

# Rationale for a BIMSTEC Free Trade Agreement

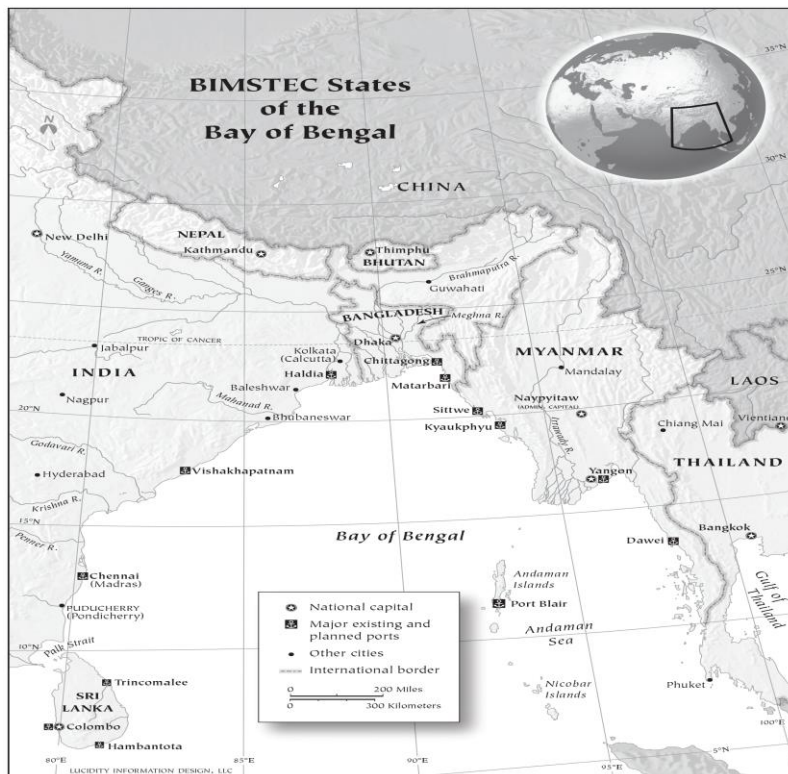
by Dr. A. Didar Singh



That most people, even of this region, haven't heard about a BIMSTEC FTA speaks volumes for the state of affairs! Member countries of BIMSTEC initiated negotiations for a Free Trade Agreement (FTA) as early as 2004<sup>1</sup>. However even after 20 rounds of negotiations (and 14 long years), the FTA itself is yet to be signed by the BIMSTEC members. (India wanted all to sign this by 2017 but that year too has passed).

### Rationale for a BIMSTEC FTA

The BIMSTEC area continues to be one of the least integrated regions across the globe, despite the fact that it's an Asian sub-region with member countries being contiguous to each other.



(This map highlights the contiguous element of the geographical position of BIMSTEC members)

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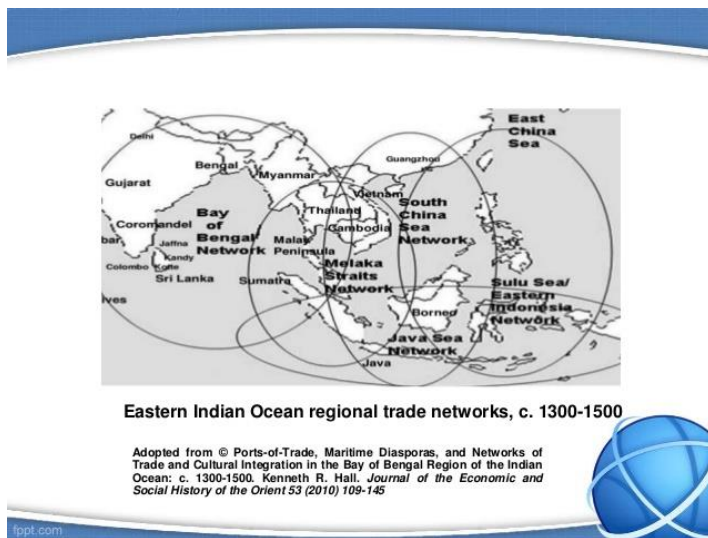


