

Informal Trade a Challenge for Cooperation in SAARC

Abstract:

SAARC, The South Asian Association for Regional Cooperation is an organization of South Asian nations, established on December 8, 1985. The main rationale behind its establishment is to develop an affable environment through summit diplomacy where all may interact peacefully with each other, cultivate sustainable peace and promote mutual economic well being by harnessing available resources in the region through the peaceful process of economic integration. Nevertheless, after 32 years of establishment, neither South Asian countries have been able to push the process of peace and economic integration into full swing nor the SAARC shows it's enough potential to promote peace, harmony and economic integration. A successful regional organization is supposed to be basically a trading organization. SAARC could not even take primary steps towards the promotion of mutual trade. One main reason behind the weak cooperation is informal trade between SAARC countries. This paper is an attempt to analyze the Informal Trade between SAARC Countries which act as a barrier in the cooperation of SAARC. This paper also offers some solutions in the form of recommendations so to speed up the progress of cooperation in South Asia.

KEY Words:

Bilateral agreements, Informal trade, South Asia, Interstate, Tariffs, SAFTA, in intra-regional, illegal trade.

Introduction

Regionalism as an important factor in international politics is a manifestation of a dominant trend in human history towards large political formation. ¹ The trigger for the creation of regional organizations is varied. They include a strong desire for reconciliation and rebuilding after a destructive war; keenness to dampen ongoing intra-regional conflicts; and a need to avoid the embarrassment of being a region devoid of a regional entity. The South Asian experiment in regionalism, however, falls under the third category because this was one of the few regions not to have made any attempt to build a regional organization until the 1980s.² Despite being one of the most coherent and viable regions, South Asia did not see any organizational development during the first four decades of the post war period. In sharp contrast to this, during the same period, a number of regional organizations of different hues have emerged in various other geographical regions of the world.³ Consequently, regional associations are fast becoming an important and effective new scene for political and economic interaction in the world. In this new environment the importance of regional communities and functional groupings has been heightened. Regional, political and religious blocs of nations now provide platforms for a number of countries to exercise influence in global affairs. Interest in greater regional economic integration, fuelled partly by the achievement of an economic union and a single currency in

¹ Indra Mohan jha, 'SAARC: The Road Ahead: A Case for Constructive Diplomacy', 2004, National Book Organisation, New Delhi, p.1.

² Kripa Sridharan, 'Regional Organisations And Conflict management: Comparing Asean Andsaarc', National University Of Singapore, March, 2008, PP.1-2.

³ E Sudhakar, SAARC Origin, Growth and Future , New Delhi: Gyan Publication, 1994 , pp. 17-18.

Europe, has grown in different parts of the world. This includes South Asia and the regional organization known as the South Asian Association for Regional Cooperation (SAARC), which has announced the goal of attaining an economic union and expressed the desire for a common currency. SAARC is a fairly recent association, established in 1985 by the seven member states of Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan, and Sri Lanka.⁴ It was established on 8th December, 1985 after about four and half years of its preparation. The basic aim of the Association is to accelerate the process of economic and social development in member countries through joint action in the agreed areas of cooperation.⁵ The South Asian Association for Regional Cooperation (SAARC) is an organization of South Asian nations; its headquarter is in Kathmandu, Nepal.⁶

The idea of regional cooperation in South Asia was first initiated by late President Zia- Ur- Rehman of Bangladesh who visited Nepal, India, Pakistan and Sri Lanka during 1977- 78 to explore the possibilities of regional economic cooperation among the SAARC Countries. The SAARC was established with good feelings and intentions to establish lasting peace in the region, economic cooperation and for solving the problems of the people living in South Asia.⁷ SAARC, despite its established offices and several permanent institutions, could neither become an adequate and productive institution nor could develop as an effective dispute resolving way. It could not even play any noteworthy role in facilitating and improving the lifestyles of the member countries.⁸ A successful regional organization is supposed to be basically a trading organization. SAARC could not even take primary steps towards the promotion of mutual trade. The states in South Asian region are still far from reaching its real collective trade potential. Illegal cross-border trade, which is perhaps higher than the legal cross-border trade, according some inspections and observations, is the main critical, factors that preventing South Asia from achieving its full trade potential. This paper is mainly intended to analyze the Informal Trade within SAARC. Efforts have been made to cover all the aspects in an elaborated manner with objectivity.

