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# SAARC IN THE NEW MILLENNIUM

## VISIONS NEED FINANCIAL WIZARDRY

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## Visions Need Financial Wizardry

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While globalisation has created new opportunities and has brought fresh challenges, the South Asia region faces certain paradoxes, in the new millennium. Reforms and liberalisation, increased private sector participation, and marketisation in the SAARC countries have not been associated with necessary 'development cooperation'. Support from the rest of the world has not been encouraging as reflected in low private capital flows, miniscule foreign investments, and declining official development assistance, not only real but nominal, with some increase in 1998. India in the region has rather faced reverse transfer of resources (totalling over US $ 1 bn.) during the four years beginning 1995-96.

### Trade at a Snail's Pace

Regional grouping for economic cooperation and integration has characterised globalisation. Thus, ASEAN in Asia, NAFTA in North America, and MERCOSUR in South America have shown expected increase in trade, the impressive performance of European Union (EU) notwithstanding. With the dawn of the euro, given the economic and financial strength of the euro-zone, high expectations for efficient and increased trade flows may really materialise over time due to the reduced transaction costs. The SAARC, in South Asia, which took-off slowly, got an impetus with certain initiatives, particularly by India, at the bilateral level, notably in terms of reduction of trade restrictions on

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imports from Bangladesh, Pakistan and Sri Lanka. Liberalisation by India has led to significant increase in exports (in US $) by Bangladesh (over 25.2 per cent) and Sri Lanka (about 30 per cent) to India during 1998-99 compared to the previous year. But, as Table 1 shows, the levels remain marginal compared to their total exports. The low levels explain the limited supply capacities for items of Indian demand and structural problems associated with them, not so much the high tariffs and other restrictions, which can be overcompensated by inherent comparative advantage, if it exists. On the other hand, India's exports declined, to Bangladesh (by $ 222 million, excluding rice) and Sri Lanka (by about $ 50 million) during 1998-99. Commodity–wise performance in case of six neighbouring countries can be seen from Table 1A. Their trade deficit, or balance of Trade (BOT) with India, as Table 2 shows, got reduced by $ 140 million (excluding rice imports) and $ 58 million respectively. Table also shows that Nepal's deficit got reduced from $ 74 million to just $ 7.4 million over the same period.

Going by the expansion of trade in recent years, intra-SAARC trade has not so far been remarkable, and at best, it has proceeded at snail's pace. The intra-SAARC exports increased from 3.2 per cent in 1990 to 4.3 per cent in 1996 of the total exports of the SAARC countries, while intra-SAARC imports increased from about 2 per cent to 4 per cent of the total imports, over the same period[1], and thus both have yet to cross 5 per cent mark, despite several bilateral concessions. The intra-regional export shares are 21 per cent in ASEAN, 51 per cent in NAFTA, and 25 per cent in MERCOSUR, and as high as 62.5 per cent in the EU, compared to 4 per cent in the SAARC. As a critical minimum, and as a medium run target, the SAARC may aim at 10 to 15 per cent intra–SAARC trade, for any further big push.

**Heavy Costs of Separate Markets**

The heavy costs of separate markets, and benefits of a single market, i.e. absence of a Union, are well recognised. The typology of costs analysed by the EC's Cecchini Committee Research Report[2] showed the resulting costs for companies, public authorities as well as



consumers. The Report laid down a suitable methodology for estimating costs and benefits covering not only manufacturing but also services. The typology means that consumers suffer from the direct higher cost by companies as well as public authorities, in addition to the higher price paid for inefficiency. The cost to the companies include duplication of product development, loss of potential economies of scale, and disadvantages of a narrow market, while those for public authorities include duplication of different procedures, not getting value of money in public projects and varying standards contributing to higher transaction costs.

The main guidelines given by the Cecchini Committee in its Report mean many things to be done particularly by business itself, i.e., the corporate management mainly in terms of competitiveness which helps public authorities to sustain reforms. This would also mean reduced "unofficial" trade, together leading to higher resource mobilisation domestically for development of necessary infrastructure and thus giving a push to a 'virtuous circle' of development which may help substantial trade liberalisation.

At one time, the SAARC countries' single market is now fragmented, with separate trading, market and pricing systems, oriented to outside the region. Intra-regional trade is beset with different kinds of restrictions signifying non-cooperation. Recent estimates of costs of non-cooperation, or 'non-SAFTA', show that cost was around 36 per cent of the actual import bill pertaining to the items covered in the case of Sri Lanka and 28 per cent with case of Pakistan[3].

Though there is increasing realisation of benefits of cooperation as well as the cost associated with non-cooperation in trade also among the SAARC countries, the gains from goods trade, least from services trade, are yet to reach the critical minimum, partly due to low supply base, but mainly because of the high sensitivity to short term balance of trade (BOT) by the neighbouring countries.

To the extent, unfavourable BOT is due to imports of industrial inputs and capital goods, capital formation increases leading to speedier growth which seems to be the case of India-Bangladesh and India-Sri Lanka trade. About 30 per cent of total exports to Bangladesh and about 45 per cent of exports to Śri Lanka comprised industrial inputs, engineering goods and project exports during 1997-98. BOT with India in 1997 as share of total BOT worked out to 6 per cent, 27 per cent and 38 per cent in case of Nepal, Bangladesh and Sri Lanka respectively. The estimates are that the share declined to 21 per cent in case of Bangladesh (excluding rice) and 30 per cent in case of Sri Lanka in 1998 (Table 2). Any way, increasing BOT with expanded imports of critical inputs, capital goods and project goods by the neighbouring countries, and higher external capital in flows by them should go together, since the levels of capital formation remain low in comparison to the 'warranted' levels for speedier growth of incomes, employment and exports.

### Resources for Infrastructure

More importantly, business and industry have been facing the infrastructural bottlenecks in the region which are associated with limited investible resources. The severe bottleneck of surface transport have constantly been reported particularly in case of India–Bangladesh trade. The financing problems of the region are apparent from the per capita low levels of incomes and the associated physical and social development indicators. Notably, per capita consumption of power (1996) is as low as 39 in Nepal, 97 in Bangladesh, 203 in Sri Lanka, 333 in Pakistan and 347 in India, compared to 687 in China, and as high as 4453 in South Korea, not to be compared with those of Japan (7083), Germany (5596), and the USA (11796), all in Kwhs, with vast divergences in development stage. Well-known are the limitations of the financial service structure constraining mobilisation of available resources even with the domestic households. The region needs many more schemes like Gold Bold Scheme initiated by India in 1999.

