About the Regional Desk Team

ICRIER created the Regional Desk Team in 2008.

Research on India’s relations with other countries will have to take on board the increasing demand being placed on India for a major role in international discussions on evolving a new global social, economic, financial and environmental architecture.

In this context, each researcher has adopted a country/region. The Team will be tracking and monitoring developments in the major countries, regions, economic blocks and India’s neighbours. ICRIER Regional Desk Team’s in-house publication ‘Regional Insights’ will provide articles on many of these countries/regions and will also contain a guest article by a renowned expert.

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Foreword

Trade was the driver of growth of the Indian economy after the big-bang reforms initiated in 1991. As India grew from being a low-income developing country to a middle-income emerging market, not only did it become increasingly integrated into the global trading system, but its voice was heard with greater attention in the various international institutions. Now, as the second fastest growing economy in the world, India is viewed as a significant player on the global economic scene and a systemically important participant in almost all international institutions. In this changed scenario, policy makers and scholars in India need to be more aware of developments taking place not only in the economies of its trading partners but in the wider world. ‘Regional Insights’ is a small initiative taken by researchers in ICRIER to bridge this information gap. The effort is to analyse one development in each of the countries covered. Each volume of Regional Insights will include contributions from some of the regional desks, with the other desks contributing in subsequent volumes. There will also be an article by a guest author.

The guest article in this issue is on the G-20; what is expected of it and what it can reasonably achieve. The expectations from it need to be grounded in reality and the reality is that in spite of the anti-protectionist declaration of the summit meeting on 15th November 2008, 17 of the 20 countries have introduced protectionist measures since then. The article urges that the G-20 should, at least for now, focus on finding a solution for the global financial crisis.

This is the second issue in this bi-monthly publication; the first issue of ‘Regional Insights’ was published in January 2009. Though the global economic crisis is the main issue currently agitating most minds, in the January issue the guest author wrote about it while most of the ICRIER researchers tried to look at other issues that they considered important but which are not occupying mind-space. The countries covered in the January issue were Britain, Canada, China, France, Iceland, Japan, and Pakistan, along with a review of a book relating to West Asia. In the March issue the countries covered are Bangladesh, China, Nepal, Pakistan, Russia, South Africa and Sri Lanka, and there is a review of a book that looks at America’s role in Asia. Most of the articles in this issue look at how the global economic and financial crisis is affecting a particular sector and what is the country’s response in addressing the sector’s concerns — this is distinct from the economy-wide response that the country may be formulating.

Regional Insights is the result of the initiative of researchers at ICRIER to put in one publication some of the developments taking place around us. The data has been collected from a variety of sources and should be viewed as indicative rather than authoritative. The observations and conclusions expressed in this volume are the personal views of the researchers and not necessarily the views of ICRIER.

Shrawan Nigam
Supervisor, Regional Desks and
Senior Consultant, ICRIER
This article attempts to examine the economic crisis that Russia has been facing since 1998, when the government defaulted on its debt and the Asian financial crisis began to ripple throughout the world. Russia was still reeling economically, socially and politically from the fall of Soviet Union just six years before. At that time Russia tried to control Rouble volatility by keeping its value close to the U.S. Dollar. It maintained a floating peg and tried to keep the exchange rate within a certain range. Whenever, the Rouble crossed that range the Russian central bank took action either by buying or selling its foreign reserves to keep it within the band. The government never made this information public so as to avoid the dangers of speculation which could potentially hamper government initiative to make the Rouble less volatile. However, it required hard currency, and at the same time energy prices were also tumbling. Therefore, Russia ended up with spending huge amounts of money and finally, on August 13, 1998, its bond, stock and currency markets all collapsed. Inflation soared to 84 per cent, massive Rouble devaluation took place and import became expensive. Suddenly all its savings was erased from the market and Russia ended up defaulting on domestic and on international debt. On average, real wages were less than half of what they were in 1991, and only about 40 per cent of the work force was being paid in full and on time. Russia ended in 1998 with a decrease in real output of 4.9 per cent. To summarise, the crisis of August 1998 did not only undermine Russia’s currency, it also erased any remaining hope that Russia could successfully reform its economy.

However, after 1998, Russia has slowly rebuilt its economy. Due to high energy prices there has been huge cash flow into the economy and gradually it paid off all its international debt. Overall fiscal balance also continued to increase; growth rate accelerated from 6.9 per cent in 2006 to 7.9 per cent in the first quarter of 2007. From a peak of almost 14 per cent in mid-2005, inflation dropped to 7½ per cent in March 2007.
Again, exactly after ten years, a similar crisis is emerging. Due to the global financial crisis, Russia –Georgia war and oil price decline, the Rouble again has started to fall, huge depletion of reserves is taking place, and Russian investors are dumping stock to raise cash. The following graph shows the recent downturn of the Russian economy.

After 1998, Russia has kept the Rouble within a range of 24-31 per dollar and it has been slowly widening its daily trading band, allowing its Rouble decline to accelerate gradually. This time also Moscow has spent money to control the spread of the crisis all over the nation but gradual process of devaluation may have bought time for banks to pay off some of the 2008 debts at the cost of eroding Russia’s foreign exchange liquidity. On the other hand, decline in Rouble value was further aggravated by the fact that Russian retail depositors are reluctant to keep money in Rouble due to uncertainty, and there has been huge capital outflow resulting in falling commodity prices and seizure of global capital markets.

Turning to the debt problem we observe that, Russian banks and firms are finding it difficult to pay off their external debt, which is evident from the fact that Russia had its debt rating cut by Fitch Ratings for the first time after 1998 (when the government defaulted on domestic debt and devalued the Rouble, wiping out the savings of millions of people overnight). The rating was lowered to BBB, the second-lowest investment grade, from BBB+. Thus the Russian banking sector appears to be moving towards a precipice. However, international banks have proposed restructuring talks with Russian companies for loans due for repayment in next four years and Russian banks also have asked for government help in this regard.

There are two potential ways to deal with the problem. One, is for the government to talk to the international banks for restructuring of debt with lower payments spread over a greater time horizon and secondly, let the banks default and seize control over the sector and then take over the bank’s debt directly as a part of the nationalisation process. The latter is a cheaper way to obtain assets of the companies. However, if the Russian government opts for the second option that would raise questions on credibility of Russian firms and private banks, and as a result foreign investors will become reluctant to extend further loans in future. Therefore, for Russia to react as a fiscally responsible state, it is important to handle the situation carefully so that it can recover from the present crisis with its credibility intact in international markets.

Debosree Banerjee
South Africa: Inflation Targeting in a Time of Crisis

According to Statistics South Africa (Stats SA), the recently released GDP figures for Q4 of 2008 has confirmed that GDP has contracted in the fourth quarter of last year by 1.8 per cent q/q seasonally adjusted and annualised (s.a.a.) rate, from 0.2 per cent q/q in Q3. This was the sharpest quarterly contraction since Q4 1992 and represents a slowdown in annual growth to 1 per cent in Q4 from 3 per cent in Q3, revised from 2.9 per cent previously. With the global financial crisis becoming a global economic crisis, the South African economy is facing challenges both from external and domestic quarters in terms of lower aggregate demand. In the following sections the author will try to argue that perusing inflation targeting in a time of crisis has made the task of the central bank to revive domestic demand more challenging. The internal growth dynamics will deteriorate further on the back of more vulnerable household sector and contracting household demand. But attributing this contraction of aggregate demand entirely to the current global economic crisis would be wrong when South African Reserve Bank (SARB) has been following a very tight monetary policy stance since June, 2006, and stricter lending criteria as a result of the new National Credit Act.

