

India and South Asian Regionalism: A Study into India's Behaviour towards Elimination of Trade Barriers in South Asia

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Abstract

The study focuses on India's role in economic cooperation in South Asia. It explores: what role India has played in conclusion of different trading arrangements in the region; and how far India has dispelled the economic concerns of smaller regional countries (SRCs). India played leading role in conclusion of SAPTA and SAFTA as well as bilateral trade arrangements with Bhutan, Bangladesh, Maldives, Nepal and Sri Lanka. The agreements with Nepal and Sri Lanka encountered difficulties after showing initial successes. SRCs including Bangladesh and Pakistan face obstacles in enhancing their exports to India. New Delhi has so far not taken enough measures to address the concerns of the SRCs. The prevailing tariffs, non-tariff and para-tariff barriers impede access to Indian market for regional products. The resultant widening trade imbalances strain relations between India and SRCs and also impede the development of overall regional cooperation process in South Asia.

Key Words: Agreement, Barriers, India, Liberalization, Pakistan, Regional, South Asia, Trade.

Introduction

Trade liberalization has been a controversial discourse in South Asia. Scholars, economic experts and leaders of South Asian states have generally remained divided on the issue. The academia, business community and ruling elites of the smaller regional countries (SRCs), except Sri Lanka, have mostly opposed the idea of trade liberalization whereas others, mostly from India, have been its strong advocates. One

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reason for these contrary views is the Indian economy's size which while it frightens the SRCs with New Delhi's economic domination gives India the confidence to stress for market integration in South Asia.

New Delhi proposed trade liberalization under the framework of South Asian Association for Regional Cooperation (SAARC) when its own market was closed to foreign goods. India suggested it as early as 1981 in the first preparatory meeting of the foreign secretaries of South Asian countries, held in Colombo.¹ But the idea could not get the support of other states.

The SRCs opposed trade liberalization on account of their continuing bilateral disputes with an economy as large as India's which they fear for its domination under the huge trade imbalances and India's practice of giving subsidies to its business class. Moreover, they have also found it hard to get access for their products to Indian market due to the prevailing tariffs, non-tariff barriers (NTBs) and para-tariff barriers (PTBs) as well as New Delhi's past policies of import substitution industrialization (ISI) and self-reliance.² Nevertheless, South Asian states have concluded a number of bilateral free trade agreements (FTAs) and regional trade arrangements (RTAs) since the 1990s. India's role in the conclusion of these agreements and in dispelling economic fears and concerns of the SRCs is worth exploring which this paper undertakes to find the state and prospects of market integration in South Asia.

The paper is divided into four sections. The first section provides a brief overview of the regional trade profile of South Asian states. The second section describes the trade liberalization process with particular reference to India's role in taking initiatives to conclude regional, sub-regional and bilateral trade arrangements. The third section discusses the economic concerns of the SRCs in respect of the prevailing barriers their exports encounter in the Indian market and New Delhi's response to them. It also touches upon some of New Delhi's policies and decisions that undermine the growth of SRCs' exports to India as well as the trade liberalization process in South Asia. The fourth section concludes the paper.

¹ SAARC Secretariat, *From SARC to SAARC: Milestones in the Evolution of Regional Cooperation in South Asia (1980–88)*, vol. I, (Katmandu, SAARC Secretariat, 1988), 1.

² Walter Andersen, "India in 1995: Year of the Long Campaign," *Asian Survey*, 36: 2 (Feb., 1996), 176; Nasir A. Naqash, *SAARC: Challenges and Opportunities*, (New Delhi: Ashish Publishing House, 1994), 107–8.

Regional Trade Profile of South Asian States

The share of South Asian regional trade in global trade was about 18 per cent in 1948.³ Later on, it shrank to and remained at around 4 per cent. No significant changes have been observed in this trade pattern even after the creation of the South Asian Association of Regional Countries (SAARC). When it was launched in 1985, regional trade had a very small share in total world trade, i.e. just 5 per cent which shrank to 2.42 per cent in 1990. However from that low it resurged to its peak 6 per cent in 2004⁴ declining to 4 per cent by 2010. This decline, however, is more a consequence of increased trade of South Asian states with the rest of the world than the result of any decrease in trade among regional countries.⁵

The share of regional trade in total trade of SAARC members varied significantly. For instance, it stood at 50 per cent in case of Nepal and 17 per cent each in case of Maldives and Sri Lanka. In respect of Bangladesh, Pakistan and India this figure remained 11, 6, and 3 per cent, respectively. Nepal relies heavily on India for its foreign trade – 35 per cent of its imports come from and 44 per cent of its exports go to India. There is also a large volume of unofficial or illegal trade among SAARC states – 30 per cent of Indo–Sri Lankan trade, 103 per cent of Indo–Nepal trade, and 138 per cent of Indo–Bangladesh trade is informal⁶ which shows the vast potential regional trade has in South Asia. The SAARC Chamber of Commerce and Industries (SCCI) in its 2011 session in Sri Lanka noted that

³ Sadiq Ahmed and Ejaz Ghani, "Making Regional Cooperation Work for South Asia's Poor," in Sadiq Ahmed, Saman Kelegama, and Ejaz Ghani, eds. *Promoting Economic Cooperation in South Asia: Beyond SAFTA*, (Washington, DC: The World Bank, 2010), 54.

⁴ Imtiaz H. Bokhari, "South Asian Regional Cooperation: Progress, Problems, Potential, and Prospects," *Asian Survey*, 25: 4, SARC: Four Views and a Comparative Perspective. (Apr., 1985), 386; Sujata Jhamb, "India's Regional Trading Arrangements," *South Asian Journal*, 11 (Jan. – Mar., 2006), 43.

⁵ Barkat – e Khuda & Selim Raihan, "Implementation of SAFTA: Bottlenecks," in Mushir Anwar, ed. *Towards an Asian Century: Future of Economic Cooperation in SAARC Countries*, 192–208, (Islamabad: Islamabad Policy Research Institute, 2013), 194.

⁶ Mohammad A. Razaque, "Weaker Economies in SAFTA: Issues and Concerns," in Ahmed, Kelegama, and Ghani, eds. *Promoting Economic Cooperation*, 380; Upreti, B.C, "India-Nepal Relations: Dynamics, Issues and Problems," *South Asian Survey*, 10: 2 (2003), 270.

there was an annual regional trade potential of US\$ 65 billion in South Asia which could not be realized mainly due to lack of interconnectivity.⁷

There are several economic factors that have impeded growth of regional trade in South Asia. SAARC members do not have complementary economies, they are rather competitive. Only India's economy is diverse because of its size. The exports of SRCs are "highly concentrated" mainly comprising primary goods and labour-intensive products. Textiles constitute the major part of their exports while they mainly import capital-intensive goods and petroleum products. Regional states pursued policies of self-sufficiency and import substitution industrialization (ISI) till late 1980s to develop local industries which resulted in inefficiency, corruption, rent seeking and growth of illegal trade among regional states.⁸ Trade barriers also paved the way for illegal trade in South Asia. There are different estimates of prevailing illegal trade in the region, more specifically between India and the SRCs. In 2004, it was estimated to be US\$ 3 billion as compared to formal trade worth US\$ 1641 million.⁹ As reported, the volume of official and non-official trade between India and Bangladesh was approximately the same, while informal trade equaled about one-third of formal trade between India and Sri Lanka, and it was more than ten times of the estimated US\$2 billion worth official trade between India and Pakistan.¹⁰

The growth of regional trade was also impeded by several tariff barriers, NTBs and PTBs, including discriminatory treatment by members against each other's products; lack of information, sustained dialogue and adequate transport facilities; travel and tourism barriers; poor banking relations; lack of finance and credit; complex and lengthy procedures; trade imbalances, absence of exportable surplus, high cost of production, threat of India's dominance, lack of credibility in regional capabilities, lack of

⁷ Editorial, "Pakistan-India Trade breakthrough," *Express Tribune* (Islamabad), November 5, 2011, <http://tribune.com.pk/story/288127/pakistan-india-trade-breakthrough/> (accessed December 15, 2014).