**Ambassador Hemant Krishan Singh  
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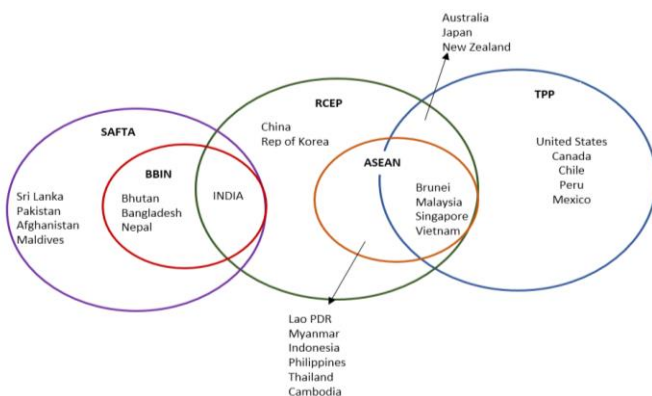
Bangladesh and India share a 4,096-km long border and there are numerous bilateral trade agreements between the two. Similarly, India and Sri Lanka signed a FTA in 2005. India also has an FTA with Thailand and has open borders with Bhutan and Nepal. India's north-eastern states have an unfenced border with Myanmar. For India, BIMSTEC is already a sub-region with few trade and investment barriers, yet trade in the region has not reached its optimum level.

However, the other countries in BIMSTEC do not have agreements amongst themselves. For instance, Thailand has trade agreements in place with countries like Australia and Peru but none bilaterally with its immediate neighbours. Multilaterally though, they are part of the ASEAN FTA. Thus, it is imperative that the member countries push forward for a timely consensus on a BIMSTEC FTA.

In effect history shows us several traditional trade routes in this area:



However, in terms of economics, connectivity, mobility, and geostrategy, countries adjacent to the Bay of Bengal are less integrated today than they were fifty years ago. Against this backdrop must be seen the host of trade agreements operating in the region:



### Why FTA?

There are three types of trade agreements: A) unilateral (eg. when a country imposes trade restrictions and no other country reciprocates or it unilaterally reduces tariffs – but this hardly happens). B) Bilateral, which are between two countries where both countries agree to loosen trade restrictions to expand business opportunities between them; and C) Multilateral, involving three or more countries, which are the most difficult to negotiate but have the greatest benefits since the whole region can benefit. Regional trade agreements have covered more than half of international trade throughout the world since the beginning of the 1990's. A shining example has been the ASEAN Free Trade Area (AFTA) which was established to improve regional economic competitiveness with a strong export focus that helped all its members improve their economic performance.

FTAs have several advantages, from increased economic growth, FDI and technology transfer to a more dynamic business environment and spreading economic reform. Free trade agreements enhance the trade of goods efficiently sourced between member countries and lead to trade creation that improves welfare.

Of course, there are some disadvantages such as possible job outsourcing (example of NAFTA where US jobs went to Mexico), crowding out of domestic industry and reduced customs revenue. All such disadvantages are short-term and the benefits of liberalization and open markets is well documented and well-known. The key is domestic regulation to protect against possible disadvantages and a transparent and liberal regime that supports business and economic growth.

### BIMSTEC FTA

Sandwiched between SAARC and ASEAN, BIMSTEC can be and is a bridge that would benefit and link both regions. In fact, the original intention of the member states of this inter-regional body was inspired by the idea of turning the two regional groupings into a free trade area and opening the door for investment, identifying priority projects on trade, transportation, tourism, energy, health and agriculture through collective action.

