SOUTH ASIA TRADE AND ENERGY SECURITY

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THE ROLE OF INDIA

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I

INTRODUCTION: TRADE AND ENERGY COOPERATION

Today, policy makers in both developed and developing countries are pursuing regionalization as a means to get easier market access, economies of scale, and welfare gains. At the same time, they are also undertaking economic reforms to weaken 'distributional cartels' and to make their economies competitive in the global marketplace. The economic gains to be accrued from these efforts have been well established. From a company's perspective, the larger the domestic market, the larger is the base for competition. In the present age, no nation can survive as an island unto itself. The goal of self- sufficiency is self-defeating and suicidal. The desire to improve the standard of living through trade has brought nation states together. Asian countries are moving rapidly in this direction.

Regional economic cooperation (REC) offers an important avenue to fight poverty jointly and to improve the welfare of their people. Recent global economic trends indicate that there is a proliferation of regional economic arrangements worldwide. The number of these arrangements reported to the World Trade Organization (WTO) after its establishment is about 400. Of these, 10 percent are customs unions. It is notable that this new wave of economic cooperation aims to be complementary to multilateral arrangements. Countries worldwide are pursuing regional and global interests through active participation in regional and multilateral forums at the same time. In this sense, regionalization is a building block towards globalization. In 2006, the WTO Negotiating Group on Rules took a formal step toward making REC partnerships the building blocks of world trade. Under the agreement reached by the Group, REC member countries have to provide information to the WTO on such matters as tariff concessions, most favored nation (MFN) duty rates, safeguards, preferential margins, quotas, balance of payments statistics, and other related matters. Fifty percent of the world trade today takes place under REC.

Another notable development in the world economy in recent years is the signing of free trade agreements (FTA) among non-contiguous countries. Mexico has concluded a comprehensive FTA with the EU, Chile, Costa Rica, and Columbia. Canada has signed an FTA with Chile and Costa Rica. The United States has signed FTA with Israel, Jordan, Singapore and Chile. The EU has signed FTA agreements with African, Asian, and Latin American countries. Japan, China, and India are also moving in the same direction. Two important economic reasons for signing FTAs with non-contiguous

countries are to secure raw materials and gain access to markets. Politically, FTAs bring political clout to member countries, hence domestic political interest in concluding international FTA deals.

Experience from North America and Western Europe suggest that the economic prosperity of a region depends upon how physical connectivity, trade, and investment links are built up among member countries. The European Union has made a major economic impact on Europe with its push to regional economic cooperation. It started the regionalization process 50 years ago. Since then, it has moved gradually from preferential trading arrangements to a customs union, to the common market, to an economic union. From 6 members in 1957, it has expanded to 27. It has reached the population size of 450 million, which is larger than NAFTA (North American Free Trade Agreement). Inter-state trading rules are in place and well enforced to enable the free movement of goods and services within the EU borders. The Euro has been established since 1999 with 17 countries as members. With failure to enforce admission criteria for common currency, some member countries faced severe debt crisis during the economic downturn. Under a new Fiscal Treaty signed in 2012, there is now renewed commitment to reinforcing the fundamental rules required for moving toward a common fiscal union. Without it, the EU cannot function effectively. With the present expansion, the EU is as large as the Unites States in terms of economic size.

In December 2007, the Treaty of Lisbon was signed by member countries. The Treaty recognized a Charter of Fundamental Rights, and also restructured the voting system. It replaced the Treaty of Rome (1957), Treaties of Maastricht (1992), Amsterdam (2006), and Nice (2000). The EU has appointed a president and foreign affairs chief. The new appointments give the Union a cohesive foreign policy. While the realization of the goal of the EU as a full-functioning federal structure where people can move for jobs without national restrictions and with Brussels as the capital are still far off, they have taken important steps in this direction. Increased interconnection of rail and rail networks has only helped to further consolidate the EU market.

In the Western American Hemisphere, NAFTA is bringing the USA, Canada, and Mexico together. By providing lower barriers to member countries, it is integrating their economies closely in many spheres of economic activity. The US economy has been an anchor to member countries. Data indicate that trade and financial sectors in the region are merging even closer. There is a surge in bilateral Foreign Direct Investment (FDI) and portfolio investment. International trade in goods and services has increased phenomenally. Oil is no longer the main export item of Mexico. The share of other manufactured goods has gone up significantly in its export menu. Canada has stepped up export of both goods and services. The US has increased export of subsidized agricultural goods and outsourced some industrial jobs to Mexico. However, Mexican farm products are finding it hard to compete with cheap agricultural products produced at large farms in the US. Despite some job losses due to trade, NAFTA, on balance, has been beneficial to all. The real problem has been the inability of NAFTA countries to compete with products coming from emerging Asian markets, particularly China, where technology and labor productivity are improving rapidly. China has replaced Mexico for cheap labor-intensive products in the US market. A strategic reason to compete against foreign countries could provide further stimulus to NAFTA member countries to cooperate.

At the hemispheric level, the Free Trade Area of America (FTAA) has been formed with members from both North and South America. As the progress of the FTAA has slowed down, twelve South American Nations have signed a Treaty for the creation of the Union of South American Nations (UNASUR) by 2020. The Treaty envisages a South American parliament and a common currency like the EU. Growing communication linkages in the region are adding to the prospect of the common market.