⁸ Yussuf A. Harun, "Regional Cooperation in South Asia: Bangladesh Perspective," in Ahmed, Kelegama, and Ghani, eds. *Promoting Economic Cooperation*, 283.

⁹ Imtiaz Alam, "South Asian Economic Blues," *South Asian Journal*, 4 (Apr. - Jun., 2004), ii; Nisha Taneja, "Informal and Free Trade Arrangements," *South Asian Journal*, 4 (Apr.-Jun., 2004), 49.

¹⁰ Ding Ding and Iyabo Masha, *India's Growth Spillovers to South Asia*, IMF Working Paper, WP/12/56. International Monetary Fund, 2012, 15.

quality control and skilled manpower constraints, etc.¹¹ Meanwhile, the cost of cross-border trade has also been very high in South Asia. For instance, trucks have to wait for about 4–5 days to cross a main border point (Petrapole–Benapole) between Bangladesh and India. Some 200 signatures are required in Nepal for trade with India and 140 signatures in India to trade with Nepal.¹² Removal of these trade barriers and regularization of illegal trade across the borders can help all SAARC members, particularly the SRCs in generating the much needed revenues as well as providing goods to consumers at much lower prices.

Trade Liberalization in South Asia: SAPTA and SAFTA

The SAARC members moved towards trade liberalization with the signing of the South Asian Preferential Trade Arrangement (SAPTA) in 1993 which became effective in 1995. Under SAPTA, they had completed four rounds of negotiations on tariff reductions by 2004 which covered 5000 items.¹³ SAPTA could not significantly increase regional trade because it covered only a small fraction of the total goods traded by SAARC members. World Bank report 2004 estimated that SAPTA covered only 8.4 per cent of tariff lines for the goods imported from non-LDCs and 6.2 per cent from LDCs.¹⁴ Meanwhile, SAARC members started negotiations to conclude a South Asian Free Trade Arrangement (SAFTA) by 2001. But the tension between India and Pakistan after nuclear detonations in 1998, the Kargil war, change of government in Pakistan in 1999 and a terrorist attack on Indian parliament in 2001 delayed the process and they could sign SAFTA only in 2004 amid various doubts about its success.¹⁵

SAFTA adopted a different approach to boost regional trade. Instead of the positive list that was adopted in SAPTA, it provided for a negative list approach. It meant that members would phase out tariffs on all imports from their partners except those put under the negative list. Under the

¹¹ P. A Joy, *SAARC: Trade and Development*, (New Delhi: Deep & Deep Publications, 1995), 221–6.

¹² Ahmed & Ghani, “Making Regional Cooperation Work,” 53–6.

¹³ SAARC Secretariat, SAARC Secretariat, *SAARC Documents*, vol. VI, 368, http://www.saarc-sec.org/areaofcooperation/detail.php?activity_id=4 (accessed February 8, 2014).

¹⁴ Dushni Weerakoon, “SAFTA: Current Status and Prospects,” in Ahmed, Kelegama, and Ghani, eds. *Promoting Economic Cooperation*, 74.

¹⁵ Ranjit Kumar, *South Asian Union: Problems, Possibilities and Prospects*, (New Delhi: Manas Publications, 2005), 30–31.

agreement, it was provided that non-LDCs members would cut tariffs to 20 per cent within the first two years and then to 0–5 per cent range within the next five years. LDCs members would cut import tariffs to 30 per cent in the first two years and then 0–5 per cent in the next eight years period.¹⁶ Sri Lanka and India maintained relatively larger negative lists as compared to Pakistan's liberal policy towards LDCs. Pakistan included only 17 per cent of its imports in its negative list compared to India and Sri Lanka's 38.4 per cent and 51.7 per cent respectively. However, Pakistan had "the largest number of items in the sensitive list of non-LDC members." It also decided to maintain a positive list approach in its trade with India. This decision on the part of Pakistan caused some disputation with regard to implementation of SAFTA which otherwise progressed as per timeframe given in the agreement. Later on, India unilaterally cut short its negative list by eliminating another 264 items being imported from LDCs even before the scheduled four-year period specified for revision of sensitive list.¹⁷

SAFTA was criticized on various grounds, such as Rules of Origin (ROOs), and exclusion of trade in services and investment. The critics observed that SAFTA did not require any "explicit commitment" from its members to address NTBs which continued to impede free trade in South Asia. It included only an understanding on the part of members to continue negotiations on NTBs. There were two types of NTBs: those that were needed to be eliminated; and those to be harmonized. The former included quotas, customs surcharges, monopolistic measures such as state controlled agencies' exclusive import rights, etc. The latter included "measures relating to technical standards, plant and animal health, and environmental protection and safety," etc.¹⁸

Bilateral, Sub-regional and Alternative Regional Trading Arrangements

India played a crucial role in concluding bilateral FTAs and alternative RTAs. The SAARC members had already taken initiatives for trade liberalization with the signing of SAPTA in 1993 and charting out a road map to move towards SAFTA in 1996. As such, there was no apparent rationale for signing the bilateral FTAs in South Asia. But New Delhi was not satisfied with the pace and scope of trade liberalization under SAPTA

¹⁶ Weerakoon, "SAFTA: Current Status and Prospects," 74.

¹⁷ Ibid., 78–80.

¹⁸ Ibid., 78–9.

which covered limited products of India's interest. The progress on SAPTA was slow while the future of SAFTA was uncertain. The process had come to a deadlock due to changing geo-political situation in South Asia in 1998–99. It prompted New Delhi to look at “bilateralism with greater interest.”¹⁹

India initiated several bilateral, sub-regional and alternative regional initiatives. It concluded some trade agreements with all SRCs except Pakistan. These included: a trade agreement with Maldives in 1981; FTA with Nepal in 1991 (renewed in 1996, renegotiated in 2002, and again renewed in 2007 and 2009); FTA with Bhutan in 1995 (renegotiated in 2006); FTA with Sri Lanka in 1998 (also initiated talks on Comprehensive Economic Partnership Agreement (CEPA) in 2004), and a trade agreement with Bangladesh in 2006 in addition to discussing an FTA which could not materialize.²⁰ In its bid to pace up trade liberalization in the region, India also joined the initiative to form sub-regional groupings such as South Asian Growth Quadrangle (SAGQ) and the Kunming Initiative, both comprising Bangladesh, Nepal, Bhutan, and parts of India. The latter also included the Yunnan province of China, and northern Myanmar.²¹ India also strived to form another sub-regional grouping that would include the Maldives, Sri Lanka and South India.²² Opposition parties in Nepal and Bangladesh had criticized their governments on their decision to join the sub-regional groupings, which they believed were part of a conspiracy to undermine SAFTA and “sideline SAARC.”²³

In 1997, India strived to broaden its agenda of cooperation outside South Asia and took initiatives for alternative RTAs. It actively pursued formation of Indian Ocean Rim–Association for Regional Cooperation (IOR–ARC) and the Bay of Bengal Initiative for Multi-Sectoral Technical

¹⁹ Deshal de Mel, “Bilateral Free Trade: Agreements in SAARC and Implications for SAFTA,” in Ahmed, Kelegama, and Ghani, eds. *Promoting Economic Cooperation*, 89.

