Is Bangladesh A Beneficiary of South Asian Free Trade Area (SAFTA)?

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Abstract

South Asian Association of Regional Cooperation (SAARC) was primarily concerned with peace thus success in enhancing intraregional trade was minimally displayed. Therefore formation of a South Asian Free Trade Area (SAFTA) was proposed with an aim of extending intraregional trade that came into force in 2006. SAFTA in terms of population is the largest of any economic bloc but has appeared as a least integrated bloc while taking trade among members into account, which is only 6.2% of total trade. To increase trade the list of commodities under sensitive categories has been revised in 2012. Taking an interpretivist approach this study reports that Bangladesh will be one of the significant beneficiaries of SAFTA as it will help reduce the longstanding trade deficit with India, create a large regional market and support its key industries such as; Readymade Garments (RMG) and pharmaceuticals to enhance competitiveness. Optimizing the benefits, however, may not be accomplished if nontariff barriers such as; mind-set, political tensions and bilateral conflicting issues are not dealt with extreme care beside tariff barriers.

Keywords: Free Trade Area, regional integration, SAARC, SAFTA.

1. Introduction

Bangladesh, the main initiator of SAARC, has a land area of 56,977 square miles, with a population of 152.51 billion. The gender distribution of the country is quite balanced with 76.35 per cent of the population female and 76.16 per cent male. Bangladesh has a labour force of 50.37 million who are above the age of 15 years. Of this labour force 50.1 million (30.85 male and 10.25 female) are employed in different sectors e.g. 47.33 per cent in agriculture, 24.3 per cent in industrial and 14.2 per cent in services and 14.68 per cent in other sectors. In addition another 1 million diasporas have made a significant contribution to the GDP. The country received a remittance of US$ 11,650.32 million from diasporas working in different countries worldwide in 2011.

In terms of density Bangladesh is one of the most densely populated countries in the world. By the end of 2011 the population density was recorded as 1015 per square kilometre. A country with a small surface land but a huge population puts extreme pressure on policy makers in terms of employment creation and meeting growth challenges. Realizing that fact the government of the country adopted an export-led growth strategy in 1980. Following that the government took a series of policy reformations in line with the growth target. As a consequence, after three decades some key industries such as readymade garments (RMG), pharmaceuticals, shipbuilding, ceramics, leather goods, consumer electronics, frozen foods, jute goods and light engineering have accomplished appreciable success with a competitive position in the global arena.

Despite political instability and a weak institutional setting the country has been successful in keeping up economic growth along with the human development indicators. According to the human development report 2013, Bangladesh is one of the few most successful countries and has ranked 146 among 187 countries in improving its position one step over the previous year. Rapid growth led by available cheap labour, a favourable exchange rate, supportive government policies and institutional configuration have made it one of the next eleven emerging countries as coined by Jim O'Neill of Goldman and Sachs. JP Morgan, considering trade and investment prospects, has ranked Bangladesh as one of the 'Frontier Five' emerging economies.

Bangladesh has been successful in managing unanticipated challenges that have stemmed from the global financial recession. In the recession period export growth has witnessed a significant increase. The growth rate between 2010 and 2012 witnessed year on year an increasing trend of 4.2 per cent, 41.7 per cent and 14.5 per cent. The growth rate of GDP in 2012 was 6.32 per cent (6.71 per cent in the previous year). The size of the GDP by the end of 2012 reached US$112 billion and per capita GDP at the same time was recorded as US$848 (US$755 in 2011) (Bangladesh Economic Review, 2012).