The Asia Pacific Economic Cooperation (APEC) was formed in 1989 to promote economic cooperation among Asia Pacific countries, extending from Asia to the Americas, to Australia. Its membership has now expanded to twenty-one countries. India also has shown interest in becoming a

member. To further promote economic advancement in member countries through open trade, APEC has decided to move step-by-step towards the creation of free trade, as envisaged in the Bogor Goals, by 2020. An agreement has been reached among member countries in freeing trade in such sectors as chemicals, medical equipment, forest products, environmental services and technology, energy, telecommunications equipment, fish and fish products, toys, and gems and jewelry. In all, fifteen sectors have been identified, out of which nine are the priority sectors. APEC member countries extend trade benefits to fellow members on MFN basis. The Association of South East Asian Nations (ASEAN) countries, who are also members of APEC, have agreed to abide by this principle. APEC may be relegated to the background if it fails to move towards free and open trade as envisaged at its foundation.

At the heart of the APEC is the US economy, so the growth and dynamism of the US economy is the key to its existence. Notwithstanding the avowed goal of APEC, there are differences among key member countries. Agriculture is well protected in Japan as part of its food security policy. It continues to resist US and Australian calls for opening the sector. The US also has currency, tariff, and intellectual property issues with China, and is also protecting farmers against foreign competition through tariffs and quotas. As member countries are slow in taking decisive steps towards free and open trade as envisaged in the APEC goal, APEC member countries are looking for alternative free trade arrangements.

The Trans-Pacific Partnership (TPP) was established in 2006 with the initiatives of APEC countries such as Brunei, Chile, New Zealand, and Singapore as members. The US, Australia, Malaysia, Vietnam, and Peru have joined the body. Member countries in the TPP have made commitments to eliminate tariff barriers on all products in 10 years. It has been termed as a "21st century agreement" in that it includes issues not addressed generally in conventional free trade area groupings, such as: competition, cooperation and capacity building, cross-border services, customs, e-commerce, environment, financial services, government procurement, intellectual property, investment, labor, legal issues, market access for goods, rules of origin, sanitary and phyto-sanitary standards (SPS)s, technical barriers to trade (TBT), telecommunications, temporary entry, textiles and apparel, and trade remedies.[1]

The problem with the TPP, however, is that all current member countries except the US are net exporters. The US is the only net importer in the region. In the situation of current economic crisis, it does not have extra appetite to liberalize its import regime further. While China can take in more US imports as it moves towards consumption-led growth, it is not yet a member and has shown no interest to join it. Japan also has not joined it. In the current circumstance, the growth of trade in the TPP region with free trade areas would likely to be marginal. China, Japan, and South Korea are also exploring a free trade agreement as a counterweight to the TPP. In October, 2009, they held a summit in Beijing to explore the economic feasibility of establishing a free trade area. The idea was further discussed among representatives of these countries on the sidelines of the East Asia Summit in Bangkok on October 2009. In May 2012, the three countries signed an agreement on investment and furthered talks on creating a free trade area.

The East Asian Summit (EAS) was started in 2005 with 10 ASEAN member countries plus China, South Korea, Japan, India, Australia, and New Zealand. The US and Russia have also become members now. Since its establishment, member countries have signed several declarations, including a Declaration on East Asian Energy Security, as part of Comprehensive Economic Partnership for East Asia (CEPEA). Yet their commitments to serious regional cooperation in East Asia are very low. The EAS is more like a forum for discussions on political and economic environments in Asia than a serious regional economic grouping. Moreover, China does not seem enthusiastic about the grouping as

it sees ASEAN + 3 (ASEAN plus China, South Korea and Japan) much more representative of East Asia.

South Asia

Regional economic cooperation started since the establishment of the South Asian Association for Regional Cooperation (SAARC) in 1985. It is moving from a preferential trading arrangement towards being a fully functioning free trade area. Currently, intraregional trade is the lowest in South Asia. Trade in energy was envisaged as a regional economic arrangement, but has not taken off. As South Asia lies between West Asia and South East Asia, and has easy access to Central Asia, its development is the key to the economic prosperity of these regions. Moreover, the location of South Asia at the heart of Indian Ocean gives it added advantages to have easy access to East Africa and West Australia. The prosperity of South Asia would immensely help the economic transformation of Asia. Accelerated economic growth in China and India has already started to make a positive impact on these regions, providing them opportunities to diversify their economic relations instead of depending solely on OECD (Organization for Economic Cooperation and Development) countries for economic growth. With growth picking up in Africa, the Indian Ocean is increasingly becoming much more economically vibrant.

South Asia is as large as the EU in terms of territory and larger than China in terms of population. Over the years, total foreign debts have gone up in South Asia as development activities are expanding. As debts multiply, there is a possibility of looking outward rather than inside the region, weakening regional economic impetus. So there is a need to keep debts within manageable limits. Intraregional linkages are as necessary as interregional linkages. Regional economic cooperation in trade and energy can provide opportunities for promoting social and economic development in South Asia. At the twelfth SAARC Summit in Islamabad, member countries adopted a social charter to place people at the heart of economic development. They have pledged to accord the highest priority for the alleviation of poverty.

As the most populous region, South Asia accounts for 23 percent of the world's population. Though literacy rate have gone up over the years, it is still the lowest worldwide. In terms of the absolute number, there is a huge illiterate population. India is the largest country in the region, accounting for 77 percent of the landmass of South Asia. The size of its economy at present is seven times larger than the combined economies of Pakistan, Bangladesh, Sri Lanka, Nepal, Bhutan, Afghanistan, and the Maldives. Given India's size and centrality, therefore, it has greater sway over the economy of the region. It has contiguous borders with Pakistan, Nepal, Bangladesh, and Bhutan. Even Sri Lanka shares its maritime boundaries with India. Afghanistan embraces both Central Asia and South Asia. It has close historic ties with South Asia since time immemorial.