²⁰ Harun, “Regional Cooperation in South Asia,” 286; Weerakoon, “SAFTA: Current Status and Prospects,” 86.

²¹ Harun, “Regional Cooperation in South Asia,” 286; Sangeeta Thapliyal, “Potential for Cooperation in South Asia: the Need for a Sub-Regional Approach,” *South Asian Survey*, 6:1 (1999), 57.

²² Sonu Jain, “Regional Cooperation in South Asia: India Perspectives,” in Ahmed, Kelegama and Ghani, eds. *Promoting Economic Cooperation*, 304.

²³ Smruti S. Pattanaik, “Making Sense of Regional Cooperation: SAARC at Twenty,” *Strategic Analysis*, (Institute for Defence Studies and Analyses), 30:1 (Jan–March 2006), 145–6.

and Economic Cooperation (BIMSTEC)²⁴ That also included a free trade agreement (BIMSTEC-FTA). India, Bangladesh and Sri Lanka, are also members of the Asia Pacific Trade Agreement (APTA) whose members were also negotiating an FTA. Meanwhile, India also signed bilateral FTAs with ASEAN, Korea and Singapore.²⁵

In fact, SAFTA was signed when members were already lowering tariffs either under bilateral FTAs or IMF/World Bank reform programmes. Particularly, in the presence of India's bilateral FTAs with other regional states, SAFTA looked like an agreement between India and Pakistan. In combination, various FTAs and alternative RTAs were "paving the way for an eventual approximation to free trade in the region."²⁶ Nonetheless, this overlapping network of different trade agreements, which included India and the SRCs besides some extra-regional states, could boost regional trade quite significantly.

India's Behaviour Towards Removal of Trade Barriers

The trade liberalization process in South Asia apparently has had positive effects in the region as it has helped increase regional trade. For instance, Indian exports to SRCs increased manifold during 2002 to 2006, as these went up more than two times to Maldives, three times to Bangladesh and in case of Nepal and Sri Lanka even higher. Similarly, Indian imports from these states also increased significantly.²⁷ The process continued throughout the coming years but this increased trade among SAARC members could not bring any significant change or increase in the share of regional trade to their overall trade. It never went beyond 6 per cent and varied significantly for different states. In 2007, India's regional trade accounted for only 2.7 per cent of its overall trade which was the lowest among all SAARC members. It stood at 6.6 per cent for Pakistan, 9.4 per cent for Bangladesh,

²⁴ Sumit Ganguly, "India in 1997: Another Year of Turmoil," *Asian Survey*, 38:2 (Feb., 1998), 129; Bhabani Sen Gupta, "India in the Twenty-First Century," *International Affairs*, 73: 2 (Apr., 1997), 307–9; Sujata Jhamb, "India's Regional Trading Arrangements," *South Asian Journal*, 11 (Jan. – Mar., 2006), 44–6.

²⁵ Harun, "Regional Cooperation in South Asia," 286; Weerakoon, "SAFTA: Current Status and Prospects," 83–6.

²⁶ Weerakoon, "SAFTA: Current Status and Prospects," 80–4.

²⁷ Razzaque, "Weaker Economies in SAFTA, 380.

12.2 per cent for Maldives, 18.9 per cent for Sri Lanka and highest 60.5 percent for Nepal.²⁸

The process of trade liberalization in South Asia faced several challenges particularly due to India's protectionist policies. The SRCs continued to face barriers against their exports to India and in efforts to correct their trade imbalances which further widened due to trade expansion in South Asia. New Delhi continued to pressurize the SRCs for further trade liberalization including areas of services and investment opportunities etc. But it hardly took the demands of smaller states seriously to remove the various barriers impeding their access into the Indian market. This behaviour on the part of New Delhi undermined the process of trade liberalization and economic integration in South Asia. The Indian attitude towards economic concerns of the smaller states is dealt with in detail in the following pages.

Bangladesh

Surrounded by India on three sides, Bangladesh may be called an India-locked country heavily reliant on New Delhi for its land merchandize. Dhaka had strived to build close economic ties with India soon after it came into being in 1971 but their trade relations have seen many ups and downs. Since the early 1990s, both states strived to promote bilateral trade. In 2006, they signed a trade agreement and also discussed an FTA but progress on that got stuck due to differences on several issues.²⁹

Expert opinion in Dhaka blames India for not fulfilling its obligations under the bilateral agreements and accuse it of "trade terrorism."³⁰ During the period from 1991 to 1996 Indo-Bangladesh formal trade increased five times with major increase in Indian exports to Bangladesh which reached a total of US \$1.1 billion. If smuggled Indian goods were included, this figure could go up over US \$2 billion per year. It had increased Dhaka's economic dependence on India in several respects. Its enhanced imports were not

²⁸ Rajeev Jain and J. B. Singh, *Trade Pattern in SAARC Countries: Emerging Trends and Issues*. Reserve Bank of India Occasional Papers, 2009 Winter, 30 (3), 82–3, http://www.rbi.org.in/scripts/bs_viewcontent.aspx?Id=2255

²⁹ "India-Bangla FTA can increase bilateral trade by over 100%," *Economic Times*, December 17, 2012, http://articles.economictimes.indiatimes.com/2012-12-17/news/35868911_1_fta-negotiations-bangladesh-bilateral-trade

³⁰ Shamsul Huq Zahid, "Trade Terrorism: India Continues to Renege on Promises," *Financial Express*, February 20, 2002.

matched by its exports to India. Rather, they dropped from 16.6 per cent in 1986 to 6.6 percent in 1996. In the same period, their trade gap widened from Tk.1.5 billion to Tk.42 billion.³¹ In order to minimize its trade deficit, Dhaka had been asking India since the early 1990s to unilaterally remove the barriers to its exports, and to place Bangladesh at par with Bhutan and Nepal in the matter of access to the Indian market. Dhaka was not in a position to reciprocate due to its small economic base and its huge trade deficit with India whose products – both legally and illegally – already dominated the Bangladeshi market India remained adamant.³²

Dhaka continued to face India's high tariffs, NTBs and PTBs. For instance, during fiscal 2000-01 its exports to India stood at \$62 million against imports worth \$1.2 billion.³³ In 2006, Dhaka imported products worth \$2231 million against its exports of \$147 million³⁴—a 15 fold disproportion. Economic experts described it as India's failure "to honour its commitment" to give zero tariff facility to selected Bangladeshi products. The officials and businessmen in Bangladesh were also concerned about smuggling from India. Dhaka believed that India would not budge until it got "something in exchange." Indian concessions could have helped decrease the trade imbalance and removed the "strong resentment" against India in Bangladesh. But India was apathetic to the economic problems of Bangladesh as could be seen when it imposed anti-dumping laws on imports of automobile batteries from Bangladesh.³⁵ Bangladesh had exported automobile batteries and parts worth \$0.38 million in 1999–2000. But Indian battery manufacturers had their government impose anti-dumping laws against this small import item of Bangladesh. New Delhi also refused to allow a Bangladeshi cargo handling firm to open its service in India by distorting the relevant law.³⁶ Despite the huge trade deficit Dhaka continued to faced several PTBs and NTBs against its exports to India. Dhaka complained of discrimination as New Delhi had given unilateral duty-free access to goods produced in Bhutan and Nepal but Bangladesh which could provide several agro-processed items to

³¹ Rehman Sobhan, "Regional Cooperation in South Asia: a Quest for Identity," *South Asian Survey*, 5 : 1 (1998), 9–10.

