ISAS Working Paper

No. 45 – Date: 26 May 2008

469A Bukit Timah Road
#07-01, Tower Block, Singapore 259770
Tel: 6516 6179 / 6516 4239
Fax: 6776 7505 / 6314 5447
Email: isasijie@nus.edu.sg
Website: www.isas.nus.edu.sg

India's Attempts at Regional Integration with South Asia and East Asia[1]

Bibek Debroy[2]

Section 1: The South Asian Perspective

We begin this introductory section with a brief sketch of the South Asian background. The South Asian Association for Regional Cooperation (SAARC) is the largest regional organisation in the world, with India, Pakistan, Bangladesh, Sri Lanka, Nepal, Maldives, Bhutan and Afghanistan (since 13 November 2005) as members, and with China,[3] Japan, South Korea and the European Union granted observer status and distant prospects of Iran eventually becoming a member.[4] The present eight member states have[5] a combined population of 1.47 billion, compared to the world population of 6.56 billion in 2005. Had the SAARC been counted as a single political entity, it would have been the largest entity in the world, judged according to the population criterion. India with 1.12 billion (17.07 percent of world population), Pakistan with 165.8 million (2.53 percent of world population) and Bangladesh with 148.96 million (2.27 percent of world population) are among the ten most populous countries in the world. Interestingly, in 1907, the global population was estimated to be 1.7 billion and British India (India, Pakistan, Bangladesh and Myanmar)[6] chipped in with 264 to 314 million. To come back to the point, the SAARC region is the 7th largest land area in the world. National gross domestic products (GDP) are in home currencies and, for comparison purposes, have to be converted into a common currency, the typical numeraire being the United States dollar. This conversion can be done using the official exchange rate[7] or purchasing power parity (PPP), the latter incorporating the idea that non-tradeables like services are relatively cheaper in developing countries and relatively more expensive in developed countries and conversions must take this into account for a fair comparison to be made. In PPP terms, the overall SAARC GDP was US$4,074 billion in 2005, making the SAARC the third largest economic entity in the world, after the United States and China.[8]

Given this background, both South Asia and the SAARC should have been much more important in the world. However, any realistic assessment should accept that South Asia and the SAARC are both somewhat irrelevant. Wikipedia is a fairly commonly used encyclopedia. On the SAARC, Wikipedia offers the following:[9] "The SAARC's inability to play a crucial role in integrating South Asia is often credited to the political and military rivalry between India and Pakistan. Though Bangladesh and Sri Lanka have much warmer relations with India, they fear that the more integrated South Asia is, the greater will be India's dominance over South Asian nations. It is due to these political and territorial disputes that South Asian nations have not been able to harness the benefits of a unified economy.

Over the years, the SAARC's role in South Asia has been greatly diminished and is now used as a mere platform for annual talks and meetings between its members."

It is impossible to disagree with the general thrust, even with the last sentence. Nor is the centre of the world's economic clout South Asia. Instead, there are the three poles of North America (extended to Latin America), Europe (extended to Eastern Europe) and East Asia (including China, Japan and South Korea in an ASEAN plus 3 framework). South Asia may not be sub-Saharan Africa, but it hasn't mattered all that much. Within South Asia, it is India that is the locomotive, particularly since India has moved to a higher growth trajectory. And within the SAARC framework, India's relationships (including economic relationships) with Bhutan, Maldives, Nepal and Sri Lanka are reasonably warm and close, with these four countries already factored into the Indian growth locomotive. While it is early days yet, that should also be true of Afghanistan. The constraints remain relationships with Bangladesh and Pakistan.

South Asia's historical irrelevance isn't difficult to understand. South Asia has been one of the poorest regions of the world. In 2005, the SAARC region's PPP per capita GDP was US$2,777.[10] With the Atlas method, it looks bleaker still. It is small consolation that the work of Angus Maddison[11] shows that greater India (India, Pakistan and Bangladesh) accounted for 32.9 percent of world PPP GDP in the 1st century.[12] The share was 28.9 percent in 1000 ACE, 24.5 percent in 1500 ACE, 22.6 percent[13] in 1600 ACE, 24.4 percent[14] in 1700 ACE and 16 percent in 1820 ACE.

Per capita income is only an average indicator of a country's standard of living, or even poverty. The percentage of population below the poverty line is a better indicator and one can either use international poverty lines of US$1 or US$2 per day[15] or the national poverty lines. Data are easier to obtain for national poverty lines than for international poverty lines.[16] But in either case, data have to be obtained through consumer surveys of income or expenditure.[17] Subject to this, the percentage of population below US$1 per day was 36 percent for Bangladesh, 37.7 percent for Nepal, 34.7 percent for India, 13.4 percent for Pakistan and 7.6 percent for Sri Lanka. The percentage of population below the national poverty line was 53 percent for Afghanistan, 49.8 percent for Bangladesh, 42 percent for Nepal, 28.6 percent for India, 25 percent for Sri Lanka and 25 percent for Pakistan.[18] While poverty is an absolute concept, inequality is a relative one and there are different dimensions to inequality also. Does one mean inequality in personal distributions, or inequality across caste, class, gender, ethnicity and religion, or inequality in a geographical sense? If it is personal distributions, does one have in mind ownership of assets or distribution of income/expenditure? Since data are generated through household surveys and sometimes these are of income and sometimes of expenditure, there is a comparability issue, since income inequality is certain to be higher than expenditure inequality. Subject to this, the Gini coefficient of income/expenditure inequality was 30.6 in Pakistan, 31.8 in Bangladesh, 32.5 in India, 33.2 in Sri Lanka and 47.2 in Nepal. According to this criterion, with the exception of Nepal, the core of the SAARC region is relatively equal.

Income or expenditure poverty isn't the only dimension of poverty. Inadequate access to health or education is also an indicator of poverty. Some of these are captured in the United Nations Development Program's (UNDP) human development index (HDI), based on per capita PPP GDP, education (adult literacy rate, gross enrollment ratio) and health (life expectancy). A HDI below 0.5 classifies a country as belonging to the low human development category, between 0.5 and 0.8 places it in the medium human development category and a HDI value of more than 0.8 places a country in the high human development league. With a HDI value of 0.755, Sri Lanka leads the SAARC group, followed by Maldives with 0.739, India with 0.611, Pakistan with 0.539, Bhutan with 0.538, Bangladesh with 0.530 and Nepal with 0.527.[19] In the 1990s, many SAARC countries (except Sri Lanka and Maldives) moved from the low human development to the medium human development zone.

The simple point is that it is because South Asia has been poor that it has been relatively irrelevant. Low incomes mean lack of consumer markets, one key determinant of foreign direct investments (FDI), with resultant multiplier benefits. Low incomes raise the spectre of dependence on foreign aid official development assistance (ODA), although doubts can legitimately be raised about effectiveness and use of ODA and about whether ODA does actually lead to competitiveness and supply-side improvements. ODA inflows are also a trickle compared to export gains from liberalisation, provided developed countries open up their markets, especially in agriculture, but also in labour intensive manufactured products. However, such market access liberalisation leads to benefits only if the exporting country is competitive and there is no automaticity about export gains. Liberalisation helps the efficient, but not those that are inefficient. Market access liberalisation in developed countries is a necessary, but not sufficient, condition for export success. This is especially important because, throughout the core of South Asia, a significant percentage of the working population is employed in agriculture. Typically, this is small land-holding agriculture, with little commercialisation and diversification and an emphasis on crop (even food-grain) output. Poverty and unemployment are both linked fundamentally to rural sector constraints – absence of land markets, inadequate credit, insurance, technology, market information and insufficient and inefficient public investments in rural infrastructure and extension services. There are the ingredients of a failed industrial revolution, with industry having failed to suck people out through offering employment opportunities and the service sector euphoria is not an opportunity every SAARC country can tap equally well. Given the sectoral compositions of GDP and of the working population, market access in developed countries is not only no panacea, since it simultaneously also brings the qui pro quo of liberalising in one's own country, there is the perception of a threat to livelihoods and food security consequent to liberalisation. This logic applies both to multilateral liberalisation through the WTO and to regional and sub-regional liberalisation.

To get back to the question of foreign aid, another issue should be flagged. Five of the eight SAARC members are least developed countries (LDCs) – Afghanistan, Bangladesh, Bhutan, Maldives and Nepal.[20] Although there is[21] a process for countries to graduate out of LDC status, there is a perverse incentive in favour of countries wishing to retain LDC status. Other than ODA, duty-free and quota-free access to markets and exemptions from commitments within multilateral agreements are privileges one loses if one graduates out of LDC status. Is there a case for Bangladesh and Maldives[22] to be classified as LDCs any longer?

The Millennium Development Goals (MDGs) are tangible and quantifiable goals[23] to measure the extent to which poverty alleviation (poverty interpreted broadly) is likely to happen in the developing world by 2015.[24] The third annual global monitoring report on MDGs states the following.[25] "South Asia, with gross national income per capita at US$594 in 2004, is home to 47 percent of the world's poor living on less than US$1 a day. Since 1990, the region has experienced rapid GDP growth, averaging 5.4 percent a year, which has helped to reduce the consumption poverty rate substantially. India has reduced its poverty rate by 5-10 percent since 1990; most other countries registered reduction in poverty over the period, except for Pakistan, where poverty has stagnated at around 33 percent (using national poverty lines)…. Looking beyond consumption poverty at other indicators of social progress, the region has had encouraging success in some areas: for example, mortality in children under five has reduced substantially between 1990 and 2004 (from 129 to 92, per 1,000), especially in Bangladesh (149 to 77, per 1,000), Nepal (145 to 76, per 1,000), and Sri Lanka (32 to 14, per 1,000), and appreciable gains have also been achieved in school enrolments at primary and secondary levels. At the same time, challenges remain in key areas such as child malnutrition, primary and secondary completion rates, maternal mortality, and gender balance in education and health outcomes; nearly half of all children under the age of five are malnourished in Bangladesh and Nepal, and youth illiteracy in the region is high – 18 percent for males and 35 percent for females. The resurgence of tuberculosis and the threat of HIV/AIDS are also a cause for concern. In general, the quality of statistics on social MDGs needs to be improved considerably to make cross-country comparison meaningful. Progress in MDGs at the average national level masks considerable sub-national variation measured at regional (state, province, district, and block) level. The average progress in MDGs is also marked by persistent social inequalities mapped on caste, region, tribal and ethnicity dimensions. This is true not just for large economies such as India with wide state-level and district-level disparities but also for smaller countries of the region such as Nepal and Bangladesh….. Sustained growth will be necessary for poverty reduction, and concomitant improvement in institutional service delivery mechanisms will be essential for achieving progress in all other dimensions of the MDGs." If one ignores goals (7) and (8), this quote effectively states that South Asia is behind target on goals (4) to (6) and also on the gender disparity goal of (3), but may very well attain goals (1) and (2), with the former largely attained because of the growth effect.

Poverty has also figured prominently in the SAARC agenda, ever since the 6th Summit in Colombo in 1991.[26] The Declaration at the 13th SAARC Summit held in Dhaka in November 2005 had three direct paragraphs on poverty alleviation and two additional ones on funding mechanisms.[27] First, 2006-2015 was declared as the SAARC Decade of Poverty Alleviation. Second, the SAARC Development Goals (SDGs), recommended by the Independent South Asian Commission on Poverty Alleviation (ISACPA), were endorsed. Third, implementation of the Plan of Action on Poverty Alleviation,[28] adopted by the 12th SAARC Summit in Islamabad in 2004 was emphasised. Fourth, a decision was taken to establish a SAARC Poverty Alleviation Fund, to function under the SAARC Development Fund (SDF), with the SDF possessing three windows – social window, infrastructure window and economic window. There are also regional poverty profiles.

