

Unlocking the Potential of
**Regional Economic Cooperation and Integration
in South Asia**

Potential, Challenges and the Way Forward





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PREFACE

Regional economic cooperation and integration, with regional trade and investments as primary drivers, has been an influential transformative force in bringing about inclusive and sustainable development outcomes and welfare gains in many parts of the world. Nearer home, South East Asian subregion, is the developing world's leading example of how rich development dividends can be reaped from regional cooperation. The ASEAN has progressively deepened economic cooperation for sharpening its collective competitive edge and thereby create policy space to address domestic socio-economic challenges. Future directions for the achievement of the Sustainable Development Goals especially in South Asia would critically depend on how state and non-state actors and stakeholders are brought together under regional economic cooperation and integration (RECI) frameworks.

As this Report argues, the South Asian subregion has a lot of ground to cover in terms of regional economic integration. The volatile and uncertain external environment ever since the onset of the global financial crisis sets a new context to revisit policy priorities in this regard. The subregion has been making progress on some indicators of trade and investment, notwithstanding certain inter-country differences in performance. But the progress has been slow at best, enabling it to exploit only less than a third of potential of intra-subregional trade.

Through the UNESCAP resolution 68/10 on “Enhancing regional economic integration in Asia and the Pacific”, countries of the Asia-Pacific region have acknowledged the potential of regional economic cooperation and integration in eliminating poverty and, in achieving inclusive and sustainable development. The Bangkok Declaration of December 2013 on Regional Economic Cooperation and Integration in Asia and the Pacific, endorsed through UNESCAP resolution 70/1, subsequently helped in securing commitment of Asia-Pacific countries to work together for economic integration. South Asia also has a number of institutional frameworks for regional cooperation like SAARC and BIMSTEC.

This Report tracks the status of regional economic cooperation and integration in the South Asia subregion and identifies policy priorities for the future in this regard. In doing so, it covers four broad areas of international collaboration as identified by the Bangkok Declaration; (i) market integration through enhanced cross-border trade and investments, (ii) development of transport, energy, ICT and people-to-people connectivity, (iii) greater financial cooperation for closing infrastructure gaps and liquidity support; and (iv) increasing economic and technical cooperation to address shared vulnerabilities and risks.

Taking into account the low baseline scenarios and massive socio-economic challenges faced by South Asia, the report underscores the need to accelerate reforms for deepening subregional economic integration with utmost urgency. This could be achieved through putting in motion a South Asia Comprehensive Economic partnership (SACEP), recommended in this report to consolidate and build upon initiatives such as trade facilitation measures for formation of production networks and regional value chains, measures for liberalization of trade in services and improvement of investment climate, and necessary reforms for overall procedural ease of trade and investment.

South Asian countries also need to take bold steps to broaden the horizons of economic relations with neighboring subregions of Central Asia, South East Asia and beyond. In this regard, South Asia's economic integration can benefit from institutional arrangements provided under overlapping regional organisations such as SAARC, ECO, and BIMSTEC. By building synergies between various related bilateral and plurilateral initiatives and agreements for economic integration which are currently in progress, the subregional countries will have greater opportunities to secure their position in the broader Eurasian economic space. With its convening authority, multi-sectoral agenda of work and strategic presence in the subregion, UNESCAP is uniquely placed to assist in strengthening regional economic cooperation in South Asia and beyond, with a larger goal of uniting Asia and the Pacific for sustainable development.



EXECUTIVE SUMMARY

As the persistent slowdown becomes the new normal for advanced economies and as the centre of gravity of the world economy shifts eastwards, regionalism within and between subregions becomes a critical strategy for sustaining the Asia-Pacific region's dynamism. With intraregional trade stagnating at around 6% of total trade of the subregion, the bulk of South Asia's intraregional potential remains to be exploited. Broad-based regional economic cooperation could enable far more effective responses to the subregion's developmental challenges. Under the framework of regional economic cooperation and integration, key priorities for the subregion are intraregional trade and investment flows, transport and information and communication technology (ICT) connectivity, and financial integration, as well as subregionally coordinated policies for addressing shared vulnerabilities such as food insecurity and disaster risks. Progress in these areas would help prepare the subregion to better participate in and benefit from broader regionalism in Asia and the Pacific.