Nepal, Bhutan, and Afghanistan are landlocked. Cooperation with transit countries such as India and Pakistan is vital for the development of their economies. Nepal shares borders with India on three sides: east, south, and west. In the North, it shares border with Tibet (the autonomous region of China). Due to rugged territory, economic intercourse with Tibet is limited. However, in recent years, improved infrastructure in Tibet has caused an increase in the flow of goods, services, and people between China and Nepal. Most Nepali industries are in the Terai in the southern part of the country, which is well connected to Indian transportation networks. Calcutta provides an outlet for the export of goods to overseas countries. It also serves as a means of reaching the sea for Bhutan. For Afghanistan, Karachi is the nearest sea port.

The 2011 Global Hunger Index (GHI), a tool developed by International Food Policy Research Index (IFPRI), shows that GHI scores for South Asia are at a very high level (Table 1.1) despite rapid economic growth. According to the 2011 GHI Report, a score above 20.0 is officially considered alarming, between 10.0 and 19.9 is termed serious, between 5.0 and 9.0 is moderate, and low is

deemed 4.9 and below.[2] In terms of absolute number, India has the largest amount of hungry people in the world. Both India and Bangladesh are at the 'alarming' level of hunger. China ranks far below South Asian countries in hunger index.

Table 1.1: The Global Hunger Index Score by Rank, 1990 and 2011

Rank	Country	Year, 1990	Year, 2011
70	Bangladesh	38.1	24.5
67	India	30.4	23.7
54	Nepal	27.1	19.9
59	Pakistan	25.7	20.7
36	Sri Lanka	20.2	14.0
4	China	11.7	5.4

Source: International Food Policy Research Institute, Global Hunger Index (2011)

Although rapid economic growth has helped lift significant numbers of people out of poverty in South Asia, a large number of people are still living below the poverty line. Table (Table 1.2) shows adult literacy rates, population growth rates and population numbers for those living below the income poverty line in the region.

Table 1.2: Poverty in South Asia

Country	Adult Literacy rate (% aged 15 and above)	Population Below Income poverty line (2000-2007) (%)		Total population (In million)	
				2007	2020
		$2 a day	National Poverty Line (2000-07)		
Bangladesh	53.5	81.3	40.0	157.8	185.6
India	63.4	75.6	28.6	1,164.7	1,367.2
Nepal	56.5	77.6	30.9	28.3	35.3
Pakistan	54.2	60.3	32.6	173.2	262.2
Sri Lanka	90.8	39.7	22.7	19.9	21.7
Total				1,543.9	1,872.0

Source: UNDP Human Development Report (2009).[3]

Removing poverty is a major challenge confronting South Asia in the twenty-first century. The region is home to the largest number of the world's poor in terms of absolute numbers. As it succeeds in reducing poverty, it will have a positive impact on the world's economic and political environment. Since India occupies a central role in South Asia, its success in combating poverty would be crucial. There is an urgent need to improve per capita food and water availability, general health care and literacy rates in the region. The population of India is projected to increase to 1.3 billion in 2020 and other South Asian countries are projected to also register significant population growth. Despite high economic growth, per capita income in the region is lower than in East Asia. Much can be done to accelerate economic growth through regional cooperation in trade, energy, and water sharing.

As past experience has shown, accelerated economic growth alone can help reduce poverty. A joint action to confront poverty can create a conducive environment for economic growth. Economic growth in the region so far is largely the outcome of economic liberalization. Regional economic integration has not yet received the priority it deserves. Intraregional trade remains low. Political instabilities in Nepal and Pakistan, combined with legacies of their past policies, have hindered intraregional trade expansion. Regional cooperation in trade and energy has the potential to expand intraregional trade to new heights and reduce poverty in the region. Economic growth requires energy, and much of energy needs can be met through active regional cooperation among South Asian countries, as well as between South Asia and Central Asia and West Asia. Central Asia is rich both in hydropower and natural gas, while West Asia is rich in natural gas.

South Asia: Shared Social, Political, and Economic Dimensions

South Asia is a very diverse region in terms of ethnicity, language, race, religion, and culture. A study by the Indian Genome Project published in April 2008 has confirmed the diversity of Indian people in terms of genetics. It identified five clusters of the population in India: the Indo-European, Dravidian, Tibeto-Burman, isolated and religious groups of the Himalayas, groups that are predominantly Dravidian, but share some genetic similarities with others, and tribal groups of Central Asia and Eastern India.[4] Muslims living in regions where dominant groups surround them share genetic similarities with these other groups. The northern part of India is largely populated by Indo-European people, the southern part by Dravidian, and the north-east and Himalayan regions by Tibeto-Burman.

This ethnic and racial diversity has given rise to linguistic diversity. Pakistan and parts of Bangladesh share similarities with the genetic characteristics of North Indians. A pan-Asian study conducted by the Human Genome Organization (HUGO) in 2009 has found that peoples living in Southern India and the rest of Asia are genetically closer. Humans came from Africa to India and then moved to other parts of Asia. People living in the same region and sharing the same language and culture are closely related genetically. Genetic diversity varied from Southeast Asia to North Asia. The study found that older the age of population, greater was the genetic diversity[5].