With the introduction of inflation targeting in early 2000, interest policy has been guided by inflation prospects over the medium term as perceived by the Monetary Policy Committee (MPC) of SARB. It has a ceiling target inflation rate (as measured by CPIX that is overall consumer inflation excluding the effects of mortgage interest rate changes) within the 3 per cent to 6 per cent range. Any threat on the upside is to be met by interest rate hikes and, similarly, a possibility of a fall below 3 per cent prompts some relaxation of policy.

Figure: Demand Contraction in South African Economy (in per cent)

Now the question that arises is, how this inflation targeting policy performed in the past and what implication does it have for the future recessionary forces working within and outside South Africa. The South African economy has been mainly driven by domestic consumer demand. Which becomes evident when we look at the economy from the expenditure side, 61.4 per cent of GDP consists of household consumption expenditure, demand from the part of government consumption expenditure is 19.7 per cent, fixed capita investment is 21.1 and net export is -2.2 per cent of GDP. In a global
recessionary time, what is needed is to induce consumer spending, and for the South African economy, what is significant is demand coming from the household sector.

But when we look at the above chart, under a very tight monetary policy, between Jan, 2006 to Nov, 2008 repo rate (repurchasing rate) was increased by 500 basis points and a huge reduction in money supply and in credit extended to private sector was undertaken. On y-o-y basis, the growth in private sector credit extension declined to 11.9 per cent in Jan, 2009 from 27.5 per cent in Oct, 2006, when it peaked. For the same period, Money supply declined to 12.9 per cent from 23.7 per cent. The period, during which global food and energy prices were driving inflation all over the world, following a contractionary monetary policy for inflation targeting has put further challenge for the policy makers. As contraction of domestic demand in South African economy started way before the spread of the global financial crisis, the slowdown can be attributed more to the domestic policy measures.

Another key factor contributing to the slowdown in household expenditure has been the record levels of household debt of approximately 49 per cent of GDP, accumulated over the past five years. The ratio of household debt to disposable income moderated to 75.3 per cent in Q3-2008, after easing to 76.6 per cent in the second quarter from a record high of 78.5 per cent in the first quarter. Unfortunately, the moderation in debt levels was partly offset by higher interest rates, keeping debt service cost at a punishing 11.7 per cent of disposable income, only slightly down from 11.9 per cent in the second quarter of 2008. Since the onset of tighter monetary policy in June 2006, the cost of servicing debt rose by nearly 50 per cent. This burden increased sharply on the portion of outstanding debt (almost two-thirds of current outstanding debt) that was incurred during the prior accommodative monetary policy cycle. This financial pressure forced households to severely cut back on spending.

As the above chart shows, after mid 2006, household finance was under stress, growth in final consumption expenditure (FCEHs) and disposable income started falling, largely eroded by higher inflation and accentuated by the increasing cost of finance and debt servicing.

Thus it is quite evident that although a tight monetary policy for inflation targeting controlled the CPIX within target range till mid 2006, but continuing further with a very high interest rate regime and contractionary measures for a longer time may have accentuated the problem of lack of domestic aggregate demand in the South African economy. Further, looking at the debt profile of the main driver of consumer demand which is the household sector, it would not be wrong to say that a rocky road is still ahead for the economy.
Imported Inflation?

Global prices have been on a rollercoaster ride since early 2008. In first half of the year inflation was in the news as it climbed to historic levels leaving no region untouched. Central to it were the rising energy and commodity prices. This was followed by prices falling across the board in the latter half of the year. Though insulated from the global economy, data released by Nepal Rastra Bank (NRB), the central bank of the country shows that prices in Nepal too experienced an upward spiral. According to B. J. Aitkin, deputy division chief of the International Monetary Fund (IMF) for Asia and Pacific, Nepal’s inflation could well be called ‘imported’ as, “Inflation in Nepal is largely catalysed by conditions in India.” A logical view considering that 60 per cent of Nepal’s total imports (around 18 per cent of Nepal’s GDP) are from India, the border between India and Nepal is porous and, Nepali Rupee is pegged to the Indian Rupee.

However, though Nepal’s prices were following the trend of prices in India up until August 2008, they have diverged thereafter. While the prices are falling in India, the prices in Nepal continue to remain high and are being driven by significant rise in prices of food and beverages (an average of 15.9 per cent) as well as non-food and service (average 11.3 per cent) during July 2008 -January, 2009.

The Finance Minister of Nepal has been blaming the cartels and syndicates of hoarding and creating artificial shortages and thereby increasing prices. However the rising prices could be a reflection of the problems that beset the country. The decade long political unrest in the country has left the economy fragile, destroyed the infrastructure and shattered private sector’s confidence. The economic growth rate has been lower than any of the South Asian countries in the 2000s. Heavily dependent on the weather, the agriculture sector is an important determinant of Nepal’s overall growth rate. This sector

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1. Various estimates have been made about the costs of conflict in Nepal. DFID estimated the cost of conflict in Nepal at 8-10 per cent of GDP. As per the estimate of Asian Development Bank, infrastructures amounting to minimum $250 million were destroyed. (Jha H.B. ‘Nepal: Economic Costs of Conflict’, Telegraphnepal.com. November 2008).
is characterized by slow growth rate (average rate of 3.3 per cent over 2003-2007), low production levels, diminishing cropland holdings and falling productivity. A recent report states that Nepal is, “…unlikely to overcome in the near future the challenges associated with increasing agricultural production, including, limited irrigation coverage, limited use of fertilizers and improved seed varieties, and increasing input costs.”

Manufacturing sector, which provides employment to the semi and unskilled urban labour, is doing no better. It grew at a low rate of 0.18 per cent during 2007-08 and at an average of 1.9 per cent over 2003-04 and 2007-08. Seventy per cent of factories in the country have shut down due to strikes called by trade unions associated with political parties. In 2007 alone labour strikes, transporter strikes and other political actions, closed business and transport operations for up to 120 days in the worst-affected district in the Terai. The 14 to 16 hour power shortage is further adding to the woes of industry. While many small and medium scale industries have either cut output or shut down resulting in a shortage of major essential items, the large industry operating with their own energy generators are passing the high operating costs by charging higher prices.

Looking at the current political conditions in Nepal the same report has warned that Nepal is facing a serious risk of stagflation, a condition of low economic growth, high unemployment and rising prices.

Nepal is one of the poorest countries in the world with an estimated 31 per cent of the population living below the poverty line. The average per capita income is just US$470. It is also predominantly agricultural. Consequently the government does not have much space to increase its resources by way of taxes to make the necessary investment. Therefore it is imperative that private sector investments along with FDI are encouraged.

