperation and suggested options ranging from alliances to collective security, security regimes and security communities. At a later stage, frameworks for communication and dialogue emerged. Each of these was experimented with; results varied from region to region.

¹ Adapted from the Keynote Address at the International Seminar on "Changing Political Context in South Asia and Prospects of Security and Regional Cooperation", 5 November 2008.

Regional economic cooperation has tended to be influenced by a set of factors relating to intra-regional relations and convergence of political interests and cultural compatibility. The potential for economic cooperation is stymied when historic fears cloud security perceptions.

II

South Asia presents a varied picture towards the end of 2008. In some areas, forces of change are resonating noticeably. Bhutan has opted for a new system of governance through a constitutional monarchy. Change is the message of the election in Maldives last week. Nepal has witnessed historic transition from a monarchy to a democratic republic with a new leadership, and a new constitution in the offing. Pakistan has reverted to civilian rule with a new Parliament and a democratically elected President.

Less specific are the readings on Bangladesh and Sri Lanka. The former seeks a return to constitutional democracy and the latter an end to internecine strife.

The conflict in Afghanistan remains a source of considerable concern and calls for innovative solutions premised on national unity.

India, having registered rapid growth in recent years, is itself moving into a period of state and national elections.

The move towards popular and democratically elected governments in South Asia, however, has not eclipsed the existing challenges to governance in all the countries of the region. Poverty and economic disparities coupled with ethnic and social divisions have created political and social fault lines that have been exploited by non-state actors with their own agendas.

Human Development indices of most countries of South Asia are not flattering and it would a miracle if the targets of the Millennium Development Goals are achieved.

Yet, economic growth has continued as most of the South Asian countries have liberalised and moved towards market economies. Regional cooperation has made headway within the framework of

SAARC which itself has expanded to include Afghanistan as well as nine observers.

New initiatives on the operationalisation of the SAARC Food Bank, establishment of the SAARC Development Fund, setting up of the South Asian University, the launching of negotiations to bring services into SAFTA and signing of the Convention of Mutual Assistance in Criminal Matters are significant for regional integration.

The question that one must ask is whether the changed and changing political context in many SAARC countries would confine itself to domestic politics or go beyond it to develop a changed context for security and economic cooperation with India? In other words, do the new political elites in our neighbourhood harbour a new paradigm of bilateral and regional cooperation?

We have to admit that the traditional pattern of bilateral state-to-state relations has already been transformed in varying degrees as a result of globalisation. Governments today do not control information or patterns of human interaction. Across the region, we see a web of connectivities between political actors, media centres, civil society organisations and commercial entities. Common people freely exchange views and ideas on their governments and their lives.

The prospects of security and economic cooperation are thus correlated to the ability of States to broad-base their relations beyond the traditional frameworks.

Let me venture to summarise some overarching themes that characterise the emergence of this new political context.

First, there is recognition of the importance of good relations with India and an advocacy for closer economic and political relations. There is also a desire for updating, where relevant, the existing instrumentalities of such cooperation to reflect the new ground level realities. The question for renegotiating existing treaties has been raised in this context.

Second, India on its part has tried— incrementally and non-reciprocally— to incentivise economic cooperation through confidence

building measures. As a result, some in our neighbourhood have begun to feel that a prosperous and economically vibrant India is an opportunity for them to reap both economic and political benefits.

Third, political elites are increasingly emphasising that the desired economic outcomes transcend investments, growth or development. The focus is on the human development of people, the quality of the lives of citizens and even Gross National Happiness!

Fourth, all countries in South Asia realise that globalisation would be meaningless without the improvement of intra-regional connectivities. Informal trade and third country trade is still predominant with formal intra-regional trade constituting under 5% of South Asia's overall trade.

On the other hand, negative security perceptions continue to cloud cooperation in tackling trans-national and cross-boundary issues. These include security concerns such as terrorism, drug-trafficking and money laundering, as well as economic and developmental issues such as food, water, climate change and energy security.

Some initiatives need to be mentioned. India has taken the lead in building infrastructure for intra-regional trade in the full knowledge that the economic importance of intra-regional trade is considerable for the smaller regional economies. Taking the theme of connectivity forward, the SAARC Transport Ministers identified specific corridors for implementation linking Nepal, Bhutan, India and Bangladesh. A draft Motor Vehicles Agreement and a draft Railway Agreement are also being negotiated.

The expectation is that cross-border trucking and container movements, improved regional air and rail links and upgraded customs and trade facilitation would knit our neighbourhood in a network of mutually beneficial economic partnerships contributing to long-term political and social stability.

Such partnerships are the need of the hour and can help address problems that cannot be solved nationally. Two instances of these lie in (i) rivers and flood control; and (ii) energy generation, energy trade and energy transit. Both are critical to the achievement of development goals of the countries of South Asia.

Experience elsewhere in the world shows that political constraints need not be permanent barriers to economic cooperation and that the latter could help create a climate of opinion to resolve conflicts.

III

We live in times of great change. The challenges we confront overflow national frontiers. The public in South Asia has, in diverse ways, signalled its impatience with the politics of the status quo. This is most evident in the younger generation. It is now for the governments to think innovatively and encapsulate this impulse in national policies.

History is witness to occasions when bold thinking has led to creativity. Why should South Asia be an exception and remain embedded in the unproductive routine and ritual of six decades?

Would it then be altogether unrealistic to hope that South Asian cooperation would seek to achieve the following?

- Free travel and trade across frontiers, a euro-style single currency, environmentally sustainable and regionally balanced development.
- Security coordination resulting in Joint action on crime and terror.
- Speak with a single voice and work closely together on trade issues and development policy.
- Develop a mechanism for dispute resolution.
- Coordinate approaches on major foreign and defence policy questions?

The meandering River of Time is mighty and can flow in many directions. The answers to the above questions lie in harnessing it for common good and regional betterment. The scholars and analysts in the region should go beyond identifying the obstacles and pitfalls and suggest solutions.





Common Challenges Facing South Asia: Perspective from Bangladesh

Ataur Rahman

Regions like nations are, in reality, ‘political communities’ where states and people make fundamental value judgments on peace, conflict, economic change, stability and progress. The political context is therefore, crucial in predicting the process of change or decay, and in identifying common challenges and common futures of a region. Reflecting on the last several decades, it can be observed that South Asia suffers from huge complexities and contradictions as a region. Although the region is a compact one with common history, it is divided into eight unequal states that vary widely in resource endowments and military capabilities and continue to search for common identity and meaningful cooperation. The current political instabilities and transnational security threats, as well as food and energy shortage, illustrate the fact that regional peace and stability can only be achieved through identification of common goals and strengthening of the the will and resolve of member states to achieve those goals.

The challenges to survival and well-being of states and individuals in South Asia come, often in contradictory fashion, from changes within states as well as from outside, compounded by the speed in which these changes are taking place. Obviously, traditional tools for dealing with these challenges need to be continually reevaluated and re-designed. This paper makes an attempt to develop a political perspective focusing on a broad array of common challenges that need to be resolved on a collective basis. Indeed, this political perspective sensitizes us to move beyond psychological barriers, suspicions, mistrusts, and it is anchored on the vision and ability of political leaders to deal with an expanding agenda of cooperation with growing awareness of the interests and priorities of the region as well as primacy of human security.

Challenge of Governance and Democratization

Regional cooperation often implies going beyond the nation state. Yet the possibilities of such cooperation and integration depend heavily

upon the coherence and viability of the states and state structures within a given region. The absence of viable states both in terms of effective state apparatus and mutually accepted territorial boundaries makes the process of region-building difficult. In South Asia, the instability of regimes, absence of democratic values, erosion of economic vitality and spread of religious and ideological extremism weaken the states and their domestic governance. The new security threats, national and transnational, in the form of terrorism, criminality, drug trafficking, illegal migration and environmental degradation, worsen public order and disrupt peaceful communication. The states erode political legitimacy and often fail to provide minimal conditions of security within their borders. As a result, instability and violence spill over and pose threat to peace and stability of the whole region.

All most all countries of South Asia have been witnessing 'governance crises' in varying degrees in the past decades, but in some countries, particularly Pakistan, Sri Lanka, Nepal and Bangladesh, these crises have deepened. The most volatile country is Pakistan which was shattered by tumultuous events, chronic instability and terrorism. The tragic assassination of former Prime Minister Benazir Bhutto, the unending series of terrorist acts, complexities of democratic transition, and ramifications of 'global war on terror' have transformed Pakistan into a 'crisis state', which has serious impact on regional security and cooperation. The internal developments within Pakistan as well as terrorist acts like the Mumbai attack emanating from it have stalled the process of peace and mutual confidence building between India and Pakistan.

Religious activism and terrorist activities in Pakistan, especially after 9/11 period, have affected internal security situation in India and Bangladesh, and created serious governance and security challenges for the region as a whole. In Pakistan, following the Red Mosque incident, terrorist incidents, particularly 'suicide attacks' have increased drastically. After a brief lull, following the elections in February 2008, the terrorist attacks have picked up in Pakistan. Undeterred by military action in Swat and Waziristan, the terrorists have increased their attacks on military and police facilities. This is a cause of serious concern because if Pakistan burns the states in the neighbourhood will certainly be affected by it.

Bangladesh has also been affected by terrorism in its own way. Following the the serial blast of August 2005, Bangladesh took strong action and six main leaders of a group called Jamaatul Mujaheedin Bangladesh (JMB) were executed in 2007. Terrorist incidents have continued nonetheless. The mutiny staged by a section of the Bangladesh Rifles (BDR) on 25 and 26 February 2009 in Dhaka demonstrated how the virus of radicalism has even affected the security forces to certain extent. In Sri Lanka, the violent armed activities perpetrated by Tamil militants had created severe security concerns until the defeat and decimation of the LTTE (Liberation Tigers of Tamil Elam) in May 2009. Nepal has witnessed several political upheavals since early 1990s and its democratic transition during 2007-2008 remains vulnerable to disruptive forces. India has been shaken by several terrorist attacks in recent years. In a statistics given by the Institute of Conflict Management total deaths in terrorist activities in India were 2598 in 2007, and 2611 in 2008. In Pakistan the number of casualty was 3599 in 2007 and 6715 in 2008. In Sri Lanka the corresponding figure was 4377 in 2007 which jumped to 11144 in 2008 and and 15565 in 2009 (till October) because of the military operations against LTTE during 2008-2009. In Nepal there were 97 casualties in 2007 and 81 in 2008. In Bangladesh there were 8 casualties in 2007 and 59 in 2008.

South Asia is a cultural boiling pot. The region has witnessed many conflicts around the issues of language, religion and ethnicity. The ongoing militancy in Kashmir, separatist movements in Northeastern India, movement for Khalistan in Punjab, Mohajir movement in Sindh and the Baloch insurgency in Pakistan and the ethnic conflict in Sri Lanka are some of the major problems that continue to test the endurance of the South Asian states. Many of these conflicts have cross-border linkages which have taken new dimension after 9/11. India and Pakistan have accused each other for supporting militant movements in their midst. India has blamed Pakistan for providing material support to Kashmir militants and extremist Islamic groups operating inside India. Similarly, Pakistan has held India responsible for adverse propaganda against her as a failed state sponsoring terror in the region. Bangladesh and Nepal have also voiced their concerns against India which, they think, has tried to marginalize them in the regional strategic and security theatre, and diminished their influence. In fact, it is an irony that when the states in the region- the most

densely populated in the world- are trying their best to improve the living standard of their people, these internal governance and security challenges cast their shadows on the prospect of regional cooperation.

The democratic deficit in South Asia further compounds the deteriorating governance situation. While there is a growing appreciation of democratization in the countries of South Asia, they are facing problems of resource mobilization, distribution and efficient execution of policies. Except India, democracy has failed to take roots in other countries in the region. The political leadership of these countries are pledged to democracy and the people are also clamouring for it, but the problems of corruption, mis-governance, criminalisation of politics and ethno-cultural cleavages have stunted the growth of democratic institutions in these countries. With liberalization of the markets and increasing assertion of civil societies in recent years, the prospects of democracy looks brighter today than ever before. . But in the short term, the transitional societies in South Asia are experiencing instabilities and violence of different sorts. . Good governance remains the avowed goal yet personality cult, bureaucratic dominance, the rent-seeking character of social forces, state repression and lack of accountability remain the main stumbling blocks for these societies. The discernible pattern of rise of religious and sectarian forces in political process erodes the democratic culture of tolerance. The South Asian countries have a long way to go to transform themselves into truly democratic societies.

There is an agonizing realization that in most of these countries, democracy as a mode of social interaction and governance has accentuated conflicts because of problem of economic inequality which seriously affect the civil and political rights of the people of all South Asian countries including India – the largest functioning democracy in Asia. It is, therefore, extremely necessary for the South Asian states to address the problems of social inequality, organized crime, corruption in public institutions and electoral arena, and poor leadership that undermine the ethos of democracy. The governments in these countries are often more responsive to demands of the politically active and best organized groupspowerful urban and rural patrons and their own vote banks rather than genuine needs of the people at large. Such politics of favouritism encourages corruption, which is rampant in all spheres of governance. . The diversion of

development aid public funds for party or individual gains has accelerated the incidence of corruption on a wider scale, particularly in Pakistan, Bangladesh and Nepal. In fact, corruption is one of the most potent factors for transnational crimes, violence, terrorism and political instabilities in these countries.

In this context, deepening of democracy through institution building and spread of a human rights culture is imperative for South Asian countries. So far, the process of democratization in these countries has been superficial. It is limited only to procedural aspects of democracy, i.e., holding of elections and adoption of a democratic framework in the shape of a constitution outlining the functions and powers of different branches of the state, i.e., the executive, the legislature and the judiciary. However, in practice, democratic values are clearly set aside while running these institutions. The degree of popular participation, the quality of debate on important issues, the availability of political alternatives and choice of policies are often less than optimal. In fact, the nature and prospects of democracy are also affected by internal as well external forces, particularly globalization, in a number of distinctive ways. This can be discerned in the formation of political parties and interest groups, the working of bureaucratic institutions, civil society and international agencies, and the way they create political space and influence the allocation of resources.

Transnational Security Challenges

The strategic environment of South Asia is conflict-ridden, and for long the relations among the states have been influenced by security considerations. The major states of the region are locked in a counter-productive arms race and competition for acquiring nuclear capability which is threatening long-term social and economic well-being of the people. India's growing superiority and strategic dominance have prompted Pakistan to develop nuclear capability as a deterrent against any possible Indian attack in future. The nuclear dimension has changed the dynamics regional security of South Asia and raised the level of international concern. However, simultaneously, there is a growing realization of a common challenges confronting these states today in the shape of non-traditional security threats, i.e., transnational crimes and terrorism, ethnic –religious violence, illegal migration,

proliferation of small arms, drug trafficking, spread of infectious diseases, climate change and environment etc. This list is growing as the states are getting increasingly aware of their limitations in dealing with these issues individually .

Terrorism and trans-border crimes have increased manifold in South Asia in the post-cold war days raising the level of mistrust and suspicions amongst nations and peoples. In fact, the issue of cross-border terrorism has been the single most important factor responsible for sharp deterioration in India-Pakistan relations. Accusations of proxy-war, suicide bombings and other acts of sabotage continue to hinder constructive engagement between these two countries. In the Northeastern part of South Asia, terrorism has thrived in the guise of ethnic separatism which has become a major bone of contention between India and Bangladesh. The Maoist insurgency in Nepal has also featured as point of worry in India-Nepal relations. The issue of Tamil separatism in Sri Lanka and India's role in the past in exacerbating the problem had affected India-Sri Lanka relations during the 1970s and 1980s. Given the ethno-cultural diversity of the region and overlapping of ethnic, religious and linguistic identities across states, it is but natural that inter-state relations will be affected by internal politics.

In the context of South Asia, the twin issues of 'freedom from want and freedom from fear'- the two main components of human security- are far from realization when one observes that issues of poverty, deprivation, environmental degradation are mixed with class, caste and group violence and the political process is manipulated by rigging, black money and extortion. This has affected the process of evolution of an efficient, effective and visionary leadership who could translate the dreams of the millions into reality. No wonder, efforts aimed at regional and sub-regional cooperation remained largely unsuccessful and often became subjects of controversy for the want of any creative thinking.

From Bangladesh perspective, transnational security challenges have assumed a new significance for a number of reasons, and among those, the inflow of small arms and drugs from external or transnational sources is the most important. Estimates differ and quantities of small arms inflow in Bangladesh perhaps will be less than what is

flowing into India or Pakistan. But it is causing security threats to Bangladesh for at least two reasons: first, the rate of inflow has stateded increasing at an alarming pace and the impact of small arms proliferation, and drug use has been easily felt in densely populated cities. The flow and use of small arms and drugs has almost become an autonomous process and escaped the control of administration and law enforcing agencies. The following major transnational security challenges can be highlighted from Bangladesh perspective:

- Transit of arms and drugs through Bangladeshi territory– the coastal areas, Cox’s Bazar in particular, are used in arms transit; ports are reportedly used as transit routes for drugs from the ‘golden triangle’.* The case of arms transit to Northeast India from or through Bangladesh remains an irritant in Bangladesh-India relations.

- India-Bangladesh borders are not easy to patrol due to resource crunch and complex geographical conditions. A bewildering array of conflicts takes place in the north-eastern sub-region involving state and non-state actors because of this. As a common transit point for India, China and Myanmar, this region poses a complex challenge for Bangladesh as well as India.

- Piracy and dumping in the Bay of Bengal is a common phenomenon today and it is likely to increase in the coming years. Because of increased dependence on marine fishing all over the world, Indian, Korean, Thai and Burmese fishing trawlers regularly enter Bangladeshi territorial waters. This has led to increased piracy and deviant shipping in the ports and dumping of hazardous waste.

- Border Skirmishes – intrusions, abductions, forcible harvesting,

* South East Asian region is known for growing narcotics for centuries. The region remains a source of concern for illicit drug production and trade even today. Poppy is grown in an area infamously known as the ‘Golden Triangle’ - a relatively lawless terrain where Myanmar, Thailand and Laos meet. The CIA Factbook says that Myanmar has emerged as the “world’s second largest producer of illicit opium”, after Afghanistan. Several poor ethnic minorities living in the remote mountainous areas of the country depend on poppy cultivation and their sale for their survival and these areas are also under the sway of several insurgent groups drawing their sustenance from the proceeds of this illicit trade.

shooting and killing along the Bangladesh-India borders have increased alarmingly over the years.

- Insurgency Problems in the Chittagong Hill Tracts (CHT) continue to pose risks to Bangladesh security. The strategic aspect of the problem of a low level but prolonged insurgency in the CHT has been removed by the 1997 Peace Accord. But problem of implementation-particularly, rehabilitation, land dispute settlement and functioning of the political process in terms of the Regional Council- remains. The armed dissident groups who are finding shelters across the borders are resorting to violence against the Bengali settlers which is a threat to internal security.

Human Security Challenge

Human security is a comprehensive term that includes protection of human beings from a wide range of threats including military, economic, social, cultural and environmental. This concept is thus linked to current themes of globalization, governance, human rights, terrorism and state collapse. The common challenges confronting the South Asian states have to be understood from human security perspective and the governments will have to be sensitized to the issues of poverty, ethnic marginalizaion, food-scarcity, non-availability of drinking water, housing and shelter and energy. South Asia the region where there is largest concentration of poverty and it is afflicted by a number of protracted conflicts and insurgencies. The region is home to all major religions of the world and about 22 per cent of the total population of the world. India occupies a central and overwhelming position because of its size, its diversity, its commitment to democracy and its economic prowess. . The India-centric character of the region is also reflected in the fact that all the six South Asian countries have land or maritime borders with India but none of them have borders with each other, excepting Sri Lanka and Maldives. A second feature is that problems of insecurity in both traditional and non-traditional terms emanate from within the region, and less from outside. More than half of the world's poor population (about 600 million) live in the region.

The issue of food security has been a primary concern in South Asian countries irrespective of their sizes and it has acquired a new

dimension in recent years. The increasing pressure on land, marginalization of small and marginal farmers, frequent occurrence of natural calamities, deteriorating level of soil fertility have all made food security a major concern for the states of the region. Food security is defined in terms of the availability of food to meet the present and future needs of the people. There is also the problem of making it accessible to all irrespective of class, gender, ethnic, religious or other considerations. The principles that guide food security, like availability, access, adequacy, policy and processes must inform public policy and system of governance.

South Asian countries have succeeded over the past decades to attain a level of self-sufficiency or near-self-sufficiency in food grains. This has been a remarkable achievement. But the natural disasters and state policy failures often lead to crises, and serious deprivation occurs for the poorer segments of the region that constitutes an overwhelming part of the population. The recent crisis of rice and other grains in Bangladesh due to severe floods and cyclone illustrates the vulnerability of a large number of people and the lack of concerted action by the regional states. To ensure sustainable food security is one of the most talked-about issues in the SAARC regional forum, but no concrete plan or strategy has ever been drawn up over the years in this regard. Indeed, regional cooperation is imperative to meet such common challenges. Similarly, energy security also requires a common regional approach in terms of detailed assessment of all energy resources, identification of major challenges in this sector including environmental fallouts, and evolution of a common strategy for harnessing energy potential for the benefits of all states in the region.

The issue of water is another crucial area where states of South Asia have hitherto failed to evolve a common approach. The Ganges is one of the mightiest rivers in the world and determines the fate of millions of people living by its sides. The water dispute between India and Bangladesh has continued for a long period from the late 1950s when India drew up a plan to construct the Farakka barrage. The claims and counter-claims leading to a series of negotiations produced a water-sharing arrangement in 1977 for a short period. The question of long-term sharing of Ganges water created lot of mistrust and suspicions between the two friendly countries. The 1996 Water Treaty

with a sharing formula and guaranteed clause has not been able to satisfy the flow and utilization of water during the lean season. The issue has also been taken by Bangladesh to the United Nations, but it has not yet been resolved despite flurries of negotiations. The water dispute between India and Bangladesh can be regarded as an early-warning for many such resource-based disputes in future which can have enormous security ramifications.

If South Asia is to develop as a region, there needs to be considerable good will among the states and a collective desire to settle disputes in a spirit of cooperation. In case of the Association of Southeast Asian Nations (ASEAN), it is remarkable that the largest state of the region - Indonesia has acted in a generous manner to allay the security fears of other states and contributed to the efforts for greater integration of the region. India with its stature and confidence can assume such a role and be prepared to sacrifice some of its interests for the long-term interests of the region. Other states in the region must also acknowledge Indian benevolence and be prepared to work with India without any prejudice to lay the foundations of a cooperative economic and security architecture.

Challenge of Climate Change

There is a painful realization in South Asia that natural disasters like floods, cyclones, earthquakes and Tsunamis pose serious threats to regional development. In fact, these phenomena related to the issue of climate change constitute a common challenge for all the states and require collective action at the national, regional and global levels. The great Himalayan eco-system and Ganges rivers system affect the agriculture and livelihood of millions of people in South Asia. These eco-systems must be sustained for economic development and energy needs of the region.

Climate change is no more a subject of scientific debate. Excessive rain in the upper catchments have led to heavy floods at one level and failure of monsoons have led to drought at the other. Human interventions in the shape of big dams and inter-linking of rivers have resulted in severe ecological and environmental problems. The rise in sea-level due to global warming and the melting of Arctic sea threatens the existence of low-lying islands like Maldives and human

habitation in coastal areas. In fact, climate change issues need to be addressed seriously as a common regional challenge which confronts both present and future generations. The 15th SAARC summit in Colombo in August 2008 reiterated the need for an integrated action programme in this regard in collaboration with the global community. It is now urgent that a comprehensive adaptation plan be developed with mutual collaboration among the neighbouring countries under the SAARC umbrella for dealing with climate change impact and adaptation issues. The SAARC Meteorological Research located in Dhaka, which has some experience in this field may work as a regional platform for this purpose.

Conclusion: The Challenge of Building Trust

The politics of South Asia is not easily explicable by familiar theories of modernization and international politics. There is a trust-deficit among nations in the region due to which they suspect each other's motives and adopt a cautious approach to regional integration.. Such misunderstanding makes it difficult to settle differences amongst them and work together on a blueprint of cooperation. Sometimes, even the low-intensity conflicts between states engender inter-ethnic and inter-communal conflicts within nations. The rising assertion of communal groups in different states presents a critical challenge for the leaders and policy makers who find it difficult to reconcile the pressures of ethnic-religious communities with the need and demand for greater regional cooperation. Negotiations between states should involve different communities and civil society groups and, therefore, seek solutions to the problems through as many tracks as possible. Track II diplomacy involving and encouraging moderate leadership may serve as an important mechanism to build trust and remove stereotyping and negative image about neighbours.

The ever-expanding communication networks need to be used to disseminate relevant information in an innovative manner for influencing popular opinion in favour of cooperation among neighbours. The communication networks can be used as an effective instrument in changing individual perceptions. The unique geopolitical reality of South Asia places India in a situation of sharing land and maritime boundaries with all South Asian states. The enormous economic weight of India has placed her in an advantageous position in trade and

investment vis-à-vis neighbors. The superiority of India in military capability and its international stature have put it in such a position that the neighbours suffer from an insecurity complex vis-à-vis India and misinterpret even enlightened gestures by India. A greater onus, thus, devolves on India to promote an environment of trust and confidence in the region. An unusual opportunity exists today to guide change with imagination. The political leadership in India is an enlightened one and has the capacity to evolve a new regional policy that can show clear vision in directing the course of change with new mindset and creativity. The external powers are no longer involved in jockeying for influence in the region as they did in the past. India is fast adapting to the changing global realities by 'rediscovering' the United States (US) as its friend and ally without jeopardizing its good relations with China and Russia. The US has also found in India a major regional power with a democratic and pluralist system that can contain China's influence.