³² Ibid, 18.

³³ Zahid, "Trade Terrorism: India Continues.

³⁴ Prabir De, "Why is Trade at Borders a Costly Affair in South Asia? An Empirical Investigation," *Contemporary South Asia*, 19: 4 (December 2011), 444.

³⁵ Zahid, 2002.

³⁶ Ibid.

northeastern Indian states adjacent to it was being blocked by imposition of a surcharge and additional customs duty on these items by India. Moreover, several NTBs also denied Bangladeshi exports an access to these states.³⁷ Bangladesh was so perturbed on its trade imbalance with India that it refused participation in Myanmar-Bangladesh-India gas pipeline project, until India took certain remedial measures.³⁸

The bilateral relations between India and Bangladesh have considerably improved since Hasina Wajed came into power in 2009. However, trade ties between the two countries are still a matter of concern in Dhaka. New Delhi has accepted Dhaka's old demand and granted Bangladeshi products duty-free and quota-free access to Indian market but the prevailing NTBs pose a major hindrance to them. Resultantly, Dhaka has not been able to significantly increase its exports to India and reduce the trade imbalance between the two states. According to a recent report, Bangladesh currently faces an annual deficit of \$5 billion in its trade with New Delhi as its imports from India stand at \$5.5 billion against its exports of around \$450 million.³⁹ In fiscal 2013–4, Bangladeshi exports to India dropped by 19 per cent from the previous fiscal level. This decline has been attributed to the present NTBs and the depreciation of Indian currency against the Bengali Taka.⁴⁰ The NTBs affect 49 out of 50 products of Bangladesh. Dhaka has urged India to cut NTBs and PTBs to help bridge trade imbalance and remove a major cause of friction in their bilateral relations.⁴¹

³⁷ Harun, "Regional Cooperation in South Asia," 284–5.

³⁸ Kamal Raj Dhungel, "Regional Energy Trade in South Asia: Problems and Prospects," *South Asia Economic Journal*, 9:1 (2008), 181.

³⁹ "Businesses want India non-tariff barriers to go for trade gap cuts: Indian minister claims Bangladesh exporters fail to understand their market, *New Age*, August 25, 2014, <http://newagebd.net/45338/businesses-want-india-non-tariff-barriers-to-go-for-trade-gap-cuts/#sthash.MjoD5H4e.nsFFqhCq.dpbs>

⁴⁰ Ziaur Rahman, "Export to India on downturn: Fluctuation of Rupee, NTBs stand in the way," *Financial Express*, August 2, 2014, <http://www.thefinancialexpress-bd.com/2014/08/02/48139/print>

⁴¹ "Cut non-tariff barriers, Tofail asks India," *Star*. September 11, 2014, <http://bd.thedailystar.net/business/cut-non-tariff-barriers-tofail-asks-india-41147>

Nepal

Nepal is another India-locked country which depends almost entirely on the big neighbour for trade and transit facilities. These issues are the main irritants in their bilateral relations. India signed a bilateral FTA with Nepal in 1991 and subsequently renewed/revised it in 1996. Later on, India forced Kathmandu to renegotiate the FTA in 2002. Both states renewed the same in 2007 and then again in 2009.⁴²

Indo–Nepal FTA of 1996, valid for a period of 5 years and extendable for another 5 years, was reportedly a “liberal” one. It had provided for duty-free and quota-free access to Nepalese manufactured goods, except those under sensitive list, without any condition related to ROOs.⁴³ Previously, the duty-free and quota-free access facility was restricted to goods with at least 50 per cent raw material of Nepalese or Nepalese–Indian origin or Nepalese labour content. In the 1996 treaty, India also agreed to give Nepalese goods a “national treatment” in terms of additional duty. The treaty provided large investment opportunities to India and other SAARC states and thus, also attracted Indian investors in joint projects in Nepal. Resultantly, Foreign Direct Investment (FDI) inflow to Nepal increased significantly and reached \$132 million in 1999. Meanwhile, Nepalese exports, particularly bulk export of a few products to India, increased considerably.⁴⁴ Albeit despite this growth in Nepalese exports, the trade balance remained heavily in India’s favour.. For instance, Nepal imported goods worth rupees 47 billion from India and exported to it products worth only rupees 27 billion facing a resultant trade deficit of 20 billion rupees during 2000–2001. An economic observer Upreti commented that trade imbalance continued to mar improvement in their bilateral relations.⁴⁵

⁴² Jain, “Regional Cooperation in South Asia, p.305; Purushottam Ojha, “Why Revise the Nepal–India Treaty of Trade?” Ministry of Commerce and Supplies, Government of Nepal. n.d. 1–3,

<http://www.mocs.gov.np/uploads/Book%20next.pdf>; M. Dev Pant, “Government-Industry Partnership in the SAARC Region: Strategic Alliance for 2010,” *South Asia Economic Journal*, 3 (2002), 135.

⁴³ Ratnakar Adhikari and Paras Kharel, “Nepal and SAFTA: Issues, Prospects and Challenges,” *South Asia Watch on Trade, Economics and Environment*. Research Report. August 2011, 5–7,

http://www.sawtee.org/Research_Reports/R2011-05.pdf

⁴⁴ Jain, “Regional Cooperation in South Asia, 305; Pant, “Government-Industry Partnership, 135–7.

⁴⁵ Upreti, “India–Nepal Relations,” 270.

The boom in their bilateral trade particularly Kathmandu's exports to India was short-lived. In December 2001, India raised the issue of anti-dumping and extended the treaty only for three months on the plea that third country products were flooding into Indian market through Nepal. Kathmandu suspected that New Delhi was retreating from the treaty on the pressure of strong Indian business lobbies who did not want free inflow of Nepalese goods.⁴⁶ In March 2002, India forced Nepal to amend the treaty and incorporate ROOs and norms of value addition. The revised treaty included several conditions – strict ROOs, imposition of quota on four major Nepalese export items, hard safeguard rules and requirement of criteria for ROOs on annual basis – that deprived Kathmandu of the preferences it was enjoying in the Indian market. These provisions targeted Nepal's main export items as well as “potential exportable goods.” The ROOs were said to have been used “as a means of disguised protection.” On the other hand no ROOs impeded Indian products from entering the Nepalese market.⁴⁷

This revision of the treaty in 2002 resulted not only in “a degree of retrogression” in Nepalese trade with India but also adversely affected the efforts to diversify Nepalese economy.⁴⁸ Nepalese exports to India had tripled between 1997 and 2001 jumping from 9 billion Nepalese rupees (NR) to NR.28 billion. However, the growth rate in exports was severely undermined in the next five years and went up only to NR.42 billion in 2007. Next year it declined to NR.39 billion. This slow growth in exports to New Delhi was attributed to several factors, including the prevailing NTBs and loss of preferences to Nepalese goods in Indian market.⁴⁹ Besides erecting quantitative barriers, India also occasionally unilaterally banned import of certain Nepalese items, such as garlic, on one pretext or the other. Several Nepalese exports including agricultural and forest products, readymade garments (RMGs) and pharmaceuticals, faced NTBs in the Indian market. Besides, PTBs such as imposition of special additional duty on Ready Made Garments (RMGs) in 2009 and countervailing duty on some items also restricted Nepalese exports to India. The revised treaty of

⁴⁶ Baral, “Reconstruction of South Asia,” 82–3.

