

INTRAREGIONAL TRADE WITHIN SAARC NATIONS-A REVIEW

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In recent years the South Asian region has emerged as the fastest growing region in the world. However, intraregional trade has lagged behind the region's deepening engagement in global trade with the effects of geopolitics and a legacy of mistrust leaving a mark on integration efforts. The current study focuses on SAARC economies to examine the impact of trade agreements on the basis of data for fifteen years i.e. from 2000 to 2015. The emphasis is on understanding the level of intraregional trade, issues, and challenges of the region and in conclusion, policy measures have been suggested to improve the integration of the region.

Keywords: SAFTA, Intraregional Trade, SAARC Nations, South Asia, Economic Integration

JEL classification: F15, F18

1. Introduction

The South Asian Association for Regional Cooperation (SAARC) countries are undertaking continuous efforts to reduce regulations and restrictions within the region for facilitating intraregional trade by private investment and freeing up of economies. However, the trade within the region at 5 per cent is still below the world average. SAARC countries together account for 21 per cent of the total world production, 3 per cent of the world area and 3.8 per cent of the world GDP (IMF, 2015). The SAARC region is extremely diverse in terms of size, geography, languages, culture, social and political development (Jain and Singh, 2009).

The initiative of regional cooperation was first considered by Bangladesh in year 1980. However, initially India and Pakistan were suspicious about the objective with other member nations welcoming the idea. Initially, SAARC was launched as a regional organization known as South Asian Regional Cooperation (SARC) in 1983. Later in year 1985 SARC was transformed into SAARC for trade promotion and cooperation among the member countries (Dash, 1996).

The first initiative was taken in year 1991 towards the establishment of Committee of Economic Cooperation (CEC). The committee recommended a draft agreement of South Asian Preferential Trade Agreement (SAPTA), which helped the member nations to prevent the marginalization of regional trade in global market (Lohani, 2008).

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The agreement of SAPTA was signed in 1993 and came into effect in December 1995. The establishment of SAPTA acted as a milestone for the member countries. To achieve the objectives of economic cooperation in greater form the framework agreement of SAFTA (South Asian Free Trade Agreement) was signed in year 2004. The vision was setup for 2015 to establish South Asian Custom Union (SACU) and in 2020 to drive the final stage of economic union (Bandara and Yu, 2003).

The establishment of a trading bloc however, has not improved trade in this region. Intraregional trade is still very low in comparison to other trading blocs in the world. The free trade in this region has generated limited scope; however individual countries are growing with high growth rate. This is one of the major criticisms against the success of SAFTA.

With this background, the current study presents macroeconomic overview of SAARC nations in Section 2. Empirical literature covering regional trade issues, highlighting some of their major findings is presented in Section 3. The intraregional trade trends for the period 2000-2015 are discussed in Section 4. In conclusion, the challenges and policy implications with regard to trade integration in South Asia are discussed in Section 5.

2. Macroeconomic Indicators of SAARC Economies

South Asia comprises of India, Bangladesh, Pakistan, Sri Lanka, Maldives, Bhutan and Nepal. Afghanistan, Bhutan, Nepal and Maldives are very small countries as per the economic indicators in comparison to the other four countries. According to World Bank classification, among the seven countries, four economies namely Bangladesh, Bhutan, Maldives and Nepal, are least developed countries (LDCs); and India, Pakistan Sri Lanka are considered developing countries. On the basis of income, Maldives is an upper middle-income country; Bhutan, India, Pakistan and Sri Lanka are lower-middle-income countries; and Bangladesh, Nepal are low-income countries (Winthrop et al., 2016).

Table 1: Macroeconomic Indicators of SAARC Economies (2015)

	Bangladesh	Bhutan	India	Maldives	Nepal	Pakistan	Sri Lanka
Population (millions)	158.9	0.77	1311.05	0.4	28.51	191.71	20.96
Population Growth Rate	1.2	1.68	1.2	1.8	1.35	1.92	0.09
Real GDP Growth, %	6.5	6.5	7.24	2.5	2.8	5.1	4.8
GDP per capita(PPP)	1776.89	5845.6	3627.14	8871.3	1252.14	2744.83	5581.68
Exports (billions of dollars)	25.6	0.63	455.27	2.33	1.68	21.7	13.6
Imports (billions of dollars)	35.4	0.967	551.61	2.265	6.19	40.4	22.3
CPI Inflation, Average, %	10.7	8.85	8.86	12.83	9.55	11.91	6.72