Therefore, peace and stability in South Asia, to a considerable extent, will depend on the way India evolves her foreign and security policies. There seems to be a built-in dissonance between India and its neighbours which needs to be overcome at all costs. There is a compelling need for political leadership in South Asia to find new ways of diagnosing and solving problems. They must envision and achieve goals beyond national boundaries, think long-term despite pressure to achieve on short-term basis. They have to respond to the new challenges faced by the region, move forward and act for continued survival and progress. In this perspective, much depends on South Asian leadership to share goals with people, to change perceptions, build communications, and develop a common outlook to cope with myriad challenges faced by the region. Indeed, there is an urgent need for a shared political approach at this point to meet the challenges faced by all the states in the region.

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Pro-Poor Thought and Strategy: Major Impediments amidst Groundswell of Change

Susil Sirivardana

Poverty cuts across all other sectors like ecology, gender, security, and hence is indelibly fused with all the other issues. Particularly in South Asia the crisis is multifaceted, and one crisis sector is connected with another. The discussion comes at a time when we are at the threshold of sixty-one years of independence in several of our countries.

The paper is in three parts. The first part is a reconstructive summary of Pro-Poor Thought and Strategy (hereafter PPTS). This is to better contextualize the issues discussed in the second part, under Major Impediments amidst Groundswell of Change. It is also a necessary backdrop to the title of this paper. The second part discusses why something which appears to be obvious to commonsense has not happened. How is it that governing elites have dismally failed to capitalize on the fact that a proven strategy for overcoming poverty has existed for decades at their very doorstep?

Finally in the third part, we try to connect the idea of the hiatus between PPTS and the Groundswell of Change. Given the state of disconnect and unfilled strategy space, are there yet grounds for sustaining the hope of bringing PPTS to centre-stage?

Pro-Poor Thought and Strategy: Reconstructive Summary

Pro-Poor Thought and Strategy (PPTS) is a well-articulated and conceptualized discourse, sustained over two decades in time, with a rich theoretical foundation. The first precise articulation of such concepts as “pro-poor perspective, pro-poor strategy and pro-poor development plan” occurred in the Report of the Independent South Asian Commission on Poverty Alleviation (1992). There is also substantial literature on the participatory development paradigm. The South Asian Perspectives Network Association (SAPNA) has played

a singular and sustained role in systematically developing the theory and practice of PPTS, with over eight interrelated book-length publications to its credit. It made a major contribution to the Report of the Independent South Asian Commission.

All South Asian countries have an array of landmark success cases in the theory and practice of PPTS. In the first generation of success cases are the Self-Employed Women's Association or SEWA of Ahmedabad, India, which started in 1972; the Bangladesh Rural Advancement Committee or BRAC, also started in 1972; the Chipko movement of the Garhwal Hills in India started in 1974; the Small Farmer Development Programme of Nepal started in 1975; SAPNA's groundbreaking first publication was published as *Towards a Theory of Rural Development* twice in 1977 and 1988; the Grameen Bank started in Bangladesh in 1976; the Working Women's Forum (WWF) in Tamil Nadu, India started in 1978; the Orangi Pilot Project (OPP) in Karachi, Pakistan, started in 1980; the Agha Khan Rural Support Programme in Gilgit in Pakistan started in 1985; and the Janasaviya Poverty Alleviation Programme in Sri Lanka started in 1989. Further, there are an unnameable number of programmes and projects which have been dotting the subcontinent. They turned to many new fields and problems that emerged from the ground up. They included savings and credit, agriculture and irrigation, housing by the poor, gender and women's development, primary health, ecology and forestry, childcare, human rights, civil liberties and spirituality. A distinctive quality cutting across the whole macro-micro scene was the massive initiatives and participation of women. Many organizations of the poor, and especially the small groups, were led by women.

These landmark success cases are associated with a rare critical mass of pioneers and visionary leaders. Ela Bhatt of SEWA, Fazle Hasan Abed of BRAC, Sunderlal Bahuguna and Chandi Prasad Bhatt of the Chipko movement, G.V.S. De Silva, Wahid-ul-Haque, Niranjan Mehta, Md Anisur Rahman and Ponna Wignaraja of SAPNA, Muhammed Yunus of Grameen Bank, Jeya Arunachalam of WWF, Akhtar Hameed Khan of Orangi PP, Shoaib Sultan Khan of AKRSP and President Ranasinghe Premadasa of Sri Lanka together with others like Akmal Hussain of Pakistan and Shaik Maqsood Ali of Bangladesh are household words in this vocation. They have demonstrated an abundance of moral imagination, moral authority, a

commitment to ethics, cultural rootedness, an experiential understanding of participatory development from within the process, innovativeness and creativity.

The large majority of the pioneers and visionary leaders and thinkers came from non-state civil society. They were invariably pioneers of the early non-governmental movements, which were to proliferate and become vapid after they were overrun by easy money and absence of serious commitment. Only in Sri Lanka the success case was state-led by a visionary political leader. Another point worthy of note is that this phalanx of South Asians was complemented by a corresponding phalanx of visionary thinkers in the developed world who acted as a unique group of catalysts, friends, learners and supporters – of the calibre of James Grant, Barbara Ward, Dag Hammarskjöld, Hans Singer and many others. They further helped to validate and deepen the discourse.

We conclude this part with a working definition of PPTS. Pro-poor is a key concept in the vocabulary of the participatory development paradigm and is immediately contradistinguished from the technocratic paradigm. Secondly, it is value-based, and therefore, sourced in the endogenous moral-spiritual culture of the South Asian poor. Third, the main actors in its development process are the poorest and the less poor, primarily identified through the indices of deprivation and assetlessness. They are placed at the centre of their own development process, and are its unambiguous owners. Within the development process they are decision-makers as well as doers, and are actively encouraged by the support system which interfaces with them. Fourth is the role of the support system, which is the state (in its programmes) or a non-state organization. The poor cannot combat poverty without external support. This support has to be sensitive and empathetic. It is neither technocratic nor purely monetary support mechanistically delivered to them from above. Fifth is the core methodology of social mobilization, without the aid of which the poor cannot understand the poverty-creating causes, its sources, its changeability, their own agency in the process, and the availability of a core methodology for doing so. Importantly, social mobilization is acquired collectively, so that large numbers can benefit from it. At its core is conscientization, which is Paulo Freire's word for the poor to fully repossess the aptitude for critically understanding their poverty

and the world around them and how they could self-reliantly renegotiate their lives out of Darkness into Light (in the words of the novel *The White Tiger*). Hence, social mobilization without the dimension of conscientization is ineffective. So we call this “rigorous” social mobilization. Through it, they come to practise an action-reflection process which is the normal method of learning and unlearning that every self-aware person uses. There is a natural evolutionary process of organizing themselves, leading to empowerment. When mature, this results in the poor acquiring countervailing power, which is the power of non-power, sans violence and arms. This methodology has to be learnt from a highly trained mobilizer or change agent, who invariably comes from outside. The net result of social mobilization is to help the poor to transform themselves from objects to subjects. The transformative dimension is critical to the success of PPTS. Sixth, the poor have an ability to save first, and then once sufficient monies are accumulated, go on to give credit to themselves. This invariably results in considerable accumulation of resources. On a national scale, this accumulation process could have a positive impact on GDP growth. Seventh, from a budgetary viewpoint, the State must ensure a net transfer of resources to the poor. In normal development practice the opposite happens: there is a net transfer out of the poor in the form of reverse flows of their savings going back to finance urban needs. Eighth is the concept of a pro-poor plan, focused exclusively on the poor, which is a component of the overall national development plan. These last two points are original findings of the 1992 SAARC Report.

Major Impediments

How do we explain to ourselves South Asia’s failure to bring PPTS to centre-stage, when overcoming poverty has been its central goal amidst overwhelming political compulsions for doing so? This is the hiatus referred to. This is all the more inexplicable when governments have been persistently embarrassed by their pathetic performance on the poverty question, and have indeed been sent out of office by the voters. We diagnose three main impediments.



The first impediment is the nature of the dominant political paradigm (DPP). We use the term “political paradigm” in its largest meaning

to cut across all connected disciplines: in other words, holistically. We need also to remind ourselves that the DPP has been temporizing for as long as sixty-one years after independence. Also, was this not one of the first premises for which the national independence struggle was fought?

The DPP conveniently falls into two distinct categories. We shall distinguish them as politics based on compacts of trust and politics based on compacts of expediency. Both are made between the people and the ruling classes or governing elites. The concepts of social contract and realpolitik bear a close parallel. This kind of politics applies equally to political classes as well as political parties.

There is an excellent characterization of these two contrasting political genres in Pavan K. Varma's *The Great Indian Middle Classes* (1998). The compacts of trust are characterized as follows:

Fortunately for the middle class in India, the freedom movement had generated a powerful ethical and intellectual legacy quite distinct from the anti-colonialism inherent in a liberation movement. This legacy was symbolized in the compellingly charismatic personalities of Gandhi and Nehru. For the educated Indian, Gandhi stood for the pursuit of morality as an absolute end in itself. His consistent stress on the means being as important as the end and his emphasis on uncompromising probity in public life were internalized by the middle class as an imperative, valid not only during the course of the freedom movement but also in the conduct of the affairs of the newly independent state. Nehru's vision of a modern Indian state, dismissive of the obscurantisms of the past and striving towards progress on the foundations of science, technology and industrialization, also had an irresistible appeal for this urban-centric class nurtured on Western concepts of rationalism and liberalism and impatient to get on with the task of "nation-building". At the same time the concern of both Gandhi and Nehru for the poor was perceived as being far more than an emotional awareness of the deprived; the middle class understood this concern to mean both the State and the society need to have a sensitivity towards redressing the problems of the poor. Gandhi's lifelong work for the upliftment of the harijans and his identification with the destitute had lent credibility to his



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unceasing exhortations on the need to work for the lowliest and the humblest. Nehru, too, as the spokesman of the Congress Left, was identified with the ideological assertion that the needs of the impoverished peasantry and the proletariat must be addressed as an intrinsic part of the building of a modern and progressive nation. (pp. 29–30)

In sharp contrast is the post-1971 Indira Gandhi regime's value-frame:

The supporting premises of this new framework could easily be codified. First, they stood on its head the Gandhian maxim that, in the pursuit of any cause, the means are as important as the end. From the din and dust and acrimony of the political scene following Shastri's death, the one inference that came through clearly was that almost any method was acceptable so long as it achieved the desired goals. Secondly, and this inference followed from the first, there was a conscious devaluing of the role of ethics and idealism as an aspect of public life. Indeed, oversensitivity to such considerations was dismissed as a refinement unsuited to the world of realpolitik where there was little place for the squeamish and the finicky. Thirdly, and this was again related to the first and second, there was the glorification of power as an absolute end in itself: the net outcome of political activity must be the retention and consolidation of power; if this is achieved, the activity however base its motivation and content, is sanctified. Fourthly, the individual, for the first time perhaps in recent history, was actually projected as more important than the cause, whose expression created leaders; then there were the leaders who because of the cause they espoused were in the reach of power, but had the capacity to deny it should that be necessary for the cause; then there were, even after Independence, both the cause and the leaders, inextricably linked, neither diminishing the other; and finally there was the leader, whose will subordinated all causes. (pp. 75–6)

Given the long hegemony of the politics of expediency, the obvious

result has been a state of disconnect between the poor and the ruling classes. It requires little reflection to realize how divergent the concerns of the two groups are. Hence we are living in dual societies in South Asia. Our cities are the classic expression of this duality. During the last few decades, this disparity and divergence has been getting cast in stone, despite the efforts to counter it by pro-poor and the pro-people activists. Given the sustained expansion of the zones of anomie in our societies, it is the multifaceted crisis which has come to centre-stage. The crises can go in any one of several familiar categories – ethnic wars and bombings, fundamentalist attacks and killings, religious killings, environmental plunder, eviction from squatter settlements and traditional commons, the oppression of women and human trafficking, the trade in children, and diverse pathologies of a similar kind. As societies, we are all engulfed in fear and insecurity.

The second major impediment, in our view, is the South Asian State itself. Again we take a broad and inclusive view of the State to comprise all its appendages like ministries, planning commissions, the plethora of corporations and authorities and the municipal corporations, plus the state machinery at state, district and local levels. The bureaucracy plays an important role in both the tasks of making and implementing policies and programmes. But the State has been showing crass inertia vis-à-vis the problem. Farmers are committing suicide in droves and it is headlines in all the media and the government writes off millions of rupees of credit taken by farmers. The irony is that this so-called benefit is not felt by the small farmers, who take credit from the informal moneylenders. In India over 60 per cent of the population is still engaged on land. A recent analysis of Indian agriculture by Mohan Guruswamy, Uma Nataraja and Shagun Khare, *The Crisis in Indian Agriculture* (2008), tells of the shocking neglect and underinvestment and marginalization of agriculture by the State. Almost every single subject and index examined reveals unimaginable shortfalls and omissions. The biggest single losers from all this are the poor.

Rajni Kothari in *Growing Amnesia* (1993, Delhi:Viking) characterizes this inertia as follows:

The ongoing erosion of the State and its institutions alongside its decline in both accountability and providing minimum

protection to the weak and the vulnerable that had already taken place during the decade of the 1980s, is bound to further push the poor and exploited sections towards new thresholds of misery, starvation and a total sense of hopelessness (women and children being the worst victims of this) while psychologically preparing the elite towards the praxis of treating the poor as unwanted and disposable. (p. 76)

These are systemic conditions and do not vary in substance from state to state. For decades these inertias and acts of omission have persisted. The reason has to do with the intellectual orthodoxy in command at the highest levels.

The prevailing intellectual orthodoxy in the discipline of economics is deeply entrenched in classical economic thinking and simplistic ideas of economic growth and trickle down. This is in spite of all the evidence to the contrary by radical economists, which includes all the thinkers of the participatory development paradigm mentioned above, and in spite of the recurring political upheavals. The establishment thinkers, policymakers and strategists have not been able to liberate their thinking nor learn from the ground.

Reflecting how the economists and planners and others of the same ilk have been blind to repeated historical reality, the National Commission for Enterprises in the Unorganised Sector, based on its report to the government presented in 2007, titled *India's Common People: Who Are they, How Many Are They and How Do They Live? Look at What They Say* sums up its findings thus:

To sum up, an overwhelming majority of the Indian population, around three quarters, is poor and vulnerable and it is a staggering 836 million as of 2004-05. This includes 70 million or 6.4 per cent who may be characterized as extremely poor with a per capita consumption of less than three-quarters of the official poverty line. To this should be added 167 million of those who are poor with consumption not more than that fixed as the official poverty line. If this is relaxed to include those with per capita consumption of up to 25 per cent above the poverty line, called marginally poor here, then we find another 207 million. These three groups account for 444 million or 40.8 per cent of the population. To this we add those with a per capita consumption between 1.25 and 2 times the poverty line as vulnerable and this group of poor and vulnerable

comes up to 836 million of Indians or well over 75 per cent of the population.

The next major finding is the close association between poverty and vulnerability with one's social identity. The two social groups who are at the bottom by this classification are the SCs/STs, who constitute the bottom layer, and the Muslims, who are in the next layer. This does not mean that the other groups are far better off. The next group is the OBCs but better than the two bottom layers. Even for those who do not belong to any of these groups, the incidence is 55 per cent.

The obverse of this is equally important. It says that in all communities there is a class of better-off, called the middle and high income group, which varies with social identity. Therefore economic differentiation across social groups is a fact of life in contemporary India albeit in varying degrees.... (*Economic and Political Weekly*, 15 March 2008)

The analysis covered the periods of very high growth in 2004-5. What is surprising is why nothing was done about this poverty level by the new government, having benefited from the famous defeat of the incumbent Chief Minister of Andhra Pradesh as well as of India Shining. It was explicitly stated in the Common Minimum Programme that the losers, who were the poor mentioned above, would become the subject of special policy and programme attention. But the findings of both the book on Indian agriculture as well as the report of the National Commission for Enterprises in the Unorganised Sector are that until now, nothing significant had been done, except piling up errors of omission.

The major foreign institutions like the World Bank and ADB and UNDP and the whole spectrum of donor organizations are equally responsible for this failure, because they are practitioners of the same orthodoxy. In fact, they are more often than not legitimizers of the orthodoxy of the states

Stirrings of Change

Yet there have been stirrings of change of two main kinds. First, there have been momentous, unexpected and dramatic political

changes, which have grabbed the attention of the South Asians. Second, there have been quiet changes – once called the Quiet Revolution and later the Long Revolution – which have been silently working their way at the community level. One of these – the Grameen – earned the Nobel Prize. In the setting of stagnation, inertia and multi-faceted crisis we have seen in the previous sections, these stirrings of change acquire an added compulsion. There is an important dialectic at work. While one part of the South Asian corpus is subject to sclerosis and is rotten, there is another part that is fighting to be born. There definitely is light shining through the darkness.

Chronologically, the first momentous breakthrough came in Nepal when its civil society waged a victorious struggle against the repressive monarchy in April 2006 and made history on the streets, causing the King to hand back power to parliament. Thereafter, the compulsions of mass people's power pushed the two polarized political forces to make a historic compromise and unite in alliance to overcome the antagonistic contradiction which was the absolutist monarchy. This was a historic moment, when those who had hitherto practised the politics of expediency transcended themselves and engaged in a compact of trust, thus fulfilling the deepest aspiration of the people. Next came Pakistan in equally exceptional and unpredictable circumstances. The moral imagination of a brave Chief Justice catalysed a people's movement through the agency of middle-class lawyers, something unheard of. Thereafter, Bhutan went through a peaceful transition to parliamentary democracy in circumstances specific to itself. Here was a country where the social contract between the monarchy and the masses still held, and the monarchy in its wisdom was giving up a feudal structure of power for a democratic structure. The most recent triumph of democracy has been in the Maldives when the president, incumbent for thirty long and repressive years, was peacefully overthrown through the ballot, and a former political prisoner was elected President. These are instances where the mainstream political process has transformed itself through forms of internal agency. What is the implication here? It is that democratic change is quietly and silently working through the interstices, hearts and minds of the people, but it is following an innovative and unpredictable pattern.

An equally heroic example is Grameen and BRAC in Bangladesh,

where two non-state sector programmes of massive scale have sustained themselves in the midst of constant governmental and natural crises. The reasons for their sustainability are many and complex. First is the exemplary conduct of the two individuals who have led them. They have fiercely kept out of the party political fray, but they have been faithful to the politics of the poor. Acting within a subsidiarity framework, they have been able to avoid conflicts with the powers that be. Their antagonists, who are many, have been overawed by the legitimacy and trust bestowed on the two organizations by the people. Once they graduated from projects to programmes, they developed an internal momentum and culture which acted as a school for learning to disseminate their particular value frame and lifestyle. They avoided negative and hurtful competition between themselves. They were large-minded. They ensured that the movements were actually owned by the poor women. Finally, they demonstrated excellent managerial track records and practised accountability to all concerned. They were vigilant enough to safeguard the movements against internal corruption. They did this by ensuring that honesty and transparency were virtues that everyone practised.

Can we look upon these different kinds of new stirrings as harbingers of a new South Asia straining to be born? Rajni Kothari in his book *Rethinking Democracy* (2005, Orient Longman) has tried to articulate these stirrings as he sees them, eloquently:

But while the mainstream political process stagnated a new political climate was coming into existence in the wake of (a) greatly increased perception among the people of the value of politics in the struggle for social change; and (b) growing perception among grassroots activists about the need to link micro-movements of constructive work, rural conscientization and organization of the poor, to a macro-movement that is consciously perceived as a political process. The political process would be different from the kind in which political parties are engaged, but it would be a political process nonetheless. The task now is to make the mass stirrings and the grassroots activism the basis of an alternative political process and, as the crisis of the state deepens, make that process the catalyst of a new structure for the state. (pp. 86–7)





Regional Cooperation for Food Security in South Asia

Sadiq Ahmed

Rapid growth since 1980 has transformed South Asia from a region of slow-growing economies in a heavily insulated environment to a rapidly growing region of outward-oriented economies (Figures 1 and 2). From a meagre 3.0 per cent growth rate between 1950 and 1980, South Asia's annual GDP growth rate climbed to around 5.7 per cent during 1980–2000, and to 6.5 per cent during 2000–2007. As of 2007, South Asia was the second-fastest growing region in the world, after East Asia. Indeed, the growth rates in South Asia and East Asia appear to be converging (see Figure 1). India experienced GDP growth of 9 per cent in 2007, close to that of China. Bangladesh, Pakistan and Sri Lanka witnessed an average growth rate of 6.5 per cent. Private investment has boomed, supported by rising national saving rates. The region now attracts global attention because of rapid growth, global outsourcing, and skill-intensive service exports. With rapid growth, poverty has come down sharply in all the South Asian countries (Figure 3). Progress has also been made in improving human development and the social indicators compare favourably with countries in other regions with similar income levels (Ahmed 2008).

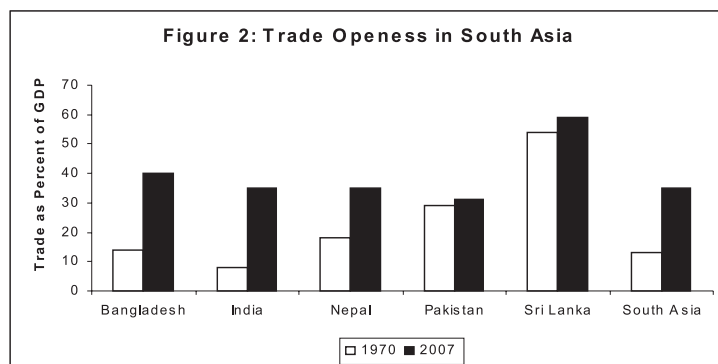
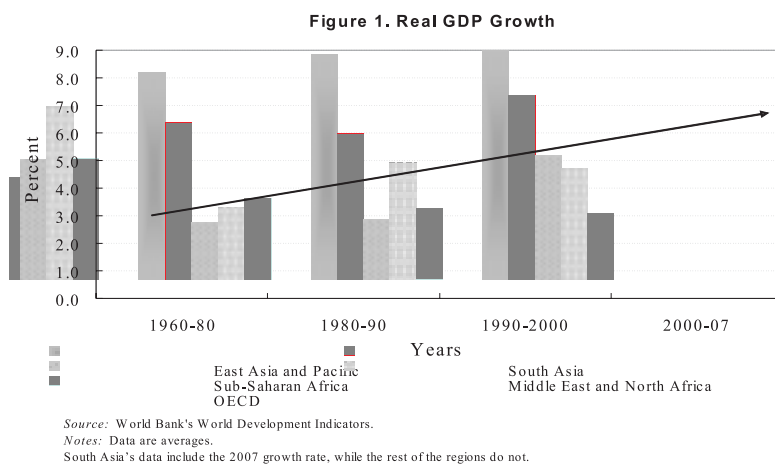
South Asia's Development Progress and Challenges

While there is much to celebrate, however, three negative developments have emerged. First, there is evidence of growing income inequality in South Asia. Second, there is growing imbalance between regions within countries and among the countries themselves. With fairly large and open borders, these growing imbalances present social and economic problems to the prosperous neighbours similar to the problems arising from imbalances within. And third, South Asia is facing serious macroeconomic imbalances from a series of terms of trade shocks and an emerging global financial

* Parts of the analysis of this paper draw from two other related works (Ahmed 2008; and Ahmed and Ghani 2008). The views expressed in this paper are those of the author and do not necessarily reflect the views of the World Bank Group. Research assistance from Moutushi Islam is gratefully acknowledged. Any errors are the author's sole responsibility.

crisis. These external shocks are threatening to decelerate South Asia's growth momentum and consequently hurt progress with poverty reduction. The adverse effect of the global food price shock has been particularly severe on the poor (Ahmed 2008)

Income growth, poverty, lagging regions and food security are interrelated. South Asia's experience shows that the incidence of poverty and income growth are negatively correlated (Figure 4). With few exceptions lagging regions exhibit higher than average rate of poverty and lower than average per capita incomes. The growing divergence between lagging and leading regions also suggests that the former on average are growing more slowly than the latter. The lagging regions indicate the following socio-economic characteristics (Ahmed and Ghani 2008):



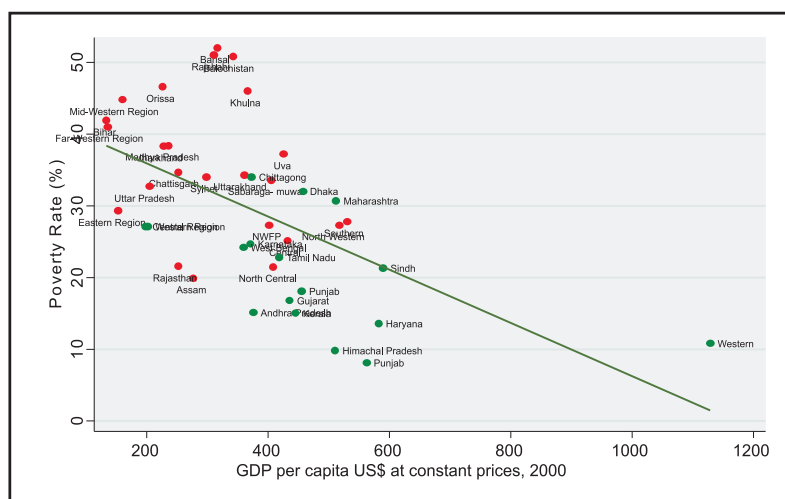
South Asia: The Quest for Regional Cooperation

- They comprise some 400 million people, of whom an estimated 200 million are poor (reference year 2005).
- Much of the population is rural (90 per cent) and most are engaged in low-productivity agriculture.
- The human development indicators tend to be below the national average and many indicators are lower than the average in South Asia.
- Infrastructure is on average poorer than in the rest of the country and poorer than the average for South Asia.
- The border regions on average tend to be more vulnerable to water shortages and flooding than other parts.

Note: Poverty estimates use national poverty lines. The respective dates are: Bangladesh (1975 and 2005); India (1974 and 2005); Nepal (1977 and 2004); Pakistan (1970 and 2005); and Sri Lanka (1976 and 2005).