Given the earlier quote about attainment of MDGs, the ISACPA's assessment on attaining MDGs should also be quoted, even though it is a long quote.[29] Since progress towards MDGs or SDGs is fundamentally a national responsibility, how does one factor in the SAARC umbrella? ISACPA suggested the following.[30] "The formulation of the SDGs allows for identifying areas which merit, and will benefit from, regional co-operation. These may include: Strengthening ongoing regional initiatives, such as on trade liberalisation/facilitation, investment promotion, infrastructure development and implementation of social charter, in order to ensure social development and pro-poor growth; Provision of regional financial resources for poverty alleviation and achievement of SDGs; the SAARC Disease Surveillance Network: activities may include developing early warning systems, promotion of regional indigenous medicine systems, regional co-operation in intellectual property rights in the health sector; Essential medicine; Prevention of human organ trade; Prevention of trafficking in women and children; Prevention of dumping of hazardous, including radioactive, waste; Wetland conservation in the region; Harmonising indicators and promoting low-cost monitoring methodologies." One can't but help feeling that these suggestions are vague and peripheral.

Why is South Asia poor? This is an extremely difficult question to answer. However, as the quotes from the afore-cited World Bank/International Monetary Fund and ISACPA reports both suggest, a key determinant of poverty reduction and employment generation is growth, although the composition of growth is also important. In turn, growth is a function of efficiency and efficiency is a function of competition. Liberalisation and reforms are about injecting this greater competition and represent a much broader canvas than the narrower focus of globalisation on free (or freer) cross-border flows of goods, services, labour, capital, technology and information. South Asia's competitiveness can thus be assumed to be an indicator of how far reforms have sunk in.[31]

Although there is subjectivity involved in the assessment[32], the World Economic Forum's Global Competitiveness Report (GCR) is an accepted measure of a country's competitiveness. The 2006-07 report covers 125 countries. The GCR's Global Competitiveness Index (GCI) is based on nine pillars – (1) institutions; (2) infrastructure; (3) macroeconomy; (4) health and primary education; (5) higher education and training; (6) market efficiency; (7) technological readiness; (8) business sophistication; and (9) innovation. The proposition is that the relative importance of these pillars changes as a country moves up the development ladder. When growth is driven by factor endowments, the first four pillars are the most important. Arguably, all the SAARC countries, except India, are at this stage. As a country moves up the development ladder to a stage where growth is driven by efficiency, pillars (5) through (7) become important and some segments of the Indian economy are at this stage. Finally, further still up the ladder, pillars (8) and (9) become critical. In the ranking of 125 countries, India comes in at 43rd, Sri Lanka at 79th, Pakistan at 91st, Bangladesh at 99th and Nepal at 110th. There is clearly some correlation between these rankings and acceptance of globalisation (and/or liberalisation), multilateral, regional and bilateral.

Such surveys do tend to incorporate value judgments, implicitly if not explicitly, and are subjective. However, the general point is the following. Since the 1980s[33], most economies in the SAARC region have implemented liberalisation, in one form or the other. These have been unilateral, part of structural adjustment packages or have been triggered by globalisation commitments[34]. Consequently, growth rates have gone up and are likely to go up even further. Savings/investment rates have increased, efficiency of capital usage has gone up,[35] there have been productivity gains and even some impact of the demographic dividend. The trickle-down effects of growth on poverty reduction are also evident, when there is something to trickle down. Obviously, the individual experience varies from country to country, but as a generalisation, the statement is probably correct. As a logical corollary, there have been two side-effects, even if they are not always very tangible. First, barring the agriculture problem, protectionist sentiments are much less now. In general, beneficiaries of liberalisation are consumers and losers can be inefficient producers. Consumer voices are heard a little bit more often and inefficient producer voices a little less. Second, there is a desire to jump onto the India Shining bandwagon for its resultant positive externalities. That too makes a SAARC process easier to accept.[36]

While growth is an indirect channel for reducing poverty, that does not eliminate the need for direct anti-poverty programmes in social sectors, or even targeted subsidies. Nor is it a case for the State to abdicate its responsibilities. However, public expenditure doesn't automatically lead to a tangible improvement in outcomes or deliver better public services. One shouldn't forget that with rising incomes and prosperity, citizens generally demand better public services and competition exists through privatised options that didn't exist earlier. One of the best antidotes to corruption is civil society vigilance and countervailing pressure and this includes the media, as well as non-government organisations. There are successful instances of such pressure having improved what can be called governance. This is in turn a function of whether political and civil liberties exist. The correlation between democracy and economic development has often been debated.[37] Arguably, such reforms that seek to improve governance have not occurred that fast throughout the SAARC region, unlike economic reforms that are commonly associated with structural adjustment programmes.

Section 2: The Indian Reform and Growth Story

After a brief sketch of the South Asian perspective, we move on to a sketch of India's reforms and the growth story.

One should begin by asking what one means by economic reforms. Sometimes expressions like first generation and second generation are also used, suggesting that the first generation reforms were introduced in the first post-1991 flush and that the second generation is what awaits us now. Unfortunately, the expressions first generation and second generation are never very precisely defined. However, two overlapping interpretations are possible. First, first generation refers to reforms that concern the external sector – elimination of quantitative restrictions on exports, rationalisation and elimination of export subsidies and their replacement by a system of export incentives[38], reduction in import duties, a market-determined exchange rate with a convertible rupee, a liberal policy on foreign institutional investments and opening up to FDI. On each of these, reforms have already been introduced, or there is a time-frame for their further introduction, although external sector reforms are also linked to negotiations, multilateral, regional or bilateral. They cannot always be introduced unilaterally. In contrast, second generation reforms concern the domestic economy, although a neat water-tight compartmentalisation between the domestic and the external isn't always possible. Understandably, political economy considerations and vested interests are stronger in domestic economic reforms, compared to the external. Second, one can also interpret the first generation as reforms that concerned and were under the purview primarily of the centre, or the Union government. In contrast, in a federal setup, second generation concerns reforms that have to be introduced at the state-government level.[39] Thanks to the first generation having been implemented, the focus of policy change has thus shifted from the centre to the states. The cutting, and the blunting edge, of reforms thus lies at the level of the states and different states have reacted differently to liberalisation. What is also of note is that most product market policies are with the centre, while most factor market (labour, land) policies are with the states.

On the first generation, that is, reforms in the external sector, the following bulleted points can be made. First, customs tax revenue as a share of total tax revenue has declined from 32.1 percent in 1995-96 to 18 percent in 2007-08.[40] Second, the average collection rate has declined from 29 percent in 1995-96 to 10 percent in 2006-07. However, higher-than-20 percent collection rates exist for food products, chemicals, man-made fibres and metals. Third, the peak basic customs duty for non-agricultural products is now 10 percent. Fourth, there is an avowed intention of reducing import duties to the Association of Southeast Asian Nations' levels, with a time-frame not quite specified. Fifth, the export/GDP ratio has increased from 5.8 percent in 1990-91 to 14.0 percent in 2006-07 and the import/GDP ratio has increased from 8.8 percent in 1990-91 to 20.9 percent in 2006-07.[41] Sixth, since 2002-03 exports of goods have grown every year by more than 20 percent in United States dollar terms, barring 2004-05, when they increased by more than 30 percent. Seventh, in total trade in goods, China's share has increased from 3.1 percent in 2001-02 to 8.3 percent in 2006-07 and China is now second to the United States (at 9.8 percent) in importance as a trading partner. Eighth, barring bindings at the World Trade Organization (WTO) in the course of the Uruguay Round, reductions in some special sectors like IT thanks to plurilateral agreements and some regional trade agreements (to be described below), trade policy reforms have fundamentally been unilateral.

Moving on to the second generation, beyond the taxonomy, there will be a reasonable degree of consensus about what the major pending reform areas are, the so-called agenda. At best, depending on one's perspective, there may be disagreement about the priorities. The following is a list of this core reform agenda.

(1) Reforms in the rural sector: Rural/urban has a census definition and according to the 2001 Census, 72.2 percent of India's population lives in rural areas. This is equated with earning a living from agriculture, but that is not quite true. Hence, there is an agricultural reform agenda and there is a rural reform agenda that goes beyond agriculture. Within the agriculture set, there are issues like allowing corporate sector involvement in agriculture, removal of government imposed restrictions on production, marketing and distribution,[42] refocus of public expenditure away from input subsidies to infrastructure[43] and extension services,[44] dis-intermediation of distribution chains, forward markets, contract farming, revamping credit and insurance, and freeing up of land markets.[45] All these are linked to encouraging commercialisation and diversification. There is also an issue of encouraging off-farm employment and this is where rural sector reforms kick in, through provision of physical and social infrastructure. Out of India's 600,000 villages, there are around 100,000 where both are hardly present.[46]

(2) Taxation reforms: These have both a direct and an indirect tax component, and the latter includes import duties. Barring agriculture, which is in a category of its own, the time-line for reduction in tariffs on industrial or manufactured products is reasonably clear. The broad shape of indirect tax reform is clear and has been set out. There should be a combined goods and service tax (GST), with service sector taxation integrated into a VAT (value added tax) framework instead of being a tax on turnover. This will be accompanied by a withdrawal of all other taxes like central excise, central sales tax, octroi, state-level sales tax, entry tax, stamp duties, transportation taxes and so on. All that has happened at the moment is a limited VAT, in the sense of unification of state-level sales tax, and the time-frame for introduction of a GST is 2010 onwards. A GST is also required to make the export incentive system WTO-compatible, introduce appropriate countervailing duties and allow better defence against anti-subsidy and anti-dumping investigations. Unfortunately, the mindset of allowing discretions and exemptions get in the way of standardisation and harmonisation. That apart, there is an even more serious issue of lack of financial devolution within states, down to urban local bodies and *panchayat*s. In its absence, it becomes impossible to eliminate local taxes. There is a parallel exemption issue for direct taxes, both for personal income taxes and corporate taxation.

(3) Public expenditure reforms: This has a centre, state and even local body aspect. Although the importance of each element is a function of the level of government that one has in mind,

a substantial chunk of public expenditure is on interest payments, wages and salaries and pensions. In the short-run, these expenditures are inflexible, although in the long run, one can borrow less, employ fewer people and enter into new pension arrangements with new entrants into the civil service. Compared to a work force of 375 million (the labour force is slightly larger at 400 million), 18.5 million people work for the government, including 3.5 million who work for the Central government and 6 million who work for the public sector. If one includes those who work for quasi-government bodies, the number increases from 18.5 million to around 30 million. On reforming civil services in India, several recommendations have been made. The issues of downsizing, identifying surplus manpower, retraining, voluntary retirement schemes, contractual appointments, lateral entry and evaluation and vertical mobility keep recurring and the reform agenda is also known. However, what are invariably implemented are hikes in salaries and a Sixth Pay Commission has now submitted its recommendations. This is estimated to cost anything up to one percent of GDP, if the impact on states and quasi-government bodies is also taken into account. In addition to borrowing and expenditure on the administrative machinery of the government, public expenditure also includes public services. These are not necessarily in areas where market failure exists, so that the classic public good argument has doubtful validity. Nor can a merit good argument be used, since subsidies are never targeted. That apart, expenditure is never linked to tangible improvement in outcomes and administrative costs of delivery are extremely high.[47] Yet, the present government has introduced or expanded several so-called public expenditure flagship programmes – National Rural Employment Guarantee, Sarva Shiksha Abhiyan,[48] the Mid-Day Meal Scheme, National Rural Health Mission, Jawaharlal Nehru Urban Renewal Mission, Bharat Nirman[49] and a Backward Regions Grant Fund. Had public expenditure alone been the answer, India would no longer have been poor and backward. This is the right place to mention why this paper will not list out two commonly-cited issues in the core reform agenda – budgetary deficits and infrastructure. The former is indeed important and there is a Fiscal Responsibility and Budget Management Act. However, deficits (fiscal or revenue) are symptoms rather than the disease and in the absence of revenue (tax and non-tax) and expenditure reform, talking about deficit reduction is neither here nor there. The second commonly-cited reform area that will not be listed separately is infrastructure, although there are estimates that if all infrastructure is available efficiently, the increment to GDP growth will be of the order of 1.5 percent. There are different kinds of infrastructure and what works for one kind of infrastructure, may not work for others.[50] Some parts of infrastructure are central government subjects, while others are state or even local body subjects. However, the reason for not listing infrastructure separately is a different one. In the absence of resolving the subsidy issue and appropriate user charges, the infrastructure problem will remain. That too, is a symptom rather than a disease.