Studies have shown that for private investment as well as FDI, a country’s business environment and institutional quality are equally if not more important than low wages or financial incentives for investments. The global competitiveness index which ranks countries on a broad range of indicators such as institutions, macroeconomics, infrastructure, business sophistication and innovations shows that Nepal has slid down from 114 in 2007-08 to 122 in 2008-09 among the group of 131 countries.

It is not that the challenges that Nepal faces cannot be overcome. However to do this and to give to the people a better life, the new Maoist-led government has to take urgent steps to improve the investment and business environment.

Manjeeta Singh
Nepal Desk

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3. Ibid.
Regional Insights

Bangladesh-India Relations: A New Partnership

India is looking forward to an improved relation between the two countries with the formation of a new government in Bangladesh. The visit of India’s Foreign Minister, Pranab Mukherjee to Bangladesh on 9 February 2009 is expected to give a major boost to economic relations between the two countries as issues that have been pending for a long time, have a good chance to be addressed. During the visit, Bangladesh and India signed two agreements on bilateral trade, and investment development and promotion. The two countries have significant trade but the bilateral investment is negligible. This article focuses on the importance of the two agreements and its implications for partnership of the two countries. These two agreements are of great significance as they can play an important role in enhancing trade and investment between two countries.

The bilateral trade agreement between Bangladesh and India was first signed in 1980 and was later amended and signed in March 2006. This agreement is valid up to March 2009. The signing of the trade agreement, which also has a separate protocol on transit, provides opportunities for Bangladesh and India to gain immensely. The renewal of trade agreement would allow Bangladesh and India to transport commodities using three different modes of transport i.e. road, rail and waterways. For a long period of time only waterways were allowed for transit, while road and rail facilities were never activated. With this deal Bangladesh will also get transit facility to Bhutan and Nepal.

Another, agreement which was signed during this visit is the ‘Agreement on Bilateral Investment Development and Promotion.’ Signing of this agreement will expand the horizon of bilateral investment between India and Bangladesh. Investment can enable Bangladesh to easily access the Indian market and help in narrowing the huge trade imbalance with India. Bangladesh’s trade deficit with India has increased from US $ 1.01 million in 2001 to US $ 2.19 million in 20071, though Bangladesh is India’s second largest trade partner in the SAARC region after Sri Lanka. Bangladesh has often expressed concern on this issue. One way to bring down the trade imbalance for Bangladesh is to attract foreign investment from India into industries that have a potential to export to the Indian market. The possible sectors where India could invest include textiles, electronics, information technology, natural gas based industries, frozen foods, leather, ceramics, light engineering and agro based industries. These are sectors in which Bangladesh has a comparative advantage. Also, India can invest in sectors that have high intra-industry trade with Bangladesh. In recent years intra-industry trade between India and Bangladesh has increased in agricultural raw materials.

Table 1: Bilateral FDI Regime between Bangladesh and India

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<th>Sources of FDI</th>
<th>India</th>
<th>Pakistan</th>
<th>Sri Lanka 6.0 (2.6 per cent)</th>
<th>Bangladesh 0.99 (0.2 per cent)</th>
<th>Nepal 5.1 (51 per cent)</th>
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<td>India</td>
<td>n.a.</td>
<td>0.59 (0.01 per cent)</td>
<td>0.79 (0.08 per cent)</td>
<td>0.41 (0.18 per cent)</td>
<td>n.a.</td>
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Source: Debapriya Bhattacharya, March 2007, Presentation on “South Asia Intra-Regional opportunities and Challenges” in expert Meeting on Regional Integration in Asia

Note: Figures in parenthesis indicates percentage share of total FDI inflow to the respective country.
Despite the significant trade between Bangladesh and India, bilateral investment is negligible and foreign direct investment flows between India and Bangladesh are insignificant. Among South Asian countries, Sri Lanka and Nepal have been important hosts for FDI from India; while Pakistan and Sri Lanka have been important destinations for Bangladeshi investments (see Table 1). The outward investments from India in 2006 to Sri Lanka and Nepal were US $ 6 million and US $ 5.1 million, respectively while it was only US $ 0.99 million in Bangladesh. On the other hand, investment from Bangladesh in 2006 was US $ 0.79 million in Pakistan followed by India US $ 0.59 million and Sri Lanka US $ 0.41 million. Within the total investment coming from the south Asia region into Bangladesh, Pakistan was the single largest source (79 per cent) in 2005 (US $ 25.5 million), while Indian investment of US $ 1 million was the single largest source of FDI (47 per cent) in 2006. Indian companies that have invested in Bangladesh include State Bank of India, Asian Paints, Marico, ACI Godrej-Agrovet and Neelkamal Padma Plastics. Clearly there is a large potential to enhance investment flows between India and Bangladesh.

There is also a huge untapped trade potential between the two countries. Bangladesh imports several items from the rest of the world which are being exported by India to markets other than Bangladesh. Similarly, India imports several items from the rest of the world but not from Bangladesh. Using the potential trade technique, the estimated export potential from Bangladesh to India is US $ 0.72 billion. Items that are of export interest to India are categories of light oils, cotton, products of iron and cane sugar, and the items that can be imported from Bangladesh are urea, leather products, tanned hides and skins of bovine animals.

The renewal of the trade agreement and the signing of the Investment Development and Promotion Agreement and Framework agreement for transit facilities, pave the way to initiate talks on a bilateral Free Trade Agreement (FTA) between India and Bangladesh. In the larger context of South Asia Free Trade Agreement (SAFTA), India has recently announced duty free concessions to the less developed countries (LDCs) of SAARC Members which include Nepal, Bhutan, Maldives and Bangladesh. It has also reduced the negative list from 744 to 480 for these Members, which is expected to go down further in the coming months. Since India already has FTA with two of the LDCs i.e. Nepal and Bhutan, India should initiate a bilateral FTA with Bangladesh that could be comprehensive in nature and include trade in goods and services, non tariff barriers, investment and connectivity.

Rashmi Rastogi
Bangladesh and Myanmar Desks

1. Author’s calculation, using Export and Import Bank of India, DGFT
2. Debapriya Bhattacharya, March 2007, presentation on ‘South Asia Intra-Regional opportunities and Challenges in expert Meeting on Regional Integration in Asia.’
3. Author’s calculation, using UN COMTRADE database and WITS.
Textile Industry of Pakistan: Problems and the Impact of Natural Gas Prices –

Given the importance of the textile industry to Pakistan, and the problems faced by it; the author argues that the recent decision of the Government to not lower oil and gas prices in line with international prices will result in further burden on this industry.

The textile industry is the most important industry of Pakistan. The All Pakistan Textile Mills Association (APTMA) has estimated this industry to employ about 38 per cent of the total labour force and to have added about 8.5 per cent of the country’s Gross Domestic Product in FY07. Cotton cloth, knitwear, bed wear, ready made garments and cotton yarn were the largest components of exports in this industry in FY08, and cotton cloth and yarn from Pakistan were about 41 per cent of world exports in 2006.