Since the 1980s the service sector has contributed substantially to the GDP which in 2011 was recorded as 49.72 per cent, for the industrial sector 30.33 per cent and for the agricultural sector 19.95 per cent. Despite the persistent enhancement of competitiveness of the industrial sector over the last two decades, because of technological backwardness and a

Table 1: Major export and import partners of Bangladesh

Country	Percentage of exports
USA	24.4
Germany	13.5
UK	9.3
France	6.3
Netherlands	6.3
Italy	3.8
China	17.7
India	15
Singapore	7.3
Japan	4.9
Malaysia	4.9
Australia	2.6
Taiwan	2.5
USA	2.2
Germany	2.2

Source: Developed by the authors compiling the data from DCCI archive

heavy dependence on low value export items, a widening gap is observed in the balance of trade. By the end of 2012 total imports were valued at US$ 35.44 billion against US$ 24.287 billion for exports. This created a huge trade deficit (DCCI, 2011). Table 1 shows that the USA and the European Union are major destinations for exports from Bangladesh as 63.6 per cent go to the EU markets and 24.4 per cent of total exports go to the USA. While imports are highly concentrated to the Asian partners as 54.9 per cent of total imports are with several Asian countries. China, India and Singapore are the dominant partners occupying a 40 per cent share of total import.

1.1. Objectives of the study

There are more than three hundred regional economic blocs in several regions of the world. SAARC among them is the least integrated economic bloc in terms of intraregional trade that represents less than 2 per cent of GDP, which is more than 20 per cent in East Asia (World Bank, 2008). According to the World Trade Organization, intraregional trade in 2005 was 51.2 per cent of which only 6.2 per cent was among SAARC member states. Despite modest concessions under SAPTA a lack of political will of member countries has been reflected in the minimal intraregional trade.

Before the formation of ASEAN, intraregional bilateral trade was minimal (7%) but it profoundly rose (to 50%) after the formation of the free trade area. In NAFTA it was 12 per cent before grouping and after integration increased to 51 per cent by 2008. In the early 1980s intraregional trade among member states of the European Union was recorded as

Table 2: Intraregional trade in some selected economic blocs

Regional blocs	Intraregional trade flows
ASEAN	50%
EU	74%
NAFTA	51%
SAFTA	6.2%

Source: Adapted from Sumanasiri & Ahsan, 2009

23 per cent and by 2008 reached to 74 per cent (Table 2). The EU in terms of intraregional trade (74%) is the most successful integration while SAFTA has appeared as the least integrated bloc (6.2%). More than 94 per cent of trade is directed to outside member countries. In 1985 before the formation of SAARC intraregional trade was 5 per cent but after more than two decades since its formation trade among members still did not reach a level of even 10 per cent by 2012. Therefore this study has dealt with two objectives; first, to identify factors inhibiting intraregional trade, and second, to explore the impact of phase-II revision of the list of sensitive products categories, which has been effective since January 2012, for Bangladesh as a member country.

1.2. Justification of the study

A report published by the World Bank on integration in South Asia and its implication into the global economy has projected that the South Asian region would experience the fastest export growth (World Bank, 2008). It indicates that there is an immense growth potential for SAFTA member countries. In addition the list of commodities under the sensitive category has been revised recently. Thus it has become important to explore major impediments and relative benefits of the revision in order to update the policy makers so that they are able to rationalize advantages by enhancing competitiveness as much as possible. Therefore the central focus of the current study is to explore to what extent SAFTA could be beneficial for Bangladesh.

2. Methodology

The purpose of doing research is either to create knowledge or to extend existing knowledge which is directly influenced by the philosophy adopted by the researcher. Johnson & Clark (2006) mentioned that researchers in social science ought to be aware of their commitment regarding the choice of research strategy, since it has a profound impact on doing research and the researcher's own judgement in the investigation. Thus the primary influence of research philosophy is likely to be the researcher's own view about the relationship between knowledge and the process by which it has been developed. Researchers who are concerned with facts (e.g. resources requirements i.e. *objectives*) are likely to have a very different view on the way research should be conducted from researchers who are concerned with attitudes and feelings *(subjective)* of human construct.