Illegal Trade: The problems that faced in cross border trade within the South Asian region are due to the aversion between the member states on signing a free trade agreement over the years. However, there are several trade agreements made by India with Maldives, Nepal, Bhutan, Sri-Lanka and Recently with Afghanistan. Due to the political and economic concerns among India, Pakistan and Bangladesh, there were no successful trade pacts among them. However In order to liberalize trade policies among SAARC countries, South Asia Preferential Trade Agreement (SAPTA) was signed by the member states in Dhaka in 1993 for lower tariffs within the region. In 2004 SAARC countries devised the South Asia Free Trade Agreement (SAFTA) which

⁴ Muhammad Jamshed Iqbal, *SAARC: Origin, Growth, Potential and Achievements*, National Institute of Historical and Cultural Research in Islamabad,(pdf), Retrieved 11 November 2013.

⁵ Charter of the United Nations "Regional Arrangements," Published by the United Nations Department of Public Information, December, 2006, DPI/511, New York- 10017, p 34.

⁶ *IOSR Journal Of Humanities And Social Science (IOSR-JHSS)*, Volume 15, Issue 6 (Sep. - Oct. 2013), PP. 01-3, Available at, <http://www.iosrjournals.Org>

⁷ Ahmad Raza Khan, 'A Research Journal of South Asian Studies', Vol. 30, No.1, January -June 2015, pp.293-94

⁸ Ahmad Raza Khan, p.294.

created a framework for the establishment of a free trade area by eliminating trade barriers and scaling down tariffs.⁹

South Asia is now looking forward to an Economic Union in 2020. The SAFTA treaty seeks to allow free cross-border movement of goods within the region, with the plan for a list of responsive items from member countries to protect national interests. It is also conceptualized that SAFTA will lead up to US \$ 31 billion approximate increase in intra-regional formal trade within the period from 2007-2019. However, the states in South Asian region are still far from reaching its real collective trade potential. Illegal cross-border trade, which is perhaps higher than the legal cross-border trade, according some inspections and observations, is the main critical, factors that preventing South Asia from achieving its full trade potential. The increase in imports will only take place if the consumer goods are less available in the market. If there are no legal trade arrangements to import or export the goods legally, the illegal import, export will eventually increase.¹⁰ According to the latest data, the informal trade in the South Asian region was over US \$ 3 billion, which is more than the formal trade in this area. India's informal trade deal with Pakistan is almost ten times the formal trade, whereas informal trade with Nepal and Bangladesh is equal to formal trade and its informal trade with Sri Lanka is almost 1/3 of the formal trade. Of the US\$ 2 billion informal trade between India and Pakistan, almost half trade is through 3rd countries like Dubai, Central Asia, while the rest is through cross border informal trade.¹¹

We will now go to informal trade details. By definition, it implies bypassing the official channel and in that sense traders have to work out the Methods of taking out such trade.

(1) Methods of Illegal Trade: Two aspects need to be considered when explaining the methods of illegal trade, first is physical transfer of goods by illegal ways and second financing for illegal trade.

(a) Physical transfer of goods by illegal ways: Illegal trade takes place through both authorized and unauthorized channels. The methods of both types of Trade are different and that is why the reason must be clear. Relatively large Traders who are engaged in formal trade take illegal trade through accredited channels. They are knowledgeable and are familiar with the policies regarding trade in the region. Information on illegal trade concerning assets and methods is closely interlinked with that of formal trade. Relatively large part of trade takes place through violation of the rules of origin treaty and the transit treaty. Such information is available in large traders engaged in formal trade. Thus, by being engaged in formal trade the information costs on trading informally are substantially reduced. In fact, in some cases, large business houses and multinational corporations operating in India are understood to realize illegal trade through authorized channels.¹²

Apart from this, small traders are engaged in illegal trade through unauthorized channels. Many stakeholders include agents who have worked in a hierarchical constellation. These groups work in the market structure where market information is a decisive factor. In such a way the cost of entry into illegal commercial activity is basically described in terms of the prices. Expenses show themselves in China's length. For a new entrance like

⁹ Muthukuda Arachchige Dona Shiroma Jeeva Shirajanie Niriella, 'Legal Cross-Border Trade vs. Illegal Cross-Border Trade: Promoting Sustainable Regional Cooperation in South Asia through Transnational Trade', (Asian Journal of Humanities and Social Sciences (AJHSS)), Volume 2, Issue—4, November, 2014 ISSN: 2320-9720, p.126.