(4) Law reforms: This category subsumes several different elements – statutory law reform, faster speed of dispute resolution and reforms of administrative law, so that procedural costs are eased. Within statutory law reform, there are issues of rationalisation and harmonisation across statutes that have been enacted at various points in time,[51] eliminating old laws that serve no purpose, junking unnecessary state intervention in many of these statutes and even introducing new legislation where none exists.[52] On faster dispute resolution, a new Arbitration Act has been in place since 1996, but conciliation/mediation is still not credible. Within the court system, there is an estimated backlog of 25 million cases stuck in courts, not including those that are stuck in quasi-judicial forums. There have been faster clearances in the Supreme Court, but not yet in High Courts and Lower Courts, with understandable variations across states. About two-thirds of pending cases are criminal ones. With amendments to the Civil Procedure Code in 2001 and 2002, dispute resolution should become

faster for civil cases and there is some evidence of this having happened. However, there hasn't been much progress on reforming the criminal justice system, despite a Malimath Committee on reforms in the criminal justice system having submitted a report in 2003. On the third strand of law reform, beyond civil service reform, the broader agenda of administrative law reform involves two kinds of relationships that can overlap – dealings between the citizen and the government and dealings between an enterprise and the government. The latter can again be divided into three phases of an enterprise's existence – entry, functioning and exit. The former involves birth certificates, death certificates, land titles, assorted requirements of establishing one's own identity and issues connected with accessing public services. For both the citizen and the entrepreneur, the years since 1991 have witnessed the exertion of countervailing pressure, documenting corruption and inadequate delivery of services, even if this countervailing pressure tends to be located in certain geographical parts of the country. Partly as a result of such pressure, a Central *Right to Information Act* has now been passed. Two commonly-cited items are again not being listed in this paper in the core reform agenda and an explanation is again in order. First, there is no separate listing of labour law reform, because that has been subsumed in this heading of law reform. Second, there is no separate listing of governance as a heading, even though that is a buzzword. While governance means different things to different people, this deliberate exclusion is because most items included in governance, unless one has in mind electoral processes, civil rights and a free press, have already been included elsewhere.

While there is no disagreement about these reform areas being important, why have the required reforms not been implemented? This is because of the political economy, not because these areas are unimportant, but because there is lack of consensus. And if one tracks the debate and distils out where there is lack of consensus, the debate boils down to one simple issue, regardless of the reform area. There is lack of consensus about the role of the government and core governance areas. The core governance areas for any state ought to be ensuring law and order, an efficient dispute resolution mechanism and intervention in some areas of physical and social infrastructure, sometimes through financing rather than through actual provisioning. It is because the Indian state is asked to do many more things that these four core reform agendas continually get stuck.

Notwithstanding this lackadaisical movement on most domestic reforms, barring the financial sector, there is no dearth of reports that are bullish about Indian growth prospects, some external, others internal or endogenous. Some of these are not concerned with the overall economy, but concentrate instead on segments like out-sourcing and software exports.[53] In this list of bullish reports, the most widely quoted continues to be Dominic Wilson and Roopa Purushothaman's 2003 paper, better known as the first Goldman Sachs BRIC (Brazil, Russia, India, China) report. Note that much of the spectacular increase in the BRIC report happens after 2020, not before. Note also that the Indian real GDP growth projected is much lower than what is prevalent internally, within the country. For instance, the BRIC report has average real Indian GDP growth of 6.1 percent from 2005-10, 5.9 percent from 2010-2015 and 5.7 percent from 2015-2020.[54] If there is disagreement between these external reports and those that emanate from within the country, that is primarily about this trend rate of growth of six percent or thereabouts, with an emphasis on the trend, as opposed to year to year fluctuations. Since reforms are equated with post-1991 developments, most external projections assume that 6 to 6.5 percent is the base-line rate of growth now. The key question is whether there has been another structural break in 2003-04, with a base-line trend growth of 8 percent or thereabouts. There are several reasons for such a belief. First, the savings rate has increased.[55] Second, the incremental capital/output ratio (ICOR) is now around 4, which suggests that real growth of 9 percent is eminently doable. There is yet another change that is sometimes ignored, at least in this context. The share of agriculture and allied activities in GDP is declining and that of services is increasing. What is pertinent is that the service sector tends to have a lower ICOR. That apart, if agriculture is growing relatively slowly and services is growing relatively fast, the sectoral shift from agriculture to services itself jacks up GDP growth as a statistical inevitability. Third, the effect of export growth on GDP growth is perhaps not always explicitly recognised. Fourth, while the demographic dividend and India's demographic transition is recognised, its impact on GDP growth is not always factored in, the BRIC report being an exception. Growth projections are thus based on capital inputs, ignoring the labour component and the Indian labour force is expected to grow at just below 2.5 percent a year between now and 2020. This labour contribution should itself add a clear percentage point to GDP growth, problems of education, skills and morbidity notwithstanding. Fifth, the population is young, with a median age of 24. This does things to entrepreneurship that we imperfectly understand. One should not therefore be surprised if GDP growth turns out to be something like 9 percent between 2010 and 2015 and accelerates to 10 percent between 2015 and 2020, ignoring the effect of exchange rate changes.

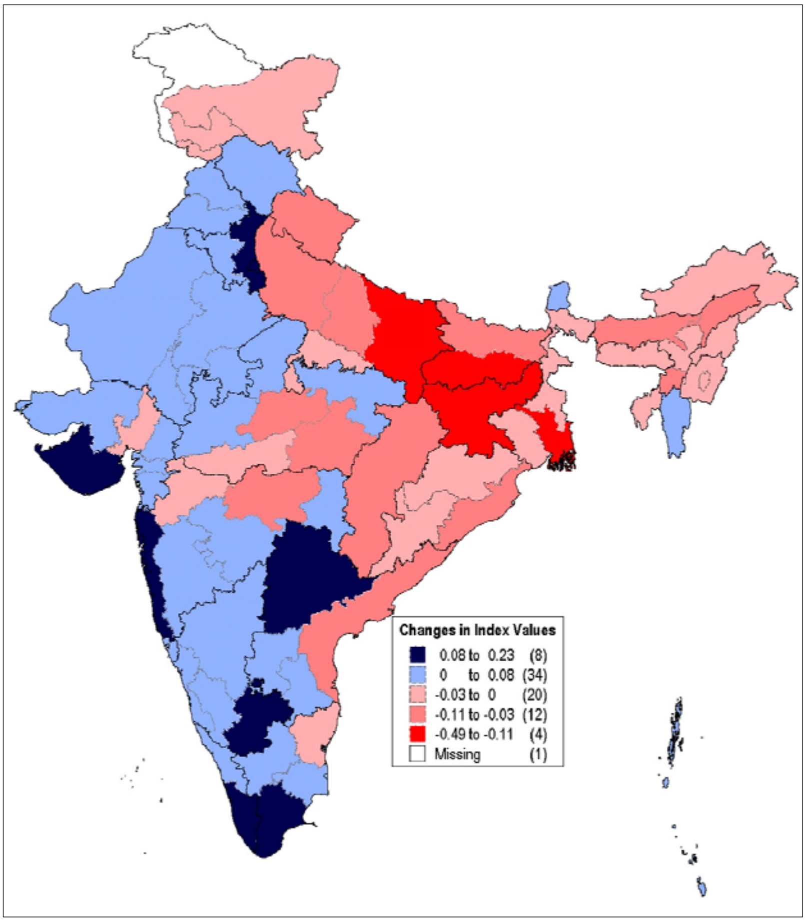
This much is known. But this is about overall growth, and there is also a point to be made about divides and disparities. This is one of India's most serious policy challenges. One interpretation of disparities is in terms of personal distributions of income. As was stated earlier, this doesn't seem to be a very important issue. Nor do disparities across caste, class, gender or religion seem to be that important.[56] The rural/urban divide seems to offer an imperfect understanding of what is happening in India today, although the divides are fundamentally geographical and spatial. To state the obvious, India is a large and heterogeneous country. There are wide divergences in development and in deprivation. Such disparities also exist in other large economies, the United States and China being two ready examples. However, the polity in China is completely different and the regional disparities in the United States are certainly not as high as they are in India today.

There are different ways to look at the economic geography of a country, depending on the administrative division one has in mind. State administrative boundaries are natural dividing lines to use. Academic work and popular impression have often used the BIMARU (Bihar, Madhya Pradesh, Rajasthan, Uttar Pradesh) nomenclature, with a pun on the word *bimar*, meaning ill or sick. While this is still useful as a starting-off point, the states of Bihar, Madhya Pradesh and Uttar Pradesh have now been sub-divided and Orissa is often worse than some of these four traditional BIMARU states. BIMARU thus becomes BIMAROU, not to speak of deprivation, according to some indicators, in Jammu & Kashmir and the North-East. Although undivided Madhya Pradesh and Rajasthan are no longer as deprived and backward as Bihar and the eastern parts of Uttar Pradesh, and Uttarakhand is better off than Uttar Pradesh, many of these traditionally backward areas tend to be concentrated in the North. In understanding India's development, especially after the 1991 reforms, one thus tends to often use a North-South framework.[57] Two simple explanations are often used to explain this phenomenon. First, in the pre-1991 era, when licensing and proximity to the centre that granted licenses was important, the North performed relatively better. With licensing having disappeared, at least for manufacturing, this relative advantage has vanished and the South has come into its own. Second, given the inadequacy of internal transport infrastructure, coastal regions, where this inadequacy is less manifest, tend to flourish. While both these arguments have a grain of truth, and property rights that govern land are also important, this North-South dichotomy is a trifle too simplistic, as is the East-West dichotomy, with a dividing line vertically drawn between Kanpur and Chennai, regions to the

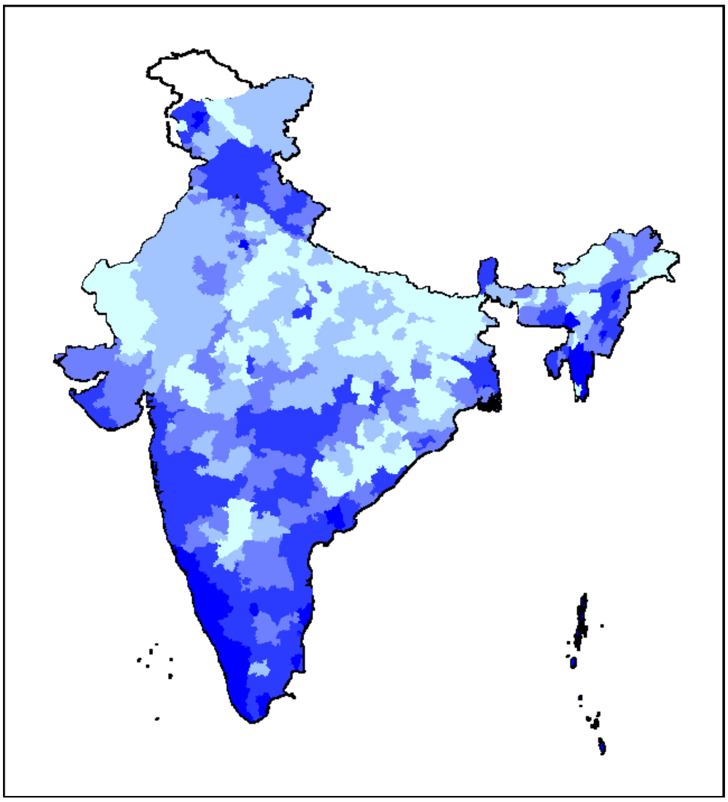
West of this line performing better than regions to the right.[58] Can the Indian polity handle these kinds of disparities? The answer is no. Can Bihar's flood problems be resolved without involving neighbouring countries?[59] Can Assam's flood problems be resolved without involving neighbouring countries? Can the North-East's infrastructure problems be resolved without neighbouring countries?

Indeed, the use of state boundaries to facilitate our understanding is itself somewhat flawed, since development and deprivation do not follow such administrative distinctions. However, there is an in-built bias in favour of using states, since data problems are easier to handle then. Data problems become more difficult to overcome if one thinks of India's regions, or even districts and villages.