Thus, the regional grouping in South Asia, i.e. the SAARC, needs to focus on mobilisation of resources at a large scale to build up infrastructure, given the limits to their own resource generating



capacities. Cooperation in trade can only be of enabling value to the various economic activities.

The total (officially estimated) domestic savings of the SAARC countries presently amount to less than US $ 100 bn. If these were not the times of 'aid fatigue', with sole emphasis on private capital flows, one would expect the total investment at a significant multiple of the savings. But, the total investment resources amount to about $ 120 bn. (1996), pointing to the limited resource mobilisation from the global pool.

### Present Foreign Resource Gap

Because, total utilisation of assistance amounted to $ 3.2 bn. average during 1995-99. Total foreign direct investment is yet to exceed $ 5 bn annually in the region. Total balance of trade (BOT) of the region is estimated at (-) $ 25.4 bn. for 1998 and in ADB forecast (-) $ 26.4 bn. for 1999 and (-) $ 29.2 bn. for 2000. Total current account balance (CAB), after adjusting the inward remittances (at about $ 20 bn.) and other net invisibles, is estimated at (-) $ 11.4 bn., i.e. 2 per cent of the region's GDP, during 1998, financed from different external inflows. These flows include non-residents' deposits which have incrementally slowed down in recent years portfolio and other foreign investment remain volatile, net assistance is on regression, while commercial borrowings have to be limited. The forecast (ADB)[4] CAB for 1999 and 2000 is higher at 3.1 and 2.5 per cent (respectively) of the region's GDP, requiring external capital inflows. It is project finance which needs greater mobilisation requiring a shelf of bankable projects as also developed financial market.

The foreign resource gap should be large enough to reflect the development needs and the region must have strategies to mobilise the required financing and co-financing to the tune of $ 30-50 bn, and which should be the focus of the SAARC by way of preparing a shelf of viable regional and sub-regional projects, including projects for exports of both goods and services. This is indeed a taxing job, requiring quality human resources as well financial resources, the need for lot of patience notwithstanding.

Project preparation requires soiling hands, entailing the need for mobilising human and financial resources. Well-known may be the moneys involved in preparing report of projects like Karnali (Nepal) which were provided by the World Bank. Economic diplomats are like 'candy in a coal-mine', given the task entailing a lot of soiling hands. It is the development banks and other financial institutions which should be involved to play the role of diplomatic players in international or regional cooperation.

**Facilitating Projects for Financing**

Furthermore, a competitive environment is expected in the region which not only facilitates and attracts projects and their financing which require sustained economy-wide reforms, notably in the financial sector for which joint efforts wherever suitable need to be discussed and initiated.

Private sector financing of projects has to be sought in a big way which is again possible and is facilitated if a ready shelf of projects is available and if innovative ways of attracting investors are devised. Recently, Nepal has opened the hydro power sector for local as well as foreign private investment, in view of the country's ironic situation of big potential faced with lack of funds and technical knowhow. The Government provides one-window system as also attractive royalty and tax concessions and 1per cent customs on machinery and equipment. As many as sixty-six most prospective sites have been identified. Certain project feasibility/design reports have been prepared. Snowy Mountain Engineering Corporation of Australia is preparing a feasibility report on a project in West Nepal, while Enron Co. is reported to have shown interest in Karnali–Chisapani project for export of power to Tibet and Northern India. Atleast five private sector projects with foreign participation are under construction or agreement.



**World Bank Lending**

The global catalyst in growth and development financing, the World Bank, has been lending to South Asia for different sectors, annual average total being $ 3.64 bn. during 1989-93 which declined to $2.84 bn. during 1994-98. The share of IDA was 52.5 per cent and 63.6 per cent respectively during these periods. Sector-wise distribution of lending during 1994-98, is shown in Table 3, broadly brought out below:

| | | | |
|---|---|---|---|
| Human development | | 31.6 | |
| Of which : | Education | | 13.1 |
| | Health and Nutrition | | 14.7 |
| | Social Sector | | 3.8 |
| Infrastructure | | 26.5 | |
| Of which : | Power | | 10.6 |
| | Oil and Gas | | 0.9 |
| | Telecommunication | | 0.3 |
| | Transport | | 8.1 |
| | Urban Development | | 2.2 |
| | Water Supply and Sanitation | | 4.4 |
| Agriculture | | 18.7 | |
| Industry and Mining | | 6.0 | |
| Public Sector Management | | 4.7 | |
| Environment | | 3.6 | |
| Finance | | 8.7 | |
| Total, including multisectoral | | 100.0 | |

Thus, infrastructure attracted sizeable lending, and including human development items i.e. social infrastructure, as much as 60 per cent of total during the recent five year period. The share of infrastructure was higher (41.7 per cent) during 1989-93, and that of human development items was much lower (10.5 per cent). The swing of lending between physical and social infrastructure is determined as much by demand side, as by supply side. A strong shelf of projects for attracting lending, greater preparedness for timely utilisation and a mobilisation strategy complementary within region may make the swing more favourable to the SAARC. The present low utilisation ratio would corroborate this.

## Co-financing Possibilities

The recent system of financial partnership, adopted by the World Bank, by way of co-financing and Trust Fund programme has aimed at implementation of its strategic agenda and maximisation of the 'development impact' of its aid operations. According to the World Bank's Annual Report[5], as shown below, the percent of cofinancing now is around 30 per cent of total aid operations (US $ millions):

| | 1995 | 1996 | 1997 | 1998 |
|---|---|---|---|---|
| World Bank Lending | 22,522 | 21,352 | 19,142 | 23,594 |
| Co-financing | 8,774 | 8,304 | 7,675 | 9,717 |
| Total | 31,296 | 29,656 | 26,817 | 33,311 |
| Share (per cent) of Co-financing in Total | 28.0 | 28.0 | 28.6 | 29.0 |

Co-financing has increased by 3.5 per cent (annual compound) compared to 1.6 per cent increase in the World Bank lending. It is cofinancing which is expected to gain great significance in the coming years.

