How China's 'One Belt One Road' Will Help India Integrate South Asia

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The dynamics generated by the new connectivity infrastructure China is pushing across Asia and Europe will impel India and Pakistan to normalise their economic relations too

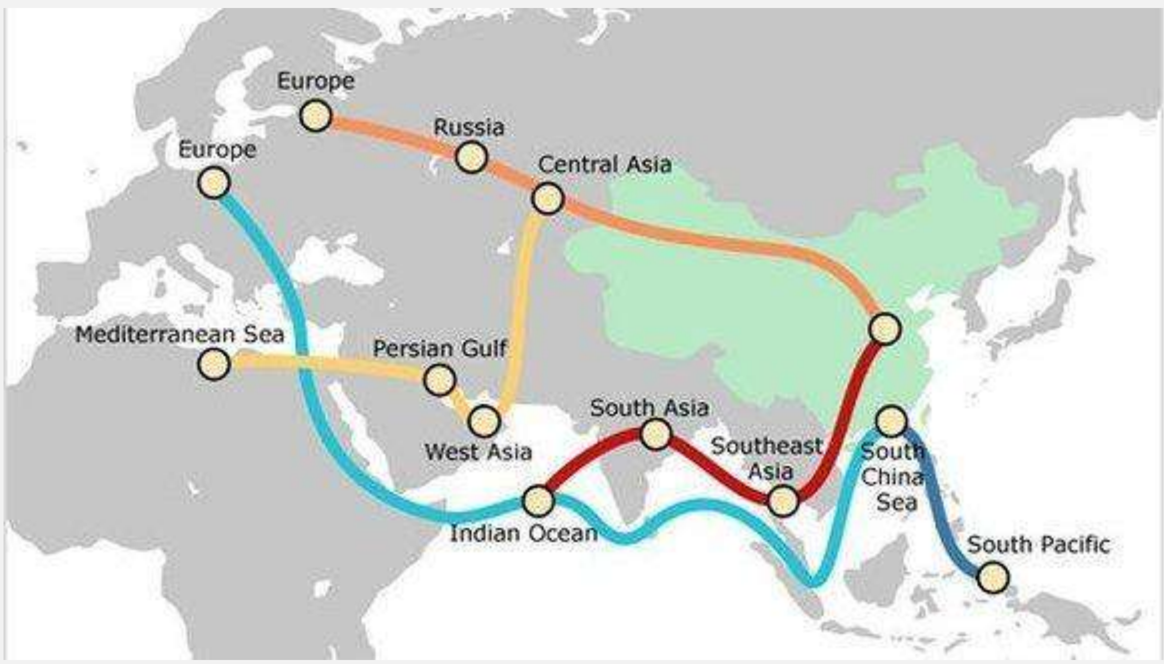
Pakistani trucks at the Wagah border. Credit: Guilhem Vellut/Flickr CC 2.0

One current trend not so well recognised by analysts is that GDP in the South Asian region is growing at close to 6% per annum in the midst of a near recession in most of the emerging economies outside of China. China itself is slowing down to relatively lower levels of growth compared to its past performance, but is still expected to clock at least 6.5%. Indeed, it is in this backdrop that China is actively pursuing plans to invest an estimated $150 billion on its One Belt One Road (OBOR) project connecting countries from Asia to Europe via rail, road, energy pipeline, sea lanes and port infrastructure.

Some western scholars have compared the scale of this proposed multi-dimensional infrastructure development along the traditional silk route – bringing South Asian economies closer to China, Central

Asia and West Asia – to the Marshall Plan under which the United States spent some $13 billion over 6 years to reconstruct infrastructure in war ravaged Europe. America used its excess industrial capacity to rebuild Europe and by the end of the exercise the US economy was nearly 50% of world GDP. It was probably the biggest stimulus package of the 20th century. China may be attempting something similar. In fact, the inflation adjusted value of $13 billion spent by the US after WWII is roughly $130 billion today – the amount China is likely to spend on its ambitious OBOR project. This will act as a huge booster for the South Asian economies whose connectivity to various world markets will improve manifold.

My contention is that OBOR, under the broader supervision of China, will force open many a trade barrier between India and Pakistan too. It will create a non-linear, positive kicker for trade between the two largest South Asian economies. Recently, Khurshid Mahmud Kasuri, former foreign minister of Pakistan, argued that Pakistan is the critical link which will connect India with West Asia and Central Asia. China's OBOR project(both land and maritime) will facilitate and deepen the conectivity between South Asia, Central Asia, West Asia, Europe and Africa. South Asia could be on the cusp of an economic transformation based on these possible developments.



The cartography of One Belt One Road. Credit: globalconnections.hsbc.com

South Asia is currently regarded as a sweet spot by global investors in the midst of world growth pessimism. The current situation therefore demands that South Asian economies, particularly India and Pakistan, explore their trade potential fully in order to buck the trend of declining trade in other regions. Can India and Pakistan leverage this situation to their advantage by further deepening economic relations? An empirical study by economists of a Delhi-based think tank, ICRIER, says the real potential for two-way trade between India and Pakistan, if all tariff and non-tariff barriers are removed and trading in energy included, is $30 billion. This is about 15 times more than the current level of trade between the two nations. Energy trading is a big component of this empirical study and OBOR will particularly facilitate a common and interlinked energy market in this larger region.

