



Rabobank

India looking East?

India has never been a big player in international trade. Nevertheless, over the past twenty years, the country has developed its trade relations. India started in 1991 with its 'Look East' policy, trying to gain better access to regional markets in Asia. In this Special Report we analyze how the policy has developed since its inception, and why success has been limited so far.

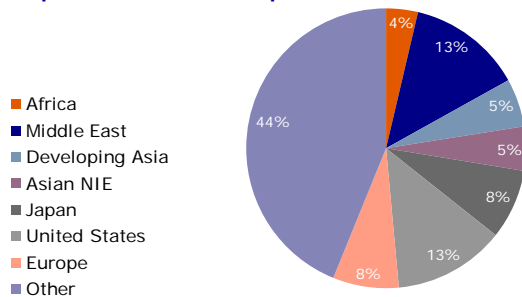
India's trade policy history

India is still a rather closed economy. The value of exports was only 20% of GDP in 2009, all imports of goods were valued at 24% of GDP in the same year. History may provide an explanation of the slow development of the external sector. Before 1991, India mostly engaged in barter trade with the Soviet Union. The only Southeast Asian nations which had serious trade relations with India were from the communist bloc at that time: Vietnam, Laos and Cambodia. During the Cold War, these states were also impoverished because of years of war and social upheaval. India's pro-Soviet stance alienated it from South East Asia. When India signed the Indo-Soviet Treaty of 1971, the country earned a lot of

distrust in the region and became further estranged. As trade with the Soviet Union collapsed India experienced a severe balance of payments crisis. As a result a series of economic reforms and new policies were put forward.

One of these initiatives was the Look East policy, initiated in 1991 by former Prime Minister Narashima Rao to improve political, strategical and economic relations primarily by developing trade links. Initially, the focus was on South East Asia, however it has since then been extended to reinforce economic relationships with the rest of Asia as well. The main trade agreements that India has signed in the region can be found in Box 1. This shows that efforts to improve regional trade connections started before 1991, but the necessity to engage in deeper connections in the region started then. One important Free Trade Agreement (FTA) has been signed in January 2010, with the Association of South East Asian Nations (ASEAN). ASEAN is comprised of ten nations: Indonesia, Malaysia, the Philippines, Singapore, Thailand, Brunei, Myanmar, Cambodia, Laos and Vietnam. The

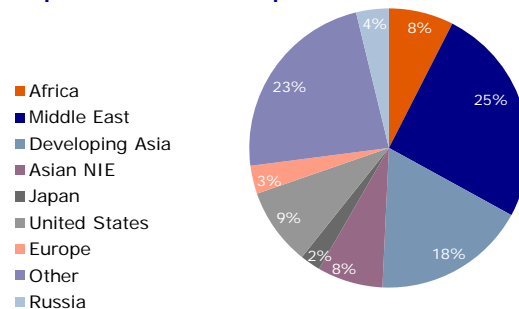
Graph 1: India's trade partners in 1991 ¹



Source: EIU

¹ Asian NIE stands for Newly Industrialized countries which include Hong Kong, Taiwan, Singapore and South Korea. The share of Other is substantial as it includes Russia and the rest of world, however data on trade with Russia is unavailable for 1991.

Graph 2: India's trade partners in 2008



Source: EIU

coming into existence of this FTA is exemplary of the troubles that India has faced in the region. Besides the important trade deals

mentioned, India engaged in a maze of Preferential Trade Agreements (PTAs), but these have been of much less importance to the overall trade policy of the country.

Box 1: Facts and figures India's trade agreements

Listed below are the three most comprehensive and important sub regional trade agreements India has signed.

Name: Asian Pacific Trade Agreement (formerly known as the Bangkok agreement)

When: 1975

Members: China, Bangladesh, India, Korea, Sri Lanka and Laos.

Significance: This is Asia's first multi-member preferential trade agreement. As it includes both India and China, the latter joining in 2001, it still has the potential to become one of the largest trade agreements in Asia.

Name: South East Asian Free Trade Agreement (SAFTA)

When: 2004

Members: India, Pakistan, Sri Lanka, Bangladesh, Bhutan, Maldives, Nepal and Afghanistan. These countries are united under the South East Asian Association for Regional Cooperation (SAARC)

Significance: SAARC aims to reduce tariffs for intraregional trade, which is expected to be completed by 2015. The member countries are currently negotiating on liberalization of the services market.

Name: Bay of Bengal Initiative for Multi-Sectoral and Technical Cooperation (BIMST-EC)

When: 1997

Members: India, Bangladesh, Sri Lanka, Thailand, Myanmar, Nepal and Bhutan.

Significance: The goal of BIMST-EC was to combine the Look West policy of Thailand and ASEAN with the Look East policy of India, with the main objective to collaborate to achieve rapid economic and social development. India finalized signing FTAs in goods with the member countries last year. The interesting part of this agreement is that it goes beyond economic cooperation, highlighted by the signing of a counter terrorism agreement in December 2009.

