

## **Potential for Regional Integration in South Asia: Lessons from the EU**

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### **Introduction**

South Asia is home to 2 billion people, roughly constituting more than one-third of the world's poor.<sup>1</sup> The region is plagued with poverty and issues of under-development despite having an enormous potential for a promising future. India and Pakistan, two of the largest economies in the region, are home to 855 million people living on less than \$2 a day.<sup>2</sup>

Bilateral relations between India and Pakistan can be described as rocky at best. The two countries, since independence, have been in one conflict or another, mainly due to their territorial issues, primarily Kashmir. All these points of contention have continued to prevent the two from having stable economic relations. In 1948-49, India and Pakistan surprisingly had quite a lot of trade, having more than 70% of its trading transactions with India.<sup>3</sup> However, what has followed throughout the years is a decline in their trading relations, owing largely to the tensions between the two countries. Although illicit/third country trade between the two countries — estimated at around \$1.5 billion per year continues, both countries remain hesitant to establish normal neighbourly trading relations.<sup>4</sup>

Figures suggest that intra-region trade facilitates economic development of a region. The European Union (EU) is a good case in point in this regard. Regional integration has greatly benefited the EU countries. Drastic increase in the GDP of Spain, Germany and France in 1999 following the launch of Euro as official currency by the EU, befittingly explains this trend. The EU, ever since the economic integration has remained the main trading partner for most of the European countries. France's top ten trading partners mostly consist of

EU members, seven to be precise.<sup>5</sup> Meanwhile, Germany and Spain also have the European Union as their largest trading partner. In the year 2019, the total exports of France valued around \$556 billion, out of which \$447 billion went to EU member states, amounting to about 80% of France's total exports.<sup>6</sup> Similarly, the EU contributed to roughly 77% of Germany's export value in 2019, and around 83% of Spain's export.<sup>7</sup>

Following the economic success of the EU as a win for regional integration, there was an increase in unionised economic cooperation globally, such as the formation of the Association of South East Asian Nations (ASEAN) economic community. The organisation helped Southeast Asia achieve remarkable economic growth, with ASEAN's GDP now being the fifth largest in the world.<sup>8</sup> Although SAARC was formed with a similar aim in mind by the member states, things have not been quite as desired for the organisation. South Asia has comparatively lagged in efforts to boost regional economic cooperation, where its intraregional trade accounts for barely 5% of South Asia's total trade.<sup>9</sup> In fact, regardless of the geographical proximity of the countries, the region's trade seems to gradually decrease over the years. In 1948, Pakistan's trade with India was worth 56% in exports and 32% in imports.<sup>10</sup> In the year 2020, Pakistan's total imports are about \$50 billion, just \$1 billion of which was from India, making it 2.01% of the total.<sup>11</sup> While, in the same year India's export valued to about \$323 billion just \$8.2 billion of which was to Bangladesh, making it as low as 2.55%.<sup>12</sup> These statistics, given the countries' geographical proximities, may seem surprising to one unfamiliar with the dynamics of South Asia, however, bearing in mind the political climate of the region, are nothing unexpected.

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The dynamics related to trade between the India and Pakistan were not always as tense, having bilateral trade valuing close to 5% of their total world trade.<sup>13</sup> However, in 1965 things began to deteriorate in the wake of another war, bilateral trade was immediately suspended after the first civilian prisoners of war were taken by Indians from the Wagah border.<sup>14</sup> A trade embargo was imposed between the two countries, that although was eased after the signing of Tashkent Agreement in 1966, yet the embargo ended only in 1974 with the official signing of the Simla Agreement in November same year.<sup>15</sup> Similarly, both states met the idea of the creation of SAARC with scepticism, fundamentally seeing it as a tool that could be weaponised by the other to further advance in their enmities.