India and Nepal are predominantly Hindu, but the former has a larger minority population of Muslims. Afghanistan, Pakistan, and Bangladesh are Islamic countries, but the latter has a large Hindu population. Sri Lanka and Bhutan are Buddhist countries, but have significant numbers of Hindus. Afghanistan and Pakistan are predominantly Sunni Muslim, but there is a large proportion of Shia. Even within a religious group, there is diversity in terms of ethnicity, language, caste, and sub-castes. Notwithstanding the differences, people inhabiting the region share a common Asian culture that transcends race, caste, and ethnicity. The land and topography of the region have also greatly affected each culture's development.

The British ruled India, Pakistan, Bangladesh, and Sri Lanka for 200 years. They laid down an infrastructure and irrigation system in Punjab. Infrastructure provided the quick movement of troops and the movement of food grains in case of emergencies. At the same time, it facilitated the intraregional movement of goods and services and people, thus strengthening age-old culture further. The British also introduced common laws. Bangladeshi economist Shobhan Rehman writes about this succinctly:

> The unified labor market was undertaken by an integrated capital market, which together served as a common market for goods and services. The coin of Arungajeb was convertible from Lahore to Dhaka and Golkonda in the South even when he was at war with Shibaji. The currency served to sustain a common market for goods not only within the Mughal Empire but in its peripheral states including what is now Sri Lanka and beyond in Southeast Asia, and what is known as West Asia. This

> unified market survived the collapse of the Mughal Empire and was expanded and further integrated by the British. Under the British Raj, the rupee was a common currency not only in what is now South Asia but also in the littoral states of the Arabian/Iranian Gulf[6].

Rehman attributes the failure to address the interests of various national communities as the single most important factor for the disintegration of the Indian Union. The Moghul Empire inherited this integrated economy from the Mauryan Empire, including a network of roads connecting the subcontinent, which they made further improvements to. With the British came a change in the economic structure in the region and a structural shift in direction of trade flows. Karachi became far more important in trade than in earlier periods. The laying out of the railways crisscrossing the continent and the opening up of the Suez Canal contributed to the change in the structure of the economy. Rehman writes, "With the expansion of railway network and the opening of the Suez canal in 1869, trade was diverted to Karachi [instead of] to Calcutta and Bombay. Karachi claimed 61.6 percent of Punjab's overseas imports and 55.26 percent of its overseas exports specially"[7].

Before the partition of the subcontinent, South Asia was one economy with the free flow of goods, services, labor, and capital. The territory that comprised modern-day Pakistan produced cotton, but its share in factory made cloths was insignificant. Bangladesh produced jute, but there was not a single jute mill.[8] The economy was further disintegrated with the emergence of India, Pakistan, and Bangladesh as separate national entities. They each pursued economic policies away from the region. India adopted inward looking policies with the public sector as the commanding sector and the private sector occupying a secondary role, while other South Asian countries pursued policies of private sector development and trade diversification to reduce their dependence on India.

However, import substitution was the common policy of all South Asian countries. Pakistan reduced economic contacts with India with the result that in just short span of time, trade with India, which was substantial earlier, was reduced to a negligible level. Other south Asian countries also provided economic incentives to divert trade away from the region. The long-term costs of these policies to South Asia in terms of social and economic development were high. They led to a widening gap further away from East Asian countries, which had accelerated ahead with outward looking strategies.

The Present Situation

Over 60 percent of people in South Asia are dependent on agriculture for living, though that sector's share of GDP is going down (Table 1.2). The central task for South Asian countries is to siphon off excess population from agriculture into other sectors. Manufacturing can absorb much of the excess population, yet its share of GDP is far lower than in China, which has succeeded in attracting foreign investment in that sector and in raising exports. The services sector is the largest, accounting for over 40 percent of GDP in South Asia.

It has been widely believed that differences in levels of economic development bring about regional specialization; countries at the lower rung of economic development would export low skill products to countries at the upper rung. The early industries in economic development, therefore, would include low skill products such as textiles, toys, and leather goods. As countries develop, they start to export high technology products. In case of India, the development path has taken a non-conventional route: its services sector is driving the economy. Tourism, finance, remittances, and information technology are accelerating the growth of the service sector, which in turn is providing impetus for the growth of manufacturing industries.

Table 1.3: Structure of Output

	GDP (millions)		Agriculture as % of GDP		Industry as % of GDP		Manufacturing as % of GDP		Services as % of GDP	
	1995	2008	1995	2008	1995	2008	1995	2008	1995	2008
B'desh	37,940	79,554	26	19	25	29	15	18	49	52
India	356,299	1,159,171	26	17	28	29	18	16	46	54
Nepal	4,401	12,615	42	34	23	17	10	7	35	50
Pakistan	60,636	164,539	26	20	24	27	16	20	50	53
Sri Lanka	13,030	40,565	23	13	27	29	16	18	50	57
China	728,007	4,326,996	20	11	47	49	34	34	33	40
Japan	5,247,610	4,910,840	2	1	34	29	23	21	64	69

