

First South Asia Economic Summit

Colombo August 28-30, 2008: Opening Statement

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It is an honour and a great pleasure to be a participant and also represent the World Bank as a co-sponsor of this First South Asia Economic Summit. It has been my privilege to work very closely with Saman Kelegama in helping design this Summit. But of course all credit goes to him and his distinguished Institute of Policy Studies for arranging and hosting this Conference.

The timing of the Conference is just right, coming in the backdrop of the 15th SAARC Summit that was successfully concluded from August 2-3 in Colombo. Also, as I will elaborate a bit, the development challenges ahead for South Asia are immense. And these cannot be tackled comprehensively without more and better regional cooperation.

a) The Challenge

South Asia has attracted global attention because it has experienced rapid GDP growth over the past 27 years, averaging nearly 6 per cent per annum. Yet, it faces many challenges. There are *two faces of South Asia*. The first South Asia is dynamic, growing rapidly, highly urbanized, and is benefiting from global integration. The second South Asia is largely agricultural, land locked, exhibits high poverty, suffers from many conflicts, and is lagging. The divergence between the two South Asias is on the rise. Many policy and institutional constraints contribute to this dichotomy. One important constraint is regional conflict that has made South Asia one of the least integrated regions of the world. While progress has been made in reducing trade barriers with the rest of the world, intra-regional trade is a mere 5 percent of total official trade as compared with 45 per cent in East Asia. Capital flows through legal channels are negligible, transit arrangements are cumbersome and expensive, and the physical connectivity is limited and restrictive. Additionally, lack of effective cooperation has constrained progress on a range of public goods including climate change, water management, HIV Aids and disaster management.

The cost of weak regional cooperation tends to hurt the poor more than the other segment of the population. Two of the poorest South Asian countries are Afghanistan and Nepal; both are land-locked. Several lagging regions in the larger South Asian countries of Bangladesh, India and Pakistan are located in the border areas and suffer from lack of market integration. Over 500 million people, most of them very poor, live in the Indus and the Ganges-Brahmaputra river basins. These great basins are shared by six nations and are characterized by almost no cooperation and, instead, marked political sensitivity and tension. Several attempts to promote cooperation have failed. Climate change is predicted to have serious impacts on the monsoon, on river flows and on the rising sea level, with increased incidence of floods and droughts in areas where current shocks already regularly and severely affect the lives and livelihoods of large numbers of people.

b) The Opportunity

In addition to policy and institutional reforms aimed at removing domestic constraints to growth and job creation, market integration and regional cooperation ought to be key elements of a regional strategy for removing the dichotomy between the two faces of South Asia and eliminate poverty over the longer term. South Asia needs two types of market integration—providing countries, especially the landlocked ones, with a broader access to regional and global markets; and integrating the lagging regions within each country with the growth centres without regard to boundaries. The geography of South Asia is such that both types of market integration will require regional cooperation. After Europe, South Asia has the second largest number of cities in the border region. Most countries share a common border with India.

The unique geography of South Asia—distance and density--has the potential to raise growth through increased trade. South Asia has the highest population density in the world. Distance of cities from border is low. These features naturally propel trade between countries, but presently this is hindered by policy barriers. For example, currently at \$1 billion, trade between India and Pakistan could jump to \$9 billion if trade restrictions are removed. Similarly, estimates suggest that intra-regional trade in South Asia could increase from \$5 billion to US\$ 20 billion if restrictions on trading with neighbours are removed.

The benefits of scale economies could be even bigger, particularly to the small landlocked countries. As in Africa, the smaller countries in South Asia do not have the necessary scale economies to invest in infrastructure (energy, telecom, transport). Regional market integration could provide the benefit of scale economies to the smaller countries to invest in infrastructure. Nepal, for example, could double its GDP if it could export hydro-based electricity to India, an energy thirsty country.

Benefits of cooperation on water and climate would be immense. From the Himalayas, where glacier melt is already changing water flows in ways that remain to be fully understood, to the coastal floodplains of Bangladesh and Pakistan, South Asian countries need to adapt to climate change. This can provide the much-needed trigger for opening a dialogue on regional water cooperation. For example, cross-border cooperation on water between India, Bangladesh and Nepal offers the only long-term solution to flood mitigation, and would benefit over 400 million people.

c) Lessons of International Experience

Along with the forces of globalization world economies are interlinked through a variety of regional and sub-regional cooperation agreements, all aimed at improving social and economic prosperity of member countries. The most advanced and effective cooperation agreements include the European Union (EU), the North American Free Trade Agreement (NAFTA), the Association of South East Asian Nations (ASEAN), the Cooperation Council for the Arab States of Gulf (GCC) and the Caribbean Community (CARICOM). Although the evidence is less clear, the African Union (AU) holds promise for being more effective than its two predecessors the Organization of the African Unity (OAU) and the African Economic Community (AEC). Two major cooperation agreements in Latin America, the MERCOSUR and the Andean Community of Nations (ANDEAN), which have suffered from recent political and economic difficulties in several member countries, have now decided to join forces to form the Union of South American Nations (UNASUR/UNASUL).

Examples of successful cooperation agreements reinforce the point that possible gains for South Asia from effective cooperation and partnerships can be substantial. In particular, the experience of East Asia is illustrative of the potential gains from more and better cooperation. Cross-border physical connectivity has improved tremendously through land, sea and air-based transport network, private sector-led vertical integration of production networks has spurred industrial productivity and growth, and e-commerce is flourishing.

International experience also suggests that political constraints and historical conflicts need not be permanent barriers to development cooperation. Neither is the presence of a dominant member country a necessary threat to cooperation and shared gains. For example, the members of the European Union have fought numerous wars in the past, many of them far more intense, long drawn and expensive in terms of loss of human lives and material resources than South Asia. Similarly, member countries diverge considerably in economic strength. Yet they have found it mutually advantageous to come together and formulate a formidable economic union. In East Asia, the economic dominance of China has not prevented very effective regional cooperation with the much smaller East Asian countries.

d) Improved Political Climate for Cooperation in South Asia

In South Asia, regional cooperation efforts culminated in the formation of the South Asian Regional Cooperation (SAARC) in 1985. Following initial teething problems and a host of political constraints, SAARC is making progress, which is evidence of improved political prospects for cooperation. In our own consultations with South Asian leaders, we find strong evidence of interest to move forward with concrete proposals.

The next step is to identify concrete areas of cooperation where multi-country efforts would yield tangible benefits for citizens. The immediate priority areas are well known: promote trade facilitation by removal of all trade barriers; improving regional transport by removing transit restrictions and opening up port facilities for international trade; promoting trade in energy in all possible ways including hydro-power, gas pipelines and regional grid facilities; and water cooperation to resolve flooding and irrigation problems. Cross-border transactions must be de-politicized and pursued on a commercial basis. Enabling national and international private investors to participate in these transactions hold the most promise of success than bilateral political deals. International financial institutions can also play a useful role. Where legal agreements are needed, these can be best pursued multilaterally to avoid any perceptions of dominance.

It is not realistic or necessary to expect that all political and social conflicts will have to be resolved first before meaningful cooperation can happen. Indeed, economic cooperation is also a powerful means for resolving political and social conflicts. Trust and goodwill at the citizens' level can be a credible way for resolving conflicts. Economic cooperation by raising citizens' welfare can be instrumental in building this trust. Political forces can provide impetus to this by reducing policy barriers to regional integration.