The objective of research philosophies discussion is not simply to inform the audience but to provide better reflection upon the philosophical choice of the researcher and defend them from alternatives that could have been adopted. The suitability of research philosophy, however, depends upon the research questions to be answered. But it is unlikely that a particular problem or research questions will always fall into only one philosophical domain. Because the way of thinking among researchers largely differs, research philosophies categorization is led into *positivism* and *interpretivism* (Saunders, Lewis & Thornhill, 2009).

Selecting a research method is not as important as to determine a research paradigm. Because the research paradigm not only guides the research method rather guides the way of investigation of a particular research problem in ontologically and epistemologically fundamental ways (Guba & Lincoln, 1994). Thus the choice of research design is dependent on how much we already know about the problem and research objectives (Burns & Bush, 2009: 116).

Most studies to investigate regional integration have taken a *positivistic* philosophical perspective. Hossain (2009) using a gravity model investigates the export potentials of Bangladesh and confirms that Bangladesh has a huge export potential in the SAFTA region. Saxena (2005) investigates the effect of common currency adoption in SAFTA, the welfare effect (Kumar & Saini, 2007), the effect of policies on poverty and income distribution (Gilbert, 2008), and welfare implications of tariff liberalization (Raihan, 2012).

The current study, however, has adopted an *interpretivist* approach as the purpose of the study is to provide a critical perspective on major impediments and the relative competitiveness of a member country. That, due to limitations of the philosophy, the *positivist* orthodoxy to a large extent fails to grasp. Moreover, the reduction of lists of sensitive categories has been effective recently. Thus, it is too early to adopt a *positivist* approach to the quest as it confines the scope of a study within predetermined variables deemed pertinent to the point of interest of the researcher (Yin, 2009).

Consequently, painting a comprehensive inference throughout the interpretation, taking the context and time into account, is prevented. That limits an alternative perspective of the phenomenon (Tashakkori & Teddlie, 1998). The current study has adopted a content analysis method in line with the philosophical approach, which was determined based on the research question in mind, so that a wider foray of compare and contrast is possible in order to accomplish more critical interpretation. A triangulation of observation, archival and published sources has been adopted for obtaining the data used in the study.

The effect of regional economic integration can be measured in several ways (e.g. employment effect, trade effect, investment effect, welfare effect etc.) that are broadly categorized into two; trade impact and investment impact. This study, however, will be more focusing on assessing trade impact of SAFTA on Bangladesh. The remainder of the paper has been structured as follows; the next section critically reviews relevant literature of economic integration with an aim to show the distinction between notions and positioning the study. The following section highlights the chronological development of SAFTA and explores major impediments in order to shed light on the prospect of this nascent bloc. The fifth section, in line with the ultimate objective of the study, focuses on implications of SAFTA for Bangladesh as a member country. The sixth section offers conclusions highlighting policy implications, limitations and a direction for future research.

3. Theoretical underpinnings of economic integration

The theoretical underpinning of regional integration is basically derived from Jacob Viner's concept of Custom's Union Issue (1950) that focuses on the welfare effect of integration. Viner critiqued it through the lens of 'trade creation' and 'trade diversion'. According to him, if trade among participating countries is promoted without any disruption of trade with non-member countries, it results in efficiency-enhancing or trade creation. But, diversion arises while trade among member states increases at the cost of trade with non-member countries.

3.1. Ambiguity of concepts and terms of integration

The most fundamental definition of Balassa (1961) mentions integration as a 'voluntary process' of economic interdependence of member states that manifests depending on the kind of integration. The concept of 'region' often leads to confusion in understanding economic integration, as it can be viewed from three levels; sub-national, supranational and international. Integration from the sub-national level means that it is to be carried out among various sectors within the geographical territory of a country if a balanced growth is expected. But it concerns us while taking an international perspective, due to the involvement of several countries with numerous international characters, new concerns and complexities are introduced. Therefore integration at an international level calls for understanding of the last two levels to understand the concept of region. While it further constitutes a source of ambiguity as economic integration can either be insertion in the global economy or appropriation of a group of geographically proximate countries. The fundamental difference between these two is that the former is universal and the latter is discriminatory (Koné, 2012).