Source: World Bank: World Development Indicators, 2010

This growth in services was fueled by globalization of trade in services. This type of economic globalization has questioned long held assumptions about the services trade, namely: that it is driven by domestic demand, that in developing countries it is considered to have lower productivity, and that service jobs in developing countries are mostly poorly paid[9]. Over last few years, the Indian business environment has become much more business friendly. Large amounts of money are being funneled into textiles, steel and aluminum, cement, construction, chemicals, fertilizers, and auto and ancillaries. These developments are rapidly transforming the manufacturing sector. According to the 2010 Global Manufacturing Competitiveness Index Report, with high skilled manpower, India is moving up the manufacturing technology ladder. Currently, it ranks second to China in competitiveness index[10]. Its engineering exports are increasing rapidly. With economic growth picking up, Pakistan is also pouring investments into the leather, textile and clothing sector. If the Indian economy continues to grow at a high level, it could act as a growth engine for the region as a whole. Further economic liberalization in other South Asian countries that are accompanied by trade facilitations, could open up opportunities for investments from Indian companies, which in turn would help build comparative advantages of the region vis-à-vis other regions. South Asian countries have been very cautious to open up to each other. It is only recently that India has withdrawn restrictions on Pakistani FDIs in India. Earlier, as trade was restricted, smuggling thrived through third country ports. There is also a high level of smuggling across the land border with Bangladesh, largely due to high levels of non-tariff barriers to Bangladeshi imports into India.

In case of Nepal and Bhutan, India permits its companies to make rupee investments subject to the condition that they abide by government regulations. With respect to investments in other South Asian countries, special permission from the Indian government is required. At the 14th SAARC meeting, India had indicated its readiness to liberalize its trade regime on a non-reciprocal basis for the least developed countries in the region. There was also a realization among member countries of the need for raising the level of investments in physical infrastructure and in human capital in order to

expand the share of manufacturing. Inefficient infrastructure and the low level of skilled labor have hindered the expansion of manufacturing activities.

Regional Cooperation in Trade and Energy in South Asia

According to the 2008 Annual Human Development Report, 1.6 billion people are living without electricity in the world, of which 45 percent are living in South Asia, 14 percent in East Asia, and 35 percent in Sub-Saharan Africa[11]. Regional economic cooperation offers opportunities for cooperation in energy issues, which is vital for overall economic development. India, which is recording high economic growth, is already in an acute shortage of energy. It is expected to grow further with rapid industrial development. Much of the momentum India has achieved in recent years will peter out if it fails to meet growing demand for energy. According to the Indian government's power survey published in 2007, the peak demand for electricity will reach 152, 746 Mw in India by 2011-12. The peak demand was 75,556 mw in 2003.[12] By 2011-12, the annual consumption would be over 755,847 Gwh.[13] The demand for electricity would be significantly high. India has received an approval for a civilian nuclear deal signed with the USA from NSG (Nuclear Suppliers Group). Even if India meets the targeted 20,000 megawatts of nuclear power by 2025 as planned, it will still be insufficient to meet much of the demand for the energy. India can meet much of its energy needs from South and Central Asian countries (hydropower from Nepal and Bhutan, natural gas from Burma, Bangladesh, and West Asia, and natural gas and hydropower from Burma and Central Asian countries).

Demands for energy are also growing in other South Asian countries. Laying gas pipeline and hydropower infrastructure from Central Asia and West Asia to India through Afghanistan and Pakistan would also help meet pan-Asian energy needs. Pakistan and Afghanistan can also meet their energy needs and earn a substantial amount of money from transit services to other South Asian countries. Pakistan's demand for natural gas and hydropower is also increasing rapidly. Moreover, a gas pipeline project and hydropower infrastructure would strengthen economic links not only within South Asia, but also between South Asia and Central and West Asian countries, paving the way for larger economic cooperation in the future. Pakistan, Afghanistan, and Central Asian countries can benefit immensely by nurturing economic links with all South Asian countries. By boosting trade in energy, South Asian countries would reap substantial development and security benefits.

South Asia can benefit from trade in energy. Regional economic cooperation in the energy sector can lower costs of energy, increase security, safeguard the environment, and make economic growth self-sustainable.[14] Most importantly, as energy costs go down, it would expand intra-regional trade. Energy security through the regional option is economical and aids in economic development. Experience from the South African Power Pool (SAPP) and Nord Pool (NP) suggests that regional cooperation in energy brings in significant gains to member countries.[15] The SAPP has brought twelve countries together for joint financing cooperation in the regional trade in energy. All countries in the region are expected to save substantial amounts of money through the optimal use of their energy systems. However, barriers to regional cooperation need to be overcome. This would require broad political support to regional development. Institution building in the energy sector is a foundation for regional development.

In the past, South Asian countries went completely for national interests rather than for regional ones, despite the immediate economic and security gains they would have reaped by working together. The policy has disrupted the sense of the common community that South Asian countries had traditionally inherited, with the result that it has estranged one country from another. A conducive regional environment is essential for economic cooperation. Realizing the importance of regional cooperation in energy, South Asia has initiated some efforts towards establishing an energy ring in the region. A SAARC Energy Centre has been set up in Pakistan and studies have been undertaken to

assess future prospects of trade in energy in the region. Some efforts have been made by the USA through SARI in dealing with energy issues from a regional perspective. However, there are still barriers to regional economic cooperation that need to be overcome. This would require broad political support to regional development in South Asian countries. There is a need to address policy issues, privatization, and infrastructure development. Member countries should also undertake efforts for the development of water resources to meet growing national demands for energy. Bilateral and regional approaches to water development would complement each other.