The textile industry has been facing a crisis-like situation since 2004. The problems are: competition from global exports, declining productivity, increases in prices of cotton, and shortage of power and gas. Figure 1, showing the share of textiles in exports of Pakistan, reflects the decline in strength of this industry. Share of textiles in exports has declined from 64 per cent (FY 2004) to 51.5 per cent (FY 2008). In 2008, decline of the textile industry is revealed even in its industrial production, which fell 0.4 per cent in July-November 2008 compared to the same period in 2007. Moreover, this decline in production occurred in all components of this industry other than in cotton ginned. And though, cotton ginned production did not decline in 2008, it fell by 9.4 per cent during July-November 2007 year-on-year.

The energy position of Pakistan has been dismal for some years now. Power shortage and load shedding in the country forced many textile units to shift to private Sui-Gas based power plants. And though Pakistan has been dependent on oil imports, even gas which is locally produced is now seeing natural decline. Moreover, gas still remains the primary contributor to thermal power generation with about 55 per cent share in FY08. So, gas availability and pricing affects textile industry both directly in case of captive power units, and indirectly in case of consumers of thermal power.
Towards the end of 2008, the country saw a period of gas load shedding. Supply to many textile units was interrupted. As many players had just made huge investments in captive gas-power plants, units shut down and there were layoffs.

The oil and gas Advisor to the Prime Minister, Mr. Asim Hussain in January 2009 refused the possibility of buying gas from Iran citing it as too expensive and blaming the last administration for the present shortfall of 700 million cubic feet per day (MMcfd), up from 500 MMcfd last year. The Government now claims to have formulated a policy that will make the country self-sufficient in gas within 3 years. Under this policy oil companies are to set up a special fund and 100 new wells will be dug for fresh exploration in FY09.

But 3 years is a long time to wait for power/gas for textile units. Their business and exports are suffering and it is not just due to slowing world demand. In the period July-December FY09, textiles exports have fallen 1.7 per cent compared with last year\(^4\).

That is not the lone repercussion of this crumbling industry. At present this industry accounts for about 23.6 per cent of the private business sector loan portfolio of the banking sector of Pakistan and defaults have begun. Total textiles defaults are estimated at present at about PKR 320 billion.

The Government has made efforts towards helping the industry. Measures to support R&D have been extended since 2004-05 and concession of 3 per cent in interest rate subsidy on loans for spinning industries has been extended up to 2009. This shifts the burden of PKR 1.2 billion from spinning industries to the Government. While these address issues of low productivity and competitiveness in global exports, energy cost is worsening for this industry. In July 2008 Pakistan increased gas prices. Though global oil prices are now falling, Pakistan has decided to keep domestic prices high. The explanation given for this is the insufficient revenue collection, which otherwise fails to meet overambitious IMF targets. Domestic gas prices are linked to international and domestic applied oil prices. So this has resulted in higher domestic gas prices.

Comparing prices for natural gas in July 2008 to those set now, effective from January 2009; prices have been raised across almost all slabs. The textile industry faces increased gas prices, which have been raised from PKR 329.54 per million British Thermal Units (MMBTU) to PKR 339.43 per MMBTU for captive power. Fixed and minimum charges have also increased. Even for gas supplied to power stations, prices have been hiked; by as much as PKR 20 per MMBTU, in the case of Water And Power Development Authority (WAPDA) and Karachi Electric Supply Company (KESC).

These price escalations increase costs for the already troubled textile industry. It would be interesting to see how this industry deals with it at this point of the financial crisis in the economy.

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\(^1\) State Bank of Pakistan export data
\(^2\) According to data from Federal Bureau of Statistics
\(^3\) Sui is Pakistan’s largest Natural Gas producing field, located in the Southern Indus basin
\(^4\) According to data from Federal Bureau of Statistics, Pakistan
Regional Insights

Guest Article

G-20: Time to Institutionalise It and Focus on Main Issues

There is a flurry of international activity as we approach the second G-20 Summit in London on 2 April. The sherpas, sous sherpas and think tankers are all getting together to try and come up with an approach for addressing the current crisis that could result in a substantive communiqué after the summit. The G-20 process itself started in 1998, as an informal get together of finance ministers and central bank governors in the wake of the Asian crisis. The first Summit in Washington on 15 November seemed to transform it overnight into becoming the principal global institutional mechanism for addressing practically all that currently ails the world. The first Summit also spawned four working groups, each with two co-chairs, which are expected to submit their recommendations to the London meeting. Dr Rakesh Mohan, Deputy Governor, RBI co-chairs Working Group I on ‘Enhancing Sound Regulation and Strengthening Transparency.’ This recognises RBI’s success in ensuring that the Indian banking system has emerged virtually unscathed from the global financial crisis. The other three Working Groups are, ‘Reinforcing International Co-Operation And Promoting Integrity In Financial Markets’; ‘Reforming The IMF’; ‘The World Bank And Other Multilateral Development Banks.’

It would appear that the terms of reference of these four Working Groups have defined the agenda for the G-20 deliberations. This is hopefully not the case as this would leave out important issues like Protectionism and Climate Change, both of which find strong reference in the Declaration issued after the Washington Summit. The only possible rationale seems to be that the four issues/areas that are covered by the G-20 Working Groups are not being addressed in any other forum. Protectionism and climate change have their own designated processes where negotiations are in progress. The less benign interpretation can be that G-20 governments do not want to circumscribe in any way their positions and negotiating stance in the current multilateral trade and climate change negotiations by having these discussed in the informal setting of the G-20. This is perhaps also the reason, due to which, going by international protocol, the G-20 working groups are headed by individuals rather than being co-chaired by member countries.

Two crucial questions with regards to the G-20 process that have been raised are, first the legitimacy of the G-20 as the primary global institutional mechanism for collectively tackling global economic and financial issues. Second, should the G-20 for the present continue to focus principally on efforts to address the global financial crises and the subsequent economic downturn or extend its mandate to also cover other important global issues.

It is clear that the G-20 process does not enjoy any real political or institutional mandate or legitimacy. It is neither backed by a treaty nor a UN resolution and not even a declaration of vision and intent. It remains an ad-hoc process, whose composition, direction and mandate varies at different times. Even in Washington, new members like Spain and the Netherlands were added. Now for London we have the Chair of The New Partnership for Africa’s Development (NEPAD), the chair of the Association of South East Asian Nations (ASEAN), the president of the EU Commission, and the chairman of the African Union Commission being invited to the Summit. These are of course in addition to the heads of all other multilateral organizations like the IMF, World Bank, WTO, OECD and other Multilateral Development Banks (MDBs) who are regular attendees. This has two implications. First that G-20 accepts a fluid and variable geometry, which while perhaps effective, may not give it the required gravitas and legitimacy to push through with any proposal that it may make. Second, not having been institutionalised in any form, it will not be taken with sufficient seriousness by governing establishments in any major country. Its success or lack of it remains a function of individual leaders and the resources and policy
attention he can mobilise for it. So a Summit being led by Gordon Brown may have a very
different outcome from one being called by a lame duck president or by an embattled head
of the government in an emerging economy. The risk is that it could be quickly perceived
by those who matter in the business and financial world as merely a ‘talking shop’ with no
real powers and allowed to wither away with the passage of time.