The main official sources of cofinancing include Inter–American Development Bank, the EU institutions, and Japan, the later being the largest contributor.

The main lending instruments for co-financiers have been investment specific to the projects in infrastructure, water supply and sanitation, and social sectors. Such loans accounted for 61 per cent of the total co-financing. Other instruments included export credit, and private co-financing. There is a comparative advantage of cofinancing in its enabling nature to the private sector projects. Private co-financing includes parallel lending, NGOs, and foundation grants/guarantees.

South Asia, however, has attracted a significance level of co-financing only in 1998. According to the World Bank's Annual Report, referred to above, the operations raised 72 additional cents for each US $ lent. The share of South Asia in total co-financing was only $ 93 million, out of $ 7.7 billion, in 1997. This has gone up to $ 2.8, out



of total $ 9.7 billion, in 1998 which works out to 28.8 per cent. This tempo needs to be maintained which calls for preparations on the part of South Asia, in Government as well as private sector, in terms of development projects which have financial attractiveness.

Given the recent emphasis of South Asian Governments on private sector investments, large scope exists for attracting co-financing, as also Trust Fund resources. The guarantees too can be of significant help in augmenting investment levels in South Asia[6].

Given the large surpluses of Japan, there is a possibility of leap forward in the amounts of co-financing and contributions by Japan, a theme propounded earlier by the UNU Wider Group comprising eminent economists of Japan and South Asia in their Reports. The main conclusions of the Group[7] remain valid today and are worth recalling (Annexure I). In the face of recession in Japan, country's interests in South Asia need to be stimulated again by way of project preparation, if possible by the Japanese assistance, with an eye on expanded exports of machinery and equipments by Japan. Large BOP surpluses are accumulating over period brought only in Table 4, totalling to trillions of dollars, annual average being about $ 230 bn. covering major surplus countries led by Japan. The surpluses have been growing estimated at $ 331 bn. for 1999, largest being in case of Japan at over $ 143 bn. According to the US Congressional Budget Office's (CBO's) estimates, the federal budget (excluding the Social Security Trust fund was balanced for the first time in 30 years, in the fiscal year that ended in September 1999. And, the CBO forecasts accumulated $ 1000 bn. surplus over the next 10 years. The budget constraint, therefore, is no more an excuse for 'aid fatigue' by the biggest economy of the world.

## Financial Support for Trade

The SAARC can proceed with cooperation within the region led by trade liberalisation initiatives only a bit and not very far. Foreign trade can be optimised and free trade expansion can materialise only if the economic structures are in place. They include production base, market system, physical and social infrastructure and institutional framework, and notably an efficient financial sector. The later covers banking and insurance, mutual funds, stock exchanges, and above all an efficient foreign exchange transaction system, preferably a Clearing Union of the SAARC, and a common currency at some stage, all to reduce the transaction costs, and risks, a'la Euro, and to give a boost to project finance particularly in the face of scarce public money for infrastructure. The share of Indian investment in project finance works out to be very low presently, compared to South East Asia and Latin America. It is monetary unions which boost project finance[8].

For all this to happen, South Asia needs to cut past ghosts and decide to bury them forever by means of economics. It is aptly observed[9] that except Pakistan, all the other neighbours are ready and willing to go forward. However, economics is yet to be given a fair chance and critical wherewithal of economic cooperation are yet to be found in the region.

It is, therefore, not surprising that the SAARC member countries were lukewarm to the measures required for forming a 'Economic Union' and took only an adhoc decision to set up a Group of Expert to prepare a draft treaty for the creation of South Asian Free Trade Area (SAFTA) by 2000, while the Group of Eminent Persons (EPG) envisaged an economic union of South Asia by the Year 2020 to be achieved in two stages-by creating a FTA by 2010 and a Customs Union by 2015.

### Visions for Cooperation and Integration

The EPG further suggested that a full - fledged treaty would be necessary for establishing the FTA, which should enter into course from January 2000. All the elements which should go into the treaty, it is claimed,[10] are spelt out by the EPG. Considering that foreign trade is a large portion of goods GDP in most of the neighbouring countries (over 50 per cent in Bangladesh, over 60 per cent in Pakistan and over 120 per cent in Sri Lanka, all in 1997) and exceeds 30 per cent in India, and that free trade in the area would require several economy–wide adjustments, the EPG has been over ambitious in its vision which would affect the life of as many as 1.24 bn. people. Such visions[11] have to undergo much wider discussion by all concerned, particularly as



their optimality and feasibility will depend upon the likely pace of development in the 'real' economies of the member countries. The visions have also to conform with the national development plans and policies of the member countries.

More than the vision of the FTA, the over ambitiousness of the EPG is clear from the measures suggested for deeper integration to pave the way for the 'Economic Union', namely cooperation for infrastructure development, particularly transport and energy; and in environmental protection trade facilitation measures including harmonisation and mutual recognition of standards, creation of a single investment area, monetary union, plans for vertical integration to promote specialisation, and several structural adjustments.

Free Trade AREA may bring tangible benefits to the region, but trade analysts believe, "it is hardly credible that reduction in tariffs will be followed by the removal of the NTBs. As yet there is no consensus among the members for the removal of the NTBs".[12] Anyway, complete removal of all barriers is not going to be a short-term process.

Neither India nor Bangladesh may be able to match Sri Lanka, Nepal and Pakistan in regard to removal of tariffs and NTBs, given their lower per capita incomes and structural problems. Thus, the vision of freer trade is beset with certain hazards.

### Search for Paradigm and Moral Hazard

It is not at all clear whether the paradigm of the EPG is that free trade will automatically lead to the above possibilities which in turn enable an Economic Union leading to all the corresponding economic advantages, or the EPG believes that once FTA is in place financial resources for the above possibilities would also follow from within and outside the region. Scant attention to mobilisation and management of financial resources cost the visions a great deal as they remained on paper.