The Aim of the Book

The adoption of the WTO rules and economic liberalization worldwide, and the advancements in communications have stimulated globalization. At the same time, countries are grouping together to protect their national interests against globalization through regional economic cooperation. Therefore, the growing number of regional cooperation arrangements we see today is partly a response to globalization and partly a quest for greater economic competition and a larger market. The interaction of globalization and regionalization is shaping the global trading system. This book discusses where South Asia stands in the great change taking place in the world economy. Energy is vital for economic development. How South Asia is planning to meet its growing energy needs is addressed in the book. Chapter Two discusses the profound effects of globalization on production and marketing. It also highlights prominent trade issues being brought up for negotiation under the aegis of the WTO. How successful the Doha Round has been in addressing South Asia's development issues is discussed in this book. The labor standard and environmental issues are also touched upon. How South Asia is bringing economies in line with developments in the global business environment is also discussed briefly in the chapter.

Chapter Three reviews the progress of regional economic integration in South Asia and the hurdles the region is facing for the establishment of a fully functioning South Asian economic community. It underlines the fact that new developments in the world economy require closer cooperation among South Asian countries than those existing so far. That regional economic cooperation and integration is growing worldwide is discussed in Chapter Four. Driven by economic growth, regionalization is growing in Asia. China's role in intensifying regional integration in Asia is examined. Its growing investments, particularly in Tibet and Xinxiang, are opening up opportunities for Central and South Asian countries. India's similar push for economic contacts with West and East Asia as part of its foreign policy is bringing significant economic fortunes for both India and these regions. Growing economic cooperation between India and China and between India and ASEAN countries is further bringing South Asia and East Asia much closer economically.

How the demand for energy is increasing in the region is brought into sharp focus in Chapter Five. India's water relations with neighboring countries are reviewed; hydropower, irrigation, and flood control benefits that India has enjoyed are explained. Chapter Six highlights the prospects of an electricity trade in South Asia and between Central Asia and South Asia. Chapter Seven looks afresh at South Asia's prospects for building strong economic linkages with West Asia, Central Asia, and East Asia. Given centrality of South Asia in the Indian Ocean, regional cooperation in trade and energy could play a very important role for the economic development in Asia as a whole.

Notes

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2

ECONOMIC GLOBALIZATION AND SOUTH ASIA

Lazer and Shaw state that the rise of "globally oriented conglomerates—rooted in two or more nations, possessing tremendous financial leverage and market power, combining product lines, merging global distribution systems, capitalizing on their combined marketing know-how, realizing efficiencies and cost savings from scale economies worldwide, and generating seamless multinational marketing networks"[1] has brought significant changes in production and marketing activities around the world. In other words, they have literally transformed the global business environment. Along with these have come changes in attitudes towards foreign companies. The mindset about global companies particularly in developing countries has gone through a remarkable transformation. Earlier, global companies were viewed as exploiters and destabilizers. Today, there is a realization that the lives of the vast number of people who live at the bottom of the pyramid can be transformed if companies are allowed to serve their needs. Economic reforms have been introduced to create an environment for the free play of entrepreneurship, procuring initiatives and growth so that companies can help contribute to economic development.

The rise of global companies is itself an outcome of advancements in communications technology and the expansion of WTO activities around the world. Advancements in communications technology have made it easier to work at any location and manage both production and employees abroad through cloud-based computing and storage, electronic mail, video-conferencing, and telephony. It is helping companies in three ways: 1) through the instantaneous transmission of large amounts of data over long distances, 2) by helping buyers and sellers obtain/produce information that contributes to the globalization of demand, and 3) by contributing to the globalization of supply and thus to the globalization of competition among suppliers in many sectors[2]. This has also opened up opportunities even for small companies to compete in world markets. Through the use of computers, companies can bypass wholesalers and importers and establish contacts with foreign customers directly. Most importantly, technological developments are helping both big and small companies to move value-chain activities to locations around the world, where costs are lower. Out-shoring and outsourcing are important business today to spur economic growth strategies.

Today most products are not produced at one location, but at different locations. The result has been the growth of worldwide trade in components and parts. The world market is increasingly be-

coming global. For example, in the case of the textile industry, yarn is made at one location, clothing, tailoring, and designing are done at other locations[3]. Each location is important in production and marketing activities. It is notable that the percentage share of wages in total production costs has gone down. Each location contributes its specialty and the final result is that value addition is less than what it would be had it taken place at one location under a conventional business model. This kind of new business has given rise to the growth of production sourcing networks as part of trade between companies and their affiliates. Value chain activities are rapidly merging national markets into regional markets and regional markets into the global market. Within OECD countries, a large part of the trade that takes place is between companies and their subsidiaries. The aging population in developed countries has further given impetus to the globalization of business. Developing countries are attracting more and more international companies with their younger workforces and reductions in tariffs and non-tariff barriers. Many US companies are outsourcing their jobs to India, China, Israel, the Philippines, and Ireland.

This is not one-way traffic. They are also outsourcing jobs to United States and other countries. Outsourcing jobs to the US is at a lower stage at present, but as these economies grow, it will pick up further. According to the US Department of Labor, the value of the US exports of "legal work, commuter programming, telecommunications, banking, engineering, management consultancy, and other private services jumped to $131.01 billion in 2003, up 8.2 from the previous year"[4]. Imports of services, on the other hand, reached $77.38 billion for the year, thus posting net export of $53.63 billion[5]. According to some US estimates, by 2010 as much as 90 percent of their Research and Development (R& D), design, and manufacturing will be in either China or India[6]. It is significant to note that the US enjoys a surplus in trade and services despite significant number of jobs outsourced abroad. The value of outsourced IT (information technology) and business process (BP) services was estimated at about $260 billion in 2001.[7] The value of outsourced business services from the US alone was $26 billion in that year.