Trade relations between India and Pakistan remained uneven yet continuous. India accorded Pakistan with the status of Most Favoured Nation (MFN) in 1996. Same year, Pakistan's list of items to be legally imported from India increased to 600.<sup>16</sup> The relations were disrupted in 1999 as a result of fighting in Kargil, leading to another suspension in trade relations. What followed soon was the aftermath of 9/11, further exacerbating the differences between the two rivaling countries. The situation began to change only when Vajpayee announced his efforts to improve relations between the two countries in 2003.<sup>17</sup> Four rounds of trade talks between 2004 and 2007 followed, a promising development in the bilateral relations, however, wounded greatly by the Mumbai Attacks in 2008. Consequentially, India ended all trade ties with Pakistan despite the country's insistence on not being involved with the incident.<sup>18</sup> It was in 2011 when both states finally had a fifth round of talks improving the relations and Pakistan granted India Most Favoured Nation (MFN) status, in November same year. From the year 2005 to 2019, although Pakistan's exports remained at around \$350-400 million, yet Indian exports increased from \$577 million to almost around \$1.9 billion.<sup>19</sup> Some have argued how one of the reasons continuous and consistent trade is unlikely between the two countries is the non-complementarity of trade, however a close analysis of the trade patterns

presents a completely opposite picture. The two frequently import and export goods of mutual interests to and from other countries, costing them a lot more than it would to trade such goods from each other. For instance, Pakistan is the second largest tea consuming country in the world, making most of its import from Kenya whereas importing it from India would cost the country \$20-25 per tonne cheaper, yet only 3% of tea is imported from India.<sup>20</sup> Similarly, although India is one of the top iron ore producing countries yet Pakistan looks for costlier alternatives like UAE. Another relevant instance is India's refusal to import cotton from Pakistan, even though Pakistan provides for a cheaper alternative to the Gulf region. However, even when either state depends upon the others' product, it imposes heavy taxes on goods, for example the 46.6% duty on Indian truck tyres.<sup>21</sup> Moreover, India favours a fairly expensive underwater route rather than an overland, cost-effective route through Pakistan, for Iran-India gas pipeline.<sup>22</sup> Both states continue seeking much more expensive alternatives than trading with the other due to prevalent trust deficit.

Pakistan remains of the view that without solving pre-existing problems between the two countries, it is impossible to lay a stable foundation for economic relations. As precedents suggest, international institutions play a vital role in helping resolve such issues, for example the initial role that the EU played in bridging the gap between France and Germany. Today these countries are each other's top trading partners. However, the problem that keeps SAARC from making somewhat of a similar development is the Article X (2) of the organisation's charter, which states, "Bilateral and contentious issues shall be excluded from the deliberations."<sup>23</sup> Hence, the organisation's inability to address issues of such fundamental importance hinders any effort or ideas that it makes towards regional progress.

Although there remains some trade between the two countries, it constitutes as a microcosm of what it could be given their potential. The estimates of the potential for bilateral trade between India and Pakistan go as high as \$10 billion or 2% of their combined trade with the rest of the world.<sup>24</sup> Being two of the biggest economies

of the region, their relations weigh heavy on the entire progress of South Asia and inevitably that of SAARC.

The functionality of SAARC in the context of intraregional trade then, is substantially dependant on India-Pakistan relations. A stable relation between India and Pakistan is crucial for any effective efforts of SAARC for economic integration. Hence, a revision in the organisation's charter on non-interference in bilateral issues may be a step in the right direction. SAARC providing the two adversaries a mediatory role may help ease tensions or at the least work on shifting the focus of their bilateral relations more towards economic rather than political. As seen in the case of Germany, France and the European Coal and Steel Community, trade most often than not, contributes to peace and cooperation between parties, helping them focus more on their mutual economic benefits over other contentions. Hence, better trade may guarantee a more secure political climate in the region. Developing trade between the two countries is a hard yet promising task, given the potentials as well as the trade records that are continuing unofficially. One of the steps that can be taken is through the simplification of the technical barriers that exist between their bilateral trade, including facilitation of cross border movement of

good, bringing to official trade-able items list the goods that are being traded through unofficial means and the elimination of other non-tariff barriers to trade. Operationalising the South Asian Free Trade Area (SAFTA) may also prove to be a promising step in the process. Increase in trade cooperation will not only act as a factor in subsiding political tensions, yet prove more cost-effective to both countries that today find more expensive alternatives than trading with each other. Hence, with lower prices for countless consumers, the two countries can work towards addressing issues that both states face collectively such as poverty and economic disparities. Another initiative could be resuming the Composite Dialogue Process (CDP) from 2004. The past initiative had some sort of a push in effective bilateral communication which was only hindered by the Mumbai Attacks of 2008.<sup>25</sup> A restart in the CDP will help open the door for positive and effective bilateral communication. A shift of focus from political to economic relations with the mediation of SAARC may not only help with the ineffectiveness of SAARC but will also help in stabilising the relations between India and Pakistan and consequently, help the region find peace and stability.

## Notes and References

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