It appears that the EPG suffers from a 'moral hazard', if not 'shame', as no clear projections, specific ideas on innovative measures, nor on mechanisms are available regarding financial resources which could be mobilised from within and more critically which should flow from the rest of the world to be calibrated such that the flow is least cost. The apparent benefits and costs of different options are brought out in Annexure II, and need wider discussion, though known in the policy quarters. The criticality of external flows can not be overemphasised until gold and silver rupees locked, over the period, with the households and businesses within the region can be mobilised for development purposes. They are estimated to be worth $ 130-150 bn.

Joint ventures within the region and mutual assistance can grow to an extent but not very far. There were India's 82, out of total 592, joint ventures (JVs) in South Asia of which 26, out of total 185, were in operation by 1995-end. There were 16, out of all 421, wholly owned subsidiaries (WOSs) of which 2, out of all 81, were in operation.[13] Total capital involved in them is meagre to complement the partner countries' resources. The total approved equity of all active JVs as on September-end 1998 amounted to $ 1.24 bn. (less than $ 1 bn. in case of WOSs), including cash remittances; capitalisation of export proceeds of plant and machinery/goods, earnings of the Indian companies by way of technical knowhow, fee, royalty, etc; and loans and guarantees. Total elimination of limit on outflow of investment, as on imports, is unlikely at least in the near future to project any jump in equity. Intra-firm transactions will always be subject to some restrictions.

Notably, JVs/WOSs in South Asia are mainly located in Sri Lanka which speak volumes for production complementarity between India and Sri Lanka, its relatively better economic environment notwithstanding, pointing to the potential for many more joint ventures but including third countries to make them economic scale-worthy. India's assistance (loans and grants commitments) to the neighbouring countries, on average, amounted to Rs 835 million annually during 1990-91 to 1997-98, besides technical assistance under ITEC[14] which may be what the country could offer, but not significant enough to complement investment requirements.

### Question of Technological Development : No SAARC for Museum

Besides investment requirements, there is a question of technological development, management practices, professional skills and R&D,



imperatives for global competitiveness and greater market access, as South Asia can not isolate itself from the rest of the world economy, to remain a museum of traditional economies. The present low levels of R&D expenditures and meagre remittances abroad, due to the bogey of BOP, have all along restricted technological changes. Technical cooperation within the SAARC has apparent limits. Technology imports are required in a substantial way and over long period entailing financial costs in one-time transactions as well as in recurring remittances. 'Development Cooperation' from the rest of the world, therefore, is a necessity, possibilities of purchases of technology from the market notwithstanding. Any shift in trade towards value added products or capturing "flying geese phenomenon" can take place only if such cooperation and possibilities are made full use of..

### Creating Funds: Sharing Among Whom ?

To say that a Fund be created to compensate the countries for whom customs revenue constitutes a major part of budgetary resources when they undertake tariff reduction, India paying major part of the total cost, and that a Fund of about $ 1 bn. be created to finance the development of infrastructure and human resources in the region's less developed countries on principle of "capacity to pay", "without having to depend on foreign aid or capital"[15] may be considered too naïve and impractical to be accepted even by the potential beneficiaries.

Firstly, tariff reduction has to be viewed in the light of efficiency and growth benefits of freerer trade. Then, going by any development criteria notably per capita income, can India be asked to be the major donor just because of its large size and population. Anyway, such measures though in the right direction can hardly give the 'big push' required in the region for development.

The EU is a role model for South Asian cooperation. Could the EU reach up to the present stage without resource support from the fellow countries in the beginning.

**Financial Wizardry**

The SAARC, at present, earnestly needs pooling together the region's financial wizardry and prophetry of the type of Narsimham and his team coming out in different papers and reports[16] which have helped initiate a number of financial sector reforms in India which saved the country from Asian financial crisis, and which can fill-in the gap in the vision for future cooperation in the region. Following Narsimham, say the least, can not South Asia ask to have even one or two global financial centers and a few financial super markets, to make resource mobilisation attractive, and offer innovative products, when elsewhere "a veritable alphabet soup of novel financial products crowds the market place", and "picturesque menagerie of facilities" are being offered, "innovative financial engineering" being the name of the game.

No doubt, the capacity to undertake external financing for development is to be guided by the debt–service or 'liability service' capability determined by buoyancy in exports of goods in services, and attractiveness of the economy for private foreign investment. The South Asia's debt service ratio was 28 per cent in 1990, which has come down to 20.1 per cent in 1997 and was 17.9 per cent in 1998. However, the ratio differed widely among the countries. It was as high as 40 per cent in case of Pakistan, and 31.8 per cent in case of India, while it was 12.1 per cent, 11.7 per cent and as low as 9 per cent in Sri Lanka, Bangladesh and Nepal respectively in 1998. The debt–service ratio increased during eighties because the share of concessional flows in total declined from 74.4 per cent in 1980 to less than 50 per cent presently, though short–term flow remained low at 5.8 per cent in 1998[17]. Foreign investment still being at low levels, the excess of 'liability service' ratio over debt service ratio remains marginal in the region.

Considering the overall debt service ratio and lower short–term flows, on the one hand, and reduced share of concessional flows on the others, South Asia region deserves considerable external financial flows to complement their invisible funds. More importantly, the net transfers, i.e. resource flows minus internal as well as repayments,



turned negative in case of India and commitments have not gathered the required momentum in recent years. Net resource flows to the region, on long–term debt, declined in absolute terms in the ninties, from $ 8.5 bn. in 1990 to $ 2.3 bn. in 1997 and was $ 6.4 bn. in 1998. All (net) resource flows amounted to $ 9.2 bn. in 1990 which increased to $ 14.7 bn. in 1997, but declined to $ 12.3 bn. in 1998. Of these, FDI increased from $ 0.5 bn. in 1990 to 4.7 in 1997 and 4.4 bn. 1998, while portfolio investment remained marginal, except 1997 when it was $ 2.5 bn. Interest payments amounted $ 4.7, 4.6 and $ 5.2 bn. respectively in these years. As a result, all net transfers to the region which were $ 4.4 billion in 1990 ($ 5.6 bn. in 1980) amounted to $ 9.8 bn. in 1997 but declined to $ 6.8 bn in 1998.[18] The decline in resource transfers speaks volumes to augment the need for external financing in this resource deficient region towards 'big push' to development of infrastructure and industries in which there may be comparative advantages due to the availability of natural resources and economical work-force. Since a significant part of the work force is relatively younger, educated, and English–speaking, the region also has comparative advantage in a number of service activities, given the institutional and basic though skeletal infrastructural network created during the foreign rule. But, their promotion required sustained investment and reforms particularly in the financial sector to competitively handle the transactions, particularly emerging 'e-commerce'.