For companies, outsourcing is an important strategy to reduce costs, avail themselves of skilled foreign manpower, and be competitive in the market. It already involves such activities as billing, payroll, training, and tax assessments. Outsourcing is also moving towards other services such as legal, finance, R and D, and biotechnology. By delegating some business activities abroad, companies are devoting their resources to core activities while their foreign subsidiary companies are taking care of secondary activities at lower costs.

Globalization has also provided opportunities for tapping natural resources. Japanese companies, for example, have owned huge forests in the USA, Canada, and Australia. In the pursuit of natural resources and markets, companies from the Middle East, China, and India are also following Japan and other OECD countries by making their way into developing and developed countries. Since WTO activities and financial liberalization are the major forces that are profoundly affecting the global business environment in recent years, we will examine these issues below.

The WTO

Since the establishment of the World Trade Organization under the Uruguay Round, world trade has increased dramatically, crossing over 30 trillion-dollar mark in 2010. This is despite the fact that imports of agricultural goods, footwear, and textiles and clothing are still subject to strict regulations. During the tenure of the General Agreement on Tariffs and Trade (GATT), developing countries were exempted from any trade liberalization. They continued to protect their markets through high tariff and non-tariff barriers, but many products that were of export interest to them, were either denied or restricted entry into their markets by developed countries. There were no reciprocal or bilateral obligations as under the WTO. GATT had a narrow agenda, which was the elimination of tariff and non-tariff barriers. In the goods sector, it left important areas such as agriculture and textiles out-

side its purview. Given the importance of these two sectors in developing countries, it was not surprising that the GATT was termed as a rich man's club. Many developing countries remained outside it. Today membership in the WTO has expanded. A large number of developing countries including least developed countries have joined this body. A powerful coalition of a Group of 20 developing countries has come into being, espousing the cause of all developing countries at world trade talks.

The WTO has gone beyond conventional trade to include agriculture, textiles, trade in services, trade related intellectual properties (TRIPS), trade related investment measures (TRIMS), dispute settlement, procurement, etc. Unlike its predecessor, it has the power to enforce the rules of trade and disciplines. Since its establishment, several rounds of talks have been held. In each round, the concern of participating countries is focused on the elimination of tariff and non-tariff barriers, both in goods and services, on the strengthening of intellectual its property regime, the phasing out of multi-fibre agreements, and the integration of the least developed countries into the mainstream of international trade. However, building a consensus among member countries on how to resolve this last problem has been difficult, yet there is a move in the positive direction. None of the member countries want to see the failure of WTO talks.

Below, we will briefly discuss some of the important WTO agreements and highlight some important issues, which still have not yet been fully addressed but have the potential to wreck the whole WTO process in the future.

Agreement on Agriculture

This Agreement aims to establish a free market oriented trading system in agriculture through the elimination of trade barriers. From this perspective it addresses the following: commitments by member countries to expand market access and reduce domestic support and export subsidies. Despite the goals, there is no fair competition in agriculture trade. In developing countries, a large number of the population is dependent on agriculture for living. It is also a source of exports and foreign exchange. In developed countries, huge amounts of subsidy are provided to protect farmers. Subsidies have distorted agricultural prices in the world market so much that developing countries have found it virtually impossible to compete—even in the areas where they have competitive advantages. The EU, the USA, and Japan are each supporting their agricultural farms and dairy industries, which means they have each raised a high wall against overseas competition. The US is providing subsidies to cotton growers such as export guarantees and crop payments. It is reluctant to reduce subsidies as it has strong domestic interests to look after.

However, the reduction of these types of subsidies is essential for the reduction of world poverty. With subsidies intact, developing countries simply cannot compete. Developed countries spend $1 billion a day in agriculture subsidies. The EU's share of agricultural subsidies to its member countries is three times what the US provides to its domestic sector. The reduction of subsidies would, therefore, not only provide food- producing countries, including those in Sub-Saharan Africa, with export opportunities, but it would also help rich countries allocate their economic resources more rationally where these are needed most. This would thereby create an environment for the increased exchange of trade in agricultural goods. Developing countries, which have protected their own farm sectors with high tariff and non-tariff barriers, would also benefit greatly from the liberalization of this sector. Chile, for example, was able to expand its agricultural exports and provide high-wage employment opportunities with the liberalization of this sector[8].

Under the WTO Agreement, member countries have made commitments to move towards the imposition of tariffs in place of all non-tariff barriers and to reduce domestic and export subsidies gradually. Tariffs would be reduced by 36 percent in the case of developed countries and by 24 percent in the case of developing countries. The least developed countries are not required to make any

reduction. Member countries are not required to make any reduction with respect to "green box" policies, such as government services. As there is a danger that the purpose of WTO agreements on agricultural trade may be undermined by manipulative sanitary and phyto-sanitary measures, general consensus on what phyto-sanitary needs are must be reached to protect interests of legitimate exporters—one based on scientific information and larger economic interests.