	Bangladesh	Bhutan	India	Maldives	Nepal	Pakistan	Sri Lanka
Fiscal Balance, % of GDP, FY Basis	5	4.8	5.9	10	3.8	4	6.8
Merchandise Export (billions of dollars)	32.37	0.44	267.14	0.24	0.66	22.18	10.5
Merchandise Import (billions of dollars)	39.46	0.99	391.97	2.26	6.5	44.21	18.93
Current Account Balance % of GDP	1.38	-27.81	-1.01	-9.27	11.88	-0.6	-2.64

Source: World Development Indicators, World Bank Report, 2016 and Asian Development Bank, 2016

The macro economic variables of South Asian Region, reflect that, India is the largest country in South Asian region in terms of land area, population and economy; while Pakistan and Bangladesh are the second and third largest country respectively (Table 1). Because of their size, these three economies will always have critical importance for successful regional integration and cooperation among these nations, and they will always play important role in success of these agreements. (Das, 2007, Behera, 2009).

3. Literature Review

A number of studies have been undertaken to analyse the impact of trade agreement on member countries. According to Robson (2003), the factors responsible for the formation of free trade areas (FTA's) in advanced countries are different from the regional trade areas (RTA's) between the developing countries.

According to the Mohanty (2003), the region has a potential of trade and investment. The member nations are not competing with each other in terms of exports of same products to the world. He estimated that export potential could be six times more than the present, if harvested completely.

Pattanaik (2006) argued that SAARC would remain stymied if small states will not integrate, they will only gain from the big economies like India and Pakistan, if SAARC prospers. An effective integration of SAFTA will require initiatives of all countries and their willingness to create favourable political environment in the region (Ghani and Din, 2006).

Magee (2003) emphasized on the political factors other than economic factors. He mentioned that countries those who are already involved in the bilateral trade are more likely to form RTAs and they are considered as natural trading partners.

Taneja (2004) mentioned in her study that South Asia is the least integrated region in comparison to other regions like Europe, Latin America, East Asia. On the other hand, the share of India in total regional trade has increased over the years, which shows that if India and Pakistan can tap more potential, SAARC intraregional trade would reach newer heights.

There are few studies (Jayaratne, 2004) which point out that some issues that have prevented effective regional integration of South Asian nations from more rapid development and benefit from cross border and global trade and investments are political disputes, macroeconomic instability, policy deficiencies, lack of a common position, and low implementation capability among others. Another topic currently under review is the issue on adopting a common currency in the region. For instance, Saxena (2005) examines if SAARC countries can satisfy the criterion to form an optimal currency area.

Dash (1996) argued from more or less neutral perspective that, given the low level of mutual trust, effects of ethnic and religious conflicts, and extent of bilateral disputes in South Asia, it is unrealistic to believe that any substantial growth of regional cooperation is possible without easing political tensions.

In sum, we can recapitulate that to achieve the objective of economic integration the mistrust among the member nations must be reduced, without easing political tension the objective of SAFTA cannot be achieved. Thus, the successful implementation of regional trade agreements in South Asia need committed efforts and strong political will from all the leaders to bring about peace, harmony, and social security in the region.

4. Overview of Intraregional Trade in South Asia

Between 1960 and 1970, the South Asian region was growing at a slow rate, however, in 1970's this region accumulated maximum growth in the world. During 1980-99 the regional growth was sustained at 5.4 per cent, which was further followed by average growth of 6.8 per cent during 2000-08. During the financial crisis the average GDP growth was down to 5.4 per cent, whereas in 2017 regional growth is expected to rise to 7.6 per cent (from 7.5 per cent in 2015) by maintaining strong competition and investment among the member nations. These projections are mainly based upon India's strong economic projections driven by economic reforms and investor's sentiment (Winthrop et al., 2016)

Table 2: GDP Growth Rate of SAARC Region (per cent)

Country	1960	1970	1980	1990	1995	2000	2005	2008	2012	2015
Bangladesh	6	5.65.9	0.81	5.94	4.9	5.9	5.9	6.19	6.7	5.6
Bhutan	---	---	---	10.87	7.07	6.9	7.12	4.67	5.57	6.7
India	3.7	5.15	6.7	5.53	7.6	5.5	8.4	6.7	6.8	7.5
Maldives	---	---	---	---	---	4.76	-4.6	12	5.4	2.5
Nepal	---	2.57	-2.3	4.6	3.46	6.2	3.12	5.8	3.8	5
Pakistan	5.9	11.35	10.2	4.45	4.96	4.2	9	4.1	2.9	4.6
Sri Lanka	4.2	3.8	5.8	6.4	5.5	6	6.24	5.9	8.2	6.6