The accompanying map is based on some work that Bibek Debroy and Laveesh Bhandari have done, using NSS (National Sample Survey) data on regions. Specifically, the question that is asked is the following. Has a region's share in India's overall economy, measured by growth variables aggregated into an index, increased or decreased in the post-1991 period? Constrained by choice of variables, this provides some answer as to what has been happening at the intra-state level. The time-frame is the 1990s, beginning with 1991-92. The broad regional picture is shown in the map. Blue shades indicate regions that have increased their economic share over time, the darker the shade of blue, the better. Red shades indicate regions that have declining economic shares over time, the darker the shade of red, the worse off the region is. This is, in that sense, a relative rather than an absolute map. The relative deprivation in Jammu & Kashmir, the centre, the East and the North-East is obvious.



Of India's 600 districts, around 100 are truly backward, by any objective criterion. The National Food for Work Programme had a list of 150 backward districts, the Rashtriya Sama Vikas Yojana increased the number to 167 and the National Rural Employment Guarantee Act originally had a list of 200 backward districts. Most of these backward districts are geographically contiguous and are also associated with violent movements. Similarly, out of India's 600,000 villages, around 125,000 are truly backward. Another map follows, based on identification of India's backward districts, done by Bibek Debroy and Laveesh Bhandari.[60] The lighter the shade, the greater the degree of backwardness. If one considers these backward districts, one notices that these are generally concentrated in Central India, extending eastwards, and going all the way up to the North-East, thus reinforcing the earlier impression. India cannot prosper if significant sections of India continue to be bypassed and marginalised.



The Institute for Conflict Management has a map of conflict in South Asia, through its South Asia Terrorism Portal. This shows an obvious correlation between deprived districts and intensity of terrorism or violence, at least at the all-India level. Apart from Jammu and Kashmir, which belongs to a special category, this correlation is obvious for the central parts of India, extending eastwards. There are spillovers of cross-border terrorism and arguably, there is a strong correlation between collective violence and economic prosperity, or its lack. India has a vested interest in reducing such regional socio-economic tensions and this cannot be done without cooperation with neighbouring countries.

Add to this the findings of a succession of reports by the Strategic Foresight Group. The most relevant is "The Second Freedom: South Asian Challenge 2005-2025".[61] If tensions can be eased, South Asian GDP will increase by between 1 to 2 percent. Alternatively, there is "Cost of Conflict between India and Pakistan".[62] Finally, there is "Final Settlement: Restructuring India-Pakistan Relations",[63] which raises a scary picture of conflict over water and requires a much longer quote.[64]

As the discussion of this section illustrates South Asia is important to India. Improved relationships with neighbours in South Asia are critical to India's economic and strategic success, and as and when necessary, such closer relationships need cross-subsidisation. But from this, it doesn't necessarily follow that the regional SAARC route is the best method to attain this objective. Bilateral agreements are also possible. Paraphrased a bit, the problem can be stated in the following way. The SAARC process has become equated with trade liberalisation, of the merchandise goods[65] variety and this is relatively irrelevant. How can the SAARC process be moulded and transformed to switch focus away from the trade agenda and focus instead on broader issues of economic development? That will partly be a function of what India seeks to do. And that indeed, should also be India's strategic intent, recognising that the SAARC remains a small component of the emerging Asian (or even South Asian) economic architecture. What are India's strategic goals? Are these best achieved through the SAARC umbrella, remembering that Myanmar is not a part of the SAARC? Within the SAARC, does one opt for a regional or sub-regional, even bilateral, option? It is indeed true that the South Asian economic space is India's turf, but is increasingly being imposed upon by China. China has become Bangladesh and Pakistan's largest trading partner and the United States is Sri Lanka's largest trading partner. However, recognition and addressing this threat doesn't necessarily mean that this has to be done through the SAARC route. Despite attempts to improve processes, warts and blemishes within the SAARC will continue. India needs to think of South Asia, rather than of the SAARC and ways of bypassing the SAARC process.

Section 3: SAARC and beyond SAARC

What is the SAARC? Is it a forum for advancing economic cooperation? Every SAARC Declaration now has significant sections on economic cooperation. The Report of the SAARC Group of Eminent Persons stated, "Looking at the SAARC in retrospect, the group felt that the association had passed through two distinct phases. The first phase was the preparatory phase, based on a gradual and step-by-step approach to initiating regional cooperation, mostly in non-controversial and peripheral areas such as confidence-building measures. The Integrated Programme of Action is an example of such an approach. It was during this phase that the minimum necessary institutional mechanisms were put in place for the operationalisation of a limited number of activities under the SAARC framework. In the second half of the evolution, the SAARC moved into its expansionary phase, when regional cooperation was expanded both in the social and core economic sectors. Many major commitments with far-reaching implications for the region, were undertaken, including the coming into force of the South Asian Preferential Trading Arrangement (SAPTA). However, the member states did not vest in the SAARC either a sufficiency of political will or adequate resources for carrying out these commitments to ensure the expected level of effectiveness. As a consequence, a disjunction developed between the decisions taken by the association and their implementation."[66] If one reads the report, one finds significant sections on trade (meaning trade in goods), trade in services, investment and finance, infrastructure coordination, macroeconomic policy coordination and adopting common positions on global economic issues.[67] The Islamabad Declaration at the 12th SAARC Summit stated, "The SAARC members should continue to safeguard their collective interests in multilateral forums by discussing, coordinating and exchanging information with a view to adopting common positions, where appropriate, on various issues."

Since the 6th Summit in Colombo in 1991, one of the SAARC's achievements has been the SAPTA, which was signed in 1993 and entered into force in 1995. This contemplated tariff reductions in successive and phased steps, while recognising the special needs of LDCs and preferential steps in their favour. The SAPTA was a prelude to the South Asian Free Trade Area (SAFTA). The SAFTA was signed during the 12th Summit in Islamabad in 2004 and entered into force in January 2006. In simple terms, the SAFTA will lead to a free trade area (FTA) by 2016.[68] Under an early harvest programme for LDCs, India, Pakistan and Sri Lanka will however reduce customs duties to 0-5 percent for imports from LDCs by January 2009. More specifically,[69] "1.Contracting States agree to the following schedule of tariff reductions: a) The tariff reduction by the Non-Least Developed Contracting States from existing tariff rates to 20 percent shall be done within a time frame of two years, from the date of coming into force of the Agreement. Contracting States are encouraged to adopt reductions in equal annual installments. If actual tariff rates after the coming into force of the Agreement are below 20 percent, there shall be an annual reduction on a Margin of Preference basis of 10 percent on actual tariff rates for each of the two years. b) The tariff reduction by the Least Developed Contracting States from existing tariff rates will be to 30 percent within the time frame of 2 years from the date of coming into force of the Agreement. If actual tariff rates on the date of coming into force of the Agreement are below 30 percent, there will be an annual reduction on a Margin of Preference basis of five percent on actual tariff rates for each of the two years. c) The subsequent tariff reduction by Non-Least Developed Contracting States from 20 percent or below to 0-5 percent shall be done within a second time frame of five years, beginning from the third year from the date of coming into force of the Agreement. However, the period of subsequent tariff reduction by Sri Lanka shall be six years. Contracting States are encouraged to adopt reductions in equal annual installments, but not less than 15 percent annually. d) The subsequent tariff reduction by the Least Developed Contracting States from 30 percent or below to 0-5 percent shall be done within a second time frame of 8 years beginning from the third year from the date of coming into force of the Agreement. The Least Developed Contracting States are encouraged to adopt reductions in equal annual installments, not less than 10 percent annually. 2. The above schedules of tariff reductions will not prevent Contracting States from immediately reducing their tariffs to 0-5 percent or from following an accelerated schedule of tariff reduction. 3. a) Contracting States may not apply the Trade Liberalisation Programme as in paragraph 1 above, to the tariff lines included in the Sensitive Lists which shall be negotiated by the Contracting States (for LDCs and non-LDCs) and incorporated in this Agreement as an integral part. The number of products in the Sensitive Lists shall be subject to maximum ceiling to be mutually agreed among the Contracting States with flexibility to Least Developed Contracting States to seek derogation in respect of the products of their export interest…. Notwithstanding the provisions contained in paragraph 1 of this Article, the Non-Least Developed Contracting States shall reduce their tariff to 0-5 percent for the products of Least Developed Contracting States within a timeframe of three years beginning from the date of coming into force of the Agreement."

Conceptually, regional trading arrangements (RTAs) can be of four different types, as one moves up the ladder – FTAs, customs unions, single markets and economic and monetary unions.[70] As of September 2006, 211 RTAs have been notified to WTO. There is overlap in these numbers, since the same country may be a member of more than one RTA. Some are under Article XXIV[71] of GATT, those that cover services are under Article V of GATS (General Agreement on Trade in Services) and those that involve developing countries are under the 1979 balance of payments enabling clause.[72]

Among RTAs, FTAs are the easiest to negotiate, although it is important to emphasise some points. First, the issue of compatibility and conflict between multilateral and regional liberalisation is very old and conceptually, the issues of trade diversion versus trade creation (and investment diversion versus investment creation) have often been debated. This is fundamentally an empirical question and except for the odd sector here or there, there is no solid evidence of trade or investment diversion.[73] Second, decision-making processes within the WTO have become very difficult, with even a single country capable of blocking a consensus through a veto, at least in principle. There is a big difference between 23 contracting parties in 1948 and 150. The Doha Work Programme (DWP) is temporarily stuck, although there have been some attempts to revive it. But there is a more serious problem here. As a result of which, the prospects of future trade liberalisation through the WTO are somewhat dim, as opposed to implementing existing agreements of the Uruguay Round or functioning as an effective dispute resolution forum. Because liberalisation negotiations are simpler among smaller groups, in all probability, RTAs are here to stay and countries like Japan, which have historically stayed away from RTAs, have also begun to adopt this route. These forces receive greater impetus when multilateral negotiations are temporarily stuck, as they are now. It was no different during the Uruguay Round. To add to this, WTO agreements don't cover everything under the sun and several RTAs have been WTO-plus, in the sense of adding liberalisation agreements to sectors where multilateral liberalisation is incomplete. Instances are services, intellectual property, labour standards and the environment. Third, protectionist pressures exist everywhere and when RTAs impose disciplines on tariff protection, protectionism surfaces through other means. Such policy substitution occurs through safeguard measures, anti-dumping investigations, general non-tariff barriers (NTBs),[74] specific NTBs like standards,[75] exclusion of some sectors through sensitive or negative lists, exclusion of other sectors on grounds of security, health and the environment and rules of origin and local content requirements. One should also remember that historically, FTAs have only covered manufactures. Some recent RTAs cover services, but agriculture has always been excluded.

If one scans the list of existing global RTAs, one finds that they are essentially restricted to the FTA or customs union stage.[76] This is understandable, since sentiments on free cross-border movements of labour are even stronger than sentiments on free cross-border movements of capital. While it is easy to argue that free labour movements should be allowed into developed countries, accepting the same logical proposition in one's own home country is not that simple. Currency unions also involve loss of national sovereignty, since one loses degrees of freedom over control of monetary, fiscal and exchange rate policy.[77] Any multilateral, plurilateral, bilateral or regional agreement involves loss of sovereignty. Economic integration is difficult enough, but political integration even more so. And within economic integration, anything more than a FTA or customs union becomes exceedingly difficult, as the experiences of these other regional groupings demonstrate. The euphoria over the SAARC's potential therefore needs to be diluted with a few doses of realism. Despite the report of the Group of Eminent Persons and the Integrated Programme of Action, that first-best solution of complete economic integration is simply too premature. One needs to look for second-best solutions. There are also systemic problems within the SAARC Secretariat.[78] It is tempting to look at Europe and cite the efficiency gains that have come about through regional integration. However, it is necessary to appreciate that these efficiency and welfare gains are consequent to industrial restructuring and have little to do with trade liberalisation alone.

This becomes important in the context of what is accepted to be the SAARC and the SAFTA's eventual goal. The Islamabad Declaration stated, "We reiterate our commitment made at the 11th SAARC Summit at Kathmandu in January 2002 for the creation of a South

Asian Economic Union. In this context, we underline that creation of a suitable political and economic environment would be conducive to the realisation of this objective." The Dhaka Declaration added, "The launching of the SAFTA would mark an important milestone on the road to a South Asian Economic Union….. The Heads of State or Government recognised the need to take the process of regional economic integration further by expanding the scope of the SAFTA to include trade in services, enhanced investment and harmonised standards." In Islamabad, SAARCFINANCE was entrusted with the task of making recommendations for implementing a South Asian Economic Union and examining the concept of a South Asian Development Bank.

