Chapter 7
Role of SAARC in Convergence of South Asian Economies

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ABSTRACT

The objective of the chapter is to analyze the role of SAARC in regional integration, trade convergence in south Asia. It also highlights the pattern and direction of export and import, share in world trade, preferential trading in South Asian countries. With strong and improving macroeconomic fundamentals, the South Asian region is well established on a high growth path. Based on secondary data on South Asian trade collected from South Asian Economic reports and other statistical volumes, the study observes a decreasing trend of export during the period 1990-2011. Consequently, the overall intra-regional trade intensity index decreased to 1.5 in the year 2010 from 4.2 in the year 2005. SAARC and SAFTA have not contributed in integration and convergence of South Asian Countries rather lead to trade divergence.

INTRODUCTION

The South Asian Association for Regional Cooperation (SAARC) was formed by eight south Asian Countries, like Bangladesh, India, Nepal, Pakistan, Sri Lanka, Bhutan and Maldives in 1985 for regional cooperation and integration. These economies aimed at progress towards regional integration. Later in 2007, Afghanistan also became a member of the organization. Recent economic progress of South Asian countries has been impressive. As per Asian Development Bank (ADB, 2011), macroeconomic fundamentals of the region have been strong as it has continued to experience an economic growth of more than 6 percent per year during the last decade. The pace and scope of globalization and trade has been unprecedented since 2000. Integral to the expansion of global trade and investment flows has been the rise of the dynamic South Asian Countries – a new breed of dynamically growing developing countries taking a more significant place in world trade and investment. This phenomenon has also led to a rapid expansion in trade among developing countries –especially in Asia. South Asia’s potential to take itself to greater heights is real. However, it still faces a regional poverty situation that is nothing
short of severe. The region is home to 40% of the world’s poor, with 29.5% of its population living on less than $1 a day. While almost a quarter of the world’s population lives in the region, South Asia accounts for only 3% of global gross domestic product (GDP), 1.9% of world exports, and 1.7% of world foreign direct investment (FDI). As with globalization, regional economic cooperation and integration are seen as a route to economic prosperity. This is the direction that this study pursues. Present data on South Asia show so much untapped economic opportunity: of the region’s total trade volume of $517.5 billion in 2007, only 4% was intraregional trade. Given the advantages of proximity, and the similarity in production structures and levels of technology, plus the familiarity of cultures, it is likely that a more pronounced set of benefits will accrue from intraregional trade and investment. Despite the establishment of the South Asian Association for Regional Cooperation (SAARC) in 1985 to promote economic growth and development through active regional collaboration and cooperation, and even as the SAARC Preferential Trading Arrangement (SAPTA) and the South Asian Free Trade Area (SAFTA) took effect in 1995 and 2006, respectively, to stimulate trade and foster deeper integration and regional cooperation, full liberalization and cooperation did not take off. High levels of protection persist. South Asia still suffers from prohibitive tariffs and the distinction of having the highest interstate barriers to trade. SAFTA’s annexed negative lists remain substantial. Interstate mobility is hampered by visa rules. Moreover, the exclusion of services and investment from SAFTA renders the agreement toothless in significant areas. Intraregional investment within the region, as well as trade, remains meager. To broaden and deepen existing agreements and strategies, three parallel initiatives are necessary: deepening SAFTA by reducing not only tariff barriers but also nontariff barriers (NTBs); focusing on key industries to demonstrate the process and benefits of reforms more succinctly; and expanding the scope of SAFTA to include trade in services and investment.

The emergence of the dynamic South and the spectacular growth of South Asian trade and investment flows – now seen as a corner stone of the new trade geography – present an important window of opportunity for all countries, regardless of their level of development. South Asian regional trade agreements (RTAs), including bilateral, regional and interregional free trade agreements (FTAs), form part of an array of important instruments for trade creation, investment and regional development. Policymakers in developing countries are increasingly giving priority attention to enhancing South Asian trade through regional and interregional cooperation arrangements. In this context, the experience of Asia, where about 85 per cent of total South-South trade in goods is now concentrated, can be considered as of practical value and holds lessons for other developing countries and South Asian accounts for the largest population consisting of 1.47 billion people among all regional coalition in the world. Although almost all the South Asian nations enjoyed a powerful and strong cultural tie among each other, the most efficient among them were India, Pakistan and Bangladesh who shared a common market and integrated market and monetary system till 1947. A spirit of regionalism supported the endeavor of the association to unite the incongruence set of European countries and to create an affluent bloc. However, in retrospect it was pre-mature and a top-down endeavor at promoting regional cooperation, since ground realities in terms of trade and investment flows, and political will were not really in place to support such an effort. Thus it was regarded as the least integrated region of the world. Further the decision of the member countries to adopt Preferential Trade Liberalization promoted much of trade diversion than trade creation making the rich countries richer and poor countries poorer and establishing a Free Trade Area which was much taxing. This led to the establishment of South Asian Preferential Trade Arrangement (SAPTA) in 1995 which marked the first major political breach for the SAARC towards regional agreement on economic