**Regional Mechanism for Larger Inflows**

As against expanded bilateral cooperation through unrestricted joint ventures a WIDER study[19] has suggested that a revolving fund may be set up to aid joint ventures, finance being contributed by partner countries, as well as by third countries such as Japan which may be interested in promoting South Asia's development cooperation, to be operated by the existing financial institutions in the subscribing countries concerned. Part of the fund should be provided as cheap finance to source capital goods required for joint ventures. Innovative financial instruments should be created to keep the cost of finance low. The suggestion is in line with the WIDER report, referred to earlier, and can lead to desired results towards resource mobilisation. However, we see no progress in this direction so far. The SAARC should recognise this and take the necessary decisions to develop regional mechanism to realise the progress.

### Rationale of Substantial International Transfers

In any case, the role and rationale of substantial international transfers for South Asia's development can not be overemphasised[20], but need wider and deeper debate.

In view of the limited capacity of developing countries to finance their development, external financing should not be totally dependent on the international capital market. "Leaving the issue of external financing for developing countries", argues a South Centre's recent paper[21], "to market forces is to renounce any responsibility on the part of international community, and specifically the North Governments, to work towards a more equal partnership".

It is true that different types of capital flows have come to the fore, they are scarcely available to the poorer countries/region, and have been attracted by relatively advanced countries. Some of them having received substantial flows have got into the financial crisis. The basic point is that such private flows can not supplant the long-term development financing requirements.

A South Centre paper has rightly suggested the need for the South to convince the North that concessional assistance is "not just good politics, but also good economics"[22], as such assistance leads to expanded market for the North's products/machinery. Select research work needs to be promoted in this area, pursuing earlier studies, with special reference to South Asia. Such joint research, as also formulation of viable project reports, will generate the much desired sense of collective purpose in hand.



**Table 1**

**India's Trade with the Major SAARC Countries**

**(US $ in millions)**

| Country | Exports | | Imports | |
|---|---|---|---|---|
| | 1997-98 | 1998-99* | 1997-98 | 1998-99* |
| 1 | 2 | 3 | 4 | 5 |
| Bangladesh | 787 (6903) | 991 (7270) | 51 (4290) | 64 (5000) |
| Pakistan | 143 (11330) | 111 (10470) | 45 (8000) | 212 (8300) |
| Sri Lanka | 489 (5850) | 440 (6265) | 30 (4650) | 39 (5000) |
| Nepal | 170 (1660) | 149 (1474) | 95 (390) | 142 (436) |
| Total of above | 1589 | 1691 | 221 | 457 |
| Aggregate | 32441 | 33642 | 38807 | 41887 |

*Provisional.

Parentheses show the estimated total imports (Cols. 2 and 3), and total exports (Cols. 4 and 5) of the respective countries.

*Source :* India : DGCI&S : *Foreign Trade Statistics of India* (Principal, Commodities and Countries).

Country Totals : ADB : *Key Indicators of Developing Asia and Pacific Countries 1999*, and *Asian Development Outlook*, April, 1999.

## Table 1A
## First Fifteen Products of India's Exports to the 6 SAARC Countries, 1997-98 and 1998-99 (Provisional)

(US $ in Millions)

| | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 |
|---|---|---|---|---|---|---|---|---|
| 1. Bangladesh | Rice (Other than Basmati) | Cotton Yarn, Fabrics Madeupset | Machinery and Instruments | Coal | Transport Equipments | GLS/GLSWR/ Ceramic/Reftrs Cement | Other Commodities | Drugs,Phrm Cutes & Fine Chemls |
| 1998-1999 | 525.36 | 123.92 | 39.81 | 26.36 | 24.93 | 24.42 | 23.71 | 23.24 |
| 1997-1998 | 96.85 | 273.27 | 47.23 | 18.92 | 34.62 | 41.30 | 20.71 | 21.50 |
| % Change | 442.5 | -54.7 | -15.7 | 39.35 | -28.0 | -40.9 | 14.52 | 8.09 |
| 2. Sri Lanka | Transport Equipment | Cotton Yarn Fabrics Madeupset | Machinery and Instruments | Drugs, Phrm- Cutes & Fine Chemls | Manufactures of Metals | Pulses | Other Commodities | Prmry & Semi-Finished Iron & Steel |
| 1998-1999 | 70.57 | 66.88 | 36.11 | 34.44 | 25.80 | 20.59 | 16.13 | 14.86 |
| 1997-1998 | 57.09 | 65.38 | 36.64 | 27.79 | 23.39 | 26.19 | 17.28 | 25.85 |
| % Change | 23.61 | 2.30 | -1.43 | 23.91 | 10.34 | -21.4 | -6.66 | -42.5 |
| 3. Nepal | Drugs, Phrm Cutes & Fine Chemls | Transport Equipments | Machinery and Instruments | Other Commodities | Prmry & Semi-Finished Iron & Steel | Paper/Wood Products | Manufactures of Metals | Cotton Yarn, Fabrics Madeupset |
| 1998-1999 | 30.71 | 23.81 | 12.14 | 9.41 | 6.25 | 6.01 | 5.79 | 5.18 |
| 1997-1998 | 25.51 | 25.31 | 17.78 | 6.20 | 21.33 | 5.75 | 5.57 | 4.64 |
| % Change | 20.38 | -5.92 | -31.8 | 51.72 | -70.7 | 4.51 | 4.05 | 11.61 |
| 4. Pakistan | Oil Meals | Drugs, Phrm Cutes & Fine Chemls | Spices | Dyes/Intmdtes & Coar Tar Chemls | Rubber mfd. Product Except Footwear | Iron Ore | Other Commodities | Paints/Enamels Varnishes etc. |
| 1998-1999 | 25.99 | 13.56 | 13.14 | 11.03 | 6.76 | 6.16 | 4.66 | 3.14 |
| 1997-1998 | 18.92 | 7.67 | 9.53 | 9.89 | 9.03 | 8.93 | 3.15 | 2.23 |
| % Change | 37.33 | 76.63 | 37.82 | 11.54 | -25.2 | -31.0 | 48.06 | 40.87 |
| 5. Bhutan | Machinery and Instruments | Rice (Other than Basmati) | Manufactures of Metals | Spirit & Beverages | Sugar | Transport Equipments | Electronic Goods | GLS/GLSWR/ Ceramic/Reftrs Cement |
| 1998-1999 | 2.36 | 1.83 | 0.84 | 0.78 | 0.55 | 0.45 | 0.45 | 0.42 |
| 1997-1998 | 2.51 | 2.69 | 0.55 | 0.59 | 0.69 | 1.34 | 0.49 | 0.49 |
| % Change | -6.02 | -32.1 | 52.50 | -31.02 | -21.4 | -65.9 | -6.70 | -15.1 |
| 6. Maldives | Fresh Vegetables | Drugs, Phrm Cutes & Fine Chemls | Cotton Yarn, Fabrics Madeupsets | Other Commodities | RMG Cotton including Accessories | Machinery and Instrument | Manufactures of Metals | Spices |
| 1998-1999 | 1.60 | 1.44 | 0.92 | 0.47 | 0.27 | 0.24 | 0.24 | 0.24 |
| 1997-1998 | 1.54 | 1.25 | 1.24 | 0.16 | 0.34 | 0.34 | 0.15 | 0.04 |
| % Change | 4.04 | 14.92 | -26.0 | 191.4 | -19.6 | -29.2 | 63.78 | 503.2 |