This concern about ensuring the effectiveness of a truly global institution has generated
several suggestions about reshaping the G-20 process. One suggestion is to reduce it to a
more manageable G-4 (Barry Eichengreen and others) that includes the US, EU, Japan and
China. This could feasibly be expanded to a G-5 by including India as not to exclude
the world’s largest democracy and fourth largest economy. The smaller formation will
lend itself better to serious consultations rather than ‘statement making’ and impressing
the galleries. But it looks unlikely that other members of the G-20 or G-8 will relinquish
their place on the high table so easily. The other suggestion has been for G-20, in either it’s
present or reduced form, to replace the G-8. This would leave it as the only truly global
formation, without any north-south or ideological divide. At the Washington Summit
in November, separate meetings were organized on the sidelines of the actual Summit,
by various G-formations like G-8 or G-77 or G-33. This is not healthy if the attempt is to
achieve collective and coordinated global action for addressing global issues. However,
it will need real statesmanship on the part of G-8 leaders like President Obama, Prime
Ministers Brown and Aso and Chancellor Merkel to take this historical step. But without
this move, it seems unreal to expect the G-20 to be able to deliver any real advance on the
global agenda. Though obviously radical, this is a necessary step forward. In the absence
of such a move, the present ‘Us and Them’ syndrome will most likely continue with more
attention being given to making new coalitions and protecting existing ones rather than
focusing on the substantive tasks at hand. The fact that BRIC countries came up with their
statement at the time of the Finance Ministers meeting in London is symptomatic of this
inherent risk in the current situation.

It would be advisable to conserve G-20’s political capital and using it to first and foremost
address the multiple and complex issues in the financial sector. And focus the remaining
political capital to preventing the rise of protectionist sentiment in any form or design.
Addressing the financial sector issues will require restoring confidence in global financial
markets; improving the regulatory systems and modalities for minimizing the collateral
damage which the smaller emerging and developing economies are forced to suffer for
virtually no fault of their own. Any extended period of financial sector distress and the
consequent economic suffering can result in rising protectionism and a sharp backlash
against globalisation. This is highly avoidable and threatens to take us back several decades
and cause unimaginable misery worldwide. Therefore, G-20 leaders could usefully focus
on getting the global financial sector back on track, get the credit flowing again and suggest
practical measures to make the next financial sector crisis less likely. Even achieving this
objective will require imagination, capacity to think boldly, acting with resolution and in
a coordinated manner and sustained follow up. At the same time G-20 leaders would do
well to examine if their commitment for none of the participants taking any protectionist
steps has been achieved. All necessary follow up must be made to ensure that members
do not renege on this commitment which will otherwise see the world get into a vicious
cycle of competitive protectionism. This two-fold and focused approach will ensure
that the two necessary conditions for the global economy to remain open and achieve
positive growth in the short term are achieved. Other objectives, however laudable, can be
attempted subsequently.

Rajiv Kumar
Director and CEO, ICRIER
The Chinese Dilemma?

China finds itself in a very unenviable situation. China’s growth has slowed down considerably, exports have fallen dramatically and unemployment rate is rising, which could lead to social unrest. The relation between China’s exchange rate policy to boost its exports, the low domestic consumption, the huge buildup in reserves which it has used to buy the US assets are all inter related. On one hand it is being accused of building huge reserves by gaining unfair trade advantage which caused the global imbalances on the other hand it is expected to fund the current bailout. On the domestic front there are huge problems due to falling exports and hence the pressure to keep its exports sector competitive. The heavy losses that China suffered on its US investments, means it needs to rethink how it uses its reserves. This article argues that China cannot solve the problem without taking a hit to its reserves because of its heavy dependence on exports to US and its large holding of US assets.

The Imbalances

The savings rate in China is one of the highest in the world and it has been increasing rapidly. In 1991 the Gross Savings as a percentage of GDP was 40 % but has increased to 53 % in 2006. This is accompanied by a low consumption rate, at less than 40 % of GDP. This means that most of what China produces it is exporting.

A low domestic consumption rate and a competitive advantage owing to its low cost labor China adopted an export led growth strategy. To support a vast population and generate employment opportunities China needed to grow rapidly and exports seemed to be a perfect driver. Exports contribute around 36 percent to China’s GDP. China has seen its exports grow at a phenomenal pace, especially to the US.

Fig: Forex Reserves and Trade Surplus*

Note:* Trade surplus with US and on the right axis. Source: US Treasury, U.S. Census Bureau and SAFE

Many believe that China’s currency is undervalued against the USD and it gives Chinese firms an unfair advantage. An under-valued Yuan means that the cost of importing Chinese goods is much lower for the US consumer as each dollar buys more Yuan. The US says that the vast trade deficit that it runs with China is a testimony of this. The trade balance has been ever widening.

1. WDI,2008
China followed a fixed exchange rate regime from 1994 to 2005. Owing to pressure from US and fearing protectionist measures, China decided to adopt a pegged exchange rate regime. What this meant was, the Chinese Central Bank will not decide the direction of Renminbi’s movement but will control the pace of movement. This was done by fixing the band in which the Renminbi could fluctuate. The RMB appreciated by around 18 percent since 2005 but has remained stagnant since July, 2008 (See Fig.) In order to maintain this peg, the PBoC built up a huge forex reserves.

After the Asian currency crisis of 1998, most developing countries started building huge reserves. China has become the largest holder of foreign exchange reserves in the world at USD 1.95 trillion at the end of 2008. The Asian crisis was a result of huge capital outflow from East Asian countries. China was relatively unscathed but it seems that it has decided to err on the safe side and started building huge reserves. A huge trade surplus against the US helped to build these reserves. In order to earn higher yield the Central bank started investing the forex reserves. The USD reserves which constitute 70 percent of the Chinese reserves are invested mainly in the US Treasury bonds (including short term bills), agency bonds (Fannie Mae, Freddie Mac, and Ginnie Mae) US corporate bonds, US equities and short term deposits.

The Current Crisis: Connecting the Dots.

The current crisis started in the US as a subprime crisis. In simple words, the households with poor credit record in the US were provided loans excessively to invest in the housing

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2. Brad Setser puts the total at USD 2.3 trillion.
3. For details see CFR working paper “China’s $ 1.7 Trillion Bet.” Brad Setser and Arpana Pandey. Fig. only shows China’s treasury holding as reported by TIC survey.
Regional Insights

market (Mortgage). The US government also ran a very high budget deficit during this period.

On one hand owing to an under valued Yuan the US consumers got access to low cost Chinese goods. This helped in keeping a low inflation and higher disposable income. On the other hand China was buying the US assets which meant that the interest rates were low in the United States. Interest rate is the cost of money so when excess capital is available (in this case Chinese buying USD based assets) the cost goes down. This meant US could have lower interest rates. This helped the capital intensive industries to borrow at a lower cost and invest more.

In the absence of regulation and with easy money availability the housing bubble grew rapidly but did burst eventually. China got caught in this situation like everyone else. It is believed that they had exposures of more than USD 400 Bn in agency bonds (Freddie Mac and Fannie Mae) which failed and had to be guaranteed by the US Govt. This means that China will no longer be very cautious in buying the US assets.