⁴⁷ Adhikari and Kharel, “Nepal and SAFTA,” 5–7.

⁴⁸ Jain, “Regional Cooperation in South Asia, 305. The modified agreement included a negative list as well as provisions that required 30 percent value addition and “quantitative restrictions” on the import of copper, zinc oxide, acrylic yarn and vegetable ghee.

⁴⁹ Ojha, “Why Revise the Nepal–India,” 1–3.

2009 stipulates that both states would “undertake measures” to eliminate or reduce NTBs, PTBs and other barriers to bilateral trade but it does not provide any mechanism or “binding commitment” to definitely abolish such barriers.⁵⁰

Nepalese trade with India has been “characterized by a persistent and widening deficit.” Currently about two-thirds of Nepalese trade is “concentrated” in India. The ratio of Nepalese exports to and its imports from India has declined continually over the period, i.e. from 72.8 per cent in 1975–6 to 15.1 per cent in 1995–6. It resurged to 47.6 per cent in 2000–1 and again went down to 13.8 per cent in 2012–3.⁵¹ Dhakal noted the inconsistency and fluctuations in the growth rate of Nepalese exports to India between 1998–8 to 2007–8 but India’s exports to Nepal increased consistently which further widened the trade imbalance between the two. It also increased Nepalese economic dependence on India as two-thirds of the former’s trade (both imports and exports) took place with New Delhi and only one-third of it with the rest of the world. In 1998–9 Nepal had only one-third of its trade with India and two-thirds of it with the rest of the world. In a decade, the trend has completely reversed. It widened the mutual trade imbalance which is a major cause of concern in Katmandu and also one of the main irritants in Indo–Nepalese relations.⁵²

Sri Lanka

In the context of slow progress on trade liberalization under SAARC and growing economic links between India and Sri Lanka since the early 1990s, both states had decided to sign a bilateral FTA in 1998. The Indo-Sri Lanka–FTA (ISL–FTA) became effective in March 2000, which increased their bilateral trade, particularly Colombo’s exports to India and flow of FDI to Sri Lanka. Foreign investors viewed it as a window for increasing sale of their products to the Indian market.⁵³ The overall effect of the ISL–FTA had shown gains for Sri Lanka. Initially its exports to India increased

⁵⁰ Adhikari & Kharel, “Nepal and SAFTA,” 5–7.

⁵¹ Mahesh K. Chaulagai, “Indo Nepal Trade Relation: The Phenomenon of Black Hole Effect,” *NRB Economic Review*, 26 : 1, (2014). 47–8.

⁵² Krishna Prasad Dhakal, *How to Address Critically Widening Nepalese Trade Deficit with India*, Ministry of Commerce and Supplies, Government of Nepal. (n.d.). 31–51, <http://www.mocs.gov.np/uploads/Book%20next.pdf>

⁵³ Jain, “Regional Cooperation in South Asia, 304–5; Mel, “Bilateral Free Trade,” 89.

significantly due to concessions given by New Delhi. Sri Lankan exports to India jumped up from \$46 million in 1999 to \$515 million in 2007, which were 6.6 per cent of its total exports. The trade balance having a 14.3 to 1 ratio in 1998 in India's favour shrank to 4 to 1. By then, Colombo's exports to India also included processed goods such as refined copper, wires, rubber, margarine, vegetable oil and fats, antibiotics, ceramics, and furniture, etc. In 2006, Sri Lanka's 75 per cent of exports received preferential treatment as compared to 22 per cent in 2001. India's investment in Sri Lanka also increased significantly. The cumulative value of India's FDI rose from \$ 2.5 million or 1.3 per cent of total FDI, in 1998 to \$ 191.2 million in 2005, i.e. 8.3 percent of total FDI in Sri Lanka. As such, India became the fifth largest investor in the country. It appears that the ISL-FTA substantially deepened their economic ties and India became Sri Lanka's largest source of imports and third largest destination of exports.⁵⁴ Due to these successes, Sri Lanka wanted to "deepen and broaden" the cooperation and thus, started negotiations with India in 2004 to sign CEPA in order to include trade in services and investment.⁵⁵

The process underwent a setback after 2005. In spite of apparent gains for Sri Lanka, a detailed and "disaggregated" scrutiny of bilateral trade had shown that the real picture was "less encouraging." Since 2006, some of Sri Lankan major exports faced difficulties in getting access to Indian market. Initially, Sri Lanka's exports to India were mainly dominated by *vanaspati* (vegetable oil) and copper. In 2006, India imposed quotas on *vanaspati* imports from Sri Lanka. Resultantly, Sri Lankan exports of *vanaspati* to India declined. Following a rise next year, India decided to remove MFN tariffs on *vanaspati* imports due to which Sri Lankan *vanaspati* exporters lost their preferential status as well as competitiveness in the Indian market. Meanwhile, India changed the invoicing method due to the complaints of under-invoicing. It hurt Sri Lankan copper exports which fell from \$145 million in 2005 to \$27 million by 2007.⁵⁶ The copper and *vanaspati* had a share of 50 per cent in Sri Lanka's total exports to India. However, India removed the MFN status for Lankan *vanaspati* exports and changed the rules for imports of copper which now stated that its "imports should conform to prices stipulated by

⁵⁴ Mel, "Bilateral Free Trade," 91–6.

⁵⁵ Weerakoon, "SAFTA: Current Status and Prospects," 82.

⁵⁶ Mel, "Bilateral Free Trade," 90, 95–6.

the London Metal Exchange.” These measures resulted in sharp decline in Sri Lankan exports to India as well as overall volume of trade with India.⁵⁷

Under the ISL-FTA, Sri Lanka’s traditional export goods such as tea and garments were not given enough access to Indian market. India had included garments in its negative list “except for a 50 per cent margin of preference for 8 million pieces.” Out of it, 6 million were required to use Indian fabrics. An observer Mel noted: “The sourcing requirement ensured that Sri Lankan garment exports to India were not competitive relative to domestic producers and, as a result, there was less than one per cent quota utilization.” However, in 2007, India agreed to allow 3 million garment pieces duty free import from Sri Lanka without sourcing requirement. In 2008, this figure was further raised to 6 million garment pieces and extra 2 million pieces with 70 per cent margin. However, the required administrative procedures to implement the decision were not finalized.⁵⁸ Under ISL-FTA, 53 per cent of Sri Lankan exports, including tea and garments, were placed under Tariff Rate Quotas (TRQs) due to which Sri Lankan exporters could not get enough access to Indian market. Therefore, they had reservations over trade agreement with India.⁵⁹

Sri Lankan exports also faced several NTBs such as India’s complex rules related to entry of foreign goods at airports and seaports, etc. Indian provincial taxes also restricted Sri Lankan exports to India.⁶⁰ Sri Lankan tea exporters continued to face hardships in getting access to Indian market due to port restrictions and ROOs. In 2007, port restrictions were relaxed but no change in RROs was made. Sri Lankan exporters had concerns on prevalence of PTBs, particularly tariffs imposed by provincial governments in India which undermined potential export competitiveness of

⁵⁷ Jagath C. Savandasa, “Indo-Sri Lanka Free Trade Agreement 2000–2010,” *Sri Lanka Guardian*, December 21, 2011, <http://www.srilankaguardian.org/2010/12/indo-sri-lanka-free-trade-agreement.html> (accessed December 25, 2013).