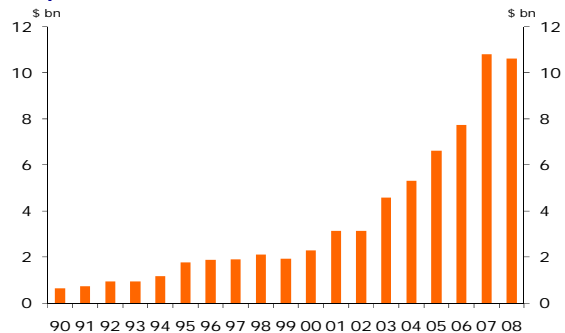
Looking East negotiations

The aforementioned mistrust of countries in Asia vis-à-vis India has led to serious problems

in establishing the final FTAs. Not only were there delays in reaching an agreement, but the results of the negotiations often lacked impact. India was more than once the culprit in not achieving the desired outcome. For instance, India negotiated a framework agreement with ASEAN, but when it came to a comprehensive trade agreement itself, Indian negotiators put so many exceptions on the table that talks almost failed. India initially had over 1,400 items on its sensitive list, items banned from trading. India has been reluctant to give in to trade concessions; negotiating this number down to a more acceptable level resulted in a six year delay. Another example is SAPTA. India did offer, on paper, the largest concessions in tariff lines in the initial discussion rounds. However, the tariff cuts were not deep enough to have a significant impact. Furthermore, they excluded items such as textile products, rubber and tea; just the products Sri Lanka and Bangladesh were competitive in.

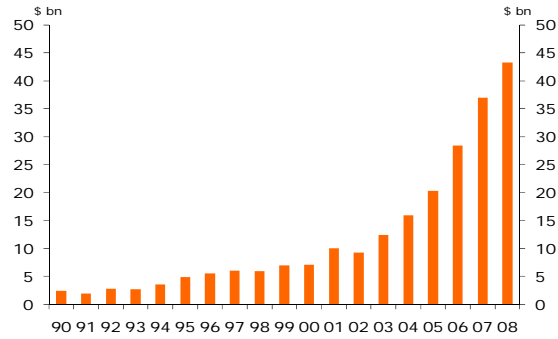
However, India's partners were also partly to blame. Political turmoil in and between member states have at times caused delays. SAFTA (2004) should have been signed in 1998, but was delayed because of the geopolitical tensions between India and Pakistan. A reason for the delays in the India-ASEAN trade negotiations is that the ASEAN countries have had a hard time letting go of viewing India from a cold war perspective, as mentioned before.

Graph 3: India-SAARC trade



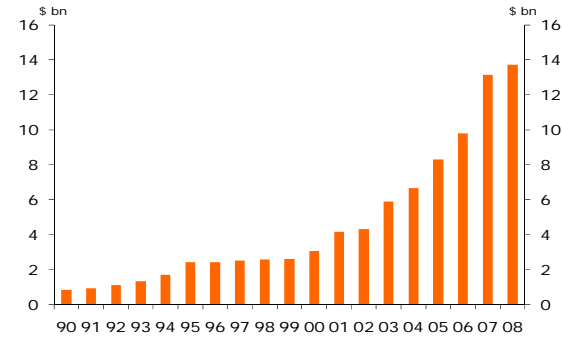
Source: EIU

Graph 4: India-ASEAN trade



Source: EIU

Graph 5: India-BIMST-EC trade



Source: EIU

20 years of opening up and looking east

We will finally take a look at how India’s trade relations have developed over the last 20 years. First, we have used the combined value exports and imports of goods to define trade. Graphs 1 and 2 demonstrate a shift away from Western economies. While 21% of India’s total trade was with the US and Europe in 1991, this had been reduced to 12% in 2008. India has diversified trade to the Middle East, the share of which grew to 25% in 2008 from 13% in 2009. This is logical as India is a net oil importer and is strategically seeking to increase ties with the Middle East. We also note from the graphs that the share of Asia increased to 21% in 2008 from 15% in 1991. As such, the Look East policy can be called effective in terms of trade diversification. Finally, from 2003 onwards trade volumes picked up. SAFTA, signed in 2004, gave India’s trade volumes a boost. Also, in 2003 a framework agreement with ASEAN spurred confidence and boosted trade. This increase in regional trade is demonstrated by graphs 3, 4, and 5.

Conclusions

The Look East policy of India, which started in 1991, has had some effect on the diversification of trade. However, it has taken a long time for the region to come to terms with their mistrust towards the Soviet-oriented policies of India’s past. This is the primary cause for trade negotiations running into trouble and lacking impact when finally concluded. We do see a trend in Asia, where the regional partners are looking towards a balance of power between China and India (and Japan) in the region. Therefore, the recently signed FTA could reinforce the exponential trend of trade we have seen since 2003. India will continue to be dependent on oil from the Middle East. However, from an economical and political point of view, creating closer ties with regional partners bodes well for India’s future.

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