What is interesting now is that the US and China have announced the two highest fiscal stimulus packages. At a time when the US fiscal deficit is already high and the house-hold saving is low, the US needs to print more money to finance the stimulus plan. This could mean that the USD depreciates and there is erosion in value of China’s holding of US assets. Now, there has been increasing concern about relying so heavily on China as a major source for external funding. This relationship seems to be getting worse with China blaming the US for its “unsustainable model of development”.

China doesn’t have much options; it needs to keep on buying the US treasuries if it wants to protect the Yuan from appreciating, which it seems it wants to. At the same time China will not like to increase its exposure to the US assets. For this the Chinese will have to let the Yuan appreciate. So, this becomes a circular problem.

If the Chinese do decide to diversify to other currencies, they risk further loss of value as an excess of US dollar liquidity could lead to its devaluation and will create huge capital depreciation for China’s assets. It may result in other countries selling the dollar in anticipation of its devaluation. One of the reasons why USD is not faltering could be because countries are building up huge reserves to defend their currencies. If Chinese do decide to diversify, things could get worse as the US interest rates would go up hampering the recovery.

The irony is that the country which caused the crisis still has the safest asset class, the US T-bonds, available. The US government 10 year bond yield is still below 3 percent. Also, the recovery is unthinkable until both the countries work together. China is finding it hard to defend its policy at home after suffering heavy losses in US asset market.

The only way forward for it seems to be to believe that the fiscal stimulus will work and the Chinese households will consume more. If this happens China could let the Yuan appreciate gradually, which would mean a capital loss in terms of its reserves but much less reliance on the US. A much better use of reserves could be buying strategic foreign assets and improving social safety net at domestic front. These has already started happening. The current crisis is an opportunity for China to rethink its strategy!

Loknath Acharya
China Desk

India-Sri Lanka Free Trade Agreement: Trends in Bilateral Trade

Almost nine years have passed since the commencement of the India-Sri Lanka Free Trade Agreement (ISFTA), and since then economic relations between the two countries have improved significantly. This article focuses particularly on the implications of the agreement on the bilateral trade between the two countries over the period 2000 to 2007.

Background

In order to give a boost to economic linkages between the two countries, the India-Sri Lanka Free Trade Agreement (ISFTA) was signed on December 28, 1998, and became operational from March 1, 2000. The agreement was aimed at expanding bilateral trade and investment flows, by offering greater market access to each other’s exports on duty free or concessional basis. The agreement had taken into account disparities that existed in the sizes of two economies and hence provided Sri Lanka a special and differential treatment. The FTA implementation period for India was 3 years (from 2000 to 2003) whereas for Sri Lanka, the implementation period was 8 years (from 2000 to 2008).

India granted duty free concessions to 1351 tariff lines in March 2000 and to another 2799 tariff lines in March 2003. India, on completion of its liberalisation programme, had provided duty free status to 4150 import items from Sri Lanka, comprising 81 per cent of all the import items. On the other side, Sri Lanka granted duty free concessions to 342 tariff lines in March 2000 and to another 880 tariff lines in March 2003. The remaining items in the residual list of Sri Lanka were entitled for duty concessions of 70 per cent with effect from March 2006 and then up to 100 per cent from March 31, 2008. By the end of its implementation period, Sri Lanka had provided duty free status to India on 3932 items, which was 77 per cent of all items. At present 1180 tariff lines remain in Sri Lanka’s negative list such as, agriculture/livestock items, rubber products, paper products, iron and steel, machinery, and electrical items and 429 items in India’s negative list (garments, plastic products and rubber products etc). Further, India has also provided quotas on exports of tea, textiles and garments to Sri Lanka, which otherwise come under the negative list.

Trends in Bilateral Trade

Table 1 shows that Sri Lanka’s exports to India increased by almost 10 times over the period from 2000 to 2007. India accounted for 6.7 per cent of Sri Lanka’s total exports to the world in 2007 and has become Sri Lanka’s third major export destination after U.S.A. and U.K (rising from 16th position in 1999). More than 90 per cent of the total value of Sri Lanka’s exports enters India under the tariff preferences offered through the FTA. In 2007, Sri Lanka exported about US$ 450-460 million of goods to India covered by FTA whereas the non-FTA exports (comprising mainly exports under the negative list) were much lower at about US$ 30-40 million. Likewise, India’s exports to Sri Lanka have grown by 5 times; increasing India’s share in total Sri Lankan imports from 7.8 per cent in 2000 to 24.4 per cent in 2007. Since 2001 India has become the largest exporter to Sri Lanka overtaking Japan, however, most of the Indian exports to Sri Lanka (around 56 per cent) fall under the non-FTA list. The non-FTA exports from India to Sri Lanka were worth around US$ 2 billion in 2007, which include minerals fuels/oils, motor vehicles, iron and steel, machinery and mechanical appliances and pharmaceuticals. The balance of trade between India and Sri Lanka, which has always been in favour of India, has continued to widen over the years, though, Sri Lanka’s imports-to-exports ratio has declined from 10.3:1 in 2000 to 5.4:1 in 2007. Thus, ISFTA has certainly led to expansion of trade between the two countries. However, an important question which could be raised here is whether the FTA has led to emergence of new products for exports and if yes, which are these products.
Table 1: Trade between Sri Lanka and India

<table>
<thead>
<tr>
<th>Year</th>
<th>Sri Lanka’s Exports to India</th>
<th>Sri Lanka’s Imports from India</th>
<th>Total Trade</th>
<th>Trade Deficit for Sri Lanka</th>
<th>SL Im/SL Ex</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Value (Million US $)</td>
<td>Share (per cent)</td>
<td>Growth (per cent)</td>
<td>Value (Million US $)</td>
<td>Share (per cent)</td>
</tr>
<tr>
<td>2000</td>
<td>58</td>
<td>1.0</td>
<td>24.1</td>
<td>600</td>
<td>7.8</td>
</tr>
<tr>
<td>2001</td>
<td>72</td>
<td>1.4</td>
<td>0.5</td>
<td>602</td>
<td>9.7</td>
</tr>
<tr>
<td>2002</td>
<td>169</td>
<td>3.6</td>
<td>134.7</td>
<td>835</td>
<td>13.8</td>
</tr>
<tr>
<td>2003</td>
<td>241</td>
<td>4.9</td>
<td>42.6</td>
<td>1076</td>
<td>16.5</td>
</tr>
<tr>
<td>2004</td>
<td>386</td>
<td>6.9</td>
<td>60.2</td>
<td>1358</td>
<td>17.3</td>
</tr>
<tr>
<td>2005</td>
<td>559</td>
<td>9.1</td>
<td>44.8</td>
<td>1440</td>
<td>17.3</td>
</tr>
<tr>
<td>2006</td>
<td>494</td>
<td>7.2</td>
<td>-11.6</td>
<td>1822</td>
<td>18.5</td>
</tr>
<tr>
<td>2007</td>
<td>516</td>
<td>6.7</td>
<td>15.7</td>
<td>2785</td>
<td>24.4</td>
</tr>
</tbody>
</table>

Source: Department of Commerce, Sri Lanka

To analyse the impact of ISFTA on composition of bilateral exports between the two countries at 6-digit level of Harmonized System (HS) Classification over the period from 1999 to 2007, the methodology developed by Baysan et al (2006) has been used here. To begin with, India’s imports from Sri Lanka have been considered for the analysis. The products with zero imports by India from Sri Lanka in 1999 have been placed in ‘category 1’. Thereafter, all the products imported by India from Sri Lanka in 1999 have been arranged in the ascending order according to their value and divided in a manner such that each category received 10 per cent of the imports in 1999. The remaining 50 per cent of the imports in 1999 (which accounted for the bulk of trade and obviously had fewer products) have been clubbed into ‘category 7’. The share of the products in each category has been computed for the subsequent years. Likewise, India’s exports to Sri Lanka in 1999 have also been classified into 7 categories and their share has been calculated for the successive years.