Source: World Development Indicators, World Bank Report, 2016

4.1 Trade in South Asia

By observing the trend of exports among SAARC nations, we can predict that SAARC has emerged as dynamic sub-region in terms of trade. If we see the trend of exports, there have been years in which exports have reduced for SAARC nations but are consistently increasing over the years. Between 2001-2011, the value of exports in current US million dollars have increased 21 fold for India, 15 fold for Bangladesh, 11 fold for Pakistan and 8 fold for Sri Lanka. Among SAARC nations, all countries have double-digit growth of exports except Nepal and Sri Lanka in the same period (Table 3).

Table 3: Exports and Imports CAGR of SAARC Nations

Country	Exports (CAGR) in percentage			Imports (CAGR) in percentage		
	1981-1991	1991-2001	2001-2011	1981-1991	1991-2001	2001-2011
Bangladesh	7.78	12.42	14.69	2.66	9.86	14.67
Bhutan	16.58	2.72	19.70	4.03	6.59	19.97
India	7.44	10.44	21.53	4.51	10.19	22.48
Maldives	9.48	9.68	16.58	6.99	9.51	13.98
Nepal	5.55	8.22	5.04	7.50	6.10	14.21
Pakistan	8.89	2.92	11.49	5.24	0.94	14.51
Sri Lanka	6.63	9.24	7.72	5.69	7.16	11.92

Source: United Nations Conference on Trade and Development Report, 2013

4.2 Trade Openness

The objective of trade agreements between SAARC nations was to increase trade openness between member nations, however, intraregional trade within countries in this regard is insignificant. This trend is partly due to not so active participation of two major economies of the region-India and Pakistan, which are not outward-oriented. The indices of trade to GDP ratio for India and Pakistan were 54.4 and 33.3 respectively in year 2010 (Table 3). A higher index indicates a more open economy. Countries like Maldives and Sri Lanka have a higher percentage of trade to GDP ratios, however their economies are very small. Therefore, their contribution to the amount of region's trade is insignificant.

The importance of trade as growth initiator has been recognized in SAARC countries as is evident from the growing trade openness of SAARC economies over the years (Table 4). However, there are wide disparities within the SAARC region. For instance, Maldives is highly dependent on external sector with 223.9 per cent trade openness ratio while Pakistan is least open country in the SAARC region. India has a huge domestic market, hence trade

forms a substantially smaller percentage of GDP, especially when compared with East Asian economies, that are small and essentially require trade for growth. The rest of the countries are fairly open to trade.

Table 4: Trade Openness in SAARC Countries

Country	1970	1980	1990	2000	2010
Bangladesh	20.8	23.38	19.65	33.21	54.5
Bhutan	...	51.35	57.48	82.47	92.41
India	7.5	15.11	15.24	26.54	54.48
Maldives	...	358.66	168.08	161.09	223.99
Nepal	13.2	30.27	32.19	55.71	41.7
Pakistan	22.4	36.59	38.9	28.13	33.38
Sri Lanka	54.05	87.01	68.24	88.63	60.67

Source: World Development Indicators, World Bank Report, 2016

The trade to GDP ratio has gone up for Bangladesh, Bhutan, India and Maldives. However, for Sri Lanka it has been high but has come down over time. With greater global economic integration the external economic environment also affects these economies much more intimately than they were before.

4.3 Share of SAARC Region in World Exports

There has been a gradual increase in the share of SAARC region in total world exports since 1980s, but still it is lower in comparison to other regional groups. During 2015, share of SAARC region in total world trade stood at 4.5 per cent (Table 5).

Table 5: Share of SAARC Region in World Trade (per cent)

Country	1980	1985	1990	1995	2000	2005	2010	2015
Bangladesh	0.04	0.05	0.05	0.07	0.09	0.08	0.11	0.12
Bhutan	---	0.001	0.002	0.001	0.001	0.001	0.003	0.003
India	0.48	0.56	0.54	0.61	0.75	1.19	1.84	1.92
Maldives	0.002	0.003	0.004	0.005	0.005	0.003	0.01	0.15
Nepal	0.01	0.013	0.004	0.016	0.016	0.009	0.008	0.009
Pakistan	0.136	0.15	0.16	0.16	0.13	0.15	0.15	0.16
Sri Lanka	0.05	0.07	0.05	0.07	0.08	0.06	0.06	0.07
SAARC	0.72	0.85	0.81	0.92	1.08	1.6	2.18	4.5