It is in this context that we should view the plans for the construction of a trans-Asian Highway and setting up airline connections linking important cities of the member countries. The motivation was the tremendous opportunities that would arise among the member countries and would be of great significance in the emerging globalised environment. Experts have examined the requisite characteristics based on the criteria of income, production and trade flows and found favourable indications for an FTA that would create relative advantages for all member states.

The free trade area idea would not only enhance trade and investment, but also liberalise trade in both goods and services and facilitate economic integration of the region. This inter-regional body could even help the countries of the region to collectively take up WTO issues for a better deal in their favour.



Every BIMSTEC Ministerial and annual summit has called for an early conclusion of a free trade agreement (as well as expeditious negotiations on the Agreement on Services and Investment) besides agreement on technology transfer, along with transportation connectivity and trade facilitation among the BIMSTEC countries. All these are linked issues that together would transform the region into a dynamic economic growth area. In effect the smaller BIMSTEC countries should see regional multilateralism as a potential check on the rising capabilities of China, India, and major external powers be they the US, UK or Europe.

All these member states around the Bay of Bengal need to recognise and work on the premise that their national economic and security interests are increasingly tied to the ability to cooperate across borders through regional institutions. An FTA is the obvious way to move forward.

Despite these obvious benefits the fact is that the FTA remains unsigned. The key issue is the negative list for each country, the pruning and tariff reduction schedule for each country.

Experts have opined that, given existing trade preferences among the BIMSTEC countries under various existing bilateral

and regional FTAs, implementing the BIMSTEC FTA may not necessarily increase intra-BIMSTEC trade in the short term, but it could certainly activate production links among member countries, generating new value chains and become globally more attractive.

### Economic Landscape

BIMSTEC members are Bangladesh, Bhutan, India, Myanmar, Nepal, Sri Lanka, and Thailand. As Table 2. below shows, there are certainly differences in Per Capita, GDP growth and Ease of

Doing Business, however all seven are developing countries that are quite dependant on trade for their growth and development.

Table 2. Development and GDP Indicators for BIMSTEC Members

	GDP Per Capita (PPP in 2016)	Average Annual GDP Growth (2012–2016)	2016 UNDP Human Development Index Rank (out of 188)	2017 World Bank Ease of Doing Business Rank (out of 190)	Trade as a Percent of GDP (2016)	2016 World Bank Logistics Performance Index Rank (out of 160)
Bangladesh	\$3,587	6.5%	139	177	38.0%	87
Bhutan	\$8,918	5.5%	132	75	82.8%	135
India	\$6,583	6.9%	131	100	39.8%	35
Myanmar	\$5,732	7.3%	145	171	45.5%	113
Nepal	\$2,483	3.7%	144	105	48.9%	124
Sri Lanka	\$12,337	5.3%	73	111	50.5%	N/A
Thailand	\$16,946	3.4%	87	26	123.1%	45

Sources: UN Development Program, World Bank

These differences in growth performance may remain for some time as the countries are at varied stages of development and yet we cannot ignore the fact that all member countries are developing countries (four are LDCs) with a whole host of common issues from addressing inequality to harnessing agricultural growth. The highly populated Bay of Bengal carries a lot of economic promise with a combined gross domestic product (GDP) close to \$2.7 trillion. IMF estimates show an overall GDP growth for this region at 6.9% against a global average of 3.1. It’s also home to 1.5 billion people with a geographical contiguity between the member states. In other words, the stage is set for things to happen here – especially for regional and mutually beneficial trade.

### Should other countries like Japan be included in a BIMSTEC FTA?

Japan has had close relations with several of the BIMSTEC countries. There is thus a case for Japan to join this regional grouping, first as an ‘observer’ and later moving up as a ‘dialogue partner’ before being accorded membership.

There are several benefits for Japan cooperating with BIMSTEC. These range from infrastructure and connectivity projects to tourism and investment. BIMSTEC presently lacks an economically and technologically advanced partner that could provide significant ODA assistance.