| 9 | 10 | 11 | 12 | 13 | 14 | 15 | 16 | 17 |
|---|---|---|---|---|---|---|---|---|
| Prmry & Semi-Finished Iron & Steel | Rubber mfd. Products Except Footwear | Manmade Yarn, Fabrics Madeups | Project Goods | Manufactures of Metals | Dyes/Intmdtes & Coar Tar Chemls | Inorganic/ Organic/Agro Chemls | Total Exports of First 15 Product Groups | Total Exports to the Country |
| 15.28 | 14.88 | 13.86 | 12.94 | 12.41 | 11.71 | 9.54 | 902.37 | 990.72 |
| 34.45 | 18.75 | 15.57 | 3.64 | 13.15 | 14.47 | 6.43 | 660.86 | 786.46 |
| -55.7 | -20.7 | -11.0 | 255.8 | -5.66 | -19.1 | 48.35 | 36.55 | 25.97 |
| Paper/Wood Products | Plastic & Linoleum Products | Manmade Yarn, Fabrics Madeups | Inorganic Organic Agro Chemls | Oil Meals | Fresh Vegetables | Processed Minerals | | |
| 14.82 | 14.03 | 13.77 | 10.98 | 8.46 | 8.37 | 6.37 | 362.20 | 440.08 |
| 17.78 | 16.74 | 9.81 | 9.96 | 13.54 | 13.15 | 0.82 | 361.42 | 489.23 |
| -16.6 | -16.2 | 40.36 | 10.25 | -37.5 | -36.3 | 676.3 | 0.22 | -10.05 |
| Tobacco Unmanufactured | Coal | GLS/GLSWR Ceramic/Reftrs Cement | Cosmetics Toiletries etc. | Inorganic/ Organic/Agro Chemicals | Spices | Misc. Processed Items | | |
| 5.01 | 4.61 | 4.60 | 3.49 | 3.33 | 3.17 | 2.94 | 126.45 | 149.35 |
| 7.01 | 4.73 | 5.49 | 3.05 | 3.32 | 3.54 | 3.94 | 143.17 | 170.05 |
| -28.6 | -2.47 | -16.2 | 14.55 | 0.05 | -10.3 | -25.4 | -11.68 | -12.17 |
| Machinery and Instruments | Inorganic/ Organic Agro Chemicals | Fruit/s Vegetable Seeds | Pulses | Manufactures of Metals | Fresh Vegetables | Iron & Steel Bar/Products etc. | | |
| 2.38 | 2.33 | 2.21 | 2.17 | 1.84 | 1.78 | 1.69 | 98.82 | 110.77 |
| 1.99 | 3.12 | 1.25 | 0.50 | 9.66 | 0.13 | 0.43 | 86.43 | 143.15 |
| 19.44 | -25.2 | 77.14 | 332.4 | -80.9 | 127.5 | 294.3 | 14.34 | -22.62 |
| Prmry & Semi-FInished Iron & Steel | Residl. Chemical & Allied Products | Other Commodities | Paints/Enamels Varnishes etc. | Other Cereals | Inorganic Organic Chemicals | Inron & Steel Bar/Rod etc. | | |
| 0.24 | 0.21 | 0.19 | 0.19 | 0.18 | 0.17 | 0.09 | 8.96 | 9.57 |
| 0.41 | 0.24 | 0.66 | 0.11 | 0.01 | 0.55 | 0.16 | 11.50 | 13.33 |
| -40.2 | -12.3 | -71.0 | 67.90 | 31.33 | -69.0 | -42.1 | -22.03 | -28.20 |
| Paper/Wood Products | Plastic & Linoleum Products | Other Ores and Minerals | GLS/GLSWR Ceramic/Reftrs Cement | Marine Products | Cosmetics Toiletries etc. | RMG Manmade Fibres | | |
| 0.22 | 0.21 | 0.18 | 0.18 | 0.17 | 0.13 | 0.12 | 6.62 | 7.74 |
| 0.37 | 0.06 | 0.06 | 0.18 | 0.23 | 0.11 | 0.08 | 6.15 | 8.74 |
| -40.3 | 259.4 | 227.9 | -3.22 | -26.2 | 11.78 | 49.56 | 7.68 | -11.35 |

Exchange Rate April-March 1998-1999 US $ = Rs. 42,0706 Exchange Rate April-March 1998-1999 US $ = Rs. 37,1648

*Source of Data:* DGCI&S, *Foreign Trade Statistics of India* (Principal Commodities and Countries).