To go back to the quote from the Report of the SAARC Group of Eminent Persons, in its preparatory phase, the SAARC had little to say on economic matters, even if that statement sounds a trifle uncharitable. In its expansionary phase, the SAARC's economic efforts became synonymous with the SAPTA/SAFTA, even though pronouncements have been made about trade in services, investment and finance, infrastructure, energy, environment, tourism, human resources and science, technology and meteorology. The SAARC has been relatively irrelevant because of this equation with trade liberalisation in manufactured products.

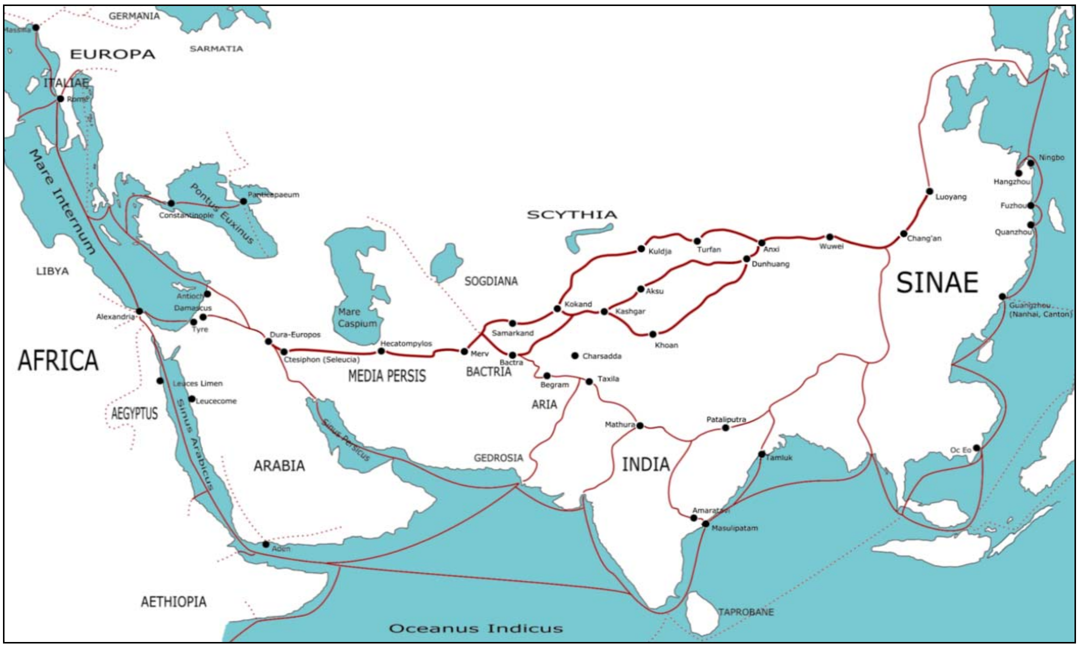
There are several reasons for this irrelevance. First, customs duties on manufactured products are increasingly irrelevant. They have been, and will be reduced, because of unilateral liberalisation, apart from the DWP eventually resurfacing. Second, given this liberalisation thrust, the timeline of 2016 is too long. Third, this liberalisation will be circumvented by NTBs, standards, sensitive lists, rules of origin, safeguards, and anti-dumping, apart from issues of revenue compensation to LDCs.[79] Fourth, India is now a party (existing or proposed) to several other sub-regional RTAs – the Bay of Bengal Initiative for MultiSectoral Technical and Economic Cooperation (BIMSTEC),[80] Chile, Singapore, Thailand, ASEAN, Japan, South Korea, United States, the European Union, GCC, Andean Community, Brazil, South Africa, MERCOSUR, SACU, China, Afghanistan, Sri Lanka and Bangladesh are examples. These overtake the SAFTA and also, strain the limited negotiating capacity and manpower resources Commerce Ministry possesses. Plus, they lead to allegations of circumvention of rules of origin. Fifth, as is but obvious, any process of bloc formation has to be cross-subsidised by the larger country, in this case, India. Even if there is no actual cross-subsidisation, the relative gains accrue more to smaller countries, theoretically, as well as empirically. If there is subsidisation by India, should that be in the area of classic trade liberalisation? Sixth, studies establishing the great potential that exists in free trade within South Asia are neither here nor there.[81] The results are tautological, since any process of liberalisation will lead to welfare gains in a net sense. The key question to ask is, what are the trade liberalisation gains within the SAARC, as compared to trade liberalisation gains with other parts of the globe, especially those parts that are economically more important – North America, Europe and ASEAN plus 3? There are issues here about the complementary nature of the SAARC economies, although this point should not be driven too hard.[82] Resources have opportunity costs. Seventh, as the focus of some of India's recent RTAs indicates, we need to move away from classic free trade agreements in manufactures to those in services (such as through comprehensive economic cooperation agreements), including agreements on freer cross-border movements of labour and capital. Does the existing SAARC trade agenda fit into this? Eighth, given the large and heterogeneous country that India is, is the idea of regional trade integration at all appropriate? Or does one have in mind economic integration between the southern parts of India and Sri Lanka and Maldives and between the eastern parts of India and Bhutan, Nepal, Bangladesh, Myanmar, Thailand and China? Or even between the northern parts of India and Pakistan?[83] Apart from the tactical intent, is there thus an economic rationale to sub-regional integration also? Should one therefore encourage direct interaction between India's states and neighbouring countries, rather than pushing everything at an all-India level? Ninth, in passing, one should mention figures on intra-SAARC trade.[84] As a percentage of total trade of the South Asian countries, the share has gone up a bit in the 1990s, from just above three percent to just above four percent. But is that because of the SAARC's initiatives, or because the South Asian economies have become more outward-looking and less insular? If the increase is because of RTAs, is it because of the SAPTA or because of bilateral trade agreements, the Indo-Sri Lanka FTA being a case in point?[85] Having said this, if one looks at shares of India's exports and imports in the 1990s, the shares have gone up for Sri Lanka (particularly for imports from Sri Lanka) and Nepal. Bangladesh's share has declined. Bhutan has greater importance as an Indian export destination, but not as a source for imports, with the Bhutanese trend more or less replicated for Maldives and Pakistan.

If these arguments are accepted, to impart relevance to the SAARC, we need to junk the equation and the obsession with the classic trade liberalisation agenda through SAPTA/SAFTA and also junk ideas of an economic or monetary union as being too premature. Within the classic trade agenda, perhaps the only areas that have some relevance are those concerning customs coordination and trade facilitation and harmonisation and mutual recognition of standards.

What ensures prosperity, growth and economic development? This is not an easy question to answer and has been debated by economists for decades. At one point, many economists might have flagged shortage of capital (domestic and foreign) as a constraint. It is doubtful that capital shortages will be mentioned anymore. Consider the first five pillars in the GCI (Global Competitiveness Index) – (1) institutions; (2) infrastructure; (3) macroeconomy; (4) health and primary education; (5) higher education and training. Most economists today will agree that this is what we need to push development – physical and social infrastructure, sound legal systems (dispute resolution, as well as law and order), property rights (including land markets), a stable policy environment and sound fiscal policies. These are usually matters of internal or national policy. But because of positive externalities and possibilities of spreading fixed costs, cooperation within South Asia is possible. This leads to a second question. Which of these represent areas where active government intervention is required, with state provisioning? One must remember that with technological changes and unbundling possibilities, many areas that were historically assumed to be characterised by market failures, will no longer be thus listed. What therefore are the areas that can be left to private sector entry, subject to state regulation? There is also the point that even if state financing through subsidisation is required, that need not necessarily be equated with state provisioning. Across diverse economic systems (capitalism, socialism, etc.), countries that have done well have invested in human capital (health, education) and physical infrastructure (road, water, electricity). If this is ensured, the rest seems to follow.

Looking back, the success of the Roman civilisation was identified with road-building. Without debating whether there was a golden age in the economic history of South Asia, in the 1st century ACE (as the map shows), trade routes encompassed the entire South Asian region, as offshoots of the famous Silk Road. So did the famous spice route. Successive Indian Prime Ministers and External Ministers have emphasised connectivity as a building block towards cooperation within South Asia. Connectivity means different things – there is transport connectivity, electronic connectivity and knowledge connectivity. The Provision of

Urban Amenities in Rural Areas mentioned three forms of connectivity, physical connectivity, electronic connectivity and knowledge connectivity. However, these other forms of connectivity come later, the core is transport connectivity. So the first element, from an Indian perspective, in making the SAARC more relevant should be to push for connectivity and cooperation in infrastructure, meaning primarily, transport, telecommunications, energy and water. This needs to be broken down into what is doable, instead of setting unnecessarily high and ambitious targets. One must also remember that public resources are scarce and some of the euphoria about private sector participation in infrastructure is unwarranted. Having said this, under the umbrella of connectivity and cooperation in infrastructure, the following should be possible. First, there should be a unilateral initiative to improve transport infrastructure (primarily rail, but also with four-lane highways) with integrated check-posts on the Indian side along the Sealdah-Bongaon-Petrapol-Benapol-Jessore, Munabao-Khokropar and Raxaul-Sirsiya stretches. Second, India should give up its resistance to allowing transit through Indian territory for cross-border traffic flows among South Asian countries, even if this opening up has to be unilateral. Third, since several private sector projects in the infrastructure sector are likely to have cross-border implications, the SAARC umbrella can be used to identify such projects that can jointly be developed. Fourth, there should be a comprehensive agreement on cross-border movement of commercial vehicles. Fifth, reciprocal liberalisation should also be pushed in areas like banking, telecommunications, electricity grids and open skies. Indeed, civil aviation is an area where unilateral liberalisation is also possible. Sixth, as a visible and showcase programme to illustrate what is possible, there can be a joint project on glaciers. Seventh, while many of India's strategic concerns on energy involve West Asia and Central Asia and within South Asia, are sub-regional or bilateral (such as with Nepal, Bhutan and even Myanmar), there is a case for setting up a SAARC Energy Centre.



Second, since many initiatives involve public expenditure, greater vigilance needs to be exercised over the outcomes of this public expenditure and this means the encouragement of civil society participation and vigilance. This has the byproduct of pushing democracy and empowerment, both desirable from India's point of view. Such initiatives can be pushed through SDF. In passing again, one fails to understand why every SAARC Declaration insists on separating out (as headings) poverty alleviation from social challenges. Logically, the two are related. In most SAARC countries, there is now an emphasis on local self-government and decentralisation, contributing to greater efficiency of public expenditure and a link between money spent and tangible improvement in outcomes. Right to Information Acts and recognition of the countervailing pressure exerted by civil society are manifestations. One should also recognise that impressions about India are often formed through people-to-people contacts, Track II so to speak. Within the civil society agenda, the following are examples of high visibility initiatives that are doable. First, building on India's strengths in education and health-care, there should be a unilateral opening up of visa restrictions for students, patients and perhaps even highly-skilled people. The dysfunctional specific political clearance required for scholars from Bangladesh and Pakistan should be scrapped. Second, unilateral scholarship schemes and youth exchange programmes can be initiated to expose Indian youth to the rest of South Asia and vice-versa. Third, India should set up separate immigration counters for SAARC nationals. Fourth, under the SAARC umbrella, India can offer to set up a SAARC Local Self-Government Centre, which can also incorporate networking, exchange of best practices and creation of databases among micro-finance institutions and self-help groups, apart from imparting training to this elected third tier of governance. Fifth, pending the setting up of the South Asian University, India can unilaterally announce the creation of a South Asian Centre at any of India's national institutions, with a specific focus on building skills. This can also be through the public-private partnership mode, with a Skill Development Fund. If successful, such an initiative is bound to eventually become regional. Sixth, the SAARC umbrella can be used to push for a protocol on migrants, involving migrants who migrate outside the region and also those who migrate within the region. Seventh, unilaterally, but later to be scaled up to the regional level, visible annual events should be institutionalised, focusing on the youth and civil society. Eighth, the SAARC umbrella can be used to boost physical infrastructure and market a Buddhist tourism circuit.

