

# ISAS Brief

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## **New Trade Links:**

### **A Step towards Asian Economic Integration?**

*The sheaf of trade- and investment-agreements that India and Bangladesh have now signed will open up opportunities for New Delhi to look at, and beyond, its near-East neighbour – towards the eastern arc of Asia.*

Deeparghya Mukherjee<sup>1</sup>

Bangladesh and India together accounted for 85% of South Asia's Gross Domestic Product (GDP) in 2013, with India alone accounting for about 79%.<sup>2</sup> Since 1971 when Bangladesh was formed as a sovereign nation-state, a handful of initiatives have been taken to improve the trade and investment linkages between the two countries. However, disagreements on a host of issues – the Teesta water-sharing, the stalemate on the Land Boundary Agreement (LBA) until recently, and issues concerning cross-border terrorism – have often proved to be impediments to maximal economic benefits through mutual engagement.

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<sup>2</sup> Calculated by the author using World Bank statistics (<http://data.worldbank.org/region/SAS>)

Bangladesh is still listed by the World Bank as a low-income country, while India is a lower-middle-income country in this classification. Bangladesh aspires to become a middle-income country by 2021.<sup>3</sup> Even as India has been trying to overcome poverty through multiple schemes, Bangladesh's Grameen Bank (a micro-finance institution) has been held out as an example which other countries might want to follow for poverty-alleviation purposes. On the other hand, Bangladesh has been struggling with its energy situation, and in the recent past India agreed to supply 100-MW electricity to Bangladesh from Tripura as well as 250-MW from West Bengal.<sup>4</sup> There are multiple aspects in which Bangladesh and India could be credible economic partners on matters of trade and investment. Currently, India enjoys a trade surplus with Bangladesh, and the bilateral trade amounts to about US\$ 6.5-billion.<sup>5</sup> While India was originally a principal trading partner of Bangladesh, China has overtaken India since 2004. Easier access to Chinese markets, and non-tariff barriers from the Indian side, are said to be responsible for this.<sup>6</sup> Most studies indicate that, apart from the purely economic factors, non-tariff barriers like delays at major trade routes, customs 'harassment', visa-related issues, rigid bureaucracy and infrastructural hurdles have ailed the trading relations between India and Bangladesh. Studies also recognise a significant amount of unofficial trade between the two countries.<sup>7</sup> The Chinese on the contrary are believed to have taken active steps to ease the entry of goods from Bangladesh into their markets. In fact, in spite of India's concessions to Bangladesh under the Asia Pacific Trade Agreement (APTA) and the South Asian Free Trade Agreement (SAFTA) – zero-tariff on all products, other than those in the sensitive list, as applicable to all the least developed countries (LDCs) – trade between the two countries did not pick up much momentum.

In the backdrop of such concerns, and India's renewed focus on improving the climate for trade and foreign investment in the domestic manufacturing sector through the "Make in India" initiative, as well as New Delhi's long-standing "Look East" policy, it can be seen that a robust trade- and investment-relationship with Bangladesh will be critical not only in itself

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<sup>3</sup> See "Perspective Plan of Bangladesh 2010-2021- Making Vision 2021 a reality" ([http://bangladesh.gov.bd/sites/default/files/files/bangladesh.gov.bd/page/6dca6a2a\\_9857\\_4656\\_bce6\\_139584b7f160/Perspective-Plan-of-Bangladesh.pdf](http://bangladesh.gov.bd/sites/default/files/files/bangladesh.gov.bd/page/6dca6a2a_9857_4656_bce6_139584b7f160/Perspective-Plan-of-Bangladesh.pdf))

<sup>4</sup> See "Tripura to supply 100MW power to Bangladesh" 7 October 2014, *Times of India* (<http://timesofindia.indiatimes.com/india/Tripura-to-supply-100MW-power-to-Bangladesh/articleshow/44588026.cms>)

<sup>5</sup> See "Bangladesh Offers 2 Special Economic Zones to Indian Companies" (<http://www.ndtv.com/india-news/bangladesh-offers-2-special-economic-zones-to-indian-companies-769498>)

<sup>6</sup> See Islam (2008) "Bangladesh-China-Northeast India: Opportunities and anxieties", Report No. 36, Institute of South Asian Studies Insights, Dhaka.