## Table 2

### Balance of Trade (BOT) of Bangladesh, Nepal and Sri Lanka with India and Total

(US $ in millions)

| | 1997 | 1998 |
|---|---|---|
| 1. **Bangladesh** | | |
| India | -736(639)* | -927(499)* |
| Total | -2735 | -2373 |
| Per cent of India | 26.9<br>(23.4)* | 39.1<br>(21.0)* |
| 2. **Nepal** | | |
| India | -74 | -7.4 |
| Total | -1245 | -992 |
| Per cent of India | 6.0 | 7.5 |
| 3. **Sri Lanka** | | |
| India | -459 | -401 |
| Total | -1213 | -1318 |
| Per cent of India | 37.8 | 30.4 |

*Excluding rice exports from India.

*Source :* India : DGCI&S: *Foreign Trade Statistics of India* (Principal, Commodities and Countries).

Total : Asian Development Bank (ADB), *Asian Economic Outlook,* April, 1999.



## Table 3

### Lending by the World Bank to South Asia, by Sector, 1989-98

(US$ in millions)

| Sector | Annual Average 1989-93 | 1994 | 1995 | 1996 | 1997 | 1998 | Annual Average 1994-98 | %Share 1994-98 |
|---|---|---|---|---|---|---|---|---|
| 1. Agriculture | 553.3 | 387.8 | 551.3 | 420.6 | 409.0 | 876.1 | 529.0 | 18.7 |
| 2. Education | 339.0 | 220.0 | 423.7 | 499.8 | ... | 718.2 | 372.3 | 13.1 |
| 3. Electric power and other energy | 801.9 | 230.0 | 250.0 | 700.0 | 24.2 | 295.0 | 299.8 | 10.6 |
| 4. Environment | 103.3 | 14.7 | 168.0 | 263.9 | 64.8 | ... | 102.3 | 3.6 |
| 5. Finance | 234.3 | ... | 916.0 | 205.0 | 105.0 | ... | 245.2 | 8.7 |
| 6. Health, nutrition and population | 270.5 | 233.1 | 257.9 | 376.7 | 593.8 | 626.4 | 417.6 | 14.7 |
| 7. Industry | 198.5 | 250.3 | 3.2 | ... | ... | ... | 50.7 | 1.8 |
| 8. Mining | 2.4 | ... | ... | 63.0 | ... | 532.0 | 119.0 | 4.2 |
| 9. Multisector | 269.5 | ... | ... | ... | ... | ... | ... | ... |
| 10. Oil and gas | 301.0 | ... | 120.8 | ... | ... | ... | 24.2 | 0.9 |
| 11. Public sector management | 33.0 | 296.8 | ... | 92.0 | 31.7 | 250.0 | 134.1 | 4.7 |
| 12. Social sector | 111.5 | ... | ... | ... | ... | 543.2 | 108.6 | 3.8 |
| 13. Telecommunications | 22.4 | ... | ... | 35.0 | ... | ... | 7.0 | 0.3 |
| 14. Transportation | 246.0 | 491.3 | ... | ... | 684.5 | 23.5 | 239.9 | 8.1 |
| 15. Urban development | | 246.0 | 39.0 | 21.5 | ... | ... | 61.3 | 2.2 |
| 16. Water supply and sanitation | 145.9 | ... | 275.8 | 251.6 | 98.6 | ... | 125.2 | 4.4 |
| Total 1-16 | 3640.8 | 2370.0 | 3005.7 | 2929.1 | 2011.6 | 3864.4 | 2836.1 | 100.00 |
| Of which : IBRD | 1728.6 | 474.0 | 1584.8 | 1161.6 | 626.5 | 1318.0 | 1033.0 | |
| : IDA | 1912.3 | 1896.0 | 1420.9 | 1767.5 | 1385.1 | 2546.4 | 1803.2 | |

*Source :* The World Bank, *Annual Report,* 1998.

## TABLE 4

### Current Account Surpluses, 1991 to 2000 (F)

(US $ in Billions)

| Country | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | Total | Average |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | | | (F) | (F) | 1991-2000 | 1991-2000 |
| Japan | 68.4 | 112.3 | 132.0 | 130.6 | 111.4 | 65.8 | 94.1 | 121.6 | 143 | 138 | 1123.7 | 112.37 |
| France | -6.2 | 3.8 | 9.2 | 7.4 | 10.9 | 20.5 | 39.4 | 41 | 37 | 42 | 211.3 | 21.13 |
| Italy | -24.5 | -30.2 | 8.4 | 12.8 | 25.1 | 40.5 | 32 | 20 | 19 | 21 | 150.7 | 15.07 |
| The Netherlands | 7.7 | 7.4 | 13.6 | 17.9 | 23.8 | 22.9 | 22.2 | 21.1 | 21.5 | 24.5 | 182.6 | 18.26 |
| Belgium-Luxembourg | 4.7 | 6.6 | 11.2 | 12.6 | 14.3 | 14.1 | 13.5 | 13.3 | 13.6 | 14.5 | 118.4 | 11.84 |
| Sweden | -4.7 | -7.8 | -3.8 | 0.8 | 5.5 | 6.5 | 6.6 | 4.8 | 4.3 | 4.1 | 16.3 | 1.63 |
| Switzerland | 10.6 | 15.1 | 19.5 | 17.5 | 21.4 | 22.0 | 22.9 | 23.8 | 24.9 | 26.1 | 203.8 | 20.38 |
| Korea, South | -8.3 | -3.9 | 1.0 | -3.9 | -8.5 | 23.0 | -8.2 | 40.5 | 26.1 | 16.0 | 73.8 | 7.38 |
| Taiwan Province of China | 13.1 | 8.5 | 7.0 | 6.5 | 5.5 | 11.0 | 7.7 | 3.5 | 5.8 | 6.1 | 74.7 | 7.47 |
| Hong Kong | 6.1 | 5.8 | 8.6 | 2.1 | -5.5 | -1.5 | -5.6 | 1.0 | 1.9 | 2.0 | 14.9 | 1.49 |
| Singapore | 4.9 | 6.0 | 4.3 | 11.5 | 14.4 | 14.5 | 15.0 | 17.6 | 14.9 | 15.4 | 118.5 | 11.85 |
| Total of above | 71.8 | 123.6 | 211.0 | 215.8 | 218.3 | 239.3 | 241.3 | 313.2 | 331.0 | 323.4 | 2288.7 | 228.87 |

*Source : IMF, World Economic Outlook*, October, 1999.