Third, within the economic relations agenda, there are obvious collective negotiating positions one can adopt at multilateral forums, such as on protection of migrants from the region, negotiating Mode IV in the services agreement, collective action against other RTAs or pushing for market access liberalisation in developed countries. But beyond this, one should forget about the classic trade agenda, except a few limited points on trade facilitation, customs procedures and harmonisation of standards. For instance, mutual recognition of standards and testing facilities is certainly an issue. Instead, one should push for free cross-border movements of labour, capital and services. Some of this is unilateral. There is no particular reason why Bangladesh and Pakistan should be the only two countries that are not allowed to invest in India under the automatic approval route. There is also a case for liberalising investment and ECB (external commercial borrowing) thresholds unilaterally for investments in the South Asian region, even if one doesn't actually subsidise investments in the region. Arguments are sometimes advanced about India unilaterally eliminating tariffs before 2009[86] or for allowing duty-free and quota-free access to exports from LDCs (meaning essentially Bangladesh), but such positive unilateralism is often interpreted as a sign of weakness. Unilateralism is best restricted to cross-border movements of labour and capital.

Fourth, and this is even more important than the other three points, to make the SAARC more relevant, one needs to have a focus. There is a temptation to bring in everything under the sun under the SAARC umbrella and the SAARC, therefore, becomes a wish list that means nothing operationally. Take for instance cooperation in tourism. Beyond easier visas, civil aviation networks and other forms of tourism-related infrastructure, what does it mean? Is tourism something governments can push, or is it something that market forces ensure, once the necessary infrastructure is in place? Beyond disaster management, what does cooperation in the environment mean? There are scarce negotiating resources too and their use needs to be prioritised and focused for the SAARC to become more relevant. India has an opportunity to influence the agenda now and should do this under the three heads (infrastructure, civil society, economic relations) outlined above. The SAPTA and the SAFTA are passé. And to reiterate a point made earlier, it is by no means obvious that SAARC's regional umbrella offers a better option of pushing this agenda than the bilateral or sub-regional route. Indeed, since the bilateral and sub-regional route has been pushed by India's trade policy negotiations, the SAARC has effectively come to mean Bangladesh and Pakistan. The other South Asian countries have been covered through those alternative channels. Given what was said about disparities and divides within India, yet another provocative statement should perhaps be made. India has a vested interest in improving economic relationships with Bangladesh. Despite energy and even water, the case for improving economic relationships with Pakistan is weaker.

Section 4: The East Asia Agenda

In the Indian trade policy discourse, mention is often made of a Look East policy, which can even be dated back to 1991. But before that, it is worthwhile to have a list of India's RTAs, though some of these have been mentioned in passing in the text earlier.

India's RTAs

RTA	Partner countries	Status
SACU (South Africa Customs Union)	South Africa, Lesotho, Swaziland, Botswana, Namibia	Signing of PTA pending, eventual transition to FTA contemplated
Mercosur	Brazil, Argentina, Uruguay, Paraguay	PTA signed in 2004
Chile	Chile	Framework agreement for economic cooperation in services and investment signed in 2005, PTA in 2006, FTA under examination
IBSA CECA (Comprehensive Economic Cooperation Agreement)	Brazil, South Africa	Joint Study Group stage
Trade and investment agreement (TIA) with EU	EU	Preliminary negotiations
CECA with Russia	Russia	Joint Study Group stage
GCC (Gulf Cooperation Council)	Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, UAE	Framework agreement for economic cooperation signed in 2004, ongoing negotiations for FTA, services and investments
Israel PTA	Israel	Ongoing negotiations
Comprehensive Economic Cooperation and Partnership Agreement (CECPA)	Mauritius	PTA, services and investment negotiations ongoing

with Mauritius		
Bangkok Agreement	Bangladesh, China, South Korea, Sri Lanka, Laos	In existence since 1975, with exchange of tariff concessions. Third round of negotiations implemented in 2006, agreement renamed Asia Pacific Trade Agreement (APTA)
BIMSTEC (Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation)	Bangladesh, Myanmar, Sri Lanka, Thailand, Bhutan, Nepal	Framework agreement for FTA, services and investments signed in 2004, negotiations ongoing
SAPTA/SAFTA	Afghanistan, Bangladesh, Bhutan, Maldives, Nepal, Pakistan, Sri Lanka	The SAFTA was in force from 2006
PTA with Afghanistan	Afghanistan	Signed in 2003
Trade agreement with Bangladesh	Bangladesh	Signed in 1980, not yet extended beyond 2001
Treaty of Trade with Nepal	Nepal	Renewed in 2007, annual quotas on four manufactured categories exported by Nepal
Trade and Commerce Agreement with Bhutan	Bhutan	FTA, extended in 2005
FTA with Sri Lanka	Sri Lanka	In force from 2000
CECPA (Comprehensive Economic and Cooperation Partnership Agreement) with South Korea	South Korea	Ongoing negotiations on goods, services and investment
Economic Partnership Agreement (EPA) with Japan	Japan	Negotiations expected to be concluded in 2008
Trade and economic cooperation with China	China	Joint Task Force stage
Trade and economic cooperation agreement with Mongolia	Mongolia	Signed in 1996
CECA with ASEAN	Brunei Darussalam, Cambodia, Indonesia, Lao, Malaysia, Myanmar, Philippines, Singapore, Thailand, Vietnam	Framework agreement signed in 2003, FTA in final stages, negotiations on services and investments pending
FTA with Thailand	Thailand	Under implementation from 2006, negotiations on services and investments ongoing
CECA with Singapore	Singapore	Implemented from 2005
CECA with Malaysia	Malaysia	Joint Study Group stage
CECA with Indonesia	Indonesia	Joint Study Group stage

For a country that earlier had only the Bangkok Agreement, and for several years a non-functional SAARC as an increment, this is an impressive list of RTAs. Given paucity of negotiating resources, is there any method and logical coherence in this madness, or are these RTAs being tagged on in ad hoc fashion? At the risk of generalisation, some assertions can probably be made. First, agreements centred around South Africa and Brazil are probably no more than attempts to cement negotiating coalitions at WTO. Second, there is implicit recognition that WTO negotiations are unlikely to head anywhere, since even a single country effectively has the right of veto. And even if the DWP does advance somewhere, RTAs will be WTO-plus, such as in the area of services. At best, service sector liberalisation within WTO will remain incomplete in the foreseeable future. Third, when services were first included in the Uruguay Round's agenda, India resisted the inclusion, perceiving this as a developed country attempt to over-load the agenda. Perceptions have changed and recognition has set in that India has a comparative advantage in services (this is much more than information technology) and India's service sector liberalisation agenda is much more than pushing for cross-border movements of labour. After all, FDI out of India is also considerable now and in selected service sectors, there are Indian interests in corporate presence abroad. This explains the switch in focus from conventional RTAs (which typically covered only goods and there too, manufactured products) to Comprehensive Economic Cooperation Agreements, which also cover services and cross-border investments. Fourth, the role of RTAs in actually pushing greater trade is debatable, not in the sense that they are unimportant, but in the sense that government-negotiated RTAs probably do no more than put a legal stamp on increased trade flows that were in any case happening because of commercial reasons. The North American Free Trade Agreement is a case in point. However, there is no denying that such negotiated RTAs provide a greater stimulus, since they also enhance mutual information flows. Consider India's exports.[87] In 2007-08, ASEAN accounted for a nine percent share and North-East Asia for 14.8 percent. South Asia had a share of 5.1 percent. For imports, ASEAN had a 9.5 percent share, North-East Asia 18.6 percent and South Asia 0.7 percent. The geographical pattern of India's trade has changed since 1991 and it us understandable that there should be a shift in trade policy towards East Asia. Incidentally, this also happens to be a high growth region. That East Asia should figure prominently in existing or potential RTAs isn't surprising. What is surprising is that Australia doesn't yet figure in the list. Fifth, there is recognition, usually left implicit, that the SAARC process is headed nowhere, the SAFTA notwithstanding. The success of the FTA with Sri Lanka has been interpreted as vindication of the belief that sub-regional RTAs are the way to go. This splices in neatly with whatever is being done with East Asia – use sub-regional RTAs to bridge the distance between South Asia and East Asia.

Endnotes

1 A preliminary version of this paper was presented at a conference organized by ADB, ANU and NCAER in Delhi on 4th April 2008 and I am indebted to the participants for useful comments. The usual caveat applies.

2 Professor Bibek Debroy is a Visiting Senior Research Fellow at the Institute of South Asian Studies, an autonomous research institute at the National University of Singapore. He can be contacted at isasbd@nus.edu.sg or bdebroy@gmail.com.

3 Unlike the other observers, China is interested in joining SAARC.

4 This is unlikely in the immediate future, because of the nuclear issue.

5 Because of time-lags, this is a 2004 figure.

6 Strictly speaking, Aden also.

7 The World Bank or Atlas method.

8 This is thanks to India. There are minor differences in figures between the IMF's *World Economic Outlook* database and the World Bank's *World Development Indicators* database. In neither ranking is the European Union (EU) counted as a single economic entity. In 2005, in both databases, EU was very marginally ahead

of the United States. In the IMF database, the United States led the league with a PPG GDP of 12,277 billion US dollars, followed by China with 9,412, Japan with 3,910 and India with 3,633. Pakistan's PPP GDP was 405 billion, Bangladesh's 306, Sri Lanka's 86, Nepal's 39, Afghanistan's 32, Bhutan's 3 and Maldives' 2.6.

9 http://en.wikipedia.org/wiki/South_Asian_Association_for_Regional_Cooperation

10 Among 181 countries ranked by IMF, the first SAARC country to figure is the Maldives, with a rank of 80th and a per capita PPP GDP figure of 7,675 US dollars. Indeed, Maldives is somewhat uncharacteristic of the general SAARC cluster. Within the SAARC cluster proper, we have Sri Lanka with PPP per capita GDP of 4,384 (rank 111th), Bhutan with 3,921 (rank 117th), India with 3,320 (rank 122nd), Pakistan with 2,653 (rank 127th), Bangladesh with 2,011 (rank 143rd), Nepal with 1,675 (rank 153rd) and Afghanistan with 1,310 (rank 163rd).

11 Angus Maddison, *Historical Statistics of the World Economy: 1-2003 AD*, OECD, Paris, 2006.

12 Ahead of Han China.

13 Mughal India.

14 Mughal India.

15 At PPP 1985 prices. 1 US $ per day roughly corresponds to the Indian national poverty line.

16 For instance, in UNDP's *Human Development Report*.

17 Not only are such surveys not annual, there are also issues of mismatch between aggregate expenditure data obtained through national accounts and expenditure data obtained through household surveys, the latter falling short of the former.

18 These are data from the *Human Development Report (HDR)* for 2005. HDR typically has data with a time-lag of two years. But in this particular case, since surveys are involved, data are for the last year when a survey was done, not necessarily 2003. In the Indian context, there has of course been a debate over NSS (National Sample Survey) data for 1999-2000 and its comparability with 1993-94 and 2004-05. For 2004-05, NSS shows an all-India poverty ratio of 28.8 percent.

19 These figures are from *Human Development Report* for 2006 and are therefore data for 2004. Information is not available for Afghanistan's score to be calculated.

20 The LDC classification is based on three criteria – low income (per capita income less than 750 US dollars), human resource weaknesses (nutrition, health, education, adult literacy) and economic vulnerability (instability of agricultural production, instability and concentration of exports, diversification of economic activity, smallness of the economy and vulnerability to natural disasters).

21 Within the UN system.

22 The SAFTA agreement builds in a clause for Maldives' graduation from LDC status, specifying that in such an eventuality, the preferences will continue.

23 There are 8 goals and at least the first 6 are precise enough. It is not very clear what the seventh and the eighth goals mean operationally. The goals *per se* are somewhat vague and imprecise, but the targets under them are more specific.

24 The eight MDGs are (1) Eradicate extreme poverty and hunger; (2) Achieve universal primary education; (3) Promote gender equality and empower women; (4) Reduce child mortality; (5) Improve maternal health; (6) Combat HIV/AIDS, malaria and other diseases; (7) Ensure environmental sustainability; and (8) Develop a global partnership for development.