⁵⁸ Mel, “Bilateral Free Trade,” 92–8.

⁵⁹ “Sri Lanka-India free trade deal helped consumers, producers: economist,” *Lanka Business Online*, May 25, 2010, <http://www.lankabusinessonline.com/fullstory.php?nid=1619783871> (accessed on September 25, 2010).

⁶⁰ Bis Wajit Nag, “Issues Related to Trade Facilitation and Non-tariff Barriers in India and Sri Lanka: A Synthesis of Secondary Literature,” in Indra Nath Mukherji and Kavita Lyengar eds. *Deepening Economic Cooperation Between India and Sri Lanka*, (Mandaluyong: Asian Development Bank, 2013), 53–91; Savandasa, “Indo-Sri Lanka Free Trade.”

neighbouring countries. For instance, foreign producers are charged two times higher provincial sales tax than those on local ones in Tamil Nadu. It deprives Sri Lankan exporters of their competitiveness there which they enjoy because of less transportation cost due to geographical proximity with Tamil Nadu.⁶¹ Occasionally, India also imposed quota restrictions on its pepper imports from Sri Lanka on the plea that imported pepper had adversely affected its prices in Kerala. It led to decline in Sri Lankan pepper exports to India. As such, India's protectionist measures resulted in decline in Sri Lankan exports to India.⁶²

Several studies have shown that Sri Lankan exports to India had witnessed a sharp decline after 2005.⁶³ In 2005, Sri Lankan exports to India had reached an all time high volume of \$568 million which later on dropped to \$328 million in 2009. The year 2009 also witnessed a dramatic decrease in India's exports to Sri Lanka, i.e. \$1724 million from \$2838 million in 2008.⁶⁴ Sri Lanka's imports from and exports to India steadily rose to \$3640 million and \$567 million, respectively, by 2012.⁶⁵

Indian measures provoked economic nationalism in Sri Lanka which severely undermined the process of deeper economic cooperation between the two countries. Sri Lanka was the only state among SRCs that wanted trade liberalization under SAARC framework from the onset. It had taken the lead in signing bilateral FTA with India and even started negotiations to conclude CEPA in 2004. But due to growing concerns among its business community over trade links with India, Sri Lanka refused to sign CEPA

⁶¹ In Tamil Nadu, producers from other Indian states and foreign countries have to pay 21 percent sales tax as compared to 10.5 percent imposed on local producers. S. Kelegama and I. Mukherjee, *Indo-Lanka Bilateral Free Trade Agreement: Six Year Performance and Beyond*, (New Delhi: Research and Information Systems (RIS) for Developing Countries, 2007), 21–2.

⁶² Mel, "Bilateral Free Trade," 97–8.

⁶³ Saman Kelegama, *The India-Sri Lanka Free Trade Agreement and the Proposed Comprehensive Economic Partnership Agreement: A Closer Look*. ADBI Working Paper No. 458, (Tokyo: Asian Development Bank Institute, 2014), 1e at <http://www.adbi.org/working-paper/2014/02/06/6131.india.sri.lanka.free.trade.agreement/>; Mel, "Bilateral Free Trade;" Savandasa, "Indo-Sri Lanka Free Trade."

⁶⁴ Chandrima Sikdar, "Potential economic impact of India-Sri Lanka bilateral trade liberalization," paper presented at the 14th Annual conference on Global Economic Analysis, Venice, Italy, 2011, <https://www.gtap.agecon.purdue.edu/resources/download/5349.pdf> and https://www.gtap.agecon.purdue.edu/resources/res_display.asp?recordid=3538

⁶⁵ Kelegama, *The India-Sri Lanka Free*, 4.

which both states had earlier agreed to conclude in 2008.⁶⁶ The opposition to CEPA is yet very strong in Sri Lanka.⁶⁷ India's policies aimed at appeasing its domestic constituency and powerful business lobbies and resultant protectionist measures have apparently shaken the confidence of Sri Lankan people including its business community and political leaders. It ultimately impeded the trade expansion and undermined the process of deepening economic cooperation and integration between the two states.

Pakistan: Indo-Pakistan trade relations faced various challenges due to several reasons since 1947. In the immediate post independence era, about 56 per cent of Pakistan's exports and 32 per cent of imports were India oriented. The "battle of rupee" and two wars between them severely undermined this bilateral trade.⁶⁸ In 1980s, both states took steps to revive trade⁶⁹ which further improved in 1990s but its volume was still small. During 1995–2005, the annual volume of Indo-Pak trade remained less than \$1 billion and both countries did not fall in each other's lists of top ten trading partners. Pakistan's average share in Indian trade was less than one per cent while India's share in Pakistan's trade remained at less than two per cent.⁷⁰ However, their bilateral trade has risen ten times in ten years since 2000. In 2011, the annual volume of official trade was about \$2.7 billion and it could jump to \$10–15 billion in a few years. There also existed illegal trade sized about two fold of the formal trade between the

⁶⁶ Ibid., 11; Dilshani Samaraweera, "Local businesses unhappy with CEPA," *Sunday Times*, July 20, 2008, <http://sundaytimes.lk/080720/FinancialTimes/ft300.html>; and also "Sri Lankan protesters march against proposed trade pact with India," *Economic Times*, May 26, 2010, http://articles.economictimes.indiatimes.com/2010-05-26/news/28434779_1_comprehensive-economic-partnership-agreement-trade-pact-cepa (accessed on October 30, 2011).

⁶⁷ Kelegama, *The India-Sri Lanka Free*, 11–4.

⁶⁸ Jamshed Ayaz Khan, "Pakistan and Regionalism," in Alyson J. K. Bailes, John Gooneratne, Mavara Inayat, Jamshed Ayaz Khan & Swaran Singh ed. *Regionalism in South Asian Diplomacy*, SIPRI Policy Paper (15). (Stockholm: SIPRI, 2007), 42–3; Asad. Sayeed, "Gains from Trade and Structural Impediments to India-Pakistan Trade" in E. Sridharan ed. *International Relations Theory and South Asia: Security, Political Economy, Domestic Politics, Identities, and Images*, vol. 2, ch. 2. Oxford: OUP; *Collective for Social Science Research*, 4–5, http://www.researchcollective.org/Documents/Gains_from_Trade.pdf

⁶⁹ Douglas C. Makeig, "War, No-War, and the India-Pakistan Negotiating Process," *Pacific Affairs*, 60: 2 (Summer, 1987), 288–290.