Table 2 shows that the composition of exports from Sri Lanka to India has surprisingly shifted to the products which Sri Lanka didn’t export at all in 1999. The share of exports from Sri Lanka to India in ‘category 1’ has increased from zero in 1999 to 74 per cent in 2007, whereas the share of exports in ‘category 7’ has declined from 50 per cent in 1999 to 7 per cent in 2007. Sri Lankan exports to India have largely consisted of new products where Sri Lanka did not traditionally have capacities. Also, there has been a noticeable shift from primary to processed and manufacturing exports from Sri Lanka to India. Vegetable/animal fats & oils, copper & copper products, electrical machinery & equipments, became the largest export items of Sri Lanka to India in the post-FTA period replacing tea and coffee, fruits & nuts etc. which were the major export items of Sri Lanka in 1999. It has also been highlighted by Kelegama and Mukherjee (2007) that ISFTA has led Sri Lanka towards finding comparative advantage in producing a number of consumer goods which have entered the Indian market.

Table 2: Distribution of Sri Lanka Exports to India (In per cent)

<table>
<thead>
<tr>
<th>Category</th>
<th>No. of Products in 1999</th>
<th>1999</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>0</td>
<td>27.0</td>
<td>29.5</td>
<td>36.9</td>
<td>68.4</td>
<td>72.5</td>
<td>83.5</td>
<td>76.2</td>
<td>74.1</td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>221</td>
<td>9.7</td>
<td>7.4</td>
<td>10.2</td>
<td>9.0</td>
<td>7.5</td>
<td>4.2</td>
<td>7.5</td>
<td>9.6</td>
<td></td>
</tr>
<tr>
<td>3</td>
<td>20</td>
<td>7.7</td>
<td>6.8</td>
<td>6.5</td>
<td>3.3</td>
<td>2.5</td>
<td>2.0</td>
<td>3.7</td>
<td>2.8</td>
<td></td>
</tr>
<tr>
<td>4</td>
<td>9</td>
<td>6.1</td>
<td>6.0</td>
<td>4.2</td>
<td>2.2</td>
<td>1.4</td>
<td>0.9</td>
<td>3.5</td>
<td>3.5</td>
<td></td>
</tr>
<tr>
<td>5</td>
<td>3</td>
<td>7.4</td>
<td>4.1</td>
<td>7.0</td>
<td>3.4</td>
<td>2.4</td>
<td>1.5</td>
<td>1.3</td>
<td>1.2</td>
<td></td>
</tr>
<tr>
<td>6</td>
<td>3</td>
<td>7.0</td>
<td>32.0</td>
<td>15.8</td>
<td>2.8</td>
<td>5.5</td>
<td>3.4</td>
<td>2.6</td>
<td>1.9</td>
<td></td>
</tr>
<tr>
<td>7</td>
<td>5</td>
<td>34.9</td>
<td>13.8</td>
<td>19.0</td>
<td>10.9</td>
<td>8.2</td>
<td>4.3</td>
<td>5.2</td>
<td>6.9</td>
<td></td>
</tr>
</tbody>
</table>

Source: Author’s calculation based on UN Comtrade Data, WITS

Table 3: Distribution of India’s Exports to Sri Lanka (In per cent)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>0</td>
<td>3.5</td>
<td>4.2</td>
<td>5.9</td>
<td>8.4</td>
<td>5.4</td>
<td>7.4</td>
<td>7.1</td>
<td>5.8</td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>1872</td>
<td>17.7</td>
<td>27.8</td>
<td>39.0</td>
<td>42.3</td>
<td>38.9</td>
<td>45.7</td>
<td>47.4</td>
<td>56.6</td>
<td></td>
</tr>
<tr>
<td>3</td>
<td>258</td>
<td>9.8</td>
<td>8.5</td>
<td>6.5</td>
<td>6.2</td>
<td>6.7</td>
<td>6.9</td>
<td>6.2</td>
<td>5.6</td>
<td></td>
</tr>
<tr>
<td>4</td>
<td>108</td>
<td>8.9</td>
<td>8.2</td>
<td>5.6</td>
<td>5.2</td>
<td>5.6</td>
<td>4.1</td>
<td>3.6</td>
<td>2.9</td>
<td></td>
</tr>
<tr>
<td>5</td>
<td>58</td>
<td>8.9</td>
<td>8.6</td>
<td>5.9</td>
<td>6.5</td>
<td>4.3</td>
<td>5.7</td>
<td>5.8</td>
<td>5.7</td>
<td></td>
</tr>
<tr>
<td>6</td>
<td>37</td>
<td>10.6</td>
<td>8.9</td>
<td>6.0</td>
<td>4.7</td>
<td>3.9</td>
<td>2.9</td>
<td>2.4</td>
<td>1.4</td>
<td></td>
</tr>
<tr>
<td>7</td>
<td>52</td>
<td>40.6</td>
<td>33.8</td>
<td>31.1</td>
<td>26.7</td>
<td>35.2</td>
<td>27.3</td>
<td>27.6</td>
<td>22.0</td>
<td></td>
</tr>
</tbody>
</table>

Source: Author’s calculation based on UN Comtrade Data, WITS

Though the same pattern has emerged in the case of exports from India to Sri Lanka, it is less distinct. The highest increase has been in case of category 2 (having maximum number of products in 1999) with its share rising from 18 per cent in 1999 to 57 per cent in 2007, whereas the share of the last category, which represented 50 per cent of the exports from India to Sri Lanka in 1999, declined to 22 per cent in 2007. In 1999-2000, cotton, automotive, vegetables, pharmaceuticals, and machinery and appliances were the top 5 items of Indian exports constituting around 50 per cent of our total exports to Sri Lanka. However, in 2006-07 mineral fuel and iron & steel replaced vegetables and machinery in the top 5 items of Indian exports to Sri Lanka. Around 30 per cent of our exports to Sri Lanka constituted mineral fuels. There hasn’t been such a stark change in composition of exports from India to Sri Lanka, with mineral fuels, iron and steel products etc having become major export products in post-FTA period. In 2007, mineral fuels accounted for around 43 per cent of total exports from India to Sri Lanka.