Source: World Bank regional database

Figure 4. Growth–Poverty Correlation in South Asia



Source: Staff estimates

A substantial part of the food security challenge is, hence, akin to the challenge of lifting growth and farm productivity in South Asia’s rural areas, many of which are located in lagging regions. Indeed, a major dichotomy underlying South Asia’s economic transformation has been the continued strong reliance on low-productivity agriculture for income for over 50 per cent of the population, even as the share of agriculture in GDP has shrunk from around 50 per cent in 1970 to less than 20 per cent in 2007. Poverty analysis at country levels shows that over 80 per cent of South Asia’s poor are located in rural areas, of whom over 50 per cent are engaged in agriculture.

Global Food Price Crisis and Implications for Food Security



The surge in global commodity prices of the past few years has presented a tremendous development challenge for South Asia. South Asia is estimated to have suffered a net income loss equivalent to some 9.6 per cent of GDP between January 2003 and April 2008. Although much of the income loss resulted from the hike in petroleum prices, the surge in food prices between January 2007 and April 2008, especially of staple food like wheat and rice, has created a tremendous adverse social impact in all South Asian countries. All of them have witnessed an unprecedented surge in food prices, although India was

largely able to limit this increase through a combination of timely interventions using stock management and public food distribution. Net food-importing countries like Afghanistan, Sri Lanka and Bangladesh have suffered the most from the food price crisis.

The adverse impact of the rise in global commodity prices on macroeconomic balances in South Asia has been substantial. All the countries in the region have seen a sharp increase in fiscal deficits and worsening balance of payments. For the first time, all South Asian countries have simultaneously experienced double-digit inflation rates, with 20-plus rates in Afghanistan, Pakistan and Sri Lanka. Meanwhile, economic growth is showing signs of slowdown as the countries in the region are trying to arrest the deterioration in macroeconomic imbalances and rising inflationary pressures through demand management measures. The emerging global financial crisis is worsening the macroeconomic imbalances.

The twin global crises of higher commodity prices and financial turmoil have come at a time when most South Asian countries are in political transition. Afghanistan, Bangladesh and India are facing national elections within the next twelve months. Nepal and Pakistan have emerged recently from the election process with new governments in place under a hugely different political environment than previously. Sri Lanka is still fighting a civil war. So, arguably, the political economy of policy management has seldom been so challenging in South Asia. In all countries, the immediate political economy concern is to stabilize domestic food prices and lower inflation. This concern is easy to see in the light of the adverse consequences for poverty reduction. In South Asia, food consumption as part of total consumption averages nearly 50 per cent, compared to 17 per cent in USA. It is even higher for the poor, who as a result have been hurt most by the increase in food prices.

While much of the immediate policy focus has been on food price stabilization, especially for the staple items – wheat and rice – the implications of the various policies used for short-term price stabilization for longer-term supply response, growth, economic efficiency and fiscal sustainability have not always been analysed or thought through. Importantly, public policy debate and discussions now show renewed focus on food security issues. This is a welcome



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development. Yet there is also a risk that the policy debate might move away from emphasis on the right issues and back to the 1970s environment of trade protection and insulation from the global economy. Therefore, there is an important need to understand the origins of the global food crisis, how this has affected South Asia, and what can be done to address the food security concerns in its proper development context.

Magnitude of Price Inflation

Global food prices have been rising for a fairly long time, particularly since 2005. Prices accelerated starting in January 2007. The World Food Price Index of the Food and Agriculture Organization (FAO) indicates that international food prices in April 2008 were 60 per cent higher than twelve months earlier. World food prices have in particular been driven by higher grain prices. The international price of wheat more than tripled between 2002 and March 2008 (Figure 5). Wheat price was relatively stable until 2006, but surged in 2007 and early 2008, reaching a global peak in March 2008. The price has since then come down, but as of August 2008 remained 70 per cent higher than the average price in 2006 and much higher than the pre-crisis period of 2004. Rice price increased nearly fivefold between 2002 and April 2008. The spike came in 2008 when the price more than doubled in four months between January and April. Rice price has also come down after April, but as of August 2008, international rice price was 128 per cent higher than the average in 2006.

Source: IMF International Financial Statistics and World Bank's Global Economic Monitoring Database.

Global food prices have increased because of a combination of factors including rising population, rapid economic growth in emerging markets, high energy and fertilizer prices, increased use of food crops for bio-fuels, rapid demand increase for some food crops, depreciation of the US dollar, and declining global stocks of food grains due to changes in buffer stock policies in the US and the European Union. Back-to-back droughts in Australia and growing global demand for grains (excluding for bio-fuel production) have been modest contributors and on their own would not have led to large price increases. Commodity investors and hedge fund activity also seem to have played a minor role. Although empirical evidence is scarce, the prevailing consensus among market analysts is that fundamentals and policy decisions are the key drivers of food price rises, rather than speculative activity (World Bank 2008a).

Global Supply-Demand Imbalance

Table 1 shows the world production and consumption trends for wheat, rice and food grain over the past ten years. A number of interesting results emerge. First, between 1999 and 2008 world food consumption has grown faster than production, causing a fairly substantial drawdown of stocks (Figure 6). Second, wheat production faced difficulties over 2005–2007, but there has been strong recovery in 2008-9. Third, in contrast to wheat, rice production increased significantly during 2005–2008 and overall production has basically exceeded consumption.

**Table 1. World Food Grain Demand-Supply Situation,
1999–2009**
(million metric tons)

Source: USDA database.

To what extent do these trends explain the rising prices? The drawdown of reserves during 1999–2008 is a clear indication of a global tightening of food markets, with obvious implications for rising prices. The acceleration of wheat price increases during 2006–2008 is partly explained by the large imbalance between supply and demand, accentuated of course by adverse market expectations and the generally low short-term supply-demand elasticity. But the behaviour of rice prices and their acceleration in 2007–8 is not explained by the global demand-supply imbalances. As noted earlier, unlike wheat, overall rice production exceeded consumption during 2006–2008 and yet prices hit the ceiling. One needs to look at other factors. Two critical factors are trade policies and cost of production.

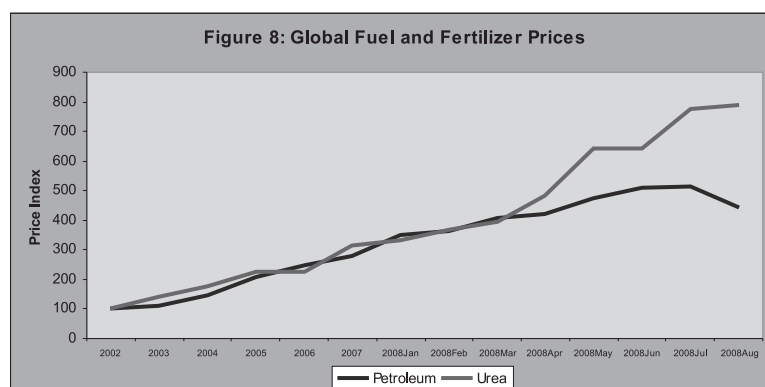
Adverse Effects of Trade Policy Bans

The introduction of export restrictions and bans – such as those imposed by India and China on rice, or by Argentina, Kazakhstan, Pakistan, and Russia on wheat – has further restricted global supply and aggravated shortages. Unilateral actions by exporting countries prompted others to quickly follow suit, undermining trust in the market and leading to worse outcomes for all. The result has been a self-reinforcing price spiral. This is illustrated dramatically by Brahmhatt and Christiaensen (2008) in the case of the thinly traded rice market. India’s decision to ban rice exports was quickly followed by export restrictions placed by Vietnam and other major players, with an immediate impact on prices (Figure 7). Actions by large rice importers, such as the Philippines, which organized big tenders for rice imports, further aggravated the problem.

**Figure 7. Rice Prices and Recent Policy Responses \$/Ton;
January 2004–April 2008**

Surge in Cost of Production

A second and more long-term factor is rising cost of production. Key inputs, such as fertilizer, diesel, electricity and transport have all gone up tremendously at the global level, linked to energy prices (Figure 8). Fertilizer prices have risen more than by four times between 2002 and 2008 and the sharpest increase came after 2006.



Source: IMF IFS Yearbook, World Bank Commodity Prices.

Expected Near- to Medium-term Outlook for International Food Prices

While short-term fluctuations in food production compounded by trade restrictions had a negative impact on short-term food prices,

one good news for near-term prices is the bumper global harvests for wheat in 2008-9. Rice production has also increased. As a result, stocks are being replenished, effecting a downward push to global prices. The lifting of the trade bans will help lower prices further. Yet, it is clear that the underlying economics of food markets has changed dramatically and unless energy prices were to collapse to the levels found in 2004, the global price of rice and wheat will not likely return to the pre-crisis prices of 2006. The expected outlook for prices in the near to medium term is shown in Table 2. These projections allow for some reduction in annual average oil and fertilizer prices. While these projected input prices are significantly lower than the local peak (especially for oil that reached a monthly average price of \$133 per barrel in July 2008), they are substantially higher than the average prices in 2004, reflecting the realities of world demand and supply.

Table 2. Projected Average Global Wheat and Rice Prices, 2007–2010

	2007	2008	2009	2010
Oil (\$/barrel)	71.1	108.1	105.5	98.5
Rice (\$/MT)	326.4	650.0	560.0	500.0
Wheat (\$/MT)	255.2	380.0	340.0	300.0
Fertilizer (\$/MT)	309.4	425.0	350.0	310.0

Source: World Bank Prospects for the Global Economy, September 2008.

Food Price Crisis and Food Security in South Asia

The concept of food security has evolved over time from a narrow definition of food availability to a broad definition of ensuring that all citizens have adequate nutritional standards.¹ The narrow definition ignores all distributional implications. Having food available by itself is no guarantee that a country has food security since this can coexist with a situation of famine. This is clearly demonstrated in Amartya Sen's path-breaking work on famine (Sen 1982) that has substantially reshaped global thinking on food security. The broad definition, however, makes food security synonymous with development and

¹ See FAO (2003) for a useful survey of the evolution of the food security concept.

therefore its reach becomes too broad. A simpler concept is to think of food security as a situation where food is available in quantities and prices that are affordable by all. What is important is that both the supply aspects of food availability and the demand aspects of making food affordable to all citizens need to be elements of a comprehensive food security strategy. For the present paper, although we shall focus more on the supply aspects of the food security question, we shall also touch upon the demand side by looking at income effects of the global crisis. On the supply side, we shall restrict our attention to South Asia's two staple food items – wheat and rice – that have attracted most policy attention. However, much of the analysis is relevant to the agricultural sector as a whole.

Tables 3 and 4 show the trends in rice and wheat production and consumption in South Asia over 2000–2008. Total food production (rice and wheat) grew at a slow pace of 1.0 per cent per annum as compared with consumption growth of 2.3 (Table 5). South Asia's production growth has been slower than world production while consumption growth rate has much exceeded the world consumption growth rate. This is partly owing to a faster pace of expansion of South Asia's population, but also reflects a positive income elasticity.

There are significant differences at the country level in terms of production and consumption behaviour, but all countries share the common result that on average food consumption has exceeded food production during 1999–2008. In India, South Asia's largest grain producer for both rice and wheat accounting for 71 and 76 per cent of production respectively, wheat production has barely expanded during 1999–2008 although rice production has shown a healthy trend. In Pakistan, a primarily wheat-consuming country and accounting for 21 per cent of South Asia's total production, wheat production has fluctuated widely annually but has been basically flat like in India during 2000–2008. Bangladesh, which is primarily a rice-consuming country and accounts for 20 per cent of South Asia's rice production, has registered a production growth of 2.0 per cent per year in rice. Overall, the rate of growth of food grain consumption in all three large grain-producing countries has outstripped production.² The story is similar in the smaller countries of Afghanistan, Nepal and Sri Lanka.

² Surprisingly, however, Pakistan's consumption growth of food grain is substantially lower than the population growth rate, suggesting a negative income elasticity. But this could reflect data reporting problem.

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The data are not very reliable for Afghanistan, but it is a hugely food-deficit country and relies mostly on wheat imports from Pakistan. Nepal's rice production has stagnated but wheat production has expanded; overall consumption growth exceeds production. In Sri Lanka, which is primarily a rice-eating country, production of rice has been somewhat higher than consumption, allowing Sri Lanka to reduce its reliance on wheat imports.

Table 3. South Asia Food Grain Production (1000 MT)

	2000/1	2001/2	2002/3	2003/4	2004/5	2005/6	2006/7	2007/8	2008/9
Afghanistan	169	157	260	174	312	315	362	335	168
Bangladesh	25,086	24,310	25,187	26,152	25,600	28,758	29,000	28,600	29,400
India	84,980	93,340	71,820	88,530	83,130	91,790	93,350	96,430	96,000
Nepal	2,808	2,774	2,752	2,752	2,968	2,857	2,804	2,810	2,850
Pakistan	4,802	3,882	4,479	4,848	5,025	5,547	5,200	5,500	5,600
Sri Lanka	1,940	1,820	2,058	1,900	1,974	2,100	2,145	2,200	2,300
<i>South Asia</i>	<i>119,785</i>	<i>126,283</i>	<i>106,556</i>	<i>124,356</i>	<i>119,009</i>	<i>131,367</i>	<i>132,861</i>	<i>135,875</i>	<i>136,318</i>
<i>World</i>	<i>398,902</i>	<i>399,700</i>	<i>378,318</i>	<i>391,861</i>	<i>401,298</i>	<i>418,313</i>	<i>420,164</i>	<i>428,989</i>	<i>430,751</i>
Afghanistan	1,469	1,597	2,686	3,480	2,293	4,265	3,200	3,800	1,500
Bangladesh	1,672	1,610	1,510	1,253	976	820	740	1,200	800
India	76,369	69,680	71,810	65,100	72,150	68,640	69,350	75,810	78,400
Nepal	1,184	1,157	1,258	1,344	1,387	1,442	1,394	1,395	1,400
Pakistan	21,079	19,024	18,227	19,183	19,500	21,612	21,277	23,300	21,500
Sri Lanka	101,794	93,088	95,511	90,380	96,326	96,799	95,981	105,325	103,620
<i>South Asia</i>	<i>582,899</i>	<i>583,078</i>	<i>568,708</i>	<i>553,838</i>	<i>625,738</i>	<i>620,851</i>	<i>596,273</i>	<i>610,537</i>	<i>670,751</i>

Source: USDA.

Table 4. South Asia Food Grain Consumption (1000 MT)

	2000/1	2001/2	2002/3	2003/4	2004/5	2005/6	2006/7	2007/8	2008/9		
Rice	Afghanistan	385	427	440	369	455	516	550	485	343	
	Bangladesh	24,958	25,553	26,100	26,700	26,900	29,000	29,764	30,600	30,600	
	India	75,960	87,611	79,860	85,630	80,861	85,088	86,940	90,760	93,000	
	Nepal	2,828	2,793	2,762	2,756	3,029	2,859	2,863	2,870	2,910	
	Pakistan	2,615	2,540	2,545	2,595	2,550	1,896	2,257	2,450	2,420	
	Sri Lanka	2,020	2,075	2,100	2,075	2,139	2,150	2,152	2,287	2,376	
	<i>South Asia</i>	<i>108,766</i>	<i>120,999</i>	<i>113,807</i>	<i>120,125</i>	<i>115,934</i>	<i>121,509</i>	<i>124,526</i>	<i>129,052</i>	<i>131,349</i>	
	<i>World</i>	<i>393,291</i>	<i>412,455</i>	<i>405,681</i>	<i>411,615</i>	<i>406,545</i>	<i>411,629</i>	<i>417,017</i>	<i>421,962</i>	<i>425,519</i>	
	Wheat	Afghanistan	2,043	2,597	3,186	3,930	3,293	4,765	4,250	4,700	3,800
		Bangladesh	2866	2950	3000	3050	3000	2950	2800	2900	2850
India		66,821	65,125	74,294	68,258	72,838	69,971	73,358	75,850	77,600	
Nepal		1,194	1,158	1,266	1,361	1,407	1,462	1,408	1,415	1,420	
Pakistan		20,500	19,800	18,380	19,100	19,600	20,900	21,900	22,400	22,600	
Sri Lanka		850	801	875	931	950	1,000	817	825	850	
<i>South Asia</i>		<i>94,294</i>	<i>92,451</i>	<i>101,028</i>	<i>96,655</i>	<i>101,118</i>	<i>101,078</i>	<i>104,563</i>	<i>108,120</i>	<i>109,150</i>	
<i>World</i>		<i>583,564</i>	<i>587,816</i>	<i>603,659</i>	<i>581,173</i>	<i>605,943</i>	<i>618,197</i>	<i>618,703</i>	<i>619,007</i>	<i>647,079</i>	

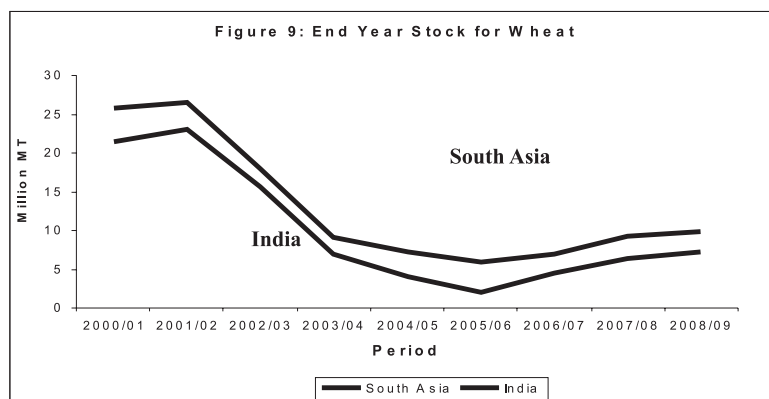
Source: USDA.

Table 5. Annual Growth Rates in Production and Consumption of Food in South Asia, 2000–2008 (per cent)

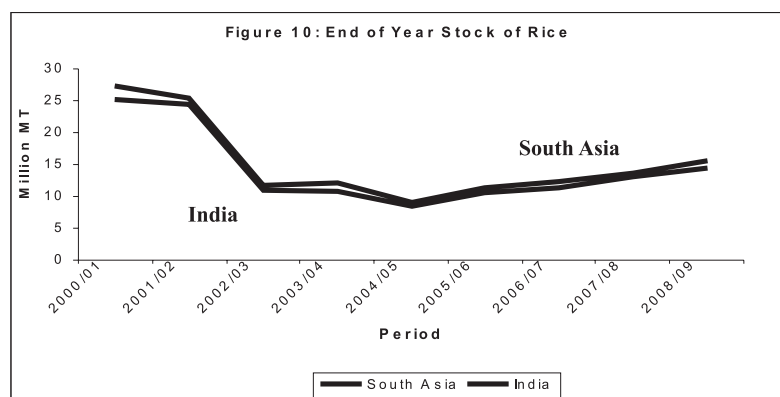
Country	Production growth			Consumption growth			Population growth
	Wheat	Rice	Total	Wheat	Rice	Total	
Bangladesh	-8.8	2.0	1.5	0.0	2.6	2.3	1.6
India	0.3	1.5	1.0	1.9	2.6	2.3	1.7
Nepal	2.1	0.2	0.8	2.2	0.4	0.9	2.3
Pakistan	0.3	1.8	0.8	1.2	-1.0	1.0	2.6
Sri Lanka	0.0	2.2	n.a.	2.0	0.0	1.6	0.9
South Asia	1.6	0.2	1.0	2.2	2.4	2.3	1.9
World	1.8	1.0	1.5	1.3	1.0	1.2	1.1

Source: Production and consumption growth rates calculated from Tables 3 and 4. Population data from World Bank World Development Indicators.

What are the implications of these production and consumption trends for food availability and prices? In 2000 South Asia had a production surplus of almost 11 million metric tons (MMT) of rice and 7.5 MMT of wheat. By 2008 the wheat surplus had vanished and converted into a deficit of about 6 MMT. The rice surplus also fell, although it still remained a surplus at around 5 MMT. The production shortfalls in wheat were met mostly by drawdown of reserves (Figures 9 and 10). South Asia's largest grain producer, India, had built up a huge food grain stock, partly for food security reasons and partly to provide price support to farmers. In 2001/2 India had accumulated stocks of 25 MMT of rice and wheat each. These reserves were drawn down over the coming years, mostly to meet the consumption gap in wheat but also to reduce fiscal cost and physical waste through rice exports. By 2005/6 the wheat stock had fallen to 2 MMT, causing a reversal in policy to build up reserves. Rice stocks also started rising in 2004/5, recovering from the low levels of 9.5 MMT. By 2008/9 stocks had recovered to 8 MMT for wheat and 15 MMT for rice. This obviously added to the demand pressure for both wheat and rice. Thus, India imported 6.7 MMT of wheat in 2006/7 and 2 MMT in 2007/8 as compared with almost zero imports in the past six years. Regarding rice, exports declined from a peak of 5.5 MMT in 2006/7 to 2.0 MMT in 2008/9. These developments in domestic supply-demand balances suggest that, similar to the global experience, domestic food shortages are an important factor underlying food price pressures in the South Asian countries.



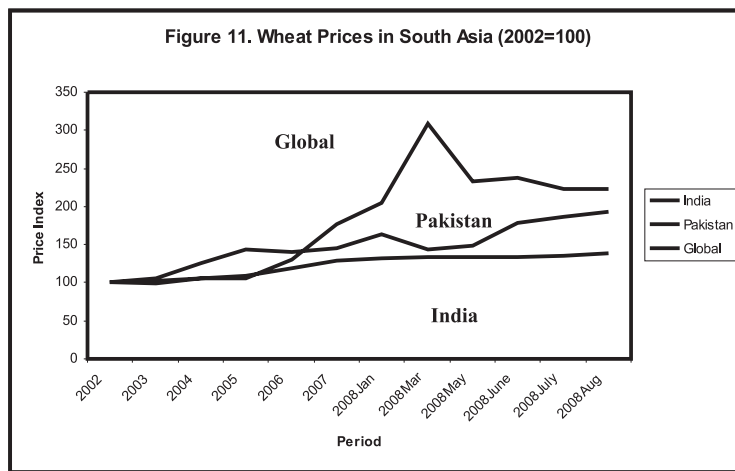
Source: USDA Database.



Source: USDA Database.

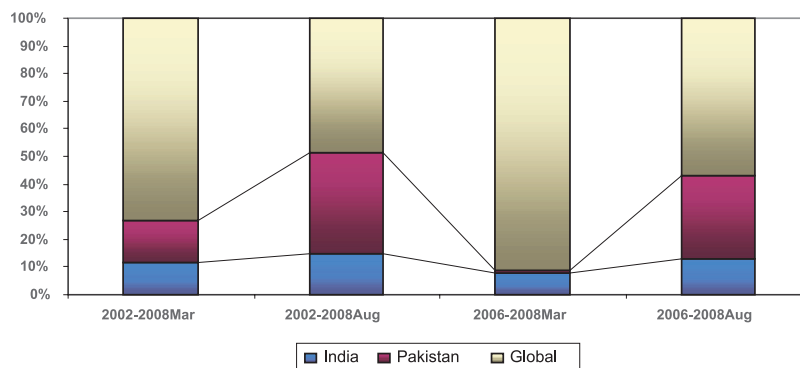
Afghanistan, India and Pakistan account for about 90 per cent of the wheat consumed in South Asia; rice is more widely consumed. The trend in wheat prices in South Asia's major wheat-consuming countries is shown in Figure 11. Since comparable data for Afghanistan are not available, we shall rely on fragmented data. It is seen from Figure 11 that wheat prices in both India and Pakistan increased in response to the global pressure, but the increases were much less intense, especially in India (Figure 12). Indeed, India managed to maintain a fairly stable wheat price that increased by only 33 per cent between 2002 and 2008 March and by only 12 per cent between 2006 and March 2008. Pakistan experienced sharper increases, in

two phases, between 2003 and 2005 and between March 2008 and August 2008. Overall, wheat prices increased by 98 per cent between 2002 and August 2008, and by 37 per cent between 2006 and August 2008. Afghanistan suffered much more: available short-term data show that the wheat prices increased by 157 to 259 per cent between May 2007 and 2008 (Table 6). The marked regional variation in price increases suggests the low mobility of food grain within the country, reflecting poor internal trade logistics, including security problems.



Source: Compiled from various data sources of authorities concerned.

Figure 12: Comparative Wheat Price Increases

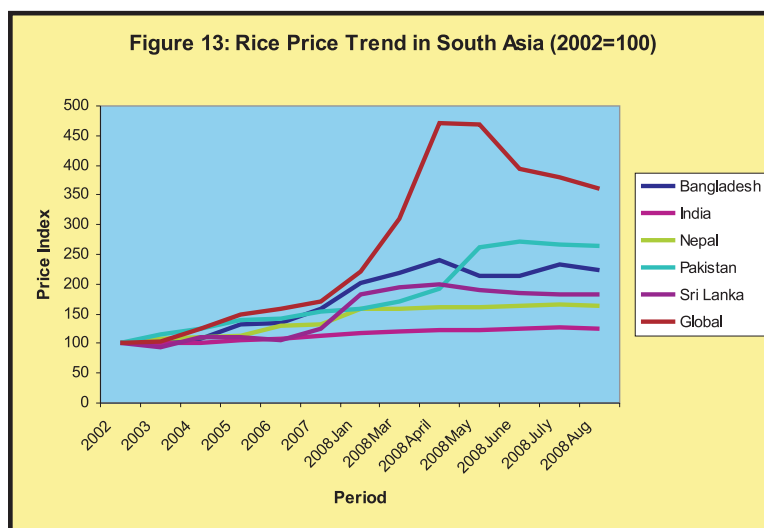


Source: Staff estimates.

Table 6. Wheat Prices in Afghanistan

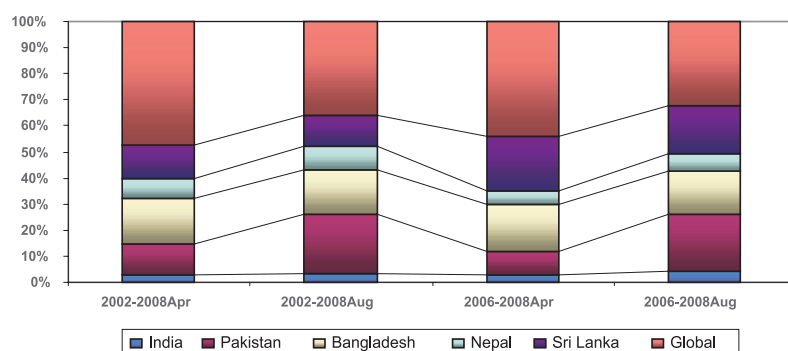
Source: World Bank (2008).