Source: United Nations Conference on Trade and Development Report, 2015

4.4 Trend in Intraregional Group Trade

Intraregional trade in South Asia is relatively low compared with other regions, such as ASEAN, APEC, APTA, MERCOSUR, NAFTA and EU. The South Asian countries

exchange goods principally with countries outside the region. SAARC had a slow start, but gained momentum with the launch of SAPTA in the mid-1990s. Since the implementation of SAFTA at the beginning of the new millennium, it has begun to perform better. Nevertheless, intraregional trade as a ratio of South Asia's total foreign trade was still low at 7.6 per cent in 2015, compared with 21.9 per cent for ASEAN member countries and 16.4 per cent for APTA (Table 6).

Table 6: Intraregional Group Trade (per cent)

Region	1960	1970	1980	1990	2000	2010	2015
APEC	47.1	57.4	57.3	68.1	72.5	64.3	65.2
APTA	1.56	1.97	2.28	3.7	7.1	14.06	16.4
MERCOSUR	7.5	9.3	9.8	11.0	20.1	15.1	15.5
ASEAN	12.8	22.4	15.9	17.2	22.4	24.3	21.9
EU	51.8	61.8	61.9	67.4	68.2	65.3	67.4
NAFTA	30.42	36.1	33	37.2	46.8	39.2	46.4
SAARC	5.1	3.2	3.5	2.7	4.5	4.6	7.6

Source: United Nations Conference on Trade and Development Report, 2015

If we compare individual countries, the intraregional trade ratio varied from a low of 1.8 per cent for India and 3.1 per cent for Pakistan to a high of 50.4 per cent for Nepal in year 2015 (Table 7). This is primarily due to the difference in the market size as well as other non-economic factors influencing trade between SAARC economies, which is not apparent for other regional groupings. For instance, Bhutan or Nepal cannot be the major export destinations for India and Pakistan. Big SAARC countries can only have a modest amount of trade with small SAARC economies. In stark contrast, the small economies of Bhutan and Nepal have maintained strong trade links with India. For instance, Nepal and Sri Lanka import around 46 and 16 per cent of their imports from India but this covers a negligible portion of Indian exports (Jain and Singh, 2009).

Table 7: Intraregional Trade Share of South Asia's Total Trade (per cent)

Country	1985	1990	1995	2000	2005	2010	2015
Bangladesh	4.6	6.2	2.8	7.7	10.3	11.2	11.5
Bhutan	---	---	---	---	---	---	---
India	1.8	1.6	2.8	2.4	2.75	2.27	1.8
Maldives	12.4	12.8	14.2	22.1	17.3	17.1	16.5
Nepal	34.5	11.7	14.6	22.2	70.11	57.9	50.4
Pakistan	3.1	2.8	2.4	2.7	3.48	5.46	3.2
Sri Lanka	5.6	5.7	7.5	7.3	15.2	19.1	17.2

Source: International Monetary Fund Report, 2015

5. Conclusion and Recommendations

The main objective of trade agreement between SAARC nations was to increase intraregional trade between the member countries. After signing the agreement trade improved from 4.5 per cent (2000) to 7.6 per cent (2015). With such a low level of regional trade and low degree of integration among these countries, it seems impossible for SAARC countries to develop a complete free trade area. In the recent SAARC summit held in Katmandu, Nepal (2014) attended by the leaders of all countries declared their commitment for developing South Asian Economic Union in a phased and planned manner. Moreover harmonization of technical trade barriers, adopting mechanisms of poverty alleviation, developing SAARC Development Fund was also included in official declaration (Winthrop et al., 2016). To boost the results of trade agreement these declarations are not enough, there is a need to take concrete steps for implementation. For the enhancement of intraregional trade, it is recommended that policy makers of these countries need to focus on the following:

(i) Strengthening of Infrastructure Facilities: The investment in infrastructural development in SAARC region is inadequate so as to achieve high growth rates with growing economies and increasing populations. According to Harris (2008), to sustain a growth of 8 per cent in region, an investment in infrastructure amounting to 7.6 per cent of GDP is required.

The total time required for exports and imports is extremely high in this region. This is due to delays at land-border crossings. Informal channels are mainly taking over the formal trade, which further leads to corruption and complexities during the cross-border trading procedures. For example, a container shipped from Delhi to Dhaka takes 45 days to reach the destination, whereas, it is estimated that the distance of 2,000 kilometers between Delhi and Dhaka could be covered by rail in 2–3 days (Subramanian and Arnold, 2001; Taneja, 2007).