25 *Strengthening Mutual Accountability – Aid, Trade and Governance*, World Bank and IMF, 2006. This report doesn't cover Afghanistan.

26 Between 1996 and 2003, there was a UNDP-sponsored South Asia Poverty Alleviation Programme (SAPAP).

27 Paragraphs 8 through 12.

28 "The Plan of Action identified some policy actions to be pursued at the domestic levels. Such internal policies, the Plan, identifies: a) good governance; b) sound macro-economic management; c) human development; d) combating rural and urban poverty; e) promotion of multi-culturism, pluralism and mass education; f) expansion of social safety nets; g) investment in human capital and social sectors; h) prudent allocation of public resources and strengthening of domestic resource mobilization; i) empowerment of local communities and governments; j) intra-regional trade and capital flows etc. The Plan also identified some external policies that affect poverty alleviation efforts such as increased ODA, increased market access, reduction of debt burden etc," http://www.saarc-sec.org/main.php?t=2.12

29 *An Engagement with Hope, SAARC Development Goals (SDGs), 2005-2010*, ISACPA, 2004. "The *first* MDG is the most fundamental: eradicating extreme poverty and hunger. Within this goal, there are two targets: firstly, to halve, between 1990 and 2015, the proportion of people whose income is less than one dollar a day, and secondly, to halve the proportion of people who suffer from hunger over the same period. The record of progress of South Asian countries on the income poverty target has been quite striking.

Poverty incidence based on national poverty line has declined from 38 to 28 percent over the last 12-year period. By current trends, South Asia as a whole appears to be on track to meet the MDG target of halving income poverty by 2015 though some countries will have to make greater efforts than others. Evidence of progress on the hunger indicator has been more mixed: the proportion of low-weight children fell from 64.1 to 48.4 percent, but nutritional indicator - proportion of population below minimum level of dietary energy consumption – fell more modestly from 26.6 to 22.8 percent. Significantly greater efforts will clearly be necessary in this area. The *second* MDG is to achieve universal primary education. Net primary enrolment for the region as a whole has increased from 73 to 82 percent. While progress for some countries has been appreciable as in Bangladesh, for some others assessment is difficult because of a lack of adequate enrollment data. Moreover, the countries are at widely varying levels of literacy in 2002. Except for Sri Lanka and Maldives, the situation is quite challenging on related indicators such as primary completion rate and full literacy. Of great concern is the fact that nearly a third of South Asian youth are illiterate. The *third* MDG is to promote gender equality and empower women. The target is to achieve gender parity in primary and secondary education preferably by 2005 and to all levels of education by 2015. There has been a steady reduction of gender disparities in primary, secondary and tertiary education in all SAARC countries. On the empowerment indicator, despite steady progress in the region, women's participation in non-agricultural employment remains modest, at around 20 percent. Gender equality also continues to fall short in the legislative arena with less than 10 percent of parliamentary seats in the region occupied by women with no clear trend of increase or decrease. The *fourth* MDG is to reduce child mortality. The target is to reduce the under-five mortality rate by two-thirds by 2015. Steep percentage declines have occurred in some countries such as Bangladesh, Bhutan and Nepal from relatively higher 1990 levels while in Sri Lanka the absolute rate has been reduced to 19 deaths per 1,000 live births, *the lowest in the region*. For SAARC countries as a whole, the rate of reduction has been 27 percent during the last 12 years. Though Bangladesh and Bhutan are on track to meet the MDG target, the region as a whole will have to make greater efforts in this respect. The *fifth* goal is to improve maternal health. No reliable data exist to assess the critical area of maternal health with precision. Available statistics indicate great divergence from a mortality rate of less than 100 per 100,000 women giving birth in Sri Lanka to a mortality rate of more than 700 in Nepal. A crucial indirect indicator here is the presence of skilled birth attendants. It would appear that more than 60 percent of women giving birth in South Asia still do so without the assistance of skilled attendants. Clearly, this is going to be one of the greatest challenges South Asia has to tackle in the coming decade. Improving data collection on relevant indicators on this goal will also have to be a priority. The *sixth* MDG is to combat HIV/AIDS, malaria and other diseases. Statistics on the spread of HIV/AIDS in South Asia is insufficient; available estimates show a low HIV infection rate of 0.05 percent but this nevertheless translates into an infected population of nearly 5 million. If unattended, this can grow to be a much bigger problem. Other infectious diseases such as malaria and tuberculosis have a longer presence in the region and continue to pose major health challenges for the population. The *seventh* goal is to ensure environmental sustainability. Five targets are identified here: forest cover, energy intensity of the economy, sustainable access to safe drinking water, and, sanitation. South Asia as a whole managed to retain its forest coverage in the 1990s at about 16 percent though with differing performances among individual countries. Nepal, Pakistan and Sri Lanka have been losing their forest cover while Bangladesh, Bhutan and India appear to have at least reversed their forest loss. Assessment, however, is rendered difficult by the fact that generation of data is resource-intensive and time-consuming and not much progress has taken place in this area. There are discrepancies between official statistics and ground-level realities. On the other indicator of environmental sustainability, namely energy intensity measured as output per unit of energy input, South Asia has seen an increase from 3.4 to 5.1 percent in the 1990s. Increase in this indicator is inevitable as the economies of the region grow and undergo structural change. However, the 2002 levels in the region compare favourably with many industrialized countries. On the target of access to safe drinking water, access for the region as a whole increased from 72 to 84 percent in the 1990s. Available data show that Bangladesh and Maldives have achieved near universal access. However, if arsenic contamination is factored in, the picture could change particularly for Bangladesh and India. Progress on sanitation in contrast remains inadequate with data suggesting nearly two-thirds of the region's population not having access to improved sanitation services. The *eighth* goal is to develop a global partnership for development. External debt remains a major impediment to development in some SAARC countries. In Pakistan, external debt servicing consumes over 20 percent of export earnings. However, during the 1990s, all SAARC member countries experienced a reduction in their debt servicing ratios. Significant declines were observed for Bangladesh, India, Nepal and Sri Lanka. The decline in ODA has been another stumbling block, particularly for LDCs. In Bangladesh, ODA as percentage of GDP declined from 7.0 percent in 1990 to 2.2 percent in 2001. The figures were 11.7 and 7.0 for Nepal, 16.5 and 11.1 for Bhutan, 1.3 and 0.7 for India, and 9.8 and 4.3 for Maldives for same period. On the other hand, accessibility to affordable drugs in the region has been steadily improving.

Telephone and computer usage improved sharply during the 1990s in almost all SAARC countries. The above summary of progress on MDG attainment in South Asia presents a mixed picture. Though compared to other developing regions or its own past, South Asian countries have made significant progress in the 1990s, progress has been mixed both in terms of targets and in terms of individual countries. The rate of progress too is an issue. Overall, the progress on MDG attainment in South Asia falls into three boxes: SAARC countries are on track on a third of the identified 18 targets; they are off-track on another third; and reliable or relevant data do not exist to assess performance in the final one-third of targets. MDGs most likely to be achieved by current trends include halving income poverty and child mortality and ensuring environmental sustainability. Less likely are other targets in the education and health sectors. Such outcomes, of course, are not pre-determined. Greater efforts and more strategic engagement can clearly alter the outcome for the better."

[30] *Ibid.*

[31] There is a separate point that it is enterprises rather than countries that actually compete. However, enterprises do function in a policy-environment that can be an enabler or a disabler.

[32] About two-thirds of the variables are based on opinion surveys.

[33] Sri Lanka began in the 1970s, but that experiment got derailed.

[34] WTO commitments, accession to the WTO commitments or liberalization through regional and bilateral agreements.

[35] Measured, for instance, by the incremental capital/output ratio.

[36] In passing, the link between reforms and corruption is not always clear. In the long run, reforms should reduce discretion and decrease corruption of certain kinds, apart from eliminating corruption linked to shortage economies. However, in the short run, some reforms may also increase discretionary opportunities and thereby increase corruption.

[37] The correlation is not that robust in the short-run, although there is a link in the longer term. And even when there is short-term correlation, the direction of causation is not clear.

[38] The latter is WTO-compatible. Even when WTO-compatible, the former can be subjected to countervailing duties by trading partners.

[39] The Seventh Schedule to the Indian Constitution sets out a Union List, a State List and a Concurrent List.

[40] Unless otherwise stated, all figures in this paragraph are from *Economic Survey, 2007-08*, Department of Economic Affairs, Ministry of Finance, Government of India.

[41] Petroleum figures prominently in both the export and the import basket. The latter is known, but the former is not often appreciated.

[42] For instance, the Agricultural Produce Marketing and Control (APMC) Acts and orders under the Essential Commodities Act.

[43] Plus decentralization in management of rural infrastructure.

[44] There is also a research and development agenda, but it is not necessarily obvious why this has to be public sector driven. Extension services will have to be largely public sector driven.

[45] There are two distinct issues of ownership laws and tenancy laws here. The former is contentious, the latter less so.

[46] Partly because villages (and habitations) where population sizes are less than 1000 are simply not viable. If the transport infrastructure improves, some of these villages will disappear and become mainstreamed.

[47] A quote by Rajiv Gandhi is often recalled, because he said that out of every one rupee that is spent on poverty alleviation programmes, not more than 15 percent reaches the target beneficiary. It is commonly assumed that 85 percent is swallowed up in leakage and corruption, but that is not quite true. Leakage and corruption no doubt exist. However, 85 percent also includes administrative costs of delivery.

[48] For primary education.

[49] For irrigation, rural roads, rural housing, rural water supply, rural electrification and rural telecom connectivity.

[50] The outstanding success of infrastructure reform is in the area of telecom and the outstanding failure in the case of power. But a revolution is happening in roads, triggered by the National Highway Development Programme (NHDP) and this revolution has probably not been sufficiently appreciated yet. It has transcended NHDP and now covers feeder roads too.

[51] Consequently, the case law also varies, causing further confusion.

[52] For instance, public monopolies may now be replaced, infrastructure is an example. Unbundling facilitates this and there will be need for regulators.

[53] Thomas Friedman's *The World is Flat: A Brief History of the Twenty-first Century*, 2005, is an example.

[54] There is a component of rupee appreciation that other projections often do not factor in and this adds around 30 percent to the per capita income increase.

[55] In parallel with the increase in the savings rate, the investment rate has also increased, fuelled by both domestic savings and foreign savings. Economic Survey, 2007-08 gives a savings rate of 34.3 percent in 2005-06 and an investment rate of 35.5 percent.

[56] The SC issue does become politicized. As does the ST issue, but the ST issue is fundamentally geographical.

[57] Contrary to the international usage of North as developed countries and South as developing countries (or least developed countries), the Indian perception has the North as under-developed and the South as developed.

[58] To dramatise what is happening, let us consider the following. Let us assume an all-India real GDP growth rate of 8 percent till 2020 and let us assume this growth (in income and in population) is distributed among the States in the ratio that it is distributed in today. Let us now project the per capita income of Indian States in the year 2020, using PPP (purchasing power parity) US dollars, assuming that the exchange rate continues to be what it is today. This gives the following list of PPP per capita dollar income figures in 2020 – Chandigarh (36,926), Pondicherry (34,583), Goa (29,074), Delhi (26,702), Karnataka (13,127), Maharashtra (12,075), Gujarat (11,782), Tamil Nadu (11,641), Haryana (10,297), Punjab (10,205), Himachal Pradesh (9,534), West Bengal (8,873), Andaman & Nicobar Islands (8,229), Kerala (8,007), Andhra Pradesh (7,351), Tripura (7,301), Meghalaya (7,122), Manipur (6,246), Rajasthan (6,048), Nagaland (4,908), Jammu & Kashmir (4,212), Arunachal Pradesh (3,837), Jharkhand (3,437), Chhattisgarh (2,928), Madhya Pradesh (2,864), Uttar Pradesh (2,750), Orissa (2,658), Assam (2,559), Bihar (1,698) and all-India (7,587). Measured in accordance with the per capita income criterion, this tells us what are going to be India's richest and poorest States. It also tells us there is going to be a serious inter-State disparity problem, unless something changes. These results can also be presented in a slightly different way. Which countries in the world have similar PPP per capita income figures today? And the list is - Chandigarh (USA), Pondicherry (USA), Goa (Switzerland), Delhi (Japan), Karnataka (Czech Republic), Maharashtra (Saudi Arabia), Gujarat (Saudi Arabia), Tamil Nadu (Saudi Arabia), Haryana (Slovak Republic), Punjab (Slovak Republic), Himachal Pradesh (Chile), West Bengal (Mexico), Andaman & Nicobar Islands (Costa Rica), Kerala (Russia), Andhra Pradesh (Brazil), Tripura (Brazil), Meghalaya (Belarus), Manipur (Thailand), Rajasthan (Colombia), Nagaland (Peru), Jammu & Kashmir (China), Arunachal Pradesh (China), Jharkhand (Sri Lanka), Chhattisgarh (Indonesia), Madhya Pradesh (Azerbaijan), Uttar Pradesh (Azerbaijan), Orissa (Zimbabwe), Assam (Zimbabwe), Bihar (Bangladesh) and all-India (Brazil). In PPP per capita income terms, the India of 2020 will be like the Brazil of today, not like the Brazil of 2020. And this is per capita income alone. No one is suggesting that in 2020, Assam will have the kind of life expectancy Zimbabwe has today.