The movement in rice prices is shown in Figure 13. As with wheat, South Asian rice prices on average rose less than in the global market and there are marked differences by countries. Pakistan witnessed the most rapid increase followed by Bangladesh, Sri Lanka, Nepal and India (Figure 14). Again, as with wheat, India experienced the lowest price increase in the region, which is strikingly lower than the global price rise.



Source: Compiled from various data sources of authorities concerned

Figure 14. Comparative Rice Price Increases



Source: Author's calculations.

Two interesting questions arise: Why did South Asia experience lower price increases of wheat and rice than the global market? And secondly, how did India manage to virtually insulate its economy from higher global rice and wheat prices than other South Asian countries? The answer to the first question is that all South Asian countries except Afghanistan rely largely on domestic grain production with low reliance on trade and use substantial trade restrictions and fiscal policy interventions that diverge domestic prices from international prices, especially during an upswing in global prices. Afghanistan's domestic production on average falls substantially behind consumption needs, leading to a relatively large reliance on trade, especially from Pakistan. Regarding the second question, India was much more agile in anticipating the need to build up stocks and responded quickly with food distribution and tightening trade restrictions with a view to protecting domestic consumers. India's policy response on the trade front has led to a major political economy debate about the role of trade in agriculture. We shall turn to this debate later.

How Has the Food and Fuel Crisis Affected South Asia?

Severe Terms of Trade Loss

While South Asia relies relatively less on grain imports, its reliance on petroleum and other commodities is quite large. As a result, given the sharp increase in commodity prices, the region has experienced severe terms of trade loss, deterioration in the external and internal

balance, and adverse economic and social impact on the poor. Figure 15 shows the effects of the terms-of-trade shock in South Asia relative to other regions, while Figure 16 shows the impact by countries within South Asia. It is seen from Figure 15 that on a net basis South Asia has suffered the greatest loss of income as per cent of GDP among all developing regions. Within South Asia, the picture at country level is quite divergent (Figure 16). Losses range from 34 per cent for the tiny archipelagic country of Maldives to 8 per cent for Bangladesh. Much of the loss has come from petroleum, where all countries have lost. In the food sector, Bangladesh has lost most, followed by Nepal and Sri Lanka. Afghanistan is especially vulnerable on food account and faced the steepest price increases in the region, although reliable data are not available for that country.

Figure 15. Comparative Regional Income Loss from Terms of Trade Shock

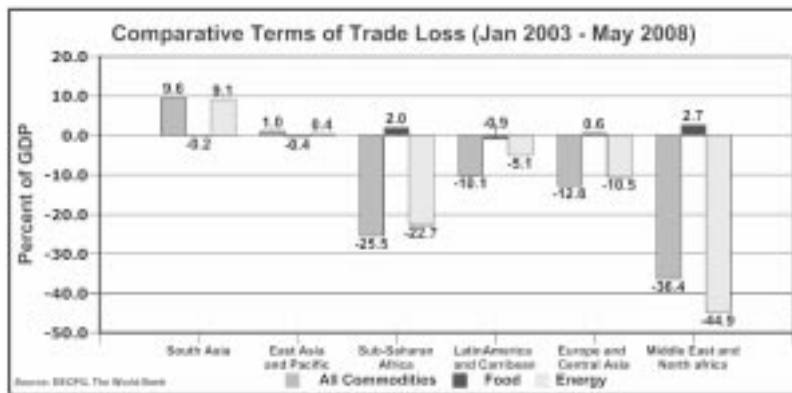


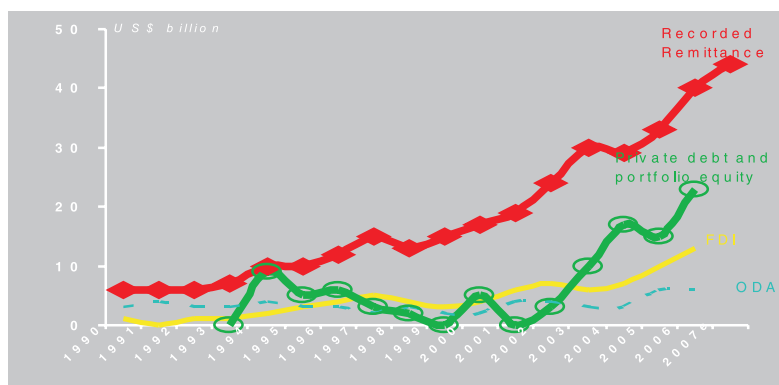
Figure 16. Income Loss from Terms of Trade Shock



Deterioration in Fiscal and External Balances

The large loss of income from terms of trade shock was partially compensated by rising remittances (Figures 17 (a) and (b)). Nevertheless, there has been a negative impact on the external balances of most South Asian countries (Figure 18). Pakistan suffered the most rapid deterioration in the current account balance, which turned from a surplus of around 4 per cent of GDP in 2003 to a deficit of over 8 per cent in 2008. Sri Lanka, similarly, registered a sharp increase in current account deficit. Even in India, the current account widened sharply from a surplus of more than 2 per cent of GDP in 2004 to a deficit of over 3 per cent in 2008. The current account balance in Nepal that was in surplus for a fairly long period finally turned into a deficit in 2008.

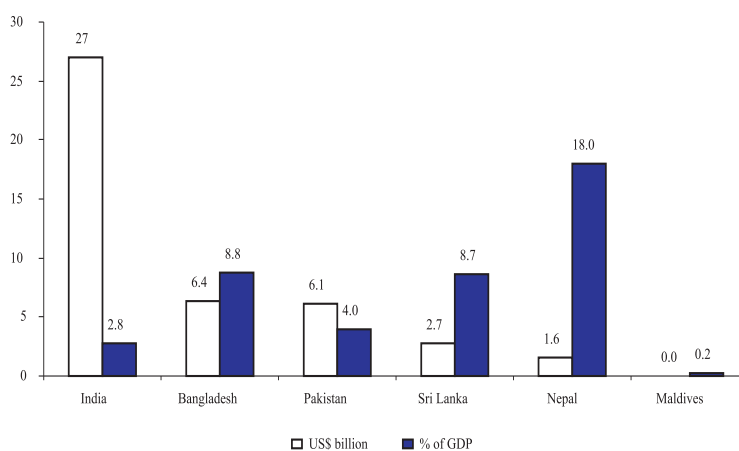
Figure 17(a). Trend in Remittance and Other Capital Inflows in South Asia



Source: Development Prospects Group (DECPG), World Bank.

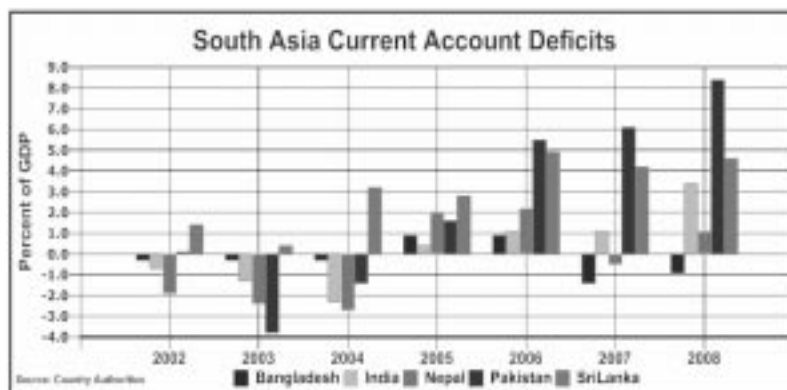
Bangladesh also lost on the trade account, but continued to enjoy a surplus in its current balance owing to remittances. These differential effects reflect a number of factors, including: the relative magnitude of terms-of-trade shocks, the differences in compensating growth of remittances, and policy responses. Bangladesh in particular benefited tremendously from the growth in remittances. Pakistan and Sri Lanka have been facing balance-of-payments pressures from expansionary fiscal and monetary policies; the terms-of-trade shocks accelerated the deterioration.

Figure 17(b). Remittance Inflows in South Asian Countries in 2007



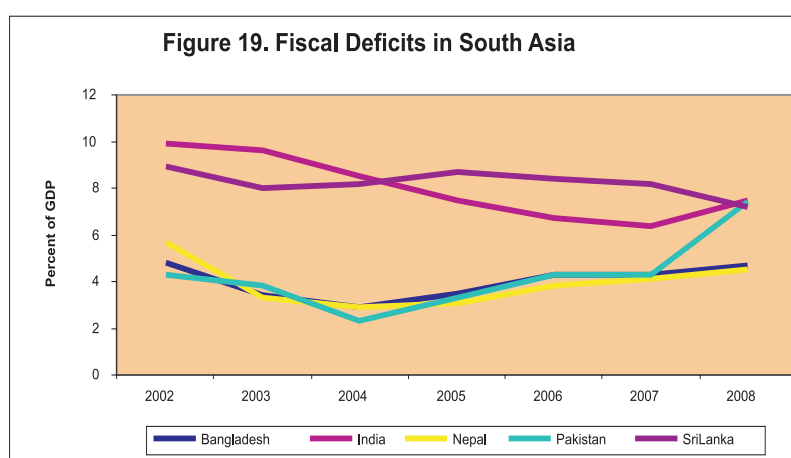
Source: Data from country authorities.

Figure 18. South Asia Current Account Deficits



In fiscal balance all countries except Sri Lanka registered sharp deterioration (Figure 19). The fiscal deficit widened most for Pakistan, rising from 2.4 per cent of GDP in 2004 to 7.4 per cent in 2008. India had made good progress in reducing fiscal deficit between 2003 and 2007. This progress was reversed in 2008 due to a sharp increase in fuel subsidy (growing from 1 per cent of GDP in FY2007 to an estimated 4 per cent of GDP in FY2009) that threatens to wipe

off the gains made painfully over the past few years. Bangladesh also struggled. Budget deficit widened to almost 5 per cent in 2008 and is projected to grow to over 6 per cent, mostly due to increases in food and petroleum subsidies.³ Nepal's fiscal deficit has also grown from its low level in 2004 owing mainly to fuel subsidy. Sri Lanka is the only surprising exception. It has long suffered from high fiscal deficits linked to the ongoing civil war. As a result, it had little wiggle room to expand further the deficit. Instead, Sri Lanka passed on most of the global price increases in petroleum to consumers.



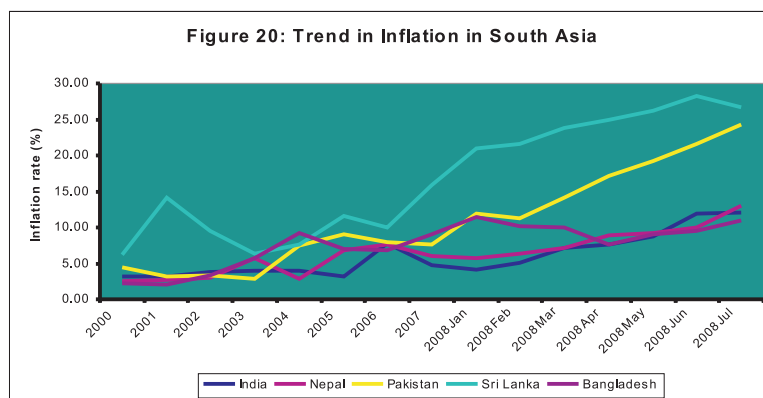
Source: Data collected from concerned government authorities

Impact on Inflation

Rising food and fuel prices have been a major source of inflationary pressure in South Asian countries (Figure 20). In Afghanistan, Sri Lanka, Pakistan, Bangladesh and Nepal, food prices made a bigger impact on inflation than fuel prices. In India, however, the main surge to inflation came from fuel price increases. Pakistan experienced the most rapid change in the rate inflation, rising from 8 per cent in 2006 to 25 per cent in July 2008. This is in part due to the global food price hike, but also due to domestic demand pressure emerging from unsustainable macroeconomic policies. Sri Lanka had

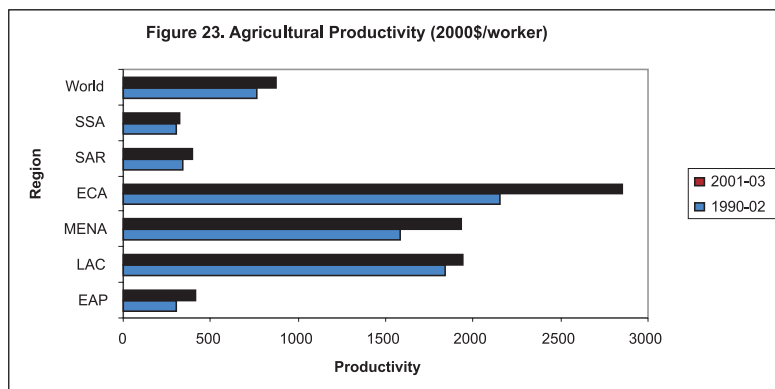
³ Includes off-budget subsidies.

already been experiencing inflationary pressure from expansionary fiscal and monetary policies; the hike in food and fuel prices accelerated the pace. Afghanistan’s inflation hike came primarily from food prices. Since the increase in grain prices for Afghanistan much exceeded those in the other South Asian countries owing to serious deficit and export ban from Pakistan, the inflation acceleration was quite intense (Figure 21). With the recent decline in global grain and petroleum prices, inflation rates are coming down in South Asia even though the effects of the decline are offset partly by rapid currency depreciation in India and Pakistan.



Source: IMF International Financial Statistics and government authorities.

Figure 21. Food and Non-Food Inflation in Afghanistan, January 07–June 08



Source: Central Statistical Office, Government of Afghanistan.

Poverty and Distributional Impacts

The impact of rising food prices on poverty in an individual country depends on several factors, including: (i) the extent world market prices are passed through to domestic prices; (ii) the initial poverty level and number of people clustered around the poverty line; (iii) the number of net buyers or net sellers of the commodities in question; (iv) the share of poor people's budgets devoted to food overall and key staples in particular; (v) the extent of own consumption relative to market purchases; and (vi) the effect of food price increases on real wages of poor people (World Bank 2007).

Preliminary results of research at the World Bank suggest that on balance higher food prices are likely to have a net adverse effect on poverty. On average, poor urban households are likely to be hit worse than poor rural households. Simulation analysis suggests that depending upon wage response, the food price increases between 2005 and 2007 may have increased global poverty by 73–105 million people (World Bank, 2008a).

In South Asia, a definitive analysis on how the food price increase affected poverty is not available.⁴ However, on average, it is likely that the net effect will be to increase poverty significantly. This can be appreciated from the following points. First, the South Asian poor on average spend between 25 and 60 per cent of their income on staple food; this share rises as we go down the expenditure/income scale. Second, there are many more poor households who are net buyers of staple food than net sellers. Third, access to official safety net programmes is hugely limited by inadequate fiscal space and ineffectiveness of many programmes.

Of all South Asian countries, Afghanistan arguably is the most vulnerable to increases in staple food prices. Afghanistan also suffered the most increase in prices in the region owing to large food deficit and export ban from Pakistan. Afghanistan's sensitivity to food prices can be gauged from the fact that its poverty estimates range from 33 per cent in the normal food season to 42 per cent in the lean season (World Bank 2008b). Some 35 per cent of Afghan households do not meet their minimum daily calorie intake and 46 per cent are classified as having very poor dietary diversity and poor food consumption.

⁴ Research is underway in World Bank to investigate this issue based on country-level data.

In India, for a five-person household living on US\$1 per person per day, a 30 per cent increase in food prices removes up to 15 per cent of their income-expenditure, if they were totally dependent on food purchases (net consumers) (World Bank 2008c). Moreover, a reduction of 12.5 per cent in calorie consumption is expected for the poorest households due to a 50 per cent price increase of food.⁵ In India, some global estimates suggest a net 2–3 percentage points possible increase in the extent of poverty using countries similar in profile to India, and an equivalent increase in the depth of poverty, which would be comparable to a loss of nearly one-third the poverty reduction gains from generalized growth in India during the past decade (World Bank 2008c). Given these possible consequences, India's success in containing the increase of staple food prices is truly commendable.

In Pakistan, a simulation based on the 2004/5 hardware-in-the-loop simulation (HIES) suggests that the 18 per cent food price inflation between January 2007 and January 2008 could have led to 7–8 percentage point increase in the national poverty headcount rate (World Bank 2008d).

For Bangladesh, a simulation study assessed the impact of the 41 per cent increase in retail rice price between October 2007 and April 2008 (World Bank 2008e). In the short run, a majority of households are adversely affected by the rice price increases because only 17 per cent of Bangladeshi households are net suppliers of rice. In the absence of any wage adjustment, a 41 per cent increase in rice price reduces real households' expenditures by an average of 5 per cent. The impact is larger for urban (6 per cent) than rural households. The impact is much worse for the bottom quintile, where average income declines by 11 per cent as compared with 3 per cent for the top two quintiles.

Among the occupation groups, only households headed by farmers (24 per cent of all households) benefit from rice price increase. The adverse effect is the highest for households headed by agricultural or non-agricultural day workers, and lowest among households headed by salaried workers. With a 5 per cent increase in nominal wages,

⁵ With a calorie-expenditure elasticity of say about 0.5 for the poorest households, all things being equal.

average income declines by 3 per cent for the population and 8 per cent for the bottom quintile. Regarding poverty impact, using the 2005 HIES survey, a 41 per cent rice price hike increases the head-count ratio by 13 per cent in the absence of any wage increase and by 7 per cent with a 5 per cent nominal wage increase. The simulation also suggests an increase in income inequality since the poorest of the poor absorb a greater share of the burden of price increase in view of their larger share of expenditure on staple food in the consumption basket.

In Sri Lanka, according to the World Bank's Poverty Assessment, a large share of the population is clustered around the poverty line, implying that relatively small changes in per capita consumption can lead to relatively large changes in poverty rates. Simulations based on the 2001/2 HIES⁶ indicate that a 10 per cent decline in per capita consumption would lead to a 6 percentage points increase in the poverty head count. Moreover, adverse effects on calories consumption per day, which is already low, would be expected (World Bank 2008f).

Longer-Term Policy Issues and Challenges for Food Security:

Moving Forward

The large magnitude of the terms-of-trade shock along with the acceleration of food prices, especially staple food grains of wheat and rice, has clearly imposed a tremendous burden on the South Asian countries, especially on the low-income economies of Afghanistan, Bangladesh and Nepal. Governments have responded in varying degrees to contain the rise in prices as well as to mitigate the adverse effects on the poor. Yet, the negative impact remains substantial and further efforts are needed to respond more effectively to the external shocks. While the recent decline in food and fuel prices is a welcome development for South Asia, this gain is being clouded by the onslaught of the global financial crisis that is threatening to substantially lower exports, investment and economic growth. Continued high food prices and supply shortages will aggravate the situation.

⁶ The Department of Census and Statistics has not yet made the unit-record data from the 2006/7 HIES available. However, summary statistics from the 2006/7 HIES suggest that inequality has not changed much since 2001/2, implying that the vulnerabilities to income/consumption shocks that were observed in 2001/2 are likely to also be present now.

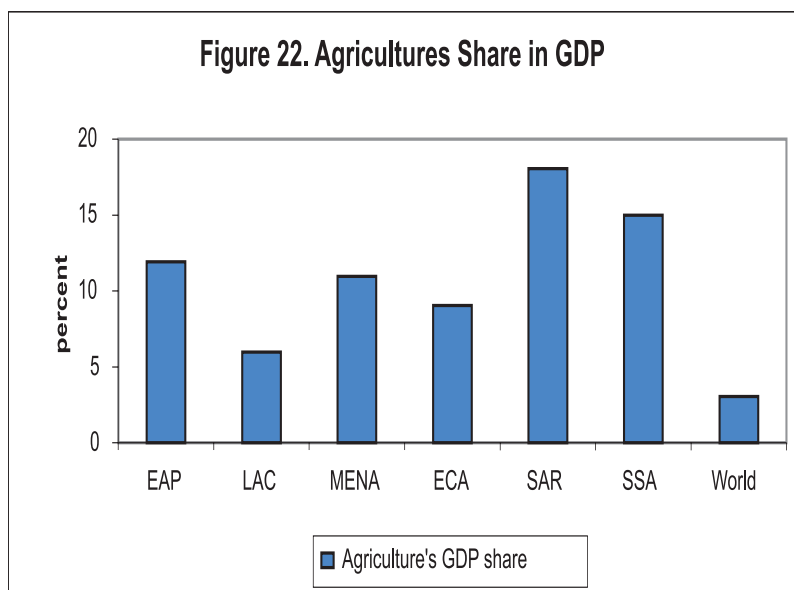
Policies taken by governments in the first round were aimed at stabilizing food prices. Some of the policies like trade bans, price controls and subsidies may have been justifiable as short-term responses on political economy grounds, but they have adverse implications for efficiency and resource allocation over the longer term. As well, the fiscal space is scarce and the magnitudes of the subsidies entailed are not likely to be sustainable. Similarly, government efforts to initiate safety net programmes are laudable; yet there is a need to examine the programmes carefully to ensure their effectiveness and fiscal sustainability. Finally, the longer-term agenda of addressing the supply-side aspects of the food security challenge remains to be fully tackled.

At the heart of South Asia's supply response is the challenge of farm productivity. Policy attention now needs to shift towards efforts to increase farm productivity, improve rural infrastructure, and lower the vulnerability of the poor. In this regard, the increase in food crop prices provides a golden opportunity to policymakers to re-examine the complex system of input-output pricing interventions, reduce spending on input subsidies and instead refocus public spending on areas that will raise farm productivity (irrigation, rural roads, rural electricity). Public policy also needs to move towards reducing the vulnerabilities resulting from climate change and inadequate attention to cross-boundary water management.

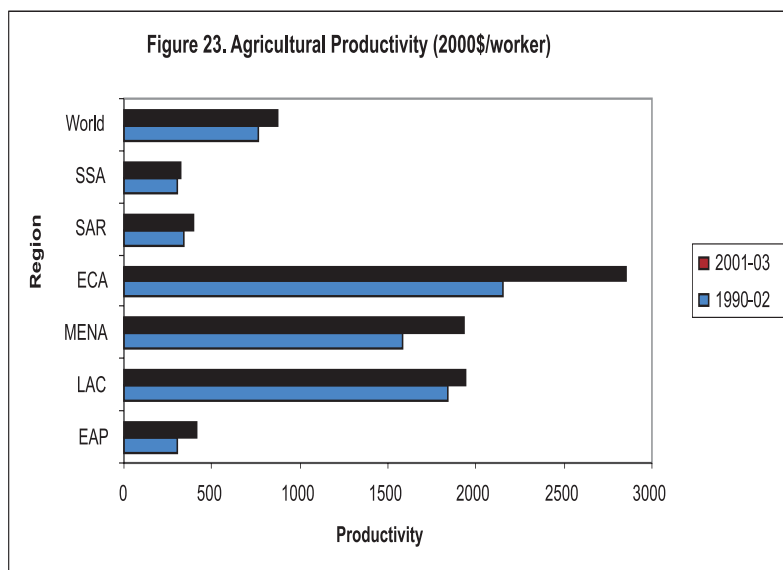
Despite rapid growth since 1980, South Asia's dependence on agriculture remains substantial. While the contribution of agriculture to value added has declined rapidly, it still remains higher than in most regions (Figure 22). More importantly, between 35 and 50 per cent of the labour force remains reliant on agriculture for livelihood, suggesting very low average productivity (Figure 23).⁷ Since world commodity prices of energy and fertilizer are likely to remain substantially higher than the levels in 2006, the only sustainable way of reconciling higher input costs with low and stable prices of wheat and rice for citizens is to pay attention to farm productivity. This is among the most urgent policy focus requirements for the South Asian governments.⁸

⁷ Employment shares range from a low of 35 per cent in Sri Lanka to a high of 50 per cent for Bangladesh (World Bank 2007).

⁸ See von Braun (2008) on the role of productivity improvements and research and development to attack the food crisis at the global level.

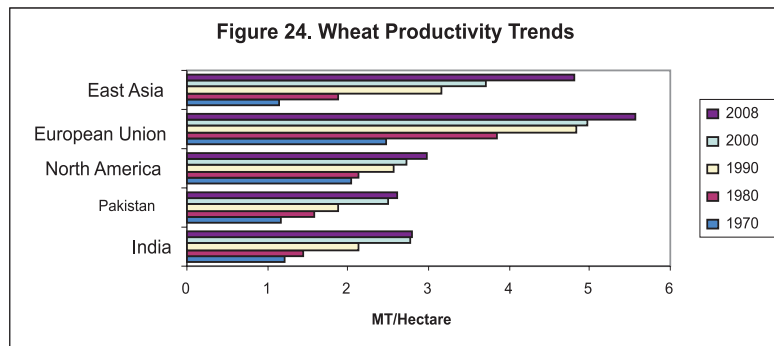


Source: World Bank (2007)

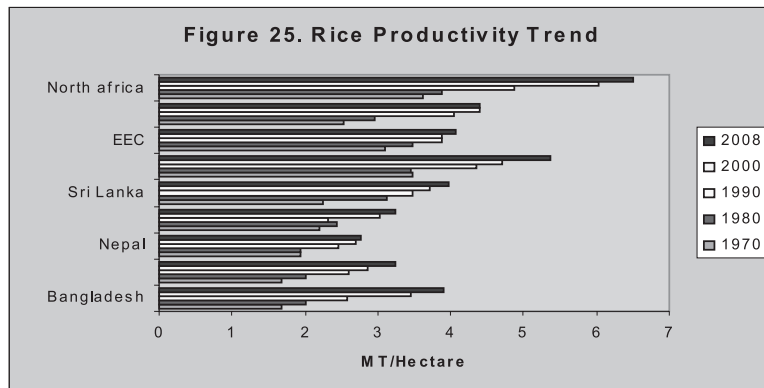


Source: World Bank (2007)

The scope for productivity improvements is clear from Figure 23, but this can be seen more specifically from the productivity comparisons of the two major food crops, wheat and rice. The trend in productivity improvements in South Asia and global comparators for wheat and rice per hectare of land cultivated are shown in Figures 24 and 25.