One possible explanation of this shift in trade pattern as pointed out by Baysan et al (2006) is that FTA preferences at the time of negotiations generally point against the existing imported products from the partner country. Products that the partner country doesn’t export during the time of negotiations are not considered as a potential threat and hence manage to receive significant preferences. The scope of trade expansion is large mainly in this category of products and perhaps this could have happened with ISFTA as well. However, this requires a more detailed examination of the bilateral exports and preferential tariffs. At present it can be concluded that ISFTA has led to emergence of new export products for both the countries, especially Sri Lanka, besides leading to a visible expansion of trade between Sri Lanka and India.
This is a well crafted tract for the new Obama administration; not much has been left unsaid about the role of America in Asia. With the growing body of literature that grounds discussion of U.S. foreign policy in Asia, the book concentrates on providing prescription to the new government on various issues that impinge on U.S. and Asian interests. The key message of this cogently argued edited volume ‘America’s Role in Asia’ is put together by a distinguished group of Asian and American policy experts, current and former diplomats, and scholars. The Asia Foundation brings experts together to develop recommendations for U.S. policy toward Asia every four years. Drawing on a series of candid, high-level workshops on both sides of the pacific, the task force from Asia and America composed of twenty leading policymakers and scholars, evaluating current U.S. policies on Asian security, economics and trade, and war on terror, energy and environment and its changing role in the post-cold war world.

The list of recommendations includes advice to promote multilateral ties and enhancing bilateral ties in Asia, improve trade relations by seeking conclusion of Doha Round under WTO, begin dialogue on energy security and environmental crisis in Asia, maintain sound relations with China, state long-term commitment in Afghanistan, provide diplomatic help in sorting out Pakistan-Afghanistan border issues, consolidate strategic partnership with India, continue the North Korea policy followed by the former administration and increase overall public diplomacy with the Asian community.

The edited volume has sections on U.S. economic policy in Asia and U.S. foreign policy towards India for the Obama administration which deserve special mention. First, Marcus Noland takes a view that the new administration will face two challenges in Asia with respect to trade diplomacy: financial market turmoil having an impact on US and Asia and the domestic political environment that makes it difficult to formulate constructive trade policy. Moreover, he rightly says that as US will host the Asia Pacific Economic Cooperation (APEC) forum in 2011; this would force Asian regional issues onto the agenda of the new administration. Apart from this, Noland argues that failure to implement US-Korea FTA would be a terrible blow to U.S. standing in Asia and also bilateral relations with Korea. In this light, he claims that U.S. congress has never in the past failed to ratify a bilateral trade agreement. However, though the Korea-U.S. Free Trade Agreement was signed in June 2007, the Democratic-led Congress in Washington was reluctant to back the FTA due to opposition from trade unions, which feared possible job losses, a fear that has been heightened amid the worsening global economic crisis. Recently at a Senate confirmation hearing in January 2009, U.S. Secretary of State, Hillary Clinton, proposed re-negotiation of the KORUS FTA, citing an imbalance in auto trade and
restrictions on beef shipments. Although the possibility of the US congress ratifying the agreement cannot be ruled out, the view that it can be done by the end of the next 4 years appears to be optimist.

Second, Ambassador Karl Inderfurth takes on the U.S. policy on India clearly answering the two questions: Can the U.S.-Indian relationship be strengthened without assuming an anti-China character? Should a new U.S. administration seek a strategic partnership with India, and if so how? He gives the following recommendations: strengthen strategic ties, increase bilateral trade potential, broaden the nuclear dialogue, allow American universities to operate in India, support India’s bid for a permanent seat in the UN Security Council, promote collaboration in the neighbourhood to stabilize Nepal, Bangladesh, Sri Lanka and Afghanistan, defer direct involvement in India and Pakistan as the countries grapple with the best approach on how to improve bilateral relations, promote a cooperation triangle among U.S., China and India. On the last recommendation made, the current scenario in the Asian region suggests that one needs to be less optimistic about the quick realization of an equal diplomatic partnership involving India, China and the United States.

Overall, this masterful account of the policy options is only but a set of suggestions for the consideration of the Obama administration. The view of the Asian contributors will give an Asian perspective to the U.S. administration and may help provide a balance to the American views presented in the book.

Sukanya Natarajan
Brazil, Chile and Venezuela Desks


2. According to U.S. Sources, South Korea exports more than 700,000 autos to the U.S. annually while importing just 6,000. South Korea contests such statistics, saying the figures include 250,000 units made in the U.S. at an Alabama plant owned by South Korea’s largest automaker, Hyundai Motor, and exclude more than 125,000 automobiles sold in South Korea by GM Daewoo, a Korean subsidiary of U.S. automaker GM.
Data Sheet

Index of Market Capitalisation (Base December, 2007)

...
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Index of Market Capitalisation (Base December, 2007)

[Graph showing changes in market capitalisation from December 2007 to February 2009 for different countries, including India, USA, UK, Germany, Japan, Australia, Canada, Mexico, Brazil, Italy, New Zealand, India, and South Africa.]
Food Inflation Rate (in per cent)

- Sri Lanka
- Russia
- China
- Nepal
- Bangladesh
- Pakistan
- India

- India
- S.Korea
- Malaysia
- Philpines
- Thailand

- Germany
- New Zealand
- South Africa
- Japan
- Mexico
- Brazil
- USA
- UK
- India
About ICRIER

ICRIER – established in August 1981 – is an autonomous, policy-oriented, not-for-profit economic policy think tank. ICRIER’s main focus is to enhance the knowledge content of policy making by undertaking analytical research that is targeted at improving India’s interface with the global economy. We have nurtured our autonomy by establishing an endowment fund, income from which enables us pursue our priority research agenda. ICRIER’s office is located in the prime institutional complex of India Habitat Centre, New Delhi.

ICRIER’s founding Chairman was Dr. K.B. Lall who led the organization since its inception till 1992 when he handed over the Chairmanship to Mr. R.N. Malhotra (1992-1996). He was followed by Dr. I.G. Patel who remained Chairman from 1997 to 2005 until his demise in July 2005. ICRIER’s current Chairperson is Dr. Isher Judge Ahluwalia. Amongst ICRIER’s founding members are: Dr. Manmohan Singh, Dr. C. Rangarajan, Dr. M.S. Swaminathan, Dr. Jagdish Bhagwati, Dr. R. J. Chelliah, Mr. Muchkund Dubey, Prof. Deepak Nayyar etc.

To effectively disseminate the research findings, ICRIER organises workshops/seminars/conferences to bring together policy makers, academicians, Union Cabinet Ministers, Members of Parliament, senior industry representatives and media persons to try and create a more informed understanding on issues of major policy interest. ICRIER invites distinguished scholars and policy makers from around the world to deliver public lectures on economic themes of interest to contemporary India.

ICRIER’s highly qualified in-house team of about 50 researchers includes several Ph.Ds from reputed Indian and foreign universities. In addition, we have 23 External Consultants working on specific projects. The team is led by Dr. Rajiv Kumar, D.Phil in Economics from Oxford University and Ph.D from Lucknow University.
ICRIER Regional Desk Team was set up in 2008. This Team will be responsible for tracking and monitoring developments in the major countries, regions, economic blocks and India’s neighbours.

ICRIER was established in August 1981, and it has successfully completed 27 years as an autonomous, premier policy-oriented, not-for-profit research institution.