Agreement on Textiles and Clothing

The textiles and clothing sector was excluded under GATT, as the sector was highly protected in developed countries. However, it was subjected to a special arrangement called the Multi Fibre Arrangement (MFA), under which individual developing countries were offered some limited quotas on products of export interest to them. Even in these product areas, competition from Newly Industrializing Developing countries such as South Korea, Hong Kong, Taiwan, and Singapore was intense. Even small and less competitive countries were offered quotas. Developed countries have started to phase out quotas from January 2005 after 40 years of protection of the sector. In most of the product areas opened for competition under the WTO, China has emerged as a major beneficiary. Other developing countries such as India, Pakistan, Bangladesh, Mexico, South Korea, Vietnam, and Indonesia are also making significant gains. They are competing both in price and quality. The textile industry still employs thousands of people in industrial countries and is a major source of earnings to the exchequer, so voices are raised from time to time for restricting imports.

Agreement on Trade in Services

The share of services today stands at about 20 percent of world trade. As countries globalize further, the share of the services trade will further increase. Thus, because of its growing importance, it has been brought under the WTO. Earlier GATT rules simply kept it outside its coverage. The General Agreement on Trade in Services (GATS) is a new addition. Member countries are required to eliminate all forms of discrimination in trade in services under it. Part I of the Agreement defines the scope of trade in services. The Agreement covers all four modes of service deliveries. Of the four modes mentioned in GATS, the movement of personnel is the least traded category as human immigration is strictly controlled in every country. The second mode, travel and tourism, is far below the value of other two modes. Part II deals with obligations and disciplines required on the part of member countries. There is also a transparency requirement under which all relevant laws are required to be published. Part III mentions market access. Each member country is entitled to treatment no less favorable than accorded to the other member.

Under the positive approach adopted by GATS, member countries can open the sector which serves their legitimate development interests. However, with respect to the sector, they should prepare a schedule of commitments specifying: "a) terms, limitations and conditions on market access, b) conditions and qualifications on national interest, c) [any] undertaking relating to additional commitments, d) where appropriate, the time-frame for implementing such programs, and, e) the date of entry into force [sic] of such commitments"[9]. The progressive liberalization of trade in services is mentioned in Part IV. Part V spells out how to handle dispute settlements. The Agreement has four important annexes: movement of labor, financial services, telecommunications and telecommunication services.

In rich countries, the service sector is a major source of GDP. For example, in the US, the sector accounts for over 80 percent of GDP. Developed countries are much more specialized and competitive in the sector than developing countries, where it is still in the infancy stage. However, as the share of services in total trade has started to expand, developing countries are increasingly giving attention to the sector. Overall, trade in services in both developed and developing countries is far more restrictive than trade in goods. As services are nationally sensitive, countries are reluctant to open up the

sector fully. Governments have monopolies over several services areas; they weigh political repercussions before they make concessions to open up.

More than 50 percent of world trade in services comes from direct foreign investment (mode-3: commercial presence). It is followed by mode-1: cross border supply (e.g. outsourcing), mode-2: consumption abroad, and then mode-4: presence of natural persons. The liberalization of the movement of natural persons has been virtually negligible as its share in total service trade is less than 1.5 percent. The inclusion of this mode under the WTO, however, has been in discussion in every country. Liberalization in the sector would be painfully slow, but on the positive side, many service activities are being brought into competition worldwide. This has remarkably expanded the contribution of the service sector to the world economy from what it was two decades ago.

Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPs)

Intellectual property rights include trademark and patent rights. During the Uruguay Round of Negotiations, developed countries argued that their rights were infringed upon in less developed countries by allowing local companies to produce goods without paying royalties to the companies created them. The infringement of rights is a loss of market for companies and a loss of taxes to the government that allows them to operate. Less developed countries were initially against the inclusion of any kind of agreement on intellectual properties under the WTO. They argued that international bodies such as the Paris Union were the right places to deal with such issues and that the inclusion of such issues would only distract the WTO from its main focus, but they had to give in. Further, less developed countries argued that if the interests of foreign companies were to be protected, there would be no creativity and the prices of important products like pharmaceuticals and foods would go up to the extent of royalties paid. They expressed their willingness to provide protection to the process through which products are manufactured, but they were against protecting products. The contrasting positions only exacerbated problems between developed and less developed countries.

To deal with these problems, rules have been crafted under the Agreement on Aspects of intellectual Property Rights (TRIPs), including Trade in Counterfeit Goods. The Agreement has three important parts. The first part sets out the scope of obligations, specifically national treatment. The term, national treatment, is one of the principles of international trading system that states that no discrimination should be made against the other WTO member country regarding tariff concessions or any other preferences. So each member should accord national treatment to the other member country no less than accorded to its own nationals. Part II deals with standards concerning the availability, scope and use of intellectual property rights. It is very comprehensive as it deals with several issues, such as: copyright and related rights including rental, computer programs, the protection of performers and producers of phonograms, geographical indications, industrial designs, patents, rights of patent holders, and protection of patents. Part III contains general obligations. Many countries have started to amend patent and trademark acts in line with the WTO agreement.

Dispute Resolution

Dispute settlement is a major task of the Dispute Settlement Body (DSB). The power the DSB has acquired over the years has made it much more effective in enforcing agreements than its predecessor, GATT. Dispute settlement occurs in the following stages: consultation, panel review, adoption of the report, and ruling implementation. Disputes are generally settled through consultation outside the courts. According to the WTO Annual Report, 2011, since the creation of the DSB in 1995, 419 disputes have been brought before Dispute Settlement Body.[10] The US, the EU, Canada, Brazil, Mexico, and India are most active users of the body. Cases have covered subsidies, biotech products, anti-dumping measures on footwear, grains, rice, dairy products, bananas, steel, aircraft, hides and skins,