Source: USDA database



Source: USDA database

Focusing on land productivity is particularly important in South Asia where land endowment is likely to emerge as a binding constraint. The two major South Asian wheat-producing countries (India and Pakistan) achieved substantial gains in wheat productivity between 1970 and 2000, but have faced stagnation since then. Productivity improvements and yield per hectare compare positively with North America but yield remains way behind the EEC countries and East

Asia. For example, the present productivity gap in wheat per hectare is 50 per cent with East Asia and 70 per cent with EEC. Concerning rice, the South Asian countries show significant gains since 1970, especially in Bangladesh and Sri Lanka. Yet the productivity gap with most of the world (except sub-Saharan Africa) is large. For example, the average per hectare yield in the better performing South Asian countries of Sri Lanka and Bangladesh (around 3.7 MT/ha) is still 80 per cent lower than the yield in North Africa (7.0 MT/ha), 60 per cent lower than North America, and 30 per cent lower than in East Asia (5.5 MT/ha). The gaps are even larger for India and Pakistan and the largest for Nepal.

These huge yield gaps in South Asia for both wheat and rice suggest the need for urgent policy attention to find ways to catch up with the performance in the high-yielding countries. This entails addressing issues related to technology, inputs (especially water, fertilizer and energy), pest control and farmer incentives. The range of policies that impact on productivity include incentive policies for farmers (pricing policies, ownership and tenancy issues, farm credit, crop insurance and public expenditure). On the input side, the rising cost of energy, the emerging water shortages, and the frequency of natural disasters especially from flooding and drought, suggest also the need to pay attention to global public goods such as climate change, cross-boundary water sharing arrangements and regional energy trade.

Regional Cooperation for Food Security

As analysed in the Ahmed and Ghani (2008) study, the lagging regions challenge requires recognition of another factor of geography that has largely been neglected in public policy debates: much of South Asia's lagging regions are either landlocked countries (Afghanistan and Nepal) or are border districts/states/provinces of the three larger countries of Bangladesh, India and Pakistan.

- The landlocked countries of both Afghanistan and Nepal are among the lowest per capita income group in the region (See Map 1).
- Out of the fourteen states of India that have borders with neigh-

bours, twelve have per capita income levels that are at or below the national average (Arunachal Pradesh, Assam, Meghalaya, Mizoram, Nagaland, Tripura, Manipur, West Bengal, Bihar, Uttar Pradesh, Jammu and Kashmir, and Rajasthan). Punjab and Gujarat are the exceptions.

- In Pakistan, per capita income is lower than average in the border provinces of North-West Frontier, Balochistan, and rural Sindh; Punjab is an exception. Similarly, urban Sindh is richer than the national average because of the dominance of the port city of Karachi.
- In Bangladesh, the border districts tend to have lower than average national per capita income.
- Most regions lagging in income also have higher than average incidence of poverty and/or poorer human development indicators (See Maps 2 and 3)

Regional cooperation can work on the demand side of the food security question by raising economic growth, reducing the gap between leading and lagging regions, and reducing the vulnerabilities of the poor. On the supply side, the yield gaps in South Asia for both wheat and rice are huge and suggest the need for urgent policy attention to find ways to catch up with the performance in the high-yielding countries. This entails addressing issues related to technology, inputs (especially water, fertilizer and energy), pest control and farmer incentives.

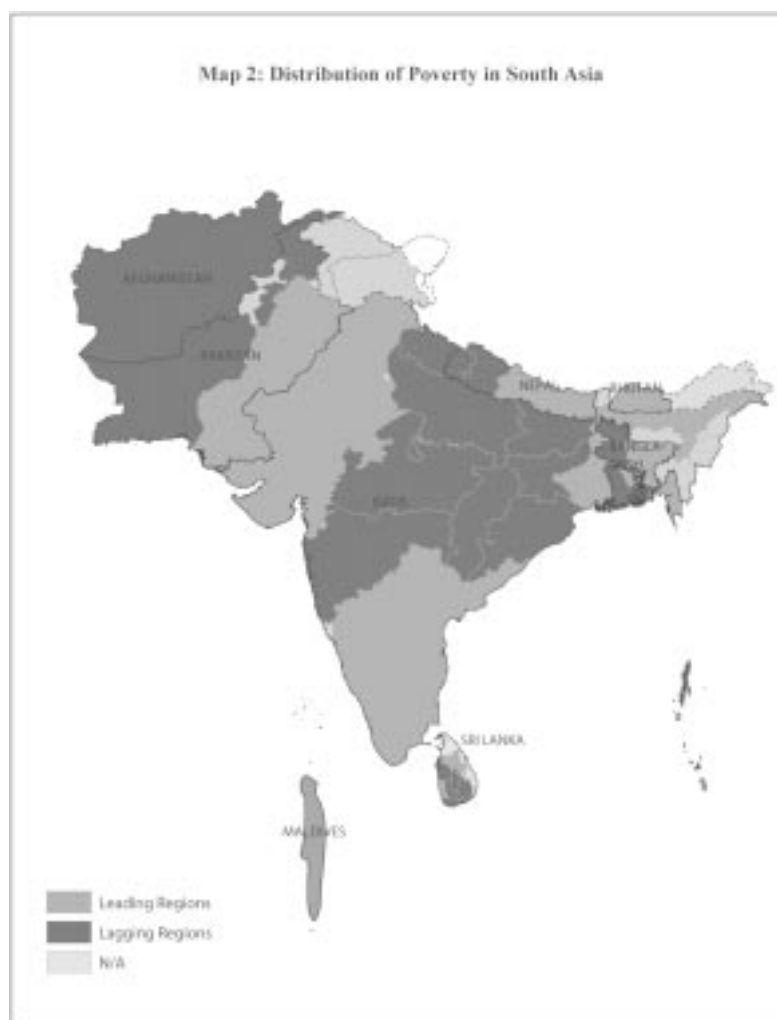
The range of policies that impact on productivity include incentive policies for farmers (pricing policies, ownership and tenancy issues, farm credit, crop insurance and public expenditure). On the input side, the rising cost of energy, the emerging water shortages, and the frequency of natural disasters especially from flooding and drought, suggest also the need to pay attention to global public goods such as climate change, cross-boundary water sharing arrangements and regional energy trade. More and better regional cooperation can be an effective way to manage the farm productivity challenge and ought to be a key element in the design of future food policy strategies in South Asia.



Notes: (1) Leading/lagging regions are defined at the national level based on per capita incomes above or below the national average. (2) Afghanistan, Bhutan and Maldives show national averages as sub-national data are not available.

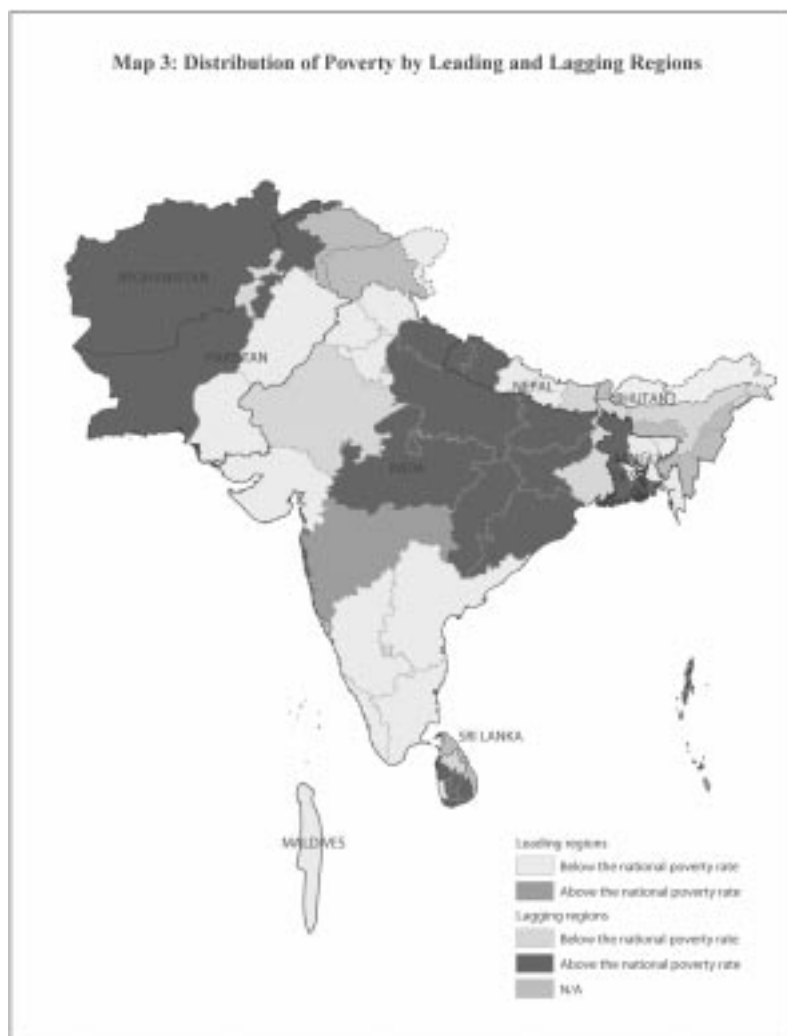
Source: Ahmed and Ghani (2008).

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Note: Afghanistan, Bhutan, and Maldives show national poverty rates.

Source: Figure 5.



Note: Afghanistan, Bhutan, Maldives show national poverty rates.
Source: Ahmed and Ghani (2008).

For Supporting Income in South Asia's Lagging Regions

A detailed analysis of how regional cooperation can help increase growth and income in the lagging regions is available in Ahmed and Ghani (2008). In summary, these channels include:

- First, South Asia is densely populated, with a significant proportion of the population living close to the borders between

countries. After Europe, South Asia has the largest concentration of people living close to the border. It has the maximum “city pairs” within 50 km with a population of more than 25,000 people. Almost all the South Asian countries share a common border with the largest regional partner (India). Regional integration initiatives will unlock the growth benefit of geography and support income convergence across regions and countries. Regional trade is more sensitive to transport costs, scale economies and factor mobility than global trade.

- Second, South Asia suffers from high trade and transportation costs compared to other regions because of border restrictions and poor transport. The cost of trading across borders is nearly double for India and Bangladesh compared to trading with China. It is more than three times higher for Afghanistan, Bhutan and Nepal. The quality of transport infrastructure, especially the highway networks, in South Asia is poor. Truck operating speeds are low, delays at state/provincial check posts are frequent and can be long, and delivery times are consequently subject to significant variation. The regions away from the main trade corridors have the poorest infrastructure and face the greatest constraints. Raising the level of the infrastructure and reducing regulatory barriers to trade, whether international or national, will help integrate the lagging regions into both the national and global economies, reducing the relative advantages of the coastal states.
- Third, factor mobility, and in particular migration rate, is low in South Asia. Only 2 million people migrate every year in India from rural to urban areas, compared to nearly 20 million people in China. Increased agricultural productivity will help to reallocate labour and capital from low-value activities (agriculture) to high-value activities (manufacturing and services sectors) and support growth.
- Fourth, South Asian firms are disproportionately small. They are unable to reap the benefits of scale economies because of labour and regulatory restrictions which prevent them from growing. The policy changes aimed at taking advantage of the interactions between geography, transportation, factor mobility, and scale economies will lift growth not only in the lagging regions

but also support higher growth rates at the country level and in South Asia.

For Supporting Farm Productivity

A major factor underlying South Asia's low farm productivity is the relatively poor rural infrastructure. While South Asia has made progress in improving irrigation facilities for agriculture, the coverage of irrigated agriculture still remains relatively low (39 per cent) (World Bank 2007). More importantly, the availability of water is a serious issue (Table 7), except for Nepal which has surplus water resources. Similarly, the rural population's access to roads and electricity is a

Table 7. Access to Water and Rural Infrastructure

Country	Renewable internal freshwater resources per capita cu. m. 2005	Rural population access to an all-season road % 1993–2004	Rural household access to electricity % 1995–2006
Bangladesh	96	37	19
India	1152	61	48
Nepal	7305	17	17
Pakistan	336	61	69
Sri Lanka	95	n.a.	n.a
China	2156	97	n.a
Indonesia	12867	94	90
Vietnam	4410	84	72

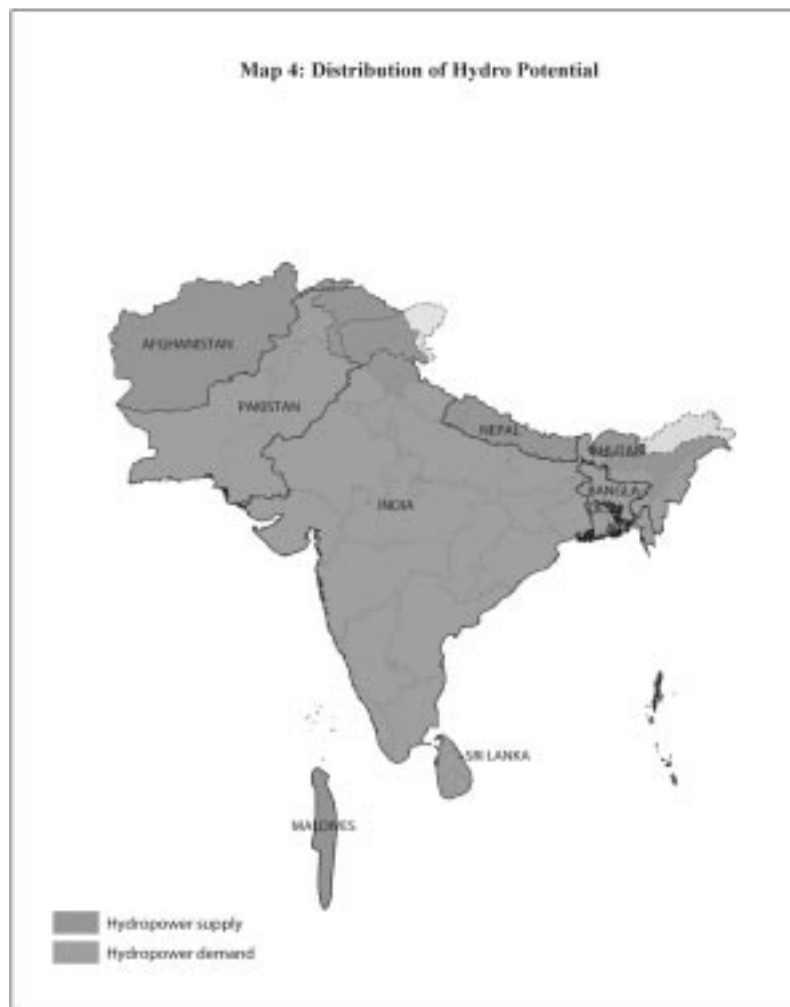
Source: World Bank (2007).

serious handicap to farm productivity and incomes. Evidence from international experience as well as from South Asia demonstrates the high rate of return from investments in rural infrastructure.

Regional cooperation can help raise farm productivity by easing energy and water constraints. It can also reduce cost and improve farm income by lowering the cost of these inputs and by improving transport bottlenecks. High trade logistics are a huge barrier to agricultural exports and regional cooperation can help lower trade logistics costs.

The potential gains from regional trade in energy are substantial. This is best seen by looking at Map 4 that shows South Asia's potential sources of hydropower (blue) and its demand (gold). The map tells a powerful story. Afghanistan, Bhutan, and Nepal are sitting on water

resources that could potentially generate some 24,000 MW of electricity from Afghanistan, 30,000 MW from Bhutan and an estimated 83,000 MW from Nepal. These together account for 90 per cent of South Asia's currently installed capacity.⁹ Bangladesh, India, and Pakistan are power-deficit countries, especially India. The growing electricity constraint is threatening the ability to sustain rapid growth. Yet, less than 2 per cent of the hydropower potential in the



Source: Ahmed and Ghani (2008)

⁹ South Asia's installed generation capacity is estimated at 152K MW. See World Bank (2008e).

region has been used so far. The reason is lack of cooperation and absence of energy trade among the regional countries. Indeed, if one were to imagine South Asia without borders, perhaps the highest priority investment would have gone to develop the hydropower resources. While all countries would benefit from the development of South Asia's hydropower resources, Afghanistan and Nepal, the two poorest South Asian countries, would benefit most.

After decades of insignificant cross-country electricity trade and the absence of any trade in natural gas through pipelines, regional political leaders and businessmen have recently evinced a great deal of interest and enthusiasm in cross-border electricity and gas trade, not only within South Asia but also with its neighbours in the west (Central Asia and Iran) and in the east (Myanmar).

There are two regional energy clusters in South Asia. The eastern market includes India, Bangladesh, Bhutan, Nepal, and Sri Lanka, extending to Myanmar, and the western market includes Pakistan, Afghanistan and India, extending to Central Asia and Iran. India bridges the two clusters. Some activities are underway, including a very successful hydropower trade between Bhutan and India in the eastern market and an ongoing project in the western market that will bring electricity from Tajikistan and Kyrgyzstan to Afghanistan and Pakistan.¹⁰

What can governments do to promote energy trade? They need to continue reducing political and security tensions; consider energy trade as enhancement of energy security and political and economic cooperation; continue energy sector reforms; improve commercial performance of the utilities; improve the credibility, competence, and accountability of regulation; adopt sustainable (cost-reflective) tariffs and a social protection framework; promote a commercial approach to energy trade; encourage private sector participation in the form of public-private-partnership (PPP) structures in cross-border investments; help the transit countries—especially Afghanistan—integrate; engage in reaching water-sharing agreements; seek accession to international agreements (such as Energy Charter

¹⁰ This is the Central Asia–South Asia (CASA) energy project that seeks to sell 1000 MW of surplus power from Tajikistan and Kyrgyzstan to Afghanistan and Pakistan. The project is being developed in cooperation with a number of multi-lateral financial institutions, including the World Bank

Treaty); strengthen regional institutions at both political and technical levels; and identify priority-trade-oriented investment projects and pursue their implementation. The success of the India–Bhutan electricity trade should offer useful lessons to other countries.

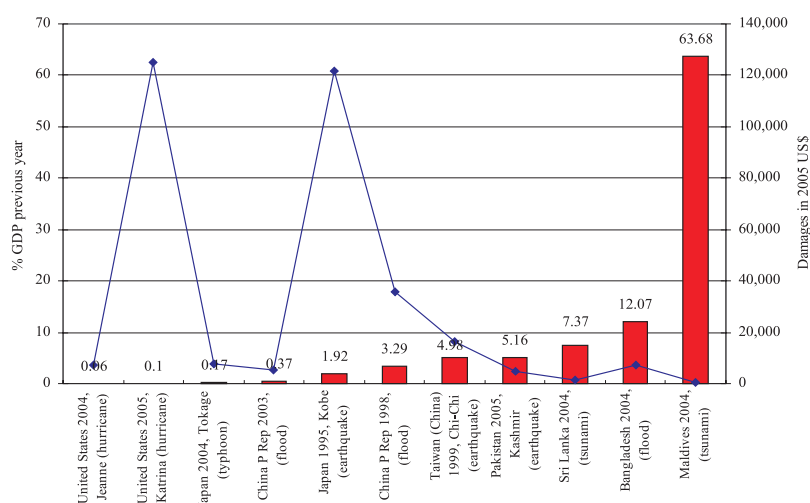
Restrictions on transport border crossings are a major constraint to global and intra-regional trade in South Asia. They especially hurt the integration of farmers in the border areas to growth centres. One specific example is the export of pomegranate from Afghanistan to India. There is a huge market for Afghanistan’s fresh pomegranates in India. This is currently heavily constrained by the lack of Afghanistan’s transit access to India via Pakistan. The result is that only a limited amount of this product reaches India via Dubai owing to huge transport cost. Removing this type of restrictions would boost trade within South Asia as well as lower the cost for international trade in general as many landlocked countries and regions will benefit from access to the closest ports.

Agricultural producers will benefit substantially as trade logistics tends to be a huge bottleneck. Currently, the efforts being made at improving trade facilitation and transport networks are fragmented, with little cooperation even where cross-border issues are involved. Establishing corridor-based approaches for improving the trade transport arrangement for intra-regional trade would be essential for improving the efficiency of regional transport and for reducing trade costs.

For Reducing the Vulnerabilities of South Asia’s Poor

Apart from being poor, the lagging regions also share a number of common vulnerabilities. First is the vulnerability to natural disasters. Figure 26 shows the impact of natural disasters in terms of the share of GDP lost. South Asia has lost a significant amount of its GDP because of natural disasters. This loss has been especially significant for Maldives, Bangladesh, Sri Lanka and Pakistan. The impact of natural disasters is particularly strong in South Asia because of its high population density. The losses are typically not insured in the financial market. It is the poor who are adversely affected by disasters.

Figure 26. Percentage of National GDP Damaged by Select Natural Disasters



Source: <http://www.unisdr.org/disaster-statistics/top50.htm>

South Asia's poor would probably gain most from regional cooperation in water and climate. This is again obvious from Map 4. From the Himalayas, where glacier melt is already changing water flows in ways that remain to be understood, to the coastal floodplains of Bangladesh and Pakistan, the South Asian countries need to adapt to climate change. The melting of Himalayan glaciers leading to the disastrous prospect of reduced water availability in the South Asian rivers, the frequency of floods and cyclones, and the evidence of rising sea level have given South Asia a wake-up call for collective action for managing climate change to reduce vulnerability and poverty over the longer term. Clearly, actions at the national level cannot alone provide sustainable solutions as much of the water flows from upstream countries of Afghanistan, Nepal, China and parts of India to Bangladesh, most of India and Pakistan. Finding sustainable solutions for flood control, irrigation and river transport will require cooperation with upstream countries. Thus, cross-border cooperation on water between India, Bangladesh, and Nepal offers the only long-term solution to flood mitigation. The benefits of cooperation are clear. For example, watershed management and storage on Ganges tributaries in Nepal could generate hydropower and irrigation benefits

in Nepal and flood mitigation benefits in Nepal, India (Uttar Pradesh, Bihar) and Bangladesh; water storage in north-east India could provide hydropower and flood control benefits in India and Bangladesh; and both would also provide increased and reliable dry season flows. There is an emerging and promising opportunity for specific cooperation between India, Nepal, and Bangladesh on the Ganges.

There are similar benefits of water cooperation between India and Pakistan and between Pakistan and Afghanistan. The Indus Water Treaty between Pakistan and India has already demonstrated that cooperation that benefits people can withstand all political obstacles. Building on this success, other water disputes and potential water markets could be developed through a similar cooperative solution. Afghanistan sits on the upper riparian of some five water basins that have huge potential for irrigation and hydropower benefits which could well transform Afghanistan's economy. Yet, there has been very little of the critical investments required to transform this natural resource into a productive asset for the benefit of the people of Afghanistan. As a result Afghanistan remains a severely water-constrained economy with also a serious power shortage. A key constraint is lack of a framework for water sharing agreements with neighbours. The Kabul River Water Basin Project, if implemented, will yield substantial hydropower and irrigation benefits for both Afghanistan and Pakistan, but is awaiting riparian agreement between the two countries.

Managing the Politics of Cooperation in South Asia: The Way Forward

The potential benefits of economic cooperation – food security and more broadly for accelerating South Asia's growth and poverty reduction – are obvious. Global examples of successful cooperation agreements reinforce the point that possible gains for South Asia from effective cooperation and partnerships can be substantial. In particular, the experience of East Asia is illustrative of the potential gains from more and better cooperation. Cross-border physical connectivity has improved tremendously through land-, sea- and air-based transport network. Private-sector-led vertical integration of production networks has spurred industrial productivity and growth, and e-commerce is flourishing. Yet, the actual experience with

cooperation in South Asia so far has been rather dismal. What are the key constraining factors?

- First is the prevalence of a number of regional disputes. These include the longstanding conflict between India and Pakistan over Kashmir. The Afghan–Pakistan relations are constrained by allegations of support for the Taliban from sources in Pakistan. Similarly, securing the immigration and security issues in the India–Bangladesh border areas is a source of concern.
- Second is the lack of good analysis and information in the public domain about the benefits of regional cooperation. On the contrary, there are unfounded populist negative perceptions in the smaller countries about how more cooperation will simply result in the greater domination of India in political and economic matters of these countries.
- A third factor has been internal political interests in countries that are divided along nationalist, religious and ethnic lines which substantially complicate policymaking that involves cross-border dialogue and cooperation.
- Finally, and perhaps most importantly, the approach to international cooperation has been seriously flawed in that this has largely been seen as a bilateral politically driven agenda rather than a cross-boundary commercial investment. The bilateral political approach has partly contributed to suspicions in the smaller countries of India's dominance.

International experience suggests that political constraints and historical conflicts need not be permanent barriers to development cooperation. Neither is the presence of a dominant member country a necessary threat to cooperation and shared gains. For example, the members of the European Union have fought numerous wars in the past, many of them far more intense, long-drawn and expensive in terms of loss of human lives and material resources than South Asia. Similarly, member countries diverge considerably in economic strength. Yet they have found it mutually advantageous to come together and devise a formidable economic union. In East Asia, the economic dominance of China has not prevented very effective regional cooperation with the much smaller East Asian countries.

Fortunately, the political environment for cooperation in South Asia

is now changing. The dialogue on economic cooperation at both the bilateral and multilateral levels is slowly taking roots with some concrete actions. Two very recent and encouraging moves are the resumption of passenger rail traffic between Dhaka and Kolkata and the opening up of trade between India and Pakistan on the Kashmir Line of Control. At the institutional level, the regional cooperation efforts in South Asia culminated in the formation of the South Asian Association for Regional Cooperation (SAARC) in 1985. Until very recently, SAARC basically functioned as an annual event for meeting of heads of government with declarations of cooperative intentions but with very limited implementation due to conflict and political difficulties. Armed with recent economic successes the political space for better regional cooperation is now growing in South Asia. The last two SAARC meetings have succeeded in bringing the countries much closer than ever before in recognizing the merits of regional cooperation and taking significant actions to realize these benefits.