F= Forecast



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*Annexure I*

## Main Conclusions on Mobilising International Surpluses for World Development

*(The WIDER Study, 1987, on a Japanese Initiative)*

1. Substantial surpluses on current account are likely to prevail for the next several years among many developed countries, and there is a need for their diversification towards meeting developing country requirements, both on intrinsic grounds, and in the interests of promoting global economic stability.

2. Japan, in particular, should take an initiative for resource transfers to developing countries, matched by other developed countries, as the joint effort would contribute significantly to world development.

3. The ideal mechanism for implementing such a Japanese initiative would be to equip a Japanese Government agency with an explicit Government guarantee that will enable it to borrow in the domestic capital market terms, with resources for an appropriate level of interest subsidy to be provided to it by a suitable reallocation of Japanese Official Development Assistance.

4. In the Japanese context, the following equivalent mechanisms are also available:

   (a) Loans raised under the guarantee of a suitable agency, a Japanese Trust Fund might be covered be private reinsurance arrangements.

   (b) Developing countries might borrow from the Japanese commercial banking system against the collateral of zero coupon bonds purchased from the Japanese or international market, or specially issued by the Japanese Government. The amounts borrowed would be a substantial multiple of the investment needed to buy these bonds, whose face value on maturity will be equivalent to the principal borrowed, thereby fully securing the "bullet" repayment of the principal.

   The most appropriate mechanism for this form of borrowing would be through a Japanese Trust Fund located in Tokyo and liaising with the World Bank and other regional development banks, for administering the scheme. It could, alternatively, be locted within the World Bank, especially if other countries were to join in adding resources to the facility. Its management might be entrusted to a Policy Co-ordination Committee including commercial bank, the Bretton Woods institutions and major developed countries in order to facilitate the evolution of longer-term policy frameworks for lending.

The Trust Fund would purchase the zero coupon bonds from the Japanese Government and from the market, borrow in its own name from the Japanese commercial banking system and from the market, and relend these monies to developing countries at a suitable blended rate.

The Trust Fund would ideally need resources from the Japanese Government for the purchase of the bonds to be used as collateral. This would have no immediate net financial impact on the Japanese budget, since the funds would return to the budget when the bonds are purchased. The interest subsidy, needed to provide a representative blended rate for lending at below the market rate for borrowing, can be met fro the duration of the lending programme, out of the increment in Official Development Assistance.

(c) Recourse could be had to the Export Import Bank of Japan to step up its co-financing arrangements by drawing more substantially on a pool of resources that are available to the Zaisei-Toyushi-the Government's Fiscal Investment and Loan Programme (FILP).

(d) The Export Import Bank of Japan has an unutilised guarantee power which could be utilised in a variety of ways for increased transfers to developing countries; the guarantee power itself could be increased either by increasing the Bank's capital or by varying its gearing ratio.

(e) The International Monetary Fund should be enabled to borrow in Japan's capital market for the purpose of programme lending to low-income developing countries, under the IMF's



Extended Financing Facility. The Japanese Government should provide an interest subsidy to reduce the cost of these funds to the user.

(f) A debt restructuring facility, utilising market mechanisms, might be established on a Japanese initiative, in order to pave the way for a resumption of lending to debtor countries.

(g) Lending under these programmes might focus on infrastructure development, in addition to normal project and programme lending in support of growth-oriented adjustment programmes.

5. Japan is in a position to aim for a tripling of Official Development Assistance over the period.

*Annexure II*

## Mobilisation of External Resources – Sources and their Apparent Benefits and Costs/Liabilities

| | Options | Benefits | Cost/Liabilities | | |
|---|---|---|---|---|---|
| | | | Economic. ST/MT Cost | LT Burden | Policy Impact |
| 1. | IDA Aid | Insignificant Cost with long maturity | A | A | A |
| 2. | i) World Bank Aid; (soft window); ii) ADB Aid . | Low cost but need for good project formulation | A | B | B |
| 3. | OECD (DAC) Aid | Low cost and useful esp. if untied. | A | A | B |
| 4. | Commercial borrowings | Freedom in imports | C | C | C |
| 5. | Non-residents' remittances | Freedom in imports | A | A | A |
| 6. | Country-Fund abroad, mobilisation through international companies | Freedom in imports | A | A | B |
| 7. | Development of Financial Centre and attracting foreign savings | High infrastructural cost + tax concessions, but large foreign exchange deposits can be expected | A | A | A |
| 8. | Large recycling of surpluses from Japan, a'la WIDER Plan | Low cost resource flow, but Japan to formulate effective wilfull policy and Plan | A | A | A |
| 9. | i) IMF Stand-By Credit ii) IMF's Extended Structural Adjustment Facility (ESAF) | Medium cost | A | A | A |
| 10. | Private Foreign (Direct) Investment | Technology Transfer and Resources without debt liability | A | B | B |
| 11. | Development contracts with capital surplus countries a'la Stoltenberg system, | Production expansion with comparative advantage | A | A | A |



## Notes to Annexure II

A. Consistent with low per capita income and development prospects.

B. Needs change in certain priorities and policy reform in favour of efficiency to be able to repay. These may include trade liberalisation, reduced fiscal deficit, cut in subsidies, change in pricing policies, and resource generation by public enterprises.

C. Imprudent from growth and financial angle as it may lead to recession and need for rescheduling if reforms do not materialise.

DAC Development Assistance Committee, members consisting of developed countries.

OECD Organisation for Economic Cooperation & Development, (Paris).

IDA International Development Association, part of World Bank artifact.

ODA Official Development Assistance, covering loans with at least 25 per cent 'grant' element.

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