[59] Rather interestingly, despite agriculture's reduced share in GDP now, overall growth is still sensitive to monsoons, although the spatial and temporal spread of rainfall is much more important than aggregate monsoon figures. Thus, whenever there is a good monsoon, the Indian economy does well. However, whenever there is a good monsoon, Bihar confronts a flood problem and Bihar's economy performs badly. There is therefore a near-perfect negative correlation between India's economic performance and Bihar's.

[60] Since data on districts aren't always available, data are used on six indicators - income poverty (poverty ratios), hunger, infant mortality rate, immunization, literacy rate and enrollment ratios. In addition, gender disparity is highlighted through female and male literacy rates, but not actually used in the process of identifying backwardness. Data used are estimates for 2001. *District-Level Deprivation in the New Millenium*, Bibek Debroy and Laveesh Bhandari, Konark Publishers and Rajiv Gandhi Institute for Contemporary Studies, Delhi, 2003.

[61] http://www.strategicforesight.com/secondfreedom.htm. To quote, "The bilateral conflict between India and Pakistan depresses investment climate to undermine GDP growth rate by 2 percent. If past experiences are any indicator, then conflict will pull down GDP growth rates by 1-2 percent in every South Asian country during 2005-2025. …. South Asia has a large terror economy with about 330000 armed combatants and over a million-strong supporting network. The total visible Gross Terror-economy Product (GTP) of the region is US$2 billion. Invisible GTP is normally 3-4 times the visible GTP. If the next 2 decades see a quantum leap, GTP of 2025 could be around 5 percent of the region's GDP…. There are around 15 Islamic extremist organisations operating in Assam. All of them have links with terrorist organisations outside India for moral and financial support. A grand alliance, AMULFA was reportedly founded with the backing of the ISI to coordinate subversive activities of Islamist terrorist element in the North-eastern region of India. The LTTE might be another source for future linkages between the Maoists and Islamic terrorism. The LTTE has connections with the People's War Group in India. South Asian terrorist groups are likely to replace Al Qaeda as premier global brands of terrorism, especially Harkat-ul-Jihad Islami (HUJI) and Lashkar-e-Toiba (LeT). There are about 170 major terrorist groups in Asia and the Middle East. Out of them 70 are based in South Asia with local, regional and global ambitions."

[62] http://www.strategicforesight.com/costofconflict.htm. To quote again, "If the troops are mobilised again in the future on the pattern of 2002 for a year, it will cost India 0.46 percent of GDP and Pakistan 2.25 percent of GDP….India and Pakistan have the potential to enjoy a trade of about $1 billion if hostile environment continues and $13.25 billion if peace prevails on a cumulative basis for the next five years (2004-08) resulting in an opportunity loss of $ 12 billion."

[63] http://www.strategicforesight.com/finalsettlement.htm

[64] "If India and Pakistan take a political decision to restructure their relations, they will have to ensure that water serves as a flow to bring them together, rather than taking them further on the course of conflict. Since 1999, every proposal made by Pakistan through track two diplomacy, either directly or indirectly, refers to water as a core issue. The statements made by Pakistan's military officials, Kashmiri leaders and newspaper editorials describe Jammu & Kashmir as a supplier of crucial rivers, and project the bloodshed there as the sacrifice made by Kashmiri youth to ensure Pakistan's water security…. Pakistan needs fresh sources of water in areas where dams can be constructed. As a result, Pakistan has been proposing, through track-two diplomacy, that it should be given parts of the Kashmir valley and Jammu, so that it can have physical control on the Chenab basin. India cannot oblige Pakistan since water availability in India's northern provinces has been declining, leading to conflict between Punjab and Haryana. The final settlement will have to be based on realistic analysis of the water situation in the entire Indus River Basin. The construction of Mangla dam has led to resentment in the Mirpur area of Kashmir on the Pakistani side of the Line of Control. There is also resentment in the Kashmir valley on the Indian side of the Line of Control, because the Indus Waters Treaty undermines the potential to develop hydroelectricity and irrigation projects. There is a direct conflict between Pakistan and the people of Jammu & Kashmir. Pakistan wants the Kashmir valley and parts of Jammu to be able to build dams to divert rivers for Punjab's benefit at the cost of the Kashmiris. On the other hand, Jammu & Kashmir needs to come out of the Indus Waters Treaty to improve its own irrigation, hydroelectricity and employment prospects. Pakistan is not interested in the full accession of Kashmir, if it involves giving equal rights to Kashmir along with other provinces. Pakistan's interest is in having Kashmir as a semi-autonomous state, which cannot demand equal rights with other provinces, but which allows the federal government to exercise political control on its resources. There is a general misunderstanding that Pakistan wants to annex the Kashmir valley for political reasons. This option would mean major disaster for Pakistan, as it will lose Chenab resulting in up to 17 percent reduction in water flows. Also, the Indus Waters Treaty may stand dissolved. Punjab will not be affected much as it will continue to draw water from Jhelum. As the flow of Indus will decline, Sindh will be compelled to start a civil war. Therefore, Pakistan is not interested in Kashmir alone. Pakistan wants Kashmir plus those districts of Jammu that form the catchment area of the Chenab. The physical control over the Chenab valley would provide Pakistan an opportunity to build dams upstream and regulate river flows to Punjab and Sindh. Currently, India has identified nine sites on Chenab for hydroelectricity development. The river has the potential for building dams, which could be bigger or comparable to Tarbela and Mangla dams in Pakistan. India, under the Indus Waters Treaty, can only build run-of-the-river hydroelectric stations. However, if Pakistan takes control of the area, it will have no such restrictions. It will be able to take more advantage of the high speed and momentum of upstream Chenab. It would also provide strategic depth for the Mangla dam and the important Pothohar region, from where more than half of the army personnel are recruited. However, India would lose the strategically vital Akhnoor area in Jammu and also access to Ladakh. India may then consider a very belligerent response, which could be devastating for both the countries. Therefore, the Chenab formula should be rejected at this stage of discussion in the interest of peace and stability in South Asia. Unilateral abrogation of the Indus Waters Treaty should not be considered by either party. For more than 40 years, the Indus Waters Treaty has proved to be an outstanding example of conflict resolution. It is based on the division of the Indus River Basin with Pakistan having effective control of the three western rivers (Indus, Jhelum and Chenab) and India having an effective control on the three eastern rivers (Ravi, Sutlej and Beas). Due to increase in the water stress in the two countries since the early 1990s, the treaty has come under strain. It may find it difficult to survive the next 10 years, even though there is no exit clause. It is imperative for both India and Pakistan, to envisage comprehensive development and planning of the Indus River Basin. A holistic approach to water resources — recognizing the linkages between water, land, users, environment and infrastructure — is necessary to evade the crisis of water scarcity in the subcontinent."

[65] And within that, manufactured products.

[66] *SAARC Vision Beyond the Year 2000, Report of the SAARC Group of Eminent Persons*.

[67] The WTO is an instance of this. Joint Statements and Joint Declarations have characterized WTO Ministerial Conferences in Geneva in 1998, Seattle in 1999 and Doha in 2001.

[68] But beginning in 2013.

[69] Article 7 of the SAFTA agreement.

[70] A preferential trade agreement (PTA) is a preparatory move towards a FTA, with preferential or reduced duties. FTAs eliminate trade barriers to movement of goods among members, without necessarily adopting a common external commercial policy vis-à-vis non-members. Customs unions add to FTAs by adding such a common external commercial policy. Single markets eliminate barriers to free cross-border movements of factors (labour and capital) in addition to eliminating barriers to free cross-border movements of goods. And economic and monetary unions transcend all these, by coordinating macroeconomic policies and even adopting common political norms.

[71] This sets out two conditions so that GATT's MFN (most favoured nation) principle is not circumvented by using the subterfuge of a RTA – first, trade barriers between members must be eliminated, not reduced; second, trade barriers vis-à-vis non-members must not go up as a result of bloc formation.

[72] The SAPTA was notified as a preferential arrangement under the balance of payments clause in April 1997. The India-Sri Lanka FTA was similarly notified in June 2002.

[73] Empirical findings depend critically on the modeling framework used. The most popular methodology is gravity models, which leave a lot to be desired.

[74] In principle, trade liberalisation covers both tariffs and NTBs. But NTBs are very difficult to measure, quantify and police.

[75] Technical barriers to trade (TBT) and sanitary and phytosanitary measures (SPS).

[76] The only ones that have implemented a common market are EU and CARICOM. CEMAC (Economic and Monetary Community of Central Africa), South American Community of Nations, GCC (Gulf Cooperation Council), SACU (Southern African Customs Union), ASEAN, EurAsEC (Euroasian Economic Community) and AEC (African Economic Community) propose common markets, but in the future, the last named as far away as 2023.

[77] Consequently, currency unions only exist in EU, CARICOM, CEMAC and, in a limited kind of way, in ECOWAS (Economic Community of West African States). Other than ECOWAS,, they are proposed in EAC (East African Community), South American Community of Nations, GCC, SACU, COMESA (Common Market for Eastern and Southern Africa) and ASEAN. While visa-free travel may be contemplated, restriction-less travel only exists in EU, with a proposal existing for ECOWAS. A political pact only exists for EU and is proposed for CARICOM, ECOWAS, EAC, MERCOSUR, South American Community of Nations and AEC. Defence pacts exist for EU, ECOWAS, CEMAC and EurAsEC and are proposed for AEC.

[78] This is over and above the processes. For instance, there are no technical persons in the technical committees. Nor is there any private sector representation.

[79] All these are built into the SAFTA agreement itself.

[80] Bangladesh, India, Myanmar, Sri Lanka, Thailand, Bhutan and Nepal.

[81] This statement should not be interpreted as a dismissal of studies that estimate illegal cross-border trade between India on the one hand and say, Bangladesh, Sri Lanka and Pakistan on the other. But one must be careful. What goes by the name of illegal trade is sometimes third-country trade and actual cross-border illegal trade is not entirely informal trade. And as the experience with Sri Lanka demonstrates, cross-border trade doesn't occur only because trade policy imposes customs duties. A large contribution is also due to high procedural costs associated with formal trade.

[82] The point should not be driven too hard because classic notions of comparative advantage, a la Heckscher-Ohlin, have changed, with large chunks of cross-border trade of the form of intra-firm trade. Revealed comparative advantage (RCA) can be used to establish complementary, or its lack, between SAARC economies, but in the last resort, RCA is a static concept.

[83] Nor can one ignore the most favoured nation (MFN) issue between India and Pakistan.

[84] Understandably, these figures exclude Afghanistan.

[85] In any event, shares can be somewhat misleading, because shares are also a function of what is happening to trade with other countries outside the bloc. For instance, an explosion in India's trade with China automatically reduces the SAARC share. Having said this, the shares also depend on whether one has a country like Nepal or Bhutan in mind, or whether one is talking about India. Understandably, intra-SAARC trade will be much more important to the former. And for India, especially if one is looking at Indian imports, one should net out the oil import component.

[86] Sensitive lists will still remain.

[87] These are only exports of goods. This and figures that immediately follow are from *Economic Survey, 2007-08*.

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