⁷⁰ Sayeed, "Gains from Trade," 3.

two states. Illegal trade was mainly one-sided, i.e. Indian goods being smuggled into Pakistan. A recent report claimed that unofficial trade between India and Pakistan stood at about \$10 billion which could be regularized.⁷¹

Pakistan has been reluctant to promote trade with India due to political and economic reasons. Pakistan wanted progress on its political disputes with India, particularly the Kashmir issue, parallel to trade liberalization, as well as “a level playing field” in the wake of prevailing huge trade imbalance with India.⁷² Some elements in Pakistan have been fearful of Indian economic domination which could transform into political dominance. A section of business groups in Pakistan and right wing political parties argued that Pakistani industries particularly those related to automobiles, pharmaceuticals, light engineering and steel would be adversely affected due to trade liberalization with India.⁷³

A parallel narrative, however, also existed which was initially weak but gradually became strong and vocal. It supported the idea of free trade with India and demanded the government to grant Most Favoured Nation (MFN) status to New Delhi. It argued that refusal to liberalize trade with India was inconsistent to Pakistan's policy of supporting a free trade regime in the world.⁷⁴ In the recent past, a broad consensus among mainstream political parties and major business groups supported by some media organizations and intellectuals in favour of trade liberalization with India has evolved in Pakistan. The process started in the mid 1990s and got impetus after 2004. The changing economic and “geo-political configurations” such as increased US interest to promote economic integration in South Asia, Pakistan's continued balance of payment problem and need to boost foreign investment helped build this consensus. Thus,

⁷¹ Ibid., 5–6; Akmal Hussain, “A Perspective on Peace and Economic Cooperation in South Asia,” in Sadiq Ahmed, Saman Kelegama, & Ejaz Ghani eds. *Promoting Economic Cooperation in South Asia: Beyond SAFTA*, (New Delhi: The World Bank, 2010), 19; “Editorial,” “Pakistan-India trade breakthrough,” *Express Tribune* (Islamabad), November 5, 2011, <http://tribune.com.pk/story/288127/pakistan-india-trade-breakthrough/>; “Pakistan business hits at barriers to India trade,” *Dawn* (Islamabad), November 27, 2011, <http://dawn.com/2011/11/27/pakistan-business-hits-at-barriers-to-india-trade/> (accessed November 30, 2011).

⁷² Shaukat Aziz, “South Asian Economic Powerhouse,” *South Asian Journal*, (Jan. – Mar., 2005), 28.

⁷³ Sayeed, “Gains from Trade,” 11.

⁷⁴ Ibid.

Pakistan's main political parties and leaders including those from Azad Kashmir favoured increased trade links with India.⁷⁵

In the last quarter of 2011, the government of Pakistan made the surprise announcement of substantially liberalizing trade with India. It announced to grant New Delhi the MFN status, shift trade with it from the positive list – containing 1958 items – to negative list, effective from 2012, and allow import of more than 7000 Indian products.⁷⁶ The decision was motivated by different domestic strategic, political, and economic considerations.⁷⁷ Later in 2012, both countries also signed comparatively a liberal visa regime particularly for business communities of the two states.⁷⁸

Different political parties, business groups and political leaders reacted differently to the government announcement to give India the MFN status. A few business groups, several leaders of opposition parties and religious circles opposed the decision.⁷⁹ Thousands of people in different

⁷⁵ Mehtab Haider, "Political Parties Agree to Tax Agri Income, Boost Trade with India," *News International* (Islamabad), April 30, 2011, <http://www.thenews.com.pk/TodaysPrintDetail.aspx?ID=44266&Cat=3>; Khaled Ahmed, "The Lonely Nawaz Sharif," *Newsweek*, September 2 and 9, 2011, issue, <http://www.newsweekpakistan.com/the-take/404>; Humayun Aziz Sandeela, "MFN Status: Pakistan and India treading the right path," *Pakistan Observer*, May 12, 2012, <http://pakobserver.net/201205/12/detailnews.asp?id=154993>

⁷⁶ "Pakistan Grants India Most Favoured Nation Trade Status," *Indian Express*, November 02, 2011, <http://www.indianexpress.com/news/pakistan-grants-india-most-favoured-nation-trade-status/869714/0>; Zia Khan, "16 years on... Pakistan finally reciprocates granting MFN status to India," *Express Tribune* (Islamabad), November 3, 2011, <http://tribune.com.pk/story/286925/16-years-on-pakistan-finally-reciprocates-granting-mfn-status-to-india/> (accessed November 20, 2012).

⁷⁷ Anthony, 2011.

⁷⁸ Augustine Anthony, "Pakistani Industries View India Trade with Alarm," *Reuters*, October 27, 2011, <http://www.reuters.com/article/2011/10/27/pakistan-india-idUSL3E7LP1RT20111027>

⁷⁹ "Nisar Expresses Concerns over Granting India MFN Status," *Dawn* (Islamabad), October 20, 2011, <http://dawn.com/2011/10/20/nisar-expresses-concerns-over-granting-india-mfn-status/>; Zahid Gishkori and Zia Khan, "Not at Kashmir's Cost: Political parties create uproar over trade concessions to India," *The Express Tribune*, October 21, 2011, <http://tribune.com.pk/story/278273/ecp-being-prevented-from-working-independently-chaudhry-nisar/>; "Senate body for briefing on MFN status for India," *Pak Tribune*, December 23, 2011, <http://paktribune.com/news/Senate-body-for-briefing-on-MFN-status-for-India-246117.html>; (accessed November 25, 2012).

parts of the country including AJK protested against the decision.⁸⁰ However, Pakistani business community had “overwhelmingly commended the decision.” Due to its strong support in its favour, no mainstream political party was in a position to seriously oppose it. However, they wanted reciprocal measures from India, particularly the removal of NTBs to Pakistani exports.⁸¹

Pakistani political parties, business groups and the government alike have serious concerns over the prevailing NTBs, PTBs, prejudices and Pakistan-phobia which have impeded Pakistani exports to India. New Delhi had given Pakistan the MFN status in 1996 and Islamabad has yet not reciprocated it. Still Indo-Pakistan trade is heavily in India's favour. For instance, during 2009–10 bilateral trade was of the order of about US\$ 1.4 billion. Indian exports stood at \$1.2 billion against its imports worth \$268 million.⁸² In 2010, bilateral trade remained at about \$1.7 billion which included Indian exports worth \$1.45 billion against its imports of \$275 million.⁸³ Pakistan's imports from India stood at over \$ 2 billion during the year 2010–11, \$ 1.5 billion during 2011–12 and \$ 2.06 billion during 2012–13. During the same financial years, Pakistani exports to India were worth \$ 332 million, \$397 million and \$542 million, respectively, showing a huge trade imbalance in favour of India.⁸⁴ This huge trade imbalance, claimed Jawad, a former Chairman of Pakistan's Export Promotion Bureau, was due to prevailing PTBs, NTBs, prejudices and “Pakistan-phobia” in India.⁸⁵ It is feared in Pakistan that unless India removes these barriers, trade liberalization with India would aggravate bilateral trade imbalance. For instance, Humayun Akhtar Khan, a former Commerce Minister, had warned that opening Pakistani market to Indian goods, and giving it the MFN

⁸⁰ “Pakistan Business Hits.”

⁸¹ Tanveer Ahmed, “PML-N accepts MFN status mutely, but also for removal of NTBs,” *Daily Times*, November 7, 2011, http://www.dailytimes.com.pk/default.asp?page=2011\11\07\story_7-11-2011_pg7_16 (accessed November 25, 2012).

⁸² Anthony, “Pakistani Industries View India.”

⁸³ Zia Khan, “16 years on... Pakistan finally.”

⁸⁴ High Commission of India, Islamabad, *Trade and Economic Relations between India and Pakistan*, <http://www.india.org.pk/eoi.php?id=Trade%20Relation> (accessed November 14, 2014).