To describe elimination of economic frontiers progressively among member states different terms are used, such as: regional economic integration, regional economic cooperation, regionalism, regional economic area, and regional trade agreements. These terms have been used interchangeably to refer to economic integration. Despite subtle differences among them from a semantic perspective, most studies do not tend to distinguish. But this is important in order to remove confusion and to understand who plays the central role to exercise power and authority. For instance, proximity is the central concern of regional integration or cooperation but is only an option in the case of economic integration. Proximity does not refer to mere geographical closeness but rather to cultural, historical, linguistic and even political similarities.

The integration and cooperation constructs indicate reversibility and irreversibility. Thus implementation of the former calls for supranational institutions, while the implementation of the latter depends on the intergovernmental initiatives. As such, without economic, political and institutional harmonization effectiveness of economic integration is quite doubtful. The term political integration and economic integration sometimes become confusing because of their proximity to the domain. But they differ from each other at least in terms of framework, objectives and mechanisms.

Economic integration seeks to liberalize trade by reduction, and even the elimination of the tariff and nontariff barriers through dialogue in order to improve the overall efficiency and economic development of the partners. While political integration seeks to manage the power, giving the exclusive rights of a nation to a broader political entity. However, economic integration may not be accomplished without political integration if the performance is taken into consideration, and that can be the absolute form of integration (Koné, 2012).

3.2. Forms of integration

Considering operational norms of the economies, integration can be broadly classified into two categories, such as market based and plan based. Market based integration is found in countries with market economies – for instance in Asia, Africa, Western Europe and in the North and the South of America. Plan based types on the other hand are existent in centrally planned economies such as the Council for Mutual Economic Assistance (COMECON). However, the burgeoning literature on regional integration suggests that removal of trade barriers and formation of common regional markets stimulate intraregional trade among member states (Krugman & Obstfeld, 2002 & Rose, 2000). Removing trade barriers, economic integration, depending on the kind of integration, allows the free flow of goods, services, labour, capital and technology among member countries. The classical school of thought, Balassa (1961), based on the degree of economic relations, suggests five typologies regarding forms of integration. These include the Free Trade Area, the Customs Union, the Common Market, the Economic Union and the Economic and Monetary Union.

According to Balassa, initially countries can integrate economically, and later through a series of trial and error processes they can move towards more complex integration levels until arriving at political integration. In line with this argument, a Free Trade Area (FTA) is the first step that refers to the removal of custom's rights and quantitative restrictions among members on a mutual understanding. Each country, however, maintains its own tariff policy to trade with non-member countries. As such there is an incremental debate that an FTA can play a discriminatory role favouring members over non-members that may result in trade diversion.

The controversy over discrimination can be stopped by transforming it to the Customs Union. Here members not only reach a consensus to remove trade barriers on mutual exchange but adopt a common external tariff and common trade policies towards non-members. The Common Market refers to the free flow of goods and services among members under common trade policies and external tariff policies to the non-members as well as approve free movement of production factors (e.g. labour, capital). The Economic Union adopts all characteristics of a Common Market and adopts harmonized social and macroeconomic policies including monetary and budgetary policies. Finally, the Economic and Monetary Union refers to the adoption of a single currency by all partners putting emphasis on implementation of common monetary and financial policies (Koné, 2012).

3.3. Pros and Cons of a Free Trade Area

Alhorr, Boal & Cowden (2012) pointed out that international trade theories argue for tariff and non-tariff barriers to protect infant industries and jobs in the domestic market. That eventually may prevent competition and raise commodity prices for the end consumers. In line with this argument there is a proposition that a free trade agreement can play a discriminatory role for non-member countries that may restrict a positive sum game of trade. In addition the free flow of industrial goods among participating countries can be restricted (Cardoso & Ferreira, 2000). Lee & Shin (2006), however, report that a free trade agreement might enhance trade opportunities (trade creation) between member and non-member countries from 6 