Moreover, BIMSTEC member countries are agrarian economies. So, a proper framework agreement to identify areas of economic cooperation including issues of Sanitary and Phytosanitary (SPS) and technical barriers to trade (TBT) is required to increase intra-BIMSTEC trade. Japan is considerably dependent on imported agricultural and food products. BIMSTEC countries can produce and supply food and agricultural products at lower price points as compared to other developed countries. This would particularly benefit the smaller countries.

Though China too is working to enlarge its footprint in the region through significant investment in infrastructure projects, not only do these investments lack transparency but could well lead to debt traps for the host countries, as many experts are today predicting. Moreover, as experts opine, bringing China into BIMSTEC may initially lead to immediate financial dividends but could weaken the organization in the long term, given Beijing's history of adopting divide-and-rule practices toward other regional organizations like ASEAN and the EU.

There is a valid case made out to open up BIMSTEC to cooperation with other extra-regional powers committed to inclusive regionalism. These could include Australia, the European Union, and the United States (and of course Japan), as well as multilateral institutions like the Asian Development Bank, World Bank, UNESCAP and IORA etc. It could also include "natural partners" beyond the region, such as Cambodia, Laos and Vietnam.

Expanding the BIMSTEC grouping may have certain pluses but it would substantially change the composition and culture of the group. This is something only member states can discuss and decide upon. Meanwhile having a regional FTA could provide a platform for specific economic and trade cooperation with key countries and regions that already have an FTA (e.g. ASEAN or even SAFTA and later RCEP).

### Conclusion and Recommendations

It's not just the FTA but in fact the idea of BIMSTEC itself that is missing from the public consciousness in the region despite the historical connect that the Bay of Bengal and South East Asia had. This perception needs to be reversed.

Trade accounts for over 60 per cent of combined GDP of BIMSTEC members. Between 2002 and 2017, the share of intraregional trade among BIMSTEC member states rose from 3.6 to 5 percent. This remains lower than comparable figures in other regional trade blocs, including 7 percent among SAARC members, and 29 percent among ASEAN states. However, tariffs are no longer the major barrier to intra-regional trade, but cost and time to trade remain relatively high. At the same time, BIMSTEC countries face huge trade burden due to a wide variety of non-tariff measures (NTMs). The way forward here is to negotiate MRAs (mutual recognition agreements, for trade in goods initially).

Any discussion on BIMSTEC and an FTA between the member states invariably raises the example of SAARC and SAFTA and the possible lessons to be learnt from there. It has been argued that Intra-regional trade among SAARC countries is low mainly because of the lack of comparative advantages in their economies. The argument is that being mostly agrarian economies they export similar products and therefore intra-regional trade remains low (at just 6-7%). One example is tea exports from India and Sri Lanka. Question is whether this holds true for BIMSTEC also? Probably does. Even though there are some complementarities in the exports and imports of the member countries, intra-regional trade is low due to many hurdles like tariff barriers, lack of connectivity and transportation problems.

While accepting the basis for this argument, it would also be important to note that trade and economic collaboration are both dynamic issues in a fast changing economic world. Comparative advantage itself is today being questioned. The classical theory (Ricardo, 1817) explained international trade in a free market concept. It is however dependent on similar stages of development of the production facilities and market. This may not be applicable to vast parts of the globe, and moreover today that market and large production in it, is based on global supply chains (and in BIMSTEC we see little signs of any strong regional value chains). The availability of productive resources (land, labour and capital) keep changing in every modern economy. Now there is a fourth factor that impacts – technology, or specifically AI (Artificial Intelligence). This can and is transforming all manufacturing, services and trade. Countries of BIMSTEC must learn to absorb the positive potential of this new technology. Sharing best practice for correct policy formulation would strengthen both

the sub-region and each of its economies. An FTA for trade and economic collaboration would ensure this.