⁸⁵ Wajid Jawad, interview in a TV program, “Aik-se-du,” *Geo News*, October 17, 2011.

status, without any agreement on removal of NTBs and PTBs by New Delhi could severely hurt Pakistani industries.⁸⁶

Pakistan had identified 27 NTBs which had impeded Pakistani exports to India. Pakistani exporters face several NTBs in India including: delay in custom clearance; dispute over pricing of Pakistani goods to determine duties; strict application of Indian standardization laws; imposition of composite tariffs on textile exports. Some of the NTBs are related to several rigid rules such as sanitary requirements for fisheries, livestock and agricultural products, quality certifications for cement and other products, and regulatory certificates which gave “bureaucracy with the leverage to discriminate between products and countries.”⁸⁷ Due to delay in clearance, which sometimes takes 8–9 months, export prices of Pakistani goods substantially increase and make them less competitive in the Indian market.⁸⁸

India’s attitude towards removal of NTBs and PTBs has not been positive. For instance, the Federation of Indian Chambers of Commerce and Industries (FICCI) claimed that after getting MFN status from India, it was Pakistan’s responsibility to increase its exports. However, Pakistani officials and exporters believed that several NTBs, PTBs and tariff barriers (latter for the agricultural products) deny Pakistani products access to Indian market.⁸⁹ The leaders of several industries pointed out that India was protecting its agricultural sector and Pakistani exporters had to pay 37 per cent tariff instead of 13 per cent – a standard tariff in India.⁹⁰ Pakistan has raised the issue of NTBs with New Delhi which, in response, had asked to highlight “Pakistan-specific” NTBs.⁹¹ In principle these regulations are applicable to all countries, but Pakistani exporters complained that they were often subjected to “arbitrary discrimination based on the regulatory structure.” Allegedly, Indian officials deliberately hold up clearing Pakistani products and its railway delays their deliveries. The high

⁸⁶ Humayan Akhtar Khan, interview with Kamran Khan, “Aj Kamran Khan Ke Sath,” *Geo News*, October 18, 2011.

⁸⁷ Haider, “Political Parties Agree;” Shahbaz Rana, “MFN status to India: Pakistan proposes safeguards for local industry,” *Express Tribune* (Islamabad), December 23, 2011, <http://tribune.com.pk/story/310649/mfn-status-to-india-pakistan-proposes-safeguards-for-local-industry/>

⁸⁸ Jawad, “Aik-se-du.”

⁸⁹ Sayeed, “Gains from Trade,” 9.

⁹⁰ “Pakistan business hits.”

⁹¹ Rana, “MFN status to India.”

transaction costs including strict visa regulations, complex tariff and duty structures, and customs clearance, etc. prevented Pakistani businessmen from making investment in sales and marketing of their products in India.⁹²

The Pakistani government believed that trade liberalization with India should be paralleled with removal of NTBs by New Delhi.⁹³ In 2011, Pakistan's Secretary Commerce had claimed that government would not move forward on trade liberalization with India without ensuring protection of domestic industries and acquiring a "level playing field for its exporters." To this end, Islamabad had proposed India three agreements. These were related to the Customs Cooperation, Grievances Agreements to address consumer protection, and Mutual Recognition Agreement for standardization of quality standards.⁹⁴ Both countries had signed these agreements in Islamabad in September 2012.⁹⁵

The progress on giving India the MFN status by Pakistan is stuck due to lack of consensus at home, pause in foreign secretaries' talks and border skirmishes between the two states.⁹⁶ In order to avoid domestic opposition to the MFN issue, the Nawaz government has decided to grant India Non-Discriminatory Market Access (NDMA) status on reciprocal basis. In response, Islamabad wants India to address its economic concerns particularly those related to "market access" including tariffs, NTBs and PTBs. Thus, the future prospects of Indo-Pak trade relations will largely depend on Indian behaviour particularly with regard to its policy either to remove or retain various barriers to Pakistani exports in its market.⁹⁷

⁹² Sayeed, "Gains from Trade," 9–10.

⁹³ Anthony, "Pakistani industries view India."

⁹⁴ Rana, "MFN status to India."

⁹⁵ Mubarak Zeb Khan, "Pakistan, India Sign Three Trade Agreements," *Dawn* (Islamabad), September 21, 2012, <http://www.dawn.com/news/751037/pakistan-india-sign-three-trade-agreements>

⁹⁶ "Pakistan working to give MFN Status to India," *Dawn* (Islamabad), July 25, 2014,

<http://www.dawn.com/news/1121496>; "Pak yet to grant most favoured nation status to India," *Times of India*, July 23, 2014,

<http://timesofindia.indiatimes.com/india/Pak-yet-to-grant-most-favoured-nation-status-to-India/articleshow/38926051.cms>

⁹⁷ Shahbaz Rana, "Non-discriminatory Market Access: Pakistan, India all but Sign Trade Normalization Deal," *Express Tribune* (Islamabad), March 15, 2014, <http://tribune.com.pk/story/683073/non-discriminatory-market-access-pakistan-india-all-but-sign-trade-normalisation-deal/>; "Pakistan seeks tariff," 2014.

Conclusion

India was very enthusiastic towards market expansion and trade liberalization even before the official launching of SAARC. However, the SRCs were apprehensive of it due to India's economic dominance, their weak economic and industrial infrastructures and prevailing barriers to their exports to India. However, India kept on pressing them for the move and played a leading role in signing of SAPTA and SAFTA. It also took the lead to conclude bilateral, sub-regional and alternative RTAs with and without some of the regional states. It showed magnanimity in its bilateral FTAs with SRCs, such as Nepal and Sri Lanka. Initially, these FTAs boosted India's bilateral trade with them. Particularly, Nepalese and Sri Lankan exports to India increased quite significantly which also helped increased inflow of FDI to these countries. However, this period of economic successes for both Nepal and Sri Lanka was short lived. Sooner Indian government bowed before the powerful domestic business lobbies and took protectionist measures depriving both these countries of their preferential status into Indian market. In 2002, New Delhi forced Nepal to revise the comparatively "liberal" trade agreement of 1996 and included stringent conditions that undermined the growth of Nepalese exports to India. It also adversely affected the inflow of FDI to Nepal and efforts to diversify its small economy. The initial success of ISL-FTA had encouraged Colombo to deepen its economic ties with New Delhi and to start negotiation on CEPA in 2004. However, the restrictive measures which New Delhi took after 2005 deprived Sri Lanka of its advantageous position in the Indian market. It severely damaged the growth of Sri Lankan exports to India as well as their bilateral trade which underwent a regression before recovering slightly. Most importantly, it destroyed the confidence of Sri Lankan businessmen and political leadership who are now reluctant to advance economic cooperation with India. The rise of economic nationalism in Colombo in response to Indian protectionist measures halted progress on CEPA which they were expected to sign in 2008. As yet, opposition to CEPA is strong in Sri Lanka. Both Nepal and Sri Lanka as well as Bangladesh and Pakistan also face various barriers that impede growth of their exports to Indian market. These barriers range from tariffs (in case of agricultural products) to several kinds of PTBs, and NTBs. All SRCs have serious concerns over prevalence of these barriers and resultant trade imbalances with India which increase their economic vulnerability

against the giant neighbour. They kept on demanding New Delhi to remove all sorts of barriers to their exports, and also to take remedial measures to correct the huge trade imbalances. India has so far not taken substantive measures to address the economic concerns of the SRCs. This behaviour on the part of India not only adversely affects trade liberalization and market expansion in South Asia but also occasionally strains New Delhi's bilateral political relations with the SRCs. This environment impedes regional cooperation in several fields among SAARC countries. In order to make South Asian regionalism successful and realize the goal of deeper economic cooperation in South Asia, India being the core and most resourceful state in the region, needs to look beyond narrow national interests and petty domestic political considerations. It has to show some large-heartedness in order to address the economic concerns of the SRCs. It needs to take concrete steps to give more access to the products of SRCs and bridge the existing trade imbalances with them. Meanwhile, the SRCs also need to increase their competitiveness and economic diversification in order to get more market access in the region and beyond. ■