To improve intraregional trade it is essential to establish corridor-based approaches to improve the efficiency of regional transport and to reduce trade costs. In an ARTNeT study, P. De, A. R. Khan and S. Chaturvedi (2008) showed that a 10 per cent fall in transaction costs at the border have an effect of increasing a country's exports by 3 per cent.

(ii) Energy Trade among SAARC Nations: Within the South Asia region, there are continued shortages and outages occurring which contribute to GDP losses. These economies have unexploited potential for undertaking energy trade with Nepal and Bhutan having developed additional capacity leading to power surpluses, where as nations such as India, Pakistan and Bangladesh have been experiencing enormous energy deficits. In the medium to long term, future energy demand (2010-2020) in the region is expected to grow exponentially (SAARC Regional Energy Trade Study, SRET, 2010). The existing energy trade between India-Nepal

and Bhutan-India represents an example that will increase revenue and contribute to their respective country's GDP.

(iii) Non-Tariff Barriers: Non-Tariff Barriers are one of the important factors discouraging trade among the SAARC member nation countries. For example, trade possibilities between India and Pakistan are potentially very high, but Pakistan due to political reasons has decided not to extend its obligation under the agreement (Dubey, 2007). Some countries have implemented para-tariffs (various levies and taxes that do not come under the SAFTA definitions of tariffs), which have eventually counter balanced the limited tariff preferences offered under the SAFTA (Taneja et al., 2011).

(iv) Cross Border Transport: SAARC nations have the advantage of common land borders. For example, India and Pakistan share the same boundary but movement of goods between these countries is only possible through air/ocean route despite having land border crossings. Because of this reason trade between India and Pakistan takes place via Singapore or Dubai, which is inefficient giving rise to informal channels. While both countries having adopted negative lists of trade, they maintain a positive list for trade through land border, which is inconsistent with the GATT principles.

For example, Pakistan maintains a positive list of 137 items, most of which belong to commodity groups like vegetables, cotton iron and steel, this clearly suggests that movement of goods should be done through air/ocean route despite having land border crossings between the two countries. (De, Raihan and Ghani, 2013)

(v) Vertical and Horizontal Investment Through Foreign Direct Investment (FDI): With respect to investment through FDI in South Asian region, the most common type of investment is horizontal FDI, however, there is a shift in the domestic-oriented manufacturing to services and construction.

According to Athukorala (2013) because of technological development in the region, investment is also taking place in vertical FDI. The most prominent case is the textile and garment sector in which Sri Lanka is emerging as the hub of technology and managerial talents. All member countries are now taking steps for value-addition in their export products to increase their competitive advantage in global markets.

(vi) Global Production Networks: There is need to create production networks within the region to facilitate trade between the member nations. The division of labour is apparent between the clothing exporters and textile exporters in South Asia. India and Pakistan are the major fabric and yarn producers, while Bangladesh and Sri Lanka are primarily textile users and clothing exporters (Tewari, 2008). Under SAFTA, the cost effectiveness of a country could be improved and exports may become more competitive globally if the identified

product of imports from a country's sensitive list is removed and tariffs are reduced (UNCTAD 2010).

(vii) *Phasing Out of Negative Lists*: The economies of SAARC nations are mainly dependent on agriculture for exports and employment. These nations have listed many commodities under negative list, which is affecting their trade in the region. Perhaps of more concern is that there is no formal and binding provision in the framework agreement requiring that negative lists are pruned down over time.

The only provision that the SAFTA treaty made is for a review of the negative list at every four years with a view to reducing the number of items (SAFTA 2004, Article 7). However, in the long run it will hamper their growth as they have comparative advantage for their products.

(viii) *Harmonization and Simplification of Trade Procedures*: The documentation procedure required during the transit of products between the SAARC nations constitutes a major portion of trade cost. There is a need to simplify the procedure for quicker clearance.

Steps have been undertaken to simplify and harmonize trade procedures, but South Asia still requires the most number of documents for cross border trade (Taylor and Wilson, 2009). For example, in case of India-Bangladesh trade, a consignment needs at least 22 documentations, more than 55 signatures and a minimum of 116 copies for final approval (Gilbert and Banik, 2010).

These policy recommendations can help promote intraregional trade in SAARC region, which in turn would boost growth. Promotion of intraregional trade would also offset political costs, which have hindered progress towards more economic integration in the region.

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