¹⁰ Ibid, p.127

¹¹ Isabel Bruto Da Costa, 'The second freedom: South Asian Challenges 2005-2025', strategic foresight group, Mumbai 2005, p.12.

¹² Nisha Tenja, 'informal trade in the SAARC region', (working paper ICIER), Lodi Road New Delhi 1999, p.17.(<http://web.worldsamk/external/southasia/ifrsa>)

this, the number of partners will be high, margin trading totals in every step. At the time of the closing number of links in China, the lower cost is low. The existence of such agencies cannot be questioned since they are registered as consult.¹³

Two-way illegal trade between India and Sri Lanka is more than exemplary than authorized trade between them and the two-way non-trademark trade Between India and Sri Lanka, is largest informal trade between India and Sri Lanka and is the largest informal trade between Sri-Lanka and any single country. This unauthorized trade between the two countries is carried out only by air and sea. According to the Central Investigation Bureau, Sri Lanka (overall) 65 -70% total contraband trades have been traded by air and the rest is carried out by the sea. The information further exposes that the total Bi way unauthorized international trade between India and Sri Lanka is approximately 25% -30% of the formal international trade. Informal imports from India are around 40% -45% of formal imports, while informal exports are roughly 25% - 30% of formal exports. This large trade excess in India's favor in informal trade does not create a healthy economic environment in Sri Lanka.¹⁴

(b) Financing for illegal trade:. How does this make an illegal market is a huge amount of black money, that traders easily accessible. This money can be transferred to any country in the world through the illegal money market. A large black economy consisting of both domestic and foreign currency makes such a trade possible. Unauthorized trade is funded by high cost precious metals like gold or silver or by liquid money from the illegal money network. In the first case, gold is smuggled physically and then converted into desired currency. The uniqueness of this system is that there is no physical money transfer. This mechanism is referred to as "Hawala" in India, 'Hundi' in Bangladesh and 'Chit' fund in Sri Lanka runs on the same principles.¹⁵

(2) Tariffs Barriers:. Within the SAARC region, high tariff encourages illegal trade. High tariff rates create a strong concern to avoid legal channels to avoid tariffs. It can be seen that tariffs on both basic and manufactured goods are more for India, Bangladesh and Pakistan. Illegal channel is particularly attractive to the export of large scale consumer goods, which is being exported illegally to other South Asian countries from India. Such products are not being developed by huge firms. Tariff makes an important proportion of the final price for such institutions and makes them illegal trade profits.¹⁶

(3) Non Tariff Barriers:. The end of the Inter SAARC trade is not due to the higher Tariffs alone, but due to the presence of non-tariff barriers (NTBs) mostly Quantity restrictions such obstacles increase illegal trade In the region. In the beginning of 1990, India and Bangladesh have proportioned the coverage of the most non-tariff barriers for both primary and ready equipment. In fact, India had a NTB coverage ratio 72 percent on basic equipment and 59 percent ratio on manufactured. Bangladesh proportions and proportionately developed the ratio of NTB of 55% and 47%.¹⁷

Several facts have influenced the increase of illegal cross-border trade. One of the identified auxiliary factors is the price of high transaction informal trade. In order to promote trade, trade related information

¹³ Ibid.

¹⁴ Muthukuda Arachchige Dona Shiroma Jeeva Shirajanie Niriella, ' Legal Cross-Border Trade vs. Illegal Cross-Border Trade: Promoting Sustainable Regional Cooperation in South Asia through Transnational Trade', (Asian Journal of Humanities and Social Sciences (AJHSS)), Volume 2, Issue—4, November, 2014 ISSN: 2320-9720, p.129.

¹⁵ Nisha Tenja, pp. 18-19.

¹⁶ Ibid, p. 19.