### BIMSTEC E-Commerce Collaboration

As an example, as with the India-ASEAN FTA, trade will jump if there is promotion of e-commerce, since digital economy and connectivity are growing across the region. The Indian e-commerce market (\$40bn) itself is expected to reach US\$64bn by 2020 and US\$200bn by 2026. This would be a large opportunity for all of BIMSTEC. The main advantage here is low entry costs which can help Start-ups and MSMEs to access both the Indian and global markets. For example, they could have shared platforms for handicrafts, arts, photography etc, all of which are so dynamic in the region. To promote this of course there would be need to establish common Market-place EC Models that would work on common standards, IPR, Payment models and skilled human resources. Such collaboration would promote innovation; PPP and socio-economic collaboration across the region. The FTA would provide an excellent platform for this.

It is also argued that all the BIMSTEC economies are labour surplus countries with high unemployment of unskilled labour as an issue. Analysis shows that removal of tariffs among the countries (FTA) would result in significant welfare gains. There may of course be some initial adverse impact on trade and industry but opportunities for employment would increase with full implementation of a BIMSTEC FTA. This is a very positive finding since it addresses the common problem of poverty and inequality that all the members face.

India is by far the region's largest economy. Its interest and responsibility has to be portrayed as particularly notable. After all India's exports to the BIMSTEC economies depends on their market and GDP. Similarly, these economies export to the Indian market opportunities and price is dependent on the exchange rate prevailing. India's role as an informal leader must be projected especially in the BIMSTEC FTA. The 'gravity model'<sup>2</sup> suggests this as an obvious choice for India. New Delhi however must back up its intentions by bolstering its investment in the organization and concluding the FTA while appreciating the interests of other members.

Prospects for an early signing are not so bright and therefore the members should focus on other trade related improvements such as trade facilitation via liberal transit, business-friendly customs, transport corridors, etc. Such a process will partly address some of the non-tariff barriers in the region and give the required fillip to trade. In fact, tariff

reductions may not matter as much as non-tariff trade barriers. It has been emphasized that these less tangible obstacles are the "actual culprits" impeding integration. BIMSTEC should focus on facilitating the (1) mutual recognition of national standards, (2) harmonization and development of common standards, and (3) identification and targeted exploration of existing value chains across the region. This would escalate any future FTA. In all of this business has a key role and the Chambers of Commerce and Industry, including the BIMSTEC Chamber have to push all of this because it is business that ultimately stands to gain.

There is also a view from experts that BIMSTEC members can consider settling for a limited FTA since a limited trade deal is currently better than no deal. It is also argued that BIMSTEC itself will take shape only after an FTA is signed. The trade negotiations have presently covered: tariff concessions on trade in goods; Customs cooperation; trade in services; investment cooperation; and dispute settlement. Four draft agreements already exist: (i) Trade in goods; (ii) Rules of Origin; (iii) Dispute Settlement; and (iv) Customs. These however, are still to be finalised.

Another very valid view holds that much water has flowed under the bridge since 2004 when the initial FTA negotiations started. It's a vastly different world and region today. It is therefore important to renegotiate the FTA 'ab initio' as BIMSTEC has the Chance to do so and come up with a comprehensive FTA that includes economic cooperation in trade in goods and services as also investment. Maybe the way forward is to mix both these ideas, i.e. Finalize the draft agreements as the basis of moving on a comprehensive FTA.

As the new BIMSTEC Secretary General, Mr. Shahidul Islam stated recently, "that FTAs were no panacea for development, but they represented a crucial first step towards spurring growth and development in the region".

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#### End note:

<sup>1</sup> The BIMSTEC Free Trade Framework Agreement was concluded in 2004 and the Trade Negotiating Committee (TNC) of BIMSTEC was set up thereafter to come to an agreement on trade related measures such as tariff concessions on trade in goods, custom cooperation, trade in services, investments and dispute settlement mechanisms.

<sup>2</sup> *The Gravity model of international trade is a model that, in its traditional form, predicts bilateral trade flows based on the economic sizes (often using GDP measurements) and distance between two units*

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