<sup>7</sup> See Taneja, N. (2001) 'Informal Trade in the SAARC Region', *Economic and Political Weekly*, 36 (11) 959-964

but also for India's links with the Southeast Asian countries. Bangladesh is located strategically between the India's state of West Bengal and Northeast which forms a gateway to Southeast Asia. Southeast Asia is an economically vibrant region, and India has interests in integrating more actively with this region through trade and by participating in the production value-chains. The opening-up of borders for easier transit of goods and services through Bangladesh would bring down the transport costs of Indian products targeted to Southeast Asian countries. Similarly, India could provide easier access for Bangladesh products bound for Nepal and Bhutan. It is in this context that the latest visit by India's Prime Minister Narendra Modi to Bangladesh and the deals signed are of particular interest.

Apart from the successful exchange of the instruments of ratification of the Land Boundary Agreement (LBA), during Mr Modi's visit to Dhaka, agreements were also signed to facilitate India's trade with Bangladesh, which will also help New Delhi connect with Southeast Asia and East Asia.

First, the two countries have reached an agreement on India setting up two Special Economic Zones (SEZs) in Bangladesh. One of these would be near the Bangladesh-India border. India is the third country, after China and Japan, to have evinced interest in developing a SEZ in Bangladesh. The US\$ 2-billion credit-line, announced by India, will help in developing these SEZs. They would also promote capital-intensive projects, which would improve and scale-up Bangladesh's road- and railway-infrastructure.

Secondly, the prospective investments by Reliance Power and the Adani Group to set up power plants (total investments worth US\$ 5-billion approximately) could be instrumental in solving Bangladesh's problem of power-deficit in a significant way. While one of these power plants would generate 3,000 Megawatt (MW), the other is slated to produce and 1,600 MW.<sup>8</sup> Three, the renewal of the 1972 protocol on Inland Waterway Trade and Transit (IWTT), in combination with the agreement on coastal shipping, has high importance for India, not only for trade with Bangladesh but also for trade with East and Southeast Asia. India's "Look East" policy cannot attain full potential without a healthy trade relation with Bangladesh, since Bangladesh is the nearest country that India encounters in the east. Four, India can integrate with the region, by using the ports of Bangladesh. A Memorandum of Understanding (MoU) was reached for India to use the Chittagong and Mongla ports. Five,

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<sup>8</sup> See "Reliance Power, Adani to Invest \$5 Billion In Bangladesh power plants during PM Modi's Trip" 6 June 2015, *The Economic Times* (<http://economictimes.indiatimes.com/industry/energy/power/reliance-poweradani-to-invest-5-billion-in-bangladesh-power-plants-during-pm-modis-trip/articleshow/47562538.cms>)

the Bilateral Cooperation Agreement between Bangladesh Standards & Testing Institution (BSTI) and the Bureau of Indian Standards (BIS) aims at achieving cooperation in the field of standardisation between the two nations. This will facilitate the recognition of goods produced by either country in terms of quality standards. Finally, the Kolkata-Dhaka-Agartala bus service and the Dhaka-Shillong-Guwahati bus service would create greater synergies through easier transit between India and Bangladesh, and further facilitate trade. The Life Insurance Corporation (LIC) of India has been allowed to start operations in Bangladesh, and this would also strengthen economic ties between the two countries.

Overall, Mr Modi's recently-concluded visit to Dhaka has key implications for the future of economic relations between India and Bangladesh. While several steps have been taken to improve bilateral trade and investment, the strategic locations of the SEZs now identified and India's likely investments there should also prove beneficial for New Delhi's links with Southeast Asia because of the anticipated reductions in trade costs. This would also help Bangladesh to reduce its trade costs in dealing with other countries in the region. However, implementation of these agreements in their true spirit at the ground-level will be crucial to realising their full potential. South Asia is no stranger to agreements and legal niceties on paper. Therefore, effective steps are required to reduce the information asymmetries among the economic agents who could benefit from these new opportunities. This holds the key to positive gains for both countries over the medium- to longer-term.

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