¹⁷ Ibid, p.20.

such as product needs, technology, expertise; knowledge, price, tariff, industrial trends, business regulations and procedures are needed. However, SAARC countries have not taken any strong mechanism to facilitate the smooth exchange of commercial information between SAARC countries. Similarly, in Transit to find the condition of goods and select the best quality and to select them officially, it is also important in the transit in traditional trades, which has a higher value of repeated cross-border trade. Trade partners are involved in informal trade; provide all the necessary assistance to reduce the above prices. Therefore, the cost of low transaction, trade in informal channels has forced the traders to select this particular stream in across cross border trade. The absence of proper multi-purpose transit arrangements within the countries in the SAARC region is another important factor in increasing the informal border within the area. Industrial disparity within SAARC countries is another reason which reduces the development of intraregional formal trade among SAARC nations which finally causes the growth of informal trade.¹⁸

(4) Transport Costs: Inaccessible transportation and transit systems in the region between India and its neighboring countries have increased high transportation costs in the region. A large part of trade therefore takes place informally. Thus, traders use the informal channel in order to save on transportation cost.¹⁹

Informal Exports Between Some SAARC Countries.

India's Informal Exports to Pakistan: Medicines, Alcoholic Beverages, Machinery, Cement, Tyres, Chemical Products, Steel Utensils, a range of low-cost mass products made by Dabar and Pioma Industries.

Pakistan's Informal Exports to India: Food items, Synthetic Fibers and Chemical Products.

India's Informal Export to Bangladesh: Cotton, Sugar, Cattle, Kerosene Oil, Automobile Components, Bicycles, other consumer goods, like Plastic items, Razor Blades, Medicines, Fruits, Fish, Spices, Sarees and Coal, etc.

Bangladesh's Informal Exports to India: Spices, Hilsa fish, Synthetic Fiber, Palm oil, Plastic shoes, Polythene and other Consumer items.²⁰

Recommendations

The South Asian Free Trade Agreement (SAFTA) charter envisages removing barriers to trade (tariff) on commodities between nations. At the first stage, there is no plan to remove barriers to service trade. The idea is that once SAFTA is achieved, service sector trade barriers would be removed. In this respect, the models of the EU/NAFTA are being followed which remove barriers. Unfortunately, this may not be the right model in the South Asian context, as it would lead to fewer gains for the member nations. As a result, members would have little inclination to focus. On the second stage of Integration i.e. free movement of services, wherein gains are large. If SAFTA is to contribute towards increased intra-SAARC trade, there needs to be an expansion in the basket of tradable commodities. SAFTA must necessarily lead to trade creation and not trade diversion. The list of tradable goods under SAFTA does not include many goods that have significant trading potential. The South Asian nations need to diversify their export structure in favor of more knowledge intensive products, and sharpen the global competitiveness of exports. This also calls for a strategic response at the national and

¹⁸ Isabel Bruto Da Costa, 'The second freedom: South Asian Challenges 2005-2025', strategic foresight group, Mumbai 2005, p.12.

¹⁹ Nisha Tenja, p.21.

²⁰ Isabel Bruto Da Costa, 'The second freedom: South Asian Challenges 2005-2025', strategic foresight group, Mumbai 2005, p.10.

regional levels and the challenges include, increasing value addition in traditional exports such as Tea, Coffee, Basmati and other commodities.²¹

Conclusion

Trade is an essential part of creating a sustainable future for any country. Similarly, the inter-regional trade between South Asian countries will bring sustainable prosperity in the SAARC region. It will help in the region to reach the goal of sustainable economic development in the region by creating economic opportunities such as manufacturing of goods, import and export of goods particularly cross-border movement of goods. However, it is unfortunate that Intra-SAARC trade represents the lower value of expected gross trade in this area. Though regional and bilateral agreements are aimed at the development of legal cross border trade within the region, yet regional cooperation is not sufficient to combat illegal cross-border trade in a successful manner due to some weaknesses of the treaties. The informal trade in SAARC is due to a large black economy consisting of both domestic and foreign currency and through goods like Silver, Gold or by Cash makes such a trade possible. Experts of the nature of trade flow show that South Asia is an important proportion of India's non-formal trade is due to tariff and non-tariff barriers. Other factors which give rise to informal trade is high transport cost and other rules of Origin. Therefore, we should look at the factors, to improve trade among SAARC members which really assists in converting illegal cross-border trade into legal channels.

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²¹ Ibid.