The next step is to identify concrete bankable projects where multi-country cooperation would yield tangible benefits to citizens. The immediate priority areas are well known: promote trade facilitation by removal of all trade barriers; improve regional transport by removing transit restrictions and opening up port facilities for international trade; promote trade in energy in all possible ways including hydropower, gas pipelines and regional grid facilities; and water cooperation to resolve flooding and irrigation problems. Cross-border transactions must be depoliticized and pursued on a commercial basis. Enabling national and international private investors to participate in these transactions holds greater promise of success than bilateral political deals. International financial institutions can also play a useful role by bringing global good practices, by providing technical assistance to smaller countries, and by mobilizing external financing. Where legal agreements are needed these can be best pursued multilaterally to avoid any perceptions of dominance.

It is not realistic or necessary to expect that all political and social conflicts will have to be resolved first before meaningful cooperation can happen. Indeed, economic cooperation is also a powerful means for resolving political and social conflicts. Trust and goodwill at the citizens' level can be a credible way for resolving conflicts. Economic cooperation by raising citizens' welfare can be instrumental in building

this trust. Political forces can provide an impetus to this by reducing policy barriers to regional integration.

Conclusions

The surge in global commodity prices of the past few years has presented a tremendous development challenge for the South Asian countries. The large loss of income from the terms-of-trade shock has worsened macroeconomic balances, fuelled rapid inflation and hurt growth. While commodity prices have come down recently, the benefits are being clouded by the emergence of a severe global financial crisis. The adverse consequences of the food price hike for the poor are large; the global financial crisis could worsen the situation due to falling economic opportunities and government revenues. The South Asian countries need to accelerate reforms to avoid facing a serious downturn in economic activity, investment, exports and income. Governments in South Asia have responded by stabilizing domestic food prices through a range of short-term measures, tightened monetary policy to reduce inflation, and increased spending on a range of safety net programmes for the poor. Some of the policies employed, such as export bans, are not consistent with long-term welfare of the country or the region. Safety net interventions need to be made consistent with longer-term poverty reduction strategy and fiscal sustainability. Most importantly, policy attention now needs to shift towards efforts to increase farm productivity, improve rural infrastructure, and lower the vulnerability of the poor. In this regard, the increase in food crop prices provides a golden opportunity to policymakers to re-examine the complex system of input-output pricing interventions, reduce spending on input subsidies and instead refocus public spending on areas that will raise farm productivity (irrigation, rural roads, rural electricity). Public policy also needs to move towards reducing the vulnerabilities resulting from climate change and inadequate attention to cross-boundary water management. More and better regional cooperation can be an effective way to manage the farm productivity challenge and ought to be a key element in the design of future food security strategies in South Asia.

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Should South Asia Look East? Assessing the Economic Effects of Closer Integration

*Ganeshan Wignaraja*¹

South Asia has increasingly been involved in the gathering momentum towards regionalism in Asia. Stimulated by the 1997-1998 Asian financial crisis, a renewal of Asian regionalism is visible in significant intra-regional trade within economically advanced East Asia and a focus on region-wide free trade agreements (FTA) around ASEAN. Following economic reforms in the 1980s and 1990s, South Asia began expanding trade and investment relations with East Asia. India's emergence as a global economic powerhouse and accelerating growth in the rest of South Asia generated increasing support for deeper regional integration across Asia. India's 1991 Look East Policy signalled its policy intent for a trade agreement with East Asia and Japan is spearheading on-going discussions on a Comprehensive Economic Partnership Agreement (CEPA) involving ASEAN+3 countries, India, Australia and New Zealand. The conclusion of the ASEAN-India FTA negotiations in August 2008 has been widely hailed as a milestone on the road to CEPA. Moves towards closer economic integration between South and East Asia are likely to be fuelled by increasing uncertainties in the global economy, including the extended delay in the Doha Round of WTO trade talks, the proliferation of bilateral FTAs, a global credit crisis and the prospect of a world recession.

This paper offers an assessment of the economic effects for South Asia, particularly India, from closer economic integration with East Asia and possible alternatives. Using computable general equilibrium (CGE) model simulations of FTA scenarios as well as analysis of trade flows and comparative policies, it addresses three pressing questions: (1) what is the extent of trade and FTA activity between South and East Asia? (2) what are the gains from India looking East, West or South in its trade agreements? and (3) what are the key

¹ I owe a debt to various co-authors of academic papers, particularly Masahiro Kawai, Joe Francois and Mike Plummer, who have influenced my thinking on Asian regionalism over several years. The views expressed in this paper are solely mine and not to be attributed to the Asian Development Bank (ADB) or its affiliated organizations.

issues in closer economic integration between South and East Asia? The remainder of the paper deals with these questions and explores policy implications. East Asia is defined here to include the ten ASEAN members, plus China, Korea and Japan. South Asia consists of the eight SAARC members (India, Pakistan, Bangladesh, Bhutan, Sri Lanka, Maldives, Nepal and Afghanistan).

Trade and FTA Activity with East Asia

The momentum towards closer integration between South and East Asia is surprisingly recent.² South and East Asia followed different economic strategies in the 1970s and 1980s. East Asia adopted outward-oriented strategies and witnessed remarkable economic prosperity while inward-oriented South Asia largely stagnated. Before 1990, South and East Asian economies were relatively isolated from one another in terms of economic relations and there was little talk of pan-Asian integration. There were limited bilateral trade and investment flows in goods or services. The only trade agreement that covered the two sub-regions was the Bangkok Agreement (now called the Asia-Pacific Trade Agreement) signed in 1975.³ This relative isolation is associated with poor connectivity, barriers to regional trade and investment, and a lack of political signals to foster South Asia–East Asia integration.

Table 1. Growth in South Asia’s Trade with East Asia, 1990–2007

Country	Exports		Imports	
	Average Annual Growth Rate, 1990–2007 ^a	Value (US\$ Mn), 2007	Average Annual Growth Rate, 1990–2007 ^a	Value (US\$ Mn), 2007
South Asia	13.9	36,221	14.9	92,727
India	16.1	33,093	18.3	66,005
Pakistan	4.3	2,021	11.6	13,108
Bangladesh	7.7	549	11.0	7,614
Sri Lanka	5.5	465	9.3	4,203
Maldives	8.2	60	10.4	521
Nepal	3.4	25	5.1	706
Afghanistan	7.7	9	4.1	569

(a) compound growth rate in US\$. No data for Bhutan; East Asia refers to 10 ASEAN members, Japan, PRC, and Korea.
Source: Computed from IMF Direction of Trade Statistics, accessed October 2008.

² The growing literature on this subject includes: Kumar, Sen and Asher (eds., 2006). For an interesting set of lessons for South Asia from East Asian integration, see Chandra and Kumar (2008).

³ This agreement covers Bangladesh, India, Sri Lanka, the Lao People’s Democratic Republic (Lao PDR), the Republic of Korea, and China.

After 1990, a rapid growth in trade between South and East Asian economies has occurred, albeit from a relatively low base. As is seen from Table 1, South Asian exports to East Asia (in US\$) grew rapidly at 13.9 per cent per year between 1990 and 2007 while imports from East Asia grew at a comparable rate (14.9 per cent). The value of total trade between South Asia and East Asia amounted to around \$129 billion in 2007 (up from \$12.7 billion in 1990). South Asia's larger economies account for the bulk of the growing trade with East Asia. The giant Indian economy (which makes up 76.9 per cent of the value of South Asia's trade with East Asia) has witnessed double-digit growth in trade relations with East Asia. Pakistan, Bangladesh and Sri Lanka have also experienced growth in trade relations with East Asia, particularly imports. The region's smaller LDC economies (Maldives, Nepal and Afghanistan) are at the early stages of trade relations with East Asia.

At least five interrelated reasons may help explain the rapid growth of trade between South and East Asia. First, the South Asian economies have adopted more market-friendly trade and investment regimes through a gradual implementation of economic reforms in the 1980s and 1990s. Second, in the decade since the Asian financial crisis of 1997/98, East Asia has re-emerged into the global economy with high growth, enviable flows of export-oriented FDI and localization of production networks geared towards regional markets.⁴ Third, the giant dynamic Chinese and Indian economies are increasing their economic relations and acting as growth poles in their respective sub-regions. Fourth, transport, communications and logistics costs in Asia have fallen significantly amidst technological progress and productivity gains. Fifth, there is a spread of FTAs involving the two sub-regions in an attempt to liberalize intra-Asian trade and provide more clarity of the rules governing such trade.

There has also been a shift in South Asia's trade shares towards East Asia. As seen in Table 2, the share of South Asia's exports to East Asia increased from 14.5 per cent to 18.8 per cent between 1990 and 2007 and the share of imports from 22.5 per cent to 28.1 per cent. Underlying this shift is a significant realignment of India towards East Asia which accounts for one-fifth of India's exports

⁴ See Plummer and Wignaraja (2006), Kawai and Wignaraja (2008) and Zhang (2006).

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and a quarter of its imports (2007). The rest of South Asia exhibits varying degrees of trade orientation towards East Asia. LDCs like Nepal and Maldives have strong export and import links while others have strong import links. India's experience underlines that closer economic links with East Asia offer South Asian economies a potentially dramatic enlargement of their economic horizons, making available a far greater regional market with which they can integrate. It is worth bearing in mind, however, that closer economic integration with South Asia offers East Asia a relatively modest increase in market size.

Table 2. Trade Shares of South Asian Countries, 1990 and 2007 (per cent)

	ASEAN+3		EU		US		ROW	
	1990	2007	1990	2007	1990	2007	1990	2007
<i>Exports, per cent share in total exports</i>								
South Asia	14.5	18.8	30.7	23.8	16.3	16.3	38.5	41.1
Afghanistan	2.0	2.8	61.8	7.4	3.4	21.3	32.8	68.4
Bangladesh	9.3	4.0	33.8	45.3	30.5	23.9	26.4	26.8
India	14.6	21.9	28.5	21.5	15.1	15.1	41.8	41.5
Maldives	30.1	34.9	26.2	35.7	24.2	2.0	19.5	27.4
Nepal	12.9	46.3	53.3	11.2	23.4	8.9	10.4	33.6
Pakistan	17.6	10.3	36.7	22.0	12.4	17.7	33.2	50.0
Sri Lanka	9.9	5.4	26.8	35.8	25.9	23.1	37.5	35.7
<i>Imports, per cent share in total imports</i>								
South Asia	22.5	28.1	28.6	16.3	10.3	6.9	38.6	48.7
Afghanistan	60.4	11.8	14.9	12.9	1.0	11.1	23.7	64.2
Bangladesh	35.5	36.5	18.3	7.4	5.1	2.4	41.1	53.7
India	15.8	26.6	33.4	17.7	11.0	7.8	39.9	47.8
Maldives	70.1	45.5	13.0	10.9	0.6	1.9	16.4	41.7
Nepal	51.5	21.6	18.0	3.3	2.4	1.0	28.0	74.1
Pakistan	27.6	33.1	24.7	14.4	12.8	5.7	34.8	46.8
Sri Lanka	35.2	32.9	16.1	14.5	7.9	2.0	40.8	50.7

No data for Bhutan; East Asia refers to ASEAN plus Japan, PRC, and Korea.

Source: Computed from IMF Direction of Trade Statistics.

The commodity composition of trade between the South and East Asian economies tends to reflect inter-country differences in comparative advantages (natural resources, capital, labour and technology) and levels of economic development. With an abundance of natural resources and labour, South Asian exports to East Asia will be more weighted towards such products. Meanwhile, South Asia's

imports from East Asia will consist mainly of finished and high-technology goods, reflecting an abundance of capital and technology. To illustrate this pattern of trade, Table 3 provides the leading items in India's trade with East Asia since 1991. India's main exports to East Asia are dominated by natural resource-intensive products (iron ore, mineral fuels, pearls and stones, cotton, fish), non-ferrous metals and ores, granite, leather, oil cake, beef, and crustaceans as well as some skill- and technology-intensive goods (chemicals, plastics and machinery). In contrast, East Asia's leading exports to South Asia feature products such as computers and integrated circuits, TV, radio and telecommunication equipment, motor vehicles and motor vehicle parts, and antibiotics. Where there is a two-way trade in the same industry, East Asian exports tend to be at a higher level of processing. For the steel industry, India's leading exports to East Asia include ferro-alloys, pig iron, and rolled steel; East Asia's leading exports to South Asia include rolled steel of a heavier grade.

Table 3. India's Top Ten Traded Commodities with East Asia
Per cent share in world trade

HS Code	Commodity Description	1991	1999	2005
Exports				
71	Natural/cultured pearls, precious/semiprecious stones, precious metals	13.9	28.6	20.0
26	Ores, slag, and ash	18.7	6.0	15.9
27	Mineral fuels, mineral oils and products or their distillation	0.0	0.1	11.9
72	Iron and steel	2.2	2.2	6.6
29	Organic chemicals	2.0	5.3	5.8
39	Plastics and their articles	0.2	0.4	3.2
84	Nuclear reactors, boilers, machinery and mechanical appliances and parts	3.7	2.6	3.0
52	Cotton	11.3	8.9	2.8
03	Fish and crustaceans, molluscs and other aquatic invertebrates	11.0	9.9	2.3
85	Electrical machinery and equipment and their parts	1.8	4.0	2.0
Imports				
85	Electrical machinery and equipment and their parts	10.1	9.7	19.4
84	Nuclear reactors, boilers, machinery and mechanical appliances and parts	11.1	15.7	17.2
15	Animal or vegetable fats and oils and their cleavage products	4.3	7.3	7.1
27	Mineral fuels, mineral oils and products or their distillation	5.6	8.1	6.0
71	Natural/cultured pearls, precious/semiprecious stones, precious metals	0.5	1.8	5.4
72	Iron and steel	6.3	3.3	3.1
39	Plastics and their articles	4.1	3.5	2.8
89	Ships, boats, and floating structures	1.7	0.9	2.8
90	Optical, photographic, measuring, medical instruments and apparatus	3.5	2.5	2.3
44	Wood, articles of wood, and wood charcoal	6.2	2.9	2.2

Sorted according to 2005 trade shares.

Source: Kumar and Sharma (2008).

Growing trade integration between South and East Asia since 1990 has been accompanied by heightened FTA activity. As is seen from Table 4, there was only one FTA linking the South and East Asian economies in 2000 (the 1975 Asia-Pacific Trade Agreement). By October 2008, five FTAs had been concluded while another fifteen were either under negotiation or were proposed. Not surprisingly, the largest economies with better trade negotiations capacity are at the forefront of South Asia's FTA activity with East Asia. India is a member of the Asia-Pacific Trade Agreement and has concluded an FTA with Singapore in 2005. Pakistan has bilateral FTAs with Malaysia (2005) and China (2007). As elsewhere, the emphasis on FTAs to shape South Asia–East Asia trade reflects the extended delay in the Doha Round of WTO trade talks. Significant South Asia–East Asia FTAs under negotiation or proposed include the ASEAN–India FTA, China–India FTA and the CEPA. Appendix Table 2 contains the full list of South Asia–East Asia FTAs by status.

Beyond East Asia, some South Asian countries are involved in FTA negotiations with major trading partners. Accordingly, India is undertaking FTA negotiations with the EU and Pakistan and Sri Lanka some initial discussions with the US. These seem early days in such cross-regional trading arrangements.

Table 4. Number of South Asian FTAs with East Asia and Other Partners, 2000 and 2008

Partner	2000		2008	
	Concluded (a)	Under Negotiation and Proposed (b)	Concluded (a)	Under Negotiation and Proposed (b)
East Asia	1	0	5	15
US and EU	0	0	0	3
South Asia only	2	0	6	2
ROW	0	0	6	20
Total	3	0	17	40

*Under Negotiation: India-EU FTA; Proposed: US-Sri Lanka FTA and US-Pakistan FTA.

Gains from India Looking East, West or South in Trade Agreements

Responding to policy interest and developments in computable

general equilibrium (CGE) models, there is a growing literature which analyses the economic effects of alternative FTAs on South Asian economies.⁵ This literature commonly uses the Global Trade Analysis Project (GTAP) database but varies in the underlying model and behaviour of agents, the policy scenarios analysed and the version of the database used. Moreover, such work tends to focus narrowly on an FTA involving goods only and exclude other aspects of the coverage of FTAs (e.g. services and trade costs). There is a need for a more comprehensive set of CGE estimates on alternative FTA scenarios for India and other South Asian countries to fill these gaps.

A CGE exercise was conducted using a variant of the GTAP model.⁶ The model used has an input-output structure (based on regional and national input-output tables) that explicitly links industries in a value added chain from primary goods, over continuously higher stages of intermediate processing, to the final assembling of goods and services for consumption. Intersectoral links are both direct, like the input of steel in the production of transport equipment, and indirect, via intermediate use in other sectors. The model captures these links by modelling firms' use of factors and intermediate inputs. The key aspects of the model are: (i) it covers world trade and production; (ii) it includes intermediate links between sectors; (iii) and it allows for trade to affect capital stocks through investment activities. The final point means that medium- to long-run investment effects are captured in the model.

The main database used is the GTAP dataset version 6.3, which included detailed national input-output, trade and final demand structures. This database was projected through to 2017 trade and production patterns to represent a post-Uruguay Round world. The coverage of FTA provisions is a stylized FTA that includes goods, services and some aspects of trade cost reduction. Hence, the analysis includes the impact of regional tariff elimination for goods, liberalization of services trade, and trade facilitation including improved trade-related infrastructure. Forward projection of the database and extending the coverage of FTAs beyond goods are recent developments in the CGE FTA studies.

⁵ The CGE literature on South Asia includes: Siriwardena (2003), Bandara and Yu (2003), Mohanty et al. (2004), Bchir and Fouquin (2006), Mohanty and Pohit (2007) and ADB-UNCTAD (2008).

⁶ For more details of the CGE model used in this paper, see Francois and Wignaraja (2008).

Using this CGE framework, some broad welfare effects from six core FTA scenarios are examined in this paper:

1. An EU-India FTA: free trade among the EU members and India;
2. A US-India FTA: free trade between the United States and India;
3. An ASEAN-India FTA: free trade among the ten ASEAN members and India;
4. An ASEAN+3 and India FTA: free trade among the ten ASEAN members plus China, Japan, Korea and India;
5. An ASEAN+3 and South Asia FTA: free trade among the ten ASEAN members plus China, Japan, Korea and all South Asian countries;
6. A South Asia FTA: free trade among all South Asian countries.

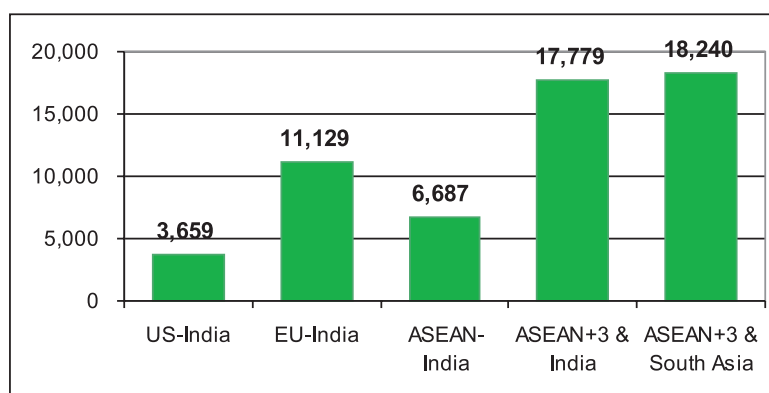
A range of important South Asian FTA possibilities are illustrated by the six scenarios chosen. Scenario 1 has been under negotiation since 2007. Scenario 2 may be a medium-term possibility in the wake of the US-India Agreement for Cooperation Concerning Peaceful Uses of Nuclear Energy (123 Agreement) signed on 10 October 2008, which allows India to buy US civil nuclear technology.⁷ In the case of scenario 3, negotiations were concluded on 28 August 2008 and the FTA is expected to be signed in December 2008. Scenario 4 reflects on-going discussions among policymakers on linking India with East Asia while scenario 5 shows the impact of including the whole of South Asia with East Asia. Scenario 6, a South Asian FTA, represents the outcome of an evolving SAFTA process – covering goods, services and trade facilitation. All results are reported relative to a 2017 baseline simulation.⁸ The discussion will focus on economic effects for India and the other South Asian countries.

⁷ While not discussing a possible India-US FTA, in July 2005 President Bush and Indian Prime Minister Singh created a Trade Policy Forum – a standing bilateral committee chaired by Indian Commerce Secretary Kamal Nath and US Trade Representative Rob Portman – to increase trade and investment flows between the two countries.

⁸ The baseline of the model is 2017 and the simulations show changes from this baseline. As the formation of some of these arrangements, particularly Asia-wide FTAs, is likely to take time, setting up the model and data set in this way provides for more realistic scenarios.

Figure 1 shows the estimated impacts on India's national income of the FTA scenarios 1 to 5. Interestingly, India gains most in terms of economic welfare from scenarios 4 and 5 involving ASEAN as well its large North Asian neighbours. The ASEAN+3 and South Asia scenario, an illustrative example of a broad region-wide scenario, offers larger gains to India's income (\$18.2 billion, measured in constant 2001 prices) than the ASEAN+3 and India scenario (\$17.8 billion). This suggests that India gains more by including the rest of South Asia in a trading arrangement with East Asia than going it alone with East Asia. Among the other three scenarios shown, the India-EU FTA scenario offers the next-largest gains for India, followed by an ASEAN-India FTA and an India-US FTA.

Figure 1. Welfare Impacts on India of FTA Scenarios
US\$ million change compared to 2017 baseline (at constant 2001 dollars)



Noting that FTAs with East Asia offer larger welfare gains for India than those with the EU or the US, Appendix Table 3 shows the detailed results for scenarios 3 to 5. The broadest scenario (5), which includes ASEAN+3 countries and all the South Asian countries, sees income gains for members of the FTA of about 2.0 per cent of base income for South Asia and 2.4 per cent for ASEAN+3 countries. In terms of changes in base income, there are substantial income gains for India and other South Asian countries. Pakistan, however, experiences smaller income gains (0.2 per cent). These results relate

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to a mix of improved market access, opening up of markets and improvements in logistics and trade costs. There are minimal negative effects for outsiders to the broad ASEAN+3 and South Asia FTA. The EU sees a small gain while the US and the rest of the world, small losses.

Comparing scenarios 3 (an ASEAN–India FTA) and 4 (an ASEAN+3 and India FTA), a consistent pattern is visible of notable gains for regional participants and minimal effects for outsiders. India’s gains increase significantly from 0.83 per cent of base income to 2.23 per cent between the two scenarios due to including the large North-East Asian neighbours into an FTA arrangement. The other South Asian countries lose by not being included in either arrangement.

Table 5. National Income Effects of SAFTA on South Asia
Value and per cent change compared to 2017 baseline (at constant 2001 dollars)

Country	Value (US\$ Mn)	per cent change
South Asia	3695	0.33
India	1138	0.14
Pakistan	625	0.42
Bangladesh	351	0.31
Sri Lanka	335	1.08
Other South Asia	1246	3.37

Other South Asia refers to Afghanistan, Bhutan, Maldives, and Nepal.

Source: Francois and Wignaraja (2008).

Lastly, we turn to scenario 6, the outcome of an evolving SAFTA process (covering goods, services and trade facilitation) in Table 5. This scenario is pertinent in view of the fact that SAARC has initiated discussions on a services agreement as an expansion of SAFTA.⁹ The welfare gain from a South Asian scenario (covering goods, services and trade facilitation) amounts to about \$3.7 billion (or 0.33 per cent of South Asia’s base income). All members see gains.¹⁰ In

⁹ For alternative views of the potential for South Asian integration see Ahmed and Ghani (eds., 2007) and ADB-UNCTAD (2008).
¹⁰ Our regional-level estimates of the economic effect of a South Asian FTA resemble Siriwardana (2003) who reports gains for South Asia of about \$4 billion. Other studies – which look mostly at goods trade liberalization – suggest gains of less than \$1 billion from a South Asian FTA. Accordingly, Bandara and Yu (2003) suggest gains for South Asia of \$771.4 million and ADB-UNCTAD (2008) \$858.3 million. Reflecting its economic size in South Asia, India sees gains of \$3.1 billion in Siriwardana (2003), \$756.2 million in Bandara and Yu (2003) and \$366 million in ADB-UNCTAD (2008).

terms of base income, the gains are notable for Sri Lanka and the rest of South Asia.

CGE simulation studies are useful in quantifying income effects of eliminating import tariffs on goods trade and liberalizing cross-border trade in services through the formation of an FTA. As they are unable to incorporate rules of origin and non-tariff measures (e.g. technical barriers to trade) which may afford more protection for domestic industries than tariffs, CGE studies are best when combined with analysis of the complex structure of FTAs and industry perceptions of the benefits of FTAs.

Key Issues for Fostering Closer Integration with East Asia

The CGE analysis in the previous section suggests that there are significant potential welfare gains for India and the rest of South Asia from closer economic integration with East Asia and also from South Asian integration. Major impediments exist, however, to realizing these potential gains. Dealing with these issues at regional and country level can further economic integration between the sub-regions.¹¹ The remainder of this section discusses five key issues for policymakers and business: (1) invest in infrastructure and logistics, (2) form comprehensive FTAs with simple rules of origin, (3) implement structural reforms, (4) promote services trade, and (5) build firm-level capabilities and government capacity.

1. Invest in Infrastructure and Logistics

For trade-related infrastructure, the dominant mode for freight transport between South and East Asia remains ocean transport and this situation is expected to continue for the foreseeable future (see Box 1). Land transport, both road and rail, will have an increasing role in bilateral trade within Asia. It may also facilitate trade between non-contiguous countries within South Asia and East Asia but this will require a significant improvement in border-crossing procedures. It is unlikely that land transport will attract a substantial share of trade flows between the two regions within the next decade, despite efforts to develop various links of the Asian Highway and the Inter-Asian Railway. Air transport is growing in importance as the value of

¹¹ For a comprehensive analysis of the challenges in promoting closer South Asia-East Asia integration see Francois, Rana and Wignaraja (eds., forthcoming).