Lack of imagination

This is a real possibility if there is relative peace, more openness and all round engagement. Currently, this possibility is beyond the imagination of most pundits who sit on both sides of the divide. Experts and state actors alike are often prone to limiting their imagination in the name of realism. State actors are risk averse and generally opt for an incrementalist approach. The real dynamism comes from below as shown by the economic agents on the ground who, inspite of myriad restrictions on trade imposed by suspicious state actors on both sides, have enabled commerce to leap by nearly ten times in a decade. And this is achieved with all manner of trade barriers still in place.

Ironically, the only other country with whom India is growing its trade at such a rapid pace is China, which too has a history of disputes with India. It makes one wonder whether there is some odd correlation between political bitterness and greater trade engagement, as also seen between China and Japan over the past decades. Or is there some subtle message coming from the economic agents on the ground telling the state actors to recognise ground realities reflecting a desire for economic progress and development?

Since Pakistan acts as a key link for South Asia to connect with Central Asia, West Asia and China, a thaw in economic ties between India and Pakistan is critical.

A positive development in India-Pak trade occurred in 2012 when the two sides decided to do away with their decades old practice of trading based on just a small positive list of items. Until 2004 Pakistan traded with India based on a small positive list of 750 items. This list of tradable items expanded marginally in later years but 80% of the more than 7,800 items of trade remained in Pakistan's negative list and were not traded at all. This arrangement changed in a matter of 12 months – from April 2011 to May 2012 – in the course of the Commerce Secretary level talks between the two countries. Now Pakistan and India just have their small negative lists, but all other items are open to being traded. However, non tariff barriers and restrictions to trading through the land border at Wagah persist. Less than 200 items are traded across the land border.This remains a huge barrier to trade still.

Going beyond the 2012 breakthrough

Pakistan took the big step of granting in-principle non-discriminatory trade treatment to India, something it should have logically done in 1996 itself when India had accorded MFN to Pakistan under the WTO mandate. India has committed to reciprocating by removing myriad non tariff barriers to trade with Pakistan. So far, however, both decisions remain unimplemented. Trade procedures are as important as the initial act of opening up the market. The devil often lies in the details of procedures. There needs to be a mindset change where suspicion is replaced by trust in bilateral trade and investment. The possibilities now are immense.

Just to give you an idea of the gradually changing reality in India-Pak economic engagement, Pakistan only allowed about 1934 items out of a list of 7800 products to be imported from India until 2009. Even out of the 1934 products in the positive list of imports, less than 150 items were allowed by Pakistan to be actually traded via the Attari-Wagah land border.

It is in these highly restrictive circumstances that trade officially grew ten times in the decade preceding 2012. As per the new free trade agreement to be implemented, Pakistan will open up the bulk of the 7800 products for imports in a phased manner and increasingly a larger number of these will be from the Wagah border. Of course, the progress in the implementation of this phased opening up of trade is affected by the general climate of political and diplomatic engagement between India and Pakistan. The past two years have not seen a very conducive environment for rapid progress on the further liberalisation of trade through Wagah border. The Modi government got off to a good start but its efforts have been marred by complications around how the new dialogue process with Pakistan should be structured after the composite dialogue framework got jettisoned post the Mumbai terror attack in 2008.

However, if the past is any guide, progress on the trade front will continue inspite of other negative political developments that may arise from time to time. As per the 2011-12 arrangement, Pakistan would eventually have a small sensitive list of items – around 600— whose import will be allowed at high duties in order to protect their local industry. Barring these high duty products, the rest of the 7000 odd items will be traded at less than 5% duty as per the broad trade agreement. India too will have a small list of sensitive items where it would impose higher duties. These include textiles, tobacco etc where India wants to protect its local industry. Of course, India can be much more generous to Pakistan and offer it the same terms as it does to Least Developed Countries in the SAFTA region like Bangladesh, Nepal, Maldives, Afghanistan and Bhutan. Eventually India's generosity is what will determine the formation of a truly robust South Asia Free Trade Zone with all products flowing across the borders at zero duty and a much freer movement of skilled workers also becoming a reality.

OBOR as catalyst for integration

The greatest irony today is that South Asian economies are separately striking free trade agreement in goods and services with nations across the seas but not among themselves inspite of sharing borders with each other. If the OBOR project becomes a reality over the next decade, there is bound to be much greater trade among the economies that get hyperconnected by the OBOR infrastructure. Once countries located along OBOR see the positive economic and trade benefits, they will also pitch in with own funds to supplement the silk road infrastructure.

The continuing shift in the axis of economic power to the east will force South Asian economies to naturally look at institutionalising SAFTA's connect with Central Asia and China in a win-win framework. The larger global dynamic will make this happen faster even if state actors are slow in recognising this. Data collected post the global economic crisis of 2008 shows a marked increase in the pace of trade and investment engagement among the Asian economies as opposed to between Asia and the West. These are historically driven forces which state actors typically recognise after a lag. Indeed, a deeper economic integration within South Asia as also between South Asia and China is embedded within the larger framework of China's attempt to build massive rail, roads and port infrastructure across the territory of Central Asia, Afghanistan and Pakistan, thereby dramatically shortening cargo transport time between Asia and Europe/Africa/Middle East.

China's grand OBOR plan could power the growth of Asia, and the world, in the next two to three decades. Institutions like the Asian Infrastructure Investment Bank, of which China, India and even European nations are members will partly finance the growth of such infrastructure. Within this larger project, I also forsee South Asia benefiting immensely through deeper trade connectivities with the global markets and both India and Pakistan will be drawn into this mega development framework.

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