Intraregional trade and investments

South Asia is often described as the world's least integrated subregion, with the value of intraregional trade less than one third of its potential, at \$26.8 billion in 2014 against a potential of \$81.2 billion, as estimated by the UNESCAP South Asia Gravity Model. This means that more than 67% of trade potential is not being exploited. This potential could also more than double by 2020 to an estimated \$172 billion. It has been shown that regional trade liberalization and enhanced facilitation to reduce trade costs can generate substantial welfare gains for all member states, especially for the poorer and smaller countries of the subregion, leading to more balanced regional development. The results of the UNESCAP-SANEM South Asia Model suggest that reducing trade costs by 40%, to the levels prevalent across countries in the Association of Southeast Asian Nations (ASEAN) would alone generate a significant impact in terms of exports and welfare gains, yielding an increase of up to almost 11% in intraregional exports and a nearly 3% increase in South Asia's gross domestic product (GDP). The potential of intraregional trade in services, as well as investments, also remains untapped, as does the scope for forming regional production networks or value chains.

The low level of intraregional trade is explained by a number of factors such as the high costs of intraregional trade, poor supply capacity in the Least Developed Countries (LDCs) in the region, poor trade facilitation at borders, and the prevalence of a variety of non-tariff barriers. To foster regional production networks or value chains, this report recommends the consolidation and upgrading of existing trade and investment cooperation initiatives into a South Asia Comprehensive Economic Partnership (SACEP). SACEP could cover seven key policy priorities, namely

a) advancing the liberalization of trade in goods, b) strengthening facilitation of transport and trade at the land borders, c) effective liberalization of regional trade in services, d) investment promotion to foster regional value chains, e) harmonizing product standards and conformity assessment procedures, f) cumulative rules of origin and industrial cooperation, g) coordination of international payment arrangements and banking cooperation.

Several ongoing and new policy initiatives can contribute to the fulfillment of these priorities set under the composite SACEP framework. Some of the most important such policy programmes are: achievement of substantial cuts in sensitive lists within an agreed timeframe under the ongoing South Asian Free Trade Area Trade Liberalization Programme (SAFTA TLP) for advancing trade in goods; utilization of new policy tools such as the UNESCAP-led Framework Agreement on the Facilitation of Cross-Border Paperless Trade in Asia and the Pacific, adopted in 2016 for the digitization of trade procedures and establishment of single-window systems; formulation of a regional common schedule for services trade liberalization under SATIS negotiations in key service sectors of interest to the subregion; measures for transparency in investment rules; and adoption of an inclusive approach involving the private sector led by the SAARC Chamber of Commerce and Industry (CCI) towards reforms in the area of regional product standards. In this context, the possibilities of utilizing advanced technologies for critical policy solutions should be explored in detail, such as the usage of realtime gross settlements (RTGS) to save time and costs of cross-border payments in South Asia proposed by a recent UNESCAP study.

Transport, energy, ICT and people-to-people connectivity

Regional connectivity in South Asia is particularly important because of its potential to turn the subregion into a land bridge between Europe, Central Asia and South-East Asia. Two trunk corridors identified by UNESCAP, which have feeder links across the breadth of South and Central Asia, are: (1) Turkey–Iran–(Islamic Republic of) Pakistan–India–Bangladesh–Myanmar (TIPI–BM) road corridor and (2) Istanbul–Tehran–Islamabad–Delhi–Kolkata–Dhaka (ITI–DKD) Rail Corridor. Both corridors are integral parts of the Asian Highway (AH) and Trans-Asian Railway (TAR) networks and have connecting sublinks to major ports. Together they offer multimodal transport options, particularly for landlocked LDCs. Key challenges to making them operational include gaps in physical infrastructure, lack of transit and transport agreements, inadequate transport facilitation measures, and the absence of a comprehensive approach through a connectivity master plan.

Regional cooperation is also the most potent policy solution to overcome South Asia's energy challenges. By linking together native sources using regional grids and effectively utilizing supply-demand complementarities through trade, cross-border investments and technical cooperation,

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