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commodities traded between the two regions increases; however, the growth in air freight has lagged behind that of ocean transport and is expected to continue to do so.

Box 1. Infrastructure and Trade Facilitation in Trade Between South and East Asia

Trade among the countries of East and South Asia benefited from the dramatic improvements in both infrastructure and services over the last three decades. The effectiveness of the sea, land, and air routes in accommodating the expected increase in trade between East and South Asia depends not only on the quality of the infrastructure and transport services provided but also on the constraints introduced at the international borders through which these corridors pass.

Sea Transport. The Southern Ocean Corridor (see Appendix 1.1) has been the principal route for trade between East and South Asia for centuries, and this situation is expected to continue in the foreseeable future. The corridor forms part of the East–West trade route that circumnavigates the globe, connecting the Mediterranean Sea via the Suez Canal to the Persian Gulf, then continuing past South Asia through the Straits of Malacca to East Asia and on across the Pacific. Rapid growth in trade has been accommodated through the introduction of larger container vessels and the expansion and diversification of feeder services. Some bottlenecks, primarily in public ports, have delayed expansion of necessary infrastructure.

Land Transport. The Northern Land Corridor connecting East and South Asia includes the Asian Highway (see Appendix Figure A1.2), a 141,000-km standard roadway crisscrossing thirty-two Asian countries between Pakistan in the west and the PRC in the east, and the Trans-Asian Railway, a network of national rail lines that connects East and South Asia from Pakistan through to the PRC. However, neither the road nor rail routes are fully operational as there are missing links and problems with the conditions of other links. It is currently estimated that an investment of \$18 billion would be required to create new roads and upgrade existing ones totalling 26,000 km of roads to complete the Asian Highway.

Air Transport. Unlike the other corridors, the Central Air Corridor has an unlimited set of potential direct routes between economic centres. The international freight hubs are used to tranship cargoes moving between Europe, the Middle East, South-East Asia, and East Asia. Collection and distribution activities are accomplished through feeder routes between the international hubs and the national gateway major airports and through domestic services connecting to the local airports. Air transport is growing in importance as the value of commodities traded between the two regions increases. However, the growth in airfreight has lagged behind that of ocean transport and is expected to continue to do so.

Logistics and Supply Chain Management. All the countries in South and East Asia have highly competitive transport services. Trucking services are privately operated and there is a large number of carriers. Likewise, there is strong competition in the ocean sector. The volume of traffic, however, is the principal constraint on the number of lines calling at the major ports and the frequency of services. There is a similar situation for air transport, but access to international operators is generally limited by bilateral agreements that restrict flights and limit the use of fifth and sixth freedoms (see note below). The different requirements of time and cost in trading goods are met by using different transport modes. Air freight is the most costly, with a range of \$0.25–0.50 per ton-km, and the fastest requiring 2–4 hours per 1000 km. Road and rail transport have similar characteristics in terms of speed, but road transport is more costly at about \$0.025–0.050 per ton-km. Ocean transport is both the cheapest (\$0.010–0.015) and the slowest.

Trade Facilitation. There are three major initiatives directed at reducing the time and improving the transparency and consistency of cargo clearance procedures at the border: (1) introduction of a harmonized system for cargo classification, (2) implementation of the provisions for trade facilitation as part of accession to the WTO (e.g. customs valuation), and (3) implementation of the customs reforms included in the Revised Kyoto Convention. The countries in South and East Asia are well advanced in adopting these initiatives but still have need to make progress to achieve full implementation.

Taking into account customs, infrastructure, ease of shipment, logistics services, ease of tracking, internal logistics costs, and timeliness, the PRC is perceived as having the best logistics, followed by Thailand. This is despite the fact that Thailand, Bangladesh, and India have the lowest internal logistics costs. The PRC and Thailand are at the top of the list while Bangladesh, Sri Lanka, and Myanmar are at the bottom because of quality of supporting infrastructure, ease of shipment, and problems with meeting schedules.

Note: The fifth freedom refers to the right to carry passengers from one's own country to a second country, and from that country to a third country. The sixth freedom refers to the right to carry passengers or cargo from a second country to a third country by stopping in one's own country.
Source: Arnold (2008).

The changing structure of supply chains used for international trade is expected to have a more profound effect on trade between South Asia and East Asia than any change in transport infrastructure. Improvements in logistics services will decrease transit time and cost while they increase reliability, allowing manufacturers to change their modes of production and retailers their methods of distribution. In this vein, Table 6 provides an indication of notable gaps in logistics efficiency between South Asian and East Asian countries using the World Bank's Logistics Performance Index. Integrated production activities are being replaced with extensive subcontracting of the different stages of production. Subcontractors locate either in a cluster around the primary manufacturer, so as to operate in a manner similar to that of an integrated industry, or they spread out in different locations where the factors of production are most favourable.

Table 6. Logistics Performance Indices of South Asian Countries, 2007

Country	Overall LPI Score	Customs	Infrastructure	International shipments	Logistics competence	Tracking and tracing	Domestic logistics cost	Timeliness
Afghanistan	1.21	1.30	1.10	1.22	1.25	1.00	3.13	1.38
Bhutan	2.16	1.95	1.95	2.06	2.18	2.27	3.36	2.57
Bangladesh	2.47	2.00	2.29	2.46	2.33	2.46	3.08	3.33
India	3.07	2.69	2.90	3.08	3.27	3.03	3.08	3.47
Nepal	2.14	1.83	1.77	2.09	2.08	2.33	3.25	2.75
Pakistan	2.62	2.41	2.37	2.72	2.71	2.57	2.86	2.93
Sri Lanka	2.40	2.25	2.13	2.31	2.45	2.58	3.08	2.69
<i>Memo items:</i>								
Japan	4.02	3.79	4.11	3.77	4.12	4.08	2.02	4.34
Singapore	4.19	3.90	4.27	4.04	4.21	4.25	2.70	4.53
China	3.32	2.99	3.20	3.31	3.40	3.37	2.97	3.68

The Logistics Performance Index (LPI) ranges from 1 (worst) to 5 (best); no data for Maldives.

Source: World Bank

Most cargo between South Asia and East Asia moves by water and air because no land transport services are operational at present. Land transit through Myanmar is currently not possible, but this will eventually change as the volume of South Asia–East Asia trade is expected to increase. Additional corridors between India and the PRC through Bhutan and Nepal will have to be developed. Land access to ports is also important for landlocked countries. In addition, international shipping lines serving the South Asia–East Asia region operate on the equatorial route connecting East Asia and the Persian

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Gulf and Mediterranean. These shipping lines call at the major transshipment hubs of Singapore and Colombo and use feeder vessels to move cargo to other ports in the region. There are some ships that call at secondary hubs such as Malaysia's Port Kelang and India's Nhava Sheva, but these are relatively few. There is a need to develop regional shipping lines so that ships call at various regional ports. Reduction of freight and inland transport costs could increase the level of trade between South Asia and East Asia significantly.

Trade cost reductions can also follow from trade facilitation measures that streamline the administrative cost of clearing goods across borders. Substantially greater cost-reduction benefits may also follow from a simple streamlining of administrative barriers in the region. Countries should thus make efforts to reduce logistic constraints to facilitate movement of goods between East and South Asia. These include delays in customs inspection, cargo handling and transfer, and processing of documents. Customs procedures could be modernized by aligning the customs code to international standards, simplifying and harmonizing procedures, making tariff structures consistent with the international harmonized tariff classification, and adopting the WTO's Customs Valuation Agreement. Improved trade facilitation with greater attention to technical barriers and "behind the border" impediments to trade could contribute to increasing economic openness and thus the capacity to benefit from greater interregional integration. Overall, the region would benefit greatly from a concerted effort to reduce physical and administrative trade costs.

2. Form Comprehensive FTAs with Simple ROOs

The WTO Doha Round is a first-best approach to global liberalization. However, the Doha trade talks are stalled and there is growing consensus that there is little prospect of concluding a comprehensive Doha trade deal in 2008 or early 2009. In the interim, comprehensive region-wide trade agreements can offer a second-best route to liberalization.¹² The previous section offered a case for a broad FTA covering ASEAN+3 and all South Asian countries. Asia should pursue a geographically broad scheme, instead of an expanding

¹² On this point, see ADB (2008) and Kawai and Wignaraja (2008).

web of bilateral and sub-regional agreements. Against a backdrop of slow progress in global trade talks, FTAs can promote continuing liberalization, induce structural reforms in the countries concerned, and widen market access across the region. With a view to making the proliferation of FTAs between South Asia and East Asia “stepping stones” rather than stumbling-blocks to multilateralism and to reduce inefficiencies due to overlapping rules of origin and others, policymakers in the region may wish to adopt the concept of “open regionalism” and broaden FTAs by creating as large and as wide a market as possible. Two further issues seem relevant in view of the growing proliferation of FTAs involving South Asian countries – the scope of South Asia–East Asia FTAs and multiple rules of origin.

The five concluded FTAs between South and East Asian countries vary in scope. Table 7 classifies these and agreements within South Asia according to increasing scope. Two agreements (India–Singapore Comprehensive Economic Cooperation Agreement and the Malaysia–Pakistan Comprehensive Economic Partnership Agreement) stand out for being comprehensive in scope (goods and services) and go beyond the WTO framework to include provisions on a host of issues (trade facilitation, investment, government procurement, competition, intellectual property, labour and so on). The Malaysia–Pakistan agreement is more comprehensive in goods because it covers agriculture and has provisions for transit. However, it lacks provisions on ICT (information and communication technology) and e-commerce, labour or movement of natural persons, and education. The India–Singapore agreement excludes agriculture and transit but has wider coverage of cooperation enhancement provisions. The Asia-Pacific Trade Agreement, China–Pakistan FTA and the PTA–Group of Eight Developing Countries are mainly goods agreements. The conclusion of comprehensive FTAs which cover goods, services and issues beyond the WTO framework can encourage a continuous liberalization process in the region, particularly in the absence of a Doha deal.

Rules of origin (ROOs) are a critical determinant of the trade effects of FTAs. There is increasing concern over potential complications to the business environment as a result of proliferating FTAs whose ROOs are inconsistent with one another. Correspondingly, there have been growing calls to develop a common

approach to ROOs across FTAs in the Asia-Pacific.¹³ The choice between competing approaches to ROOs in important new trade agreements has potentially significant implications for the future trading environment within and between the two regions.

Table 8 provides an analysis of the ROOs in South Asian FTAs and comparisons with those in South Asia–East Asia FTAs. The data indicate that different FTAs have different ROOs and that there may be a risk of increased transactions costs to business arising from the so-called Asian Noodle Bowl effect. At the same time, any proposals for new trade arrangements in South Asia and East Asia should take into account the need to develop sensible and efficient rules (e.g. regional cumulation and co-equality of ROOs) for the conduct of regional trade, where these are needed to supplement or rationalize existing rules, as in the case of rules of origin.

3. Implement Structural Reforms

While there is technically an increasingly complex web of bilateral and sub-regional agreements across Asia, the levels of most favoured nation (MFN) protection and rules and regulations affecting business remain basic elements in the incentive regime facing business. In conjunction with infrastructure- and rules-based costs, the pattern of trade between South and East Asia reflects variations in incentives. Tariff protection has been falling in recent years in South Asia but overall levels are still higher than in East Asia and reductions can stimulate business.

Table 9 shows import tariffs for manufactures along with information on business procedures. The average manufacturing tariff in India, for example, is 15.6 per cent (2005), while for China (following accession to the WTO) it is around 9 per cent. While tariffs seem low in many East Asian countries, there is some room for reduction in protection, especially in non-tariff measures (NTMs). Similar comments apply typically to business procedures. East Asia is typically a more open destination than South Asia in terms of procedures affecting business start-up and exporting, and hence serves as a preferred destination for FDI. It also benefits more from the potential for regional integration of industries.

¹³ See Baldwin (2006).

Table 9. Levels of Openness and Market Orientation of South Asian Countries

Country	Average Applied Import Tariff Rates (Manufactured goods, in per cent)				Documents for Export (number), 2008	Time to start a business (no. of days), 2008
	2000	2002	2004	2006		
Afghanistan	...	...	...	...	12	9
Bhutan	15.5 ₁₉₉₆	16.5	19.1	19.1 ₂₀₀₅	8	48
Bangladesh	21.8	20.5	18.3	15.1	7	74
India	33.7 ₁₉₉₉	31.3 ₂₀₀₁	28.7	15.6 ₂₀₀₅	8	33
Maldives	21.2	21.2	22.3	22.3	8	9
Nepal	13.4	13.8	13.9	12.4	9	31
Pakistan	47.8 ₁₉₉₈	17.3	16.8	14.5	9	24
Sri Lanka	8.2	8.2 ₂₀₀₁	8.9	9.7	8	39
<i>Memo items:</i>						
Japan	3.9	3.7	3.3	3.4	4	23
Singapore	0	0	0	0	4	5
China	16.0	14.9 ₂₀₀₁	9.7	8.9	7	35

Note: The subscript indicates the latest available data prior to the year as shown in column headings; no data for Afghanistan.

Source: UNCTAD Handbook of Statistics and World Bank Doing Business.

Trade liberalization efforts need to be embedded in a wider programme of economic reforms. These efforts may include monetary, fiscal, and labour market policies; competition; deregulation; and other requisite structural reforms. South Asian countries exhibit a relatively narrow range of comparative advantages compared to the economies of East Asia. They also face formidable competition from East Asia in all of the products in which they have comparative advantage. There is evidence that they are lagging in manufacturing competitiveness with their East Asian competitors.¹⁴

Increases in South Asian exports to East Asia have tended to be concentrated in the natural resources sectors rather than in manufacturing. In parallel to trade liberalization, the South Asian economies should therefore take steps to boost the international competitiveness of the industries in which they have comparative advantages. This would require efforts to attract FDI; promote the development of small and medium-sized enterprises (SMEs); improve metrology standards and quality management; and increase spending on research and development.¹⁵ South Asian countries and several

¹⁴ A recent ranking of manufacturing competitiveness performance in 80 developing and transition economies reported that seven East Asian countries were in the top 10. Meanwhile, Sri Lanka was 28th, India 37th, Nepal 42nd, Bangladesh 44th, and Pakistan 49th. See Wignaraja and Taylor (2003).

¹⁵ For more on this point see Wignaraja (2003 and 2008).

East Asian countries also need to make progress in implementing the so-called second-generation reforms to enhance transparency, good governance, and the quality of fiscal adjustment. These include reforms to the civil service and delivery of public goods; creation of an environment conducive to private sector opportunities; and reforms to institutions that create human capital, such as health and education. Comparative data from South and East Asian economies suggest that increasing education and skill levels should be a particular priority in South Asia.

4. Promote Services Trade

Growth in all economies in South Asia and East Asia has been associated with an expanding service sector. Not only has the sector been growing in absolute size but its share in output has also generally been rising with economic development. To varying degrees, these economies have been able to be rising with economic development. To varying degrees, these economies have been able to internationalize their services sector at the same time. They have reformed their domestic policies to facilitate services imports in various modes. They have found success in exports as well, but the extent to which this has occurred varies between countries and over time. Services exports from members of ASEAN that had been growing rapidly in the 1990s were severely affected by the financial crisis. The PRC's services exports have grown steadily, including since accession to the WTO. South Asian exports of services have also grown steadily but have been dominated by India.¹⁶ Selected services exports are growing between the regions.

Exports of information technology (IT) services from India to the PRC and Korea together represent a mere 0.13 per cent of total IT exports during 2004/5 and there is enormous potential for expansion. In total, East Asia and South Asia accounted for around 5.9 per cent and 0.9 per cent of total IT exports from India during 2000/1. However, top Indian IT firms are currently attempting to diversify their markets using various strategies, such as setting up offices in the PRC to serve the local market and to attract Japanese outsourcing business by employing workers from the PRC and Japan to overcome the language barriers.

¹⁶ See Findlay, Ochiai, and Dee (forthcoming).

Contractual construction and labour service are the PRC's major service sectors, especially in Asia. In Asia, approximately 69 per cent of construction exports (through 2004) have been to East Asia, with the remaining 31 per cent destined for South Asia. In South Asia, Pakistan is one of the most important markets for contractual construction service exports from the PRC. The PRC also has some history of construction and labour exports to Sri Lanka and Bangladesh.

Meanwhile, data show the significance of remittances, especially for small developing countries such as Nepal and Bangladesh. South Asian and ASEAN countries tend to be exporters of labour services, but it is of interest that payments of remittances from these economies are also growing rapidly.

There are certainly complementarities between the regions, as these examples and as the divergences in comparative advantage suggest. However, there is evidence of important impediments to trade and investment inhibiting integration between the regions. Although data sets are incomplete, reviews of country policy show significant impediments and other regulatory barriers affecting operations in many sectors.

Deregulation and policy reform in the service sectors should be pursued in a gradual manner. This has the potential to boost productivity and exports. India provides an example for other South Asian countries. The policy reforms initiated in the services sector since the early 1990s have been wide ranging and phased in with significant variations in progress across different sub-sectors. The telecommunications sector has been at the forefront of the process in terms of opening up activities to domestic private and foreign investment, privatizing government providers, establishing and strengthening an independent regulator, and changing associated legislation. Private-sector entry was also permitted in power generation, civil aviation, and oil and gas exploration during the early 1990s. Private-sector entry into insurance was permitted at the end of the 1990s and an independent regulator gained status in 2000. The government is currently contemplating setting up regulatory authorities for petroleum, civil aviation, and railways. The turnaround in railways'

performance and recent policy initiatives—such as the permission accorded to private operators to run container traffic and the inauguration of a separate freight corridor between Mumbai and Delhi—have been acknowledged as unprecedented and valuable measures in relaxing infrastructure constraints on India’s growth and development. In particular, domestic deregulation and liberalization in general and telecommunications reforms were keys to the observed growth in services, especially IT and IT-enabled services (ITeS) during the 1990s. International trade and investment reforms also appear to have contributed to growth in services. This can be surmised from the observed increase in service sector exports and FDI inflows in the telecommunications and IT sectors.

Conclusions

Nearly two decades have passed since India adopted a Look East Policy in an attempt to forge closer economic ties with the economically advanced East Asia. This policy had far-reaching implications for India’s destination of trade as well as spill-over effects on the integration of the rest of South Asia. This paper examined the economic effects for South Asia, particularly India, from closer economic integration with East Asia. It considered the impact on trade patterns, welfare gains from alternative FTA scenarios and key issues for developing closer integration with East Asia.

Four broad points emerge from the research. First, South Asia–East Asia trade links are growing rapidly from a small base driven by India–East Asia trade. Second, a careful consideration of different FTA scenarios using CGE analysis indicates that India gains the most from an FTA arrangement that involves East Asia as well as the rest of South Asia. Third, several key issues – including infrastructure and logistics, proliferating shallow FTAs with the risk of Asian noodle bowl effects, gaps in structural reforms, barriers to services trade and weaknesses in firm-level and government capabilities – impede the development of closer economic integration between South Asia and East Asia. Fourth, remedies at the regional and national levels are required to deal with these issues. The following implications are suggested: invest in trade-related infrastructure and streamline cross-border procedures; continue lowering trade and non-tariff barriers; implement a wider programme of structural reforms; develop a broad

FTA covering ASEAN+3 and South Asia which is comprehensive in scope and contains simplified rules of origin; promote services trade by reducing barriers; increase support for technological development and build government trade policy capacity.

It is increasingly recognized that the process of “regionalism is too complex and sui generis to generate universal operational rules.”¹⁷ Nonetheless, rules of thumb or lessons of experience can be drawn from Asia’s experience that might be relevant to the development of a coherent pan-Asian regional integration strategy in most circumstances.

Four lessons can be distinguished, as follows.

1. *Integrate with a large neighbouring economy.* Not all partners are equal. Integration into dynamic production networks of a large open neighbouring economy can bring numerous externalities to a given economy and its enterprises.
2. *Emphasize market orientation in regional strategy.* Emphasis on markets for resource allocation and promotion of greater competition on domestic markets encourages efficiency. Where market imperfections arise, however, intervention may be required.
3. *Tailor policy mix to national circumstances.* There is no one-size-fits-all strategy. Key ingredients of regional strategy—investment in infrastructure, improvement of logistics, open trade and investment policies, measures to improve export competitiveness, and public–private sector partnerships—need to be modified and sequenced to suit individual country needs and priorities.
4. *Involve the private sector in developing regional strategy.* The behaviour of foreign and domestic firms influences the formation and deepening of regional production networks in different industries. Accordingly, close involvement of the private sector in discussions of regional strategy and FTA negotiations is critical.

¹⁷ Schiff and Winters (2003): 25.

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Appendices

Table 1. Country Profiles, 2007

Country	Real GDP per capita (US\$, 2000 prices)	Population (million)	Openness (per cent of GDP)	Manufacturing value added (per cent of GDP)	Poverty Headcount Ratio (PPP, at \$1/day)
Afghanistan	...	...	76.8 ₂₀₀₅	14.9 ₂₀₀₅	...
Bhutan	1276.9	0.7	108.9	5.1	...
Bangladesh	439.4	158.6	50.8	17.9	49.8 ₂₀₀₀
India	685.6	1123.3	45.8	16.4	28.6 ₂₀₀₀
Maldives	3668.1	0.3	172.7 ₂₀₀₄	...	...
Nepal	242.5	28.1	41.0	7.7	30.9 ₂₀₀₄
Pakistan	660.5	162.4	36.2	19.5	...
Sri Lanka	1143.6	19.9	68.8	18.5	22.7 ₂₀₀₂

Data shown are dated 2007 unless stated by subscript; openness is defined as exports and imports of goods and services as per cent of GDP (in current US\$).

Source: World Bank World Development Indicators.

Table 2: List of FTAs Between South and East Asia

FTAs	Coverage
<i>Under Implementation</i>	
Asia-Pacific Trade Agreement (1976)	goods only
India-Singapore Comprehensive Economic Cooperation Agreement (2005)	WTO-plus
Malaysia-Pakistan Closer Economic Partnership Agreement (2005)	WTO-plus
People's Republic of China-Pakistan Free Trade Agreement (2007)	goods and investment
<i>Signed</i>	
Preferential Tariff Arrangement-Group of Eight Developing Countries (2006)	goods only
<i>Under Negotiation</i>	
ASEAN-India Regional Trade and Investment Area (2004)	n.a.
Bangladesh, India, Myanmar, Sri Lanka, Thailand Economic Cooperation (BIMSTEC) Free Trade Area (2004)	n.a.
India-Thailand Free Trade Area (2004)	n.a.
Pakistan-Indonesia Free Trade Agreement (2005)	n.a.
Pakistan-Singapore Free Trade Agreement (2005)	n.a.
India-Korea Comprehensive Economic Partnership Agreement (2006)	n.a.
Japan-India Economic Partnership Agreement (2007)	n.a.
<i>Proposed</i>	
Comprehensive Economic Partnership Agreement between Singapore and Sri Lanka (2003)	n.a.
People's Republic of China-India Regional Trading Arrangement (2003)	n.a.
Pakistan-Philippines Free Trade Agreement (2004)	n.a.
Pakistan-Thailand Free Trade Agreement (2004)	n.a.
East Asia Summit Free Trade Area (ASEAN+6) (2005)	n.a.
India-Indonesia Comprehensive Economic Cooperation Arrangement (2005)	n.a.
Malaysia-India Comprehensive Economic Cooperation Agreement (2005)	n.a.
Pakistan-Brunei Darussalam Free Trade Agreement (2007)	n.a.

Source: ADB ARIC FTA database (data as of October 2008).


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Table 3: National Income Effects of Alternative Scenarios

Value and per cent change compared to 2017 baseline (at constant 2001 dollars)

Country/Region	ASEAN–India FTA		ASEAN+3 and India FTA		ASEAN+3 and South Asia FTA	
	Value (US\$ Mn)	per cent change	Value (US\$ Mn)	per cent change	Value (US\$ Mn)	per cent change
South Asia	6466	0.57	16,199	1.44	22,423	1.99
India	6630	0.83	17,779	2.23	18,240	2.29
Pakistan	–46	–0.03	–862	–0.58	298	0.20
Bangladesh	–31	–0.03	–355	–0.31	1,874	1.66
Sri Lanka	–11	–0.04	–123	–0.40	631	2.03
Other South Asia	–75	–0.20	–240	–0.65	1,380	3.73
ASEAN+3	5264	0.05	240,810	2.38	243,296	2.40
China	–882	–0.03	43,289	1.32	43,454	1.32
Japan	–664	–0.01	78,080	1.61	78,650	1.62
Korea	–396	–0.05	51,545	6.46	52,100	6.53
Cambodia	1	0.01	106	1.18	79	0.88
Indonesia	1384	0.46	8,818	2.93	9,090	3.02
Malaysia	1925	1.03	12,014	6.40	12,376	6.60
Philippines	392	0.33	3,521	2.93	3,495	2.91
Singapore	1644	0.99	9,285	5.60	9,717	5.86
Thailand	1879	0.85	28,220	12.78	28,534	12.92
Vietnam	194	0.27	5,449	7.57	5,428	7.54
Other South-East Asia	–214	–0.19	483	0.43	374	0.33
EU	1130	0.01	9,248	0.08	10,300	0.09
US	1036	0.01	–3,214	–0.02	–1,924	–0.01
Rest of the World	1008	0.01	–11,681	–0.13	–13,188	–0.14
World	14,904	0.03	251,363	0.52	260,907	0.54

Other South Asia refers to Afghanistan, Bhutan, Maldives, and Nepal. ASEAN+ 3 refers to the ten ASEAN members plus Japan, PRC, and Korea. Other South-East Asia refers to Brunei Darussalam, Lao PDR, and Myanmar.
Source: Estimates based on CGE model in Francois and Wignaraja (2008).



Regional Cooperation in South Asia: 15th SAARC Summit and Emerging Issues

Saman Kelegama

The theme of the 15th SAARC Summit that was held in Colombo in early August 2008 was “Partnership for Growth for our People”. This was basically a follow-up of the theme of the 14th Summit, “Towards Greater Connectivity”. The Colombo declaration made reference to environment, water resources, poverty alleviation, transport, ICT (information and communication technology), science and technology, culture, SAARC Social Charter, women and children, education, combating terrorism, among others. SAARC declarations usually feature a gamut of issues but only a handful of them constitute the main agenda of the SAARC annual activities. From an economic integration point of view, five issues are noteworthy, viz., (i) desire to strengthen SAFTA and trade facilitation, (ii) initiative to incorporate trade in services into SAFTA, (iii) initiatives for promoting regional tourism, (iv) renewed emphasis on cooperation in energy, and (v) defining the role of the Observers. Each of them needs to be looked at in detail to shed some light on the current challenges before SAARC.

The declaration made reference to SAFTA and trade facilitation. In regard to SAFTA, it was stated that the “sensitive list” should be revised, and non-tariff barriers (NTB) and para-tariffs should be removed expeditiously to enhance trade. In the context of trade facilitation, the signing of the agreement on the establishment of a South Asian Regional Standards Organization was a positive step. However, what is relevant here is reducing the “sensitive list” and NTB removal within a specific timeframe and this was not mentioned in the declaration. Neither were specific measures on trade facilitation mentioned. A few areas in trade facilitation should have been identified – where cooperation is easy and where benefits are large and tangible in the short to medium term – and make them binding commitments.

Time and again lip-service has been paid in SAARC declarations for NTB removal without any genuine commitment. The same applies

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to trade facilitation. Most often trade facilitation measures can be more effective than preferential tariffs in moving trade. Trade facilitation will also reduce the high levels of informal trade taking place in the region and encourage trade via legal routes. It is in this context that trade facilitation measures need more serious attention, in particular the ones related to simplifying procedures at ports and customs.

The declaration welcomed the RIS Study on Trade in Services in the region and requested the member states to commence negotiations on the Framework Agreement on Trade in Services. It may be noted that the barriers to intra-regional trade are more restrictive in services than in goods, resulting in missed opportunities for mutually beneficial trade. Previous studies have shown that there are more complementarities in services than in goods in the SAARC region. The RIS study shows that trade in services within the region is more balanced, with smaller and less developed economies generally enjoying a surplus with the larger economies, thus helping to bridge the asymmetries that exist in trade in goods in the region. Thus, it is all the more important that the Framework Agreement is made available for ratification at the 16th SAARC Summit in Male so that liberalization in services could commence thereafter. Some argue that SAFTA should be fully operational with duty-free movement of goods before services come in for liberalization, but this argument is misplaced because services liberalization (and trade facilitation) support trade in goods and, in fact, will strengthen SAFTA to deliver a larger output.



The declaration emphasized promoting regional tourism and agreed to implement a comprehensive action plan which includes “facilitating the movement of people through improved travel infrastructure and air, sea, and land connectivity among the SAARC countries ... and promotion of SAARC as a common destination through public-private partnerships and joint campaigns”. In this regard, what is most relevant is improving air connectivity by further liberalization of airspace, and reducing visa issuance procedures. In regard to the former, member countries should offer fifth freedom right to a few designated airlines in the region. India has so far offered fifth freedom right to designated airlines from South Asia on a reciprocal basis. However, to make use of this offer the other member countries should offer the same to

improve air connectivity. Sri Lanka and Maldives have a visa-at-arrival policy and Nepal too has a liberal policy for issuance of visas but not the other member states. This area also needs reform to facilitate movement of people.

The time is ripe for SAARC to consider the ASEAN Air Pass systems where travelling to one ASEAN country qualifies the traveller to visit the other ASEAN countries at a concessionary air fare and the ASEAN Hotel Pass (Hip-Hop Pass) with a similar incentive. Twinning of cities programme in the SAARC region, publication of an Annual South Asian Tourism Events Directory, promoting tour circuits such as the Ramayana Trail, Buddhist circuit, etc., under private-public partnership should be initiated to promote intra-regional tourist flows.

The declaration placed renewed emphasis on cooperation in energy and also to engage in energy trade. It stressed "... the urgent need to develop the regional hydro potential, grid connectivity and gas pipelines ... possibility of evolving an appropriate regional inter-governmental framework may be explored to facilitate such endeavour". It may be noted that there are complementary energy resource endowments in the region: Bangladesh and Pakistan – natural gas; Nepal and Bhutan – hydropower; India – coal and petroleum products. This provides a basis for regional energy cooperation. Energy trade is already taking place between Bhutan and India. Negotiations are underway for the construction of an undersea cable to connect the national grids of Sri Lanka and India. In the current setting, the suggested intergovernmental framework should be discussed at the Third Meeting of SAARC Energy Ministers in Colombo during early 2009 and explore ways and means of improving energy connectivity in the region.

The guidelines for the seven Observers (China, Japan, South Korea, Iran, Mauritius, USA and EU) for cooperation were approved at the Colombo Summit. In accordance with the SAARC Charter, the Observers can now contribute for cooperation and development in the region. For instance, some Observers could contribute to the SAARC Development Fund (SDF) that was signed during the Summit. The SDF Secretariat will be located in Bhutan and contributions from Observer states to mutually acceptable projects



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will be welcome. Already projects under the Social Window of the SDF – Women’s Empowerment, Maternal and Child Health – are being launched from the available funds, including the generous contribution from the Government of India.

The Colombo declaration stated that the SAARC region should forge greater cooperation with the international community to ensure food availability and nutrition security in the region. In this case too, the Observers can coordinate closely with SAARC member states at multilateral fora to fulfil SAARC objectives.

While declarations are good on paper in implementation SAARC’s track record is far from satisfactory. The declaration stated that it is essential to “ensure effective implementation of all SAARC programmes and mechanisms by rationalization and performance evaluation on a regular basis”. If this is to become a reality then the current SAARC Chair, Sri Lanka, has to take the lead and be proactive in driving the contemporary SAARC issues with the support of the SAARC Secretariat. It is most likely that the others will then follow and give implementation a chance. This will give the much-needed fresh face to the SAARC process and generate a new spirit for South Asian cooperation.



India and Regional Peace and Cooperation

S. D. Muni

The scope of the subject given to me is fairly wide, covering both cooperation and regional security. Both these concepts are mutually reinforcing in the South Asian context. From India's perspective, regional security and cooperation have to be pursued simultaneously and seriously not only because they are good for the region as a whole but because, above all, they are in India's own vital interest. India cannot have peace and security if the region around it is caught in conflict. There is an inevitable spill-over into India of conflict in any of India's neighbouring countries and conflict in the region is detrimental to mutual cooperation either through the South Asian Association of Regional Cooperation (SAARC) or even at the bilateral level. India's stable and cooperative relations with its neighbours are also a precondition for seeking its own legitimate and aspired role in the comity of nations. A country of India's size and capabilities is expected to carry its neighbours along in harmonious relations, failing which it will be seen as incapable of undertaking global responsibilities in keeping with its status.

Therefore, it is not philanthropy or generosity if India contributes, nay dedicates itself, to building regional peace and stability. This realization is dawning gradually on India after years of policy confusion and debate. There was no dearth of policymakers and executioners in India who thought that India was too big, its interests were too diversified and widespread and its stakes were too high in the world as a whole to bother about immediate and smaller neighbours. India joined SAARC reluctantly as its policymakers felt that this regional grouping could not be an adequate and effective instrument to carry India's interests and aspirations forward. The neighbours were seen as difficult entities, interested in undermining India's interests and too small and weak to provide any economic or other incentives to India. They were a strategic liability because their security affected India's security and they were capable and willing, either on their own or at the instigation of interested outside powers, to hurt and harm India. This understanding is now changing; and changing fast and for good.

For nearly a decade now, the realization has grown in India that it has to carry its neighbours along. A serious beginning was made in this respect by the “Gujral Doctrine” in 1997 when Prime Minister I.K. Gujral promised that India was not looking for reciprocity from the neighbours and was prepared to go more than half the distance to meet their legitimate sensitivities and interests. Politically motivated critics disapproved of the “Doctrine” and dubbed it as a proposition to sacrifice India’s national interests. But the thrust of the “Doctrine” has lasted longer than the strength of its critics. The successive governments of Atal Behari Vajpayee and Manmohan Singh have followed its direction though not often enough giving due recognition and acknowledgement to this “Doctrine”. The underlying assumption of the “Doctrine” was that while India tried to accommodate the neighbours, the neighbours in turn would have to carry India along if they wanted to make sense of their own national interests. India’s neighbours have always put the blame of regional discord and lack of cooperation on India, expecting it to do more than what it can possibly do in this respect. It needs two to tango.

There is no doubt, however, that India can and must do more than its neighbours in promoting the cause of security and cooperation in the region. India is both capable and obliged to do so in view of its location and resources in the region. One can identify five areas where India can take the initiative and offer as much support as possible. First, in building regional confidence; second, in creating and consolidating mutual economic stakes; third, in strengthening democratic and liberal political forces; fourth, in facilitating the evolution of a regional security architecture; and fifth, in preserving strategic identity and integrity of the region. India has already taken the initiative in some of these areas. The need is to strengthen it and keep up the momentum against all possible odds.

Building Confidence

The power divide in South Asia between India and its neighbours has been the most important contributing factor to the lack of mutual confidence in the region. India has been perceived as a bully and a “big brother” by its smaller neighbours. Many factors contributed to building up this perception. Broadly, even all the neighbours put

together cannot match India's geographic area, power and resources. This itself makes them feel inferior. For the best part of the past six decades, while India has remained a democratic polity, the neighbours have been experimenting with a variety of quasi-democratic and authoritarian systems and have felt insecure because India, both at the governmental and popular levels has been a source of inspiration and support to the democratic forces fighting against these undemocratic regimes. The unique bilateral discord between India and Pakistan, that precipitated four wars between them, has made the single most contribution in keeping South Asia's atmosphere and image conflict prone. Extra-regional powers have exploited the India–Pakistan conflict as also the tensions between India and its other neighbours to suit their respective strategic and economic interests. The Cold War had a mutually reinforcing relationship with the regional conflicts in South Asia. One wonders if India–Pakistan relations would have been different in the absence of a Cold War. The Sino–Indian conflict dented India's regional image seriously and encouraged its smaller neighbours to play with India's sensitive security interests at the cost of regional cohesion and harmony. Last but not least, India's own diplomatic style and approach towards its neighbours, which was acutely reciprocal in style and petty in calculation of long-term interests, driven as it was by its own sense of insecurity and constraint, alienated the neighbours. This regional hiatus between India, the proverbial “bully”, and the smaller countries, is gradually fading out. Many would suggest that the regional situation has not changed, but in reality it has changed radically and we must take note of it.

The external environment is also changing. The Cold War has ended. There is a turnaround in Indo–US relations and there is a growing understanding between China and India. Above all, there is a peace process in place between India and Pakistan, which has been stalled following the Mumbai terror attack; but it is hoped that with Pakistan's cooperation in bringing the Mumbai attackers to book and with the renewed efforts by the Obama administration in the US to promote India–Pakistan confidence building, it will get back on the rails.

The significant rise in India's self-confidence has been reflected in its approach towards regional cooperation. Several statements have

been made by the Indian Prime Ministers, Foreign Ministers, Foreign Secretaries and other officials during the last decade offering India as an opportunity to the neighbours. They have been saying that the whole world is engaging with India constructively and the neighbours should take note of it and join in.

Regional cooperation can take off only if every single country in the region realizes that it can grow by contributing to the growth of the others. Also, as the largest country, India has to play a larger role than the neighbours expect of it. India needs to work on its behaviour. It must address unresolved and irksome issues. India has changed its treaty with Bhutan and has also agreed to do so in relation to Nepal to meet Nepal's longstanding demand: the process of renegotiation is already on with Nepal. The substantive issue concerning water sharing with neighbours—of Kosi, Chenab, Ganga, and Brahmaputra—also needs to be resolved. Resolving this issue can go a long way in building mutual trust and prosperity between India and Pakistan and can also contribute significantly to the development and prosperity of Jammu and Kashmir.

Regarding border issues and cross-border movement of both people and goods, there are lessons to be learnt from what China has done vis-à-vis its neighbours. Through massive investments in the border areas of the neighbouring countries, China has created strong friendly constituencies in all these areas and has also contributed to their economic development. India's federal dynamics involving relations between the Centre and the states bordering India's neighbours impinge heavily on border-related issues. The question of illegal migration from Bangladesh and the flow of Indian insurgents into sanctuaries in its north-eastern neighbours—Bangladesh, Myanmar and Bhutan—needs to be discussed bilaterally and without linking it to any other issue. The first precondition is that this issue should in no event be politicized by the national and regional political parties.

India's policy towards its neighbours is not fully evolved and defined in its foreign policymaking establishments, i.e. the Ministry of External Affairs and the Prime Minister's Office. Other Ministries and Departments—Commerce, Finance, Water Resources, Home, Oil and Petroleum Ministry, etc.—are yet to tune themselves to this

strategic thinking that constructive engagement with neighbours is in India's interest. This strategic thinking needs to percolate down in these different establishments to the levels of not just ministers and secretaries but joint secretaries.

If this happens, it will expedite the sweeping change in India's approach towards the neighbours. It will facilitate and enhance the scope for improving economic and commercial ties with the neighbours. There is a clear need to leverage culture and heritage also in building confidence at the popular levels. Bollywood has proved a great binding factor between India and the people of Asia even without much official patronage so far. A conscious effort to use Bollywood in policy can strengthen this bonding. India can make use of its educational and health facilities and also tourism to give greater access to the neighbours and encourage civil society engagement, which is already taking place but with much less support from the powers that be in the whole region. India has developed a very useful mechanism to enhance cultural engagement with the neighbours in the form of bilateral foundations, like the Indo-Nepal B.P. Koirala Foundation and the Indo-Sri Lanka Foundation. But this mechanism is inadequately and ineptly used because the Ambassadors for the countries concerned have been put in charge of these foundations, resulting in patronage distribution and bureaucratization. Giving these foundations to professionals may attain better effect. Similarly, the newly set up Public Diplomacy Division also needs to be broadened in its conceptualization and execution by involving people from outside the Ministry of External Affairs and government.

Liberalizing visa and other regimes and increasing high diplomatic visits would go far in increasing the interaction between the legislators and political leaders. India's political parties have only token relations with their counterparts in the neighbouring countries. Prime Minister Manmohan Singh has often talked about going out of box in India's foreign policy, but not much has been done to go out of box in cultivating the neighbours. There is a need and scope for not only *talking* out of box but *doing* out of box. For instance, instead of inviting new Prime Ministers and Presidents of the neighbouring countries to India, India needs to send its high political leaders to the neighbouring countries as frequently as possible. A colossal political change took place in Nepal in 2006: it was a change brought on by

the people of Nepal. After this change, the Indian government insisted on the Nepali Prime Minister visiting New Delhi. Why could the Indian Prime Minister or Foreign Minister not go to Nepal to register and acclaim the victory of the Nepalese people? This could have been done also in the case of Bangladesh, where at least the Minister for External Affairs paid a visit. So things are changing, but not fast enough as yet. There is enough scope for India to have more frequent visits to the neighbours. Recall the example of Rajiv Gandhi. When President Jayewardene was in New Delhi, he took him along and said, "Look, Bangladesh is suffering from floods, let's go and see what we can do". One may not do anything immediately, but it is a tremendous gesture in building the comfort level of a neighbour.

Strengthening Mutual Economic Stakes

Then comes the issue of economic stakes and interdependence. Such interdependence should be built not only through trade and developmental assistance but also by encouraging and incentivizing investments from India in the neighbouring countries. India's official assistance should focus more on the developmental sector and direct more efforts towards health, education, civil amenities, infrastructure and human resource development and not provide budgetary support for helping deficit financing, which the neighbours currently demand. On the issue of trade, India is moving slowly but surely in the positive direction. Recall the economic context of India's relations with Sri Lanka that radically changed in a positive direction after the conclusion of the Free Trade Agreement in 1998. The conclusion of a Comprehensive Economic Partnership Agreement with Sri Lanka will boost bilateral economic cooperation further. This change was being pushed more by circumstances than as consciously devised policy moves. Under the current government, the thrust on economic foreign policy is changing the situation.

India has, for instance, replaced China as the top exporter to Bangladesh. India has also offered an ad hoc gesture of 8 million pieces of apparel to be imported without duty from Bangladesh; Bangladesh has so far exported only 3 million. In terms of the negative list, out of 101 items which Bangladesh wanted, 50 have already been granted.

So a big shift is taking place on trade and other matters for the less developed countries (LDCs). But most such moves need to be institutionalized rather than being ad hoc.

As regards investment promotion by the private sector, some private investors (Dabur in Nepal and Tata in Bangladesh) have found that the overall atmosphere is not encouraging in India's neighbourhood. Bangladesh raised the question of investment in the last SAARC summit in Colombo. But investment will come only if the host countries create a congenial economic, administrative and political atmosphere for investors. On connectivity, which also has been emphasized by SAARC, a lot can be done.

Now there is also a need to move from bilateral to sub-regional integration arrangements. There is a great deal of emphasis in the Indian policymaking circles that bilaterally India can do this and that and it is being done in bits and pieces. It is, however, more important to move to sub-regional theatres. There are two sub-regions at least, if not three—North East of India, North West of India and the Southern peninsula. There is a lot more identity of interests in these areas.

The North East sub-region was perhaps identified within the SAARC framework, but not enough work has been done even at the bilateral level to bring this sub-region together. Through BIMSTEC or within SAARC, vigorous attempts can be made to encourage economic and connectivity linkages between India, Bangladesh, Bhutan and Myanmar. India, Sri Lanka and Maldives form an ideal grouping in the Southern peninsula. In the North West, India, Pakistan and Afghanistan, with the possibility of Iran brought in, can do wonders in improving both the economic as well as the security situation for the whole region. The Obama administration in the US is focusing attention on the security dimension. It should also explore the possibility of regional cooperation framework through SAARC to straighten security bulges among these countries.

Lastly, how to face the global economic challenges, which were never anticipated but which we are now confronted with. Is there scope for India to make any gesture to Pakistan at this juncture? Many Indians genuinely suspect that such assistance may ultimately

land in the lap of the Taliban. These are political considerations. But let us recall the South East Asian example. In 1997, during the financial crisis, China came out with gestures which most of these countries still cherish. India needs to project its regional leadership and initiative at this time of economic crisis which is affecting everyone adversely. Is it possible for South Asia to get together and evolve a regional mechanism to address some of the unforeseen, unpredictable challenges or emergencies which may arise from time to time?

Democratising South Asia

Coming to the democratic and plural institutions, it is time that the Indian policymakers shed their imperial chessboard kind of politics in the neighbourhood and approach political arrangements with the neighbours in terms of what people in these countries really want. In South Asia democracy is on the move but sectarian and extremist forces are also on the move. The former has to be encouraged, the latter contained. Five out of seven South Asian countries are facing serious internal problems because of the rise of sectarian and extremist forces. They have to be dealt with. For India to deal with them, it would have to be done proactively.

India can engage creatively rather than keep away, without bothering about the allegation of interference in others' affairs. Such creative engagement worked in Nepal and can help the countries overcome internal problems and move in a suitable direction. In the South Asia situation, however, collateral contacts are minimal. For example, the political parties in India would not have much idea of how the political parties in Pakistan, Nepal or Bangladesh are working. They lack institutional links. The existing civil society links have come up on their own and may not last long enough: they need to be encouraged, supported, and strengthened. There are also a diversity of stakeholders around India's policymaking establishment that resist radical moves in promoting democratic and secular forces in the neighbouring countries.

Engaging constructively is best done through best practices rather than through influence. India's own democratic credibility and success of secular practices and plural institutions matter a lot in this regard,

but India itself has been facing challenges in keeping up its democratic credentials. Several senior Indian leaders (for example, Minister of External Affairs Pranab Mukerjee in his interview to the *Hindustan Times* on 1 November 2008) have acknowledged that India's body politic is vitiated by various regional and sectarian forces. The Speaker of Parliament, Dr. Somnath Chatterjee, also held a round table discussion in which the consensus was that parliamentary democracy in India has to be put back on the rails. India has to meet these challenges and come up as an impressive and inspiring example.

South Asian Security Architecture

Looking at the possibility of a South Asian security architecture, does regional security architecture or a framework exist in South Asia in any form? Are there even rudimentary elements from which one can start constructing a security architecture? Is there a corresponding example of a security architecture in any of the sub-regions of Asia, like South East Asia or Central Asia, from which South Asia can learn and borrow? Can the ASEAN Regional Forum (ARF) or the Shanghai Cooperation Organization (SCO) be taken as models of security architecture in Asia?

Any exploration of security architecture must start with a question as to what are the security threats to be addressed. In South Asia, are outright bilateral conflicts ruled out, really? With the Indian and Pakistani forces facing each other on the borders in the tense context of the Mumbai terror attack, and the Sino-Indian border issue still far from resolution in the foreseeable time, bilateral conflicts cannot be completely ruled out in South Asia. However, it may be hoped that with terrorism gripping Pakistan internally much tighter than at any time earlier and both India and China developing stakes in constructive economic engagement with each other, having confidence-building measures in place already, a bilateral armed conflict in the region is not an area of concern in the near future. The question of nuclear stability in South Asia is also a bit elusive. Pakistan wants to catch up with India for a credible deterrence; and India has to reliably bridge its nuclear gap with China. The expected security architecture has to ensure that nuclear imbalance in the region does not lead to a

destabilization move by any of the three nuclear weapon states.

South Asia faces two serious challenges—the overall global insecurity and terrorism. The presence of US and NATO forces in the region to fight the global war on terror has become a necessary evil. It has the potential of affecting South Asian regional relations in positive as well as negative ways. While it is in the interest of the US, as outlined in the Obama administration's AfPak strategy on 27 March 2009, to get Afghanistan, Pakistan and India together in supporting and facilitating the war on terror, any adventurist move to vitiate the Kashmir issue can prove counterproductive. The US record of handling the Kashmir issue has been pathetic. All the US can and should do in this respect is to encourage the two neighbours to sort the issue out by themselves. Undue injection of military assistance to Pakistan that does not correspond with the requirements of fighting terrorists on the ground may also be not in the long-term interest of regional balance and stability.



Secondly, internal turbulence is assuming alarming proportions in some South Asian countries. The rise of terrorism and extremism in Pakistan is seriously threatening the existence of its society and State. Democratic political forces that should join hands and display commitment and resolve to fight the forces of disruption are in disarray on account of their mutual struggle for power. In Nepal, the peace process is fragile and discordant. In Bangladesh the delicate civil-military relations threaten to damage the newly revived democratic order. In Sri Lanka, the government claims to be able to conclude the ethnic war in a matter of weeks, but that may take a heavy toll of civilian casualties. Even after the war is concluded through the victory of the security forces, one is not sure if a viable resolution of the ethnic problem will emerge. The democratic institutions and processes remain fragile.

In South Asia's fight against terrorism, there are clearly two sectors which need to be focused upon—the North-East (i.e. India, Bangladesh, Bhutan, Nepal and Myanmar) and North-West (India, Pakistan and Afghanistan). The problems of the two sub-regions are similar in many ways, except that there is no presence of extra-regional forces in the North East. The fight against terrorism cannot

succeed until the regional and directly affected actors join hands. There are feeble indications that Pakistan and India may be moving closer to each other in this fight. Voices in Pakistan have started advocating India and Pakistan taking a joint view of regional security. The *Daily Times* editorial of 30 October 2008 argued, for example, that Pakistan recognized “India’s legitimate stakes in the stability of Afghanistan”. If that is so, it may be possible for Pakistan and Afghanistan to sit together with India and explore the parameters of a regional approach. One can go back to 1979-80, when Prime Minister Narasimaha Rao visited Pakistan and said that India and Pakistan could think of evolving a regional response to the intervention by the Soviet Union. Neither Pakistan nor the US approved of the idea. Circumstances seem relatively more congenial for that idea to be taken seriously. The US is talking about it and Afghanistan endorses it. Is it possible to expect a change in Pakistan’s position?

SAARC is inherently incapable of substituting for a security architecture in South Asia. In the twenty years since it first adopted the regional convention to fight terrorism, it has not been able to take a single concrete step. One hopes that the rising challenge of terrorism in every South Asian country may be able to instil a sense of seriousness and commitment in this respect. SAARC, when it gets going in a meaningful manner on developmental and social issues, has the potential to provide a human security cover to South Asia. But there again, so far concrete actions and implementation of decisions have fallen far short of the promises made and hopes aroused.

India’s defence capabilities are of course available to the neighbours if they want to use them. Some of them are using these. One wonders if the time is ripe for considering setting up a forum of South Asian Defence Ministers to deliberate upon regional security concerns and areas of mutual cooperation to meet such concerns. Such a forum may meet periodically, and even if it does not take actionable decisions, discussions in a friendly and congenial atmosphere may go a long way in building mutual confidence in the region in security matters. This is happening in many other regions. Such a forum may also be possibly backed up by a Track Two kind of arrangement where wider participation can be encouraged. India’s



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naval capabilities are also available for naval defence of any country which wants to use them in the North-East quadrangle of security. India and Bangladesh may have to think afresh, shed their biases and give a new turn to their bilateral relationship.

As India appears willing and capable of undertaking its regional obligations seriously, it is high time for India's neighbours to come forward and energize the framework of regional cooperation. There is a need for them to perceive what kind of relationship they want to have with India which is huge, resourceful, growing and becoming increasingly self-confident. One can find several faults in Indian diplomacy, such as that it has not been sensitive to the needs of the neighbours in the past. But this is changing and Indian diplomacy is promising to be more accommodative of the neighbours' legitimate concerns. At the same time, India's neighbours need to learn to be able to appreciate the complexities of the problems India has had to face. At times, they have taken steps consciously and launched initiatives to vitiate India's security and stability. A change of perspective on both sides of the diplomatic equation would lay the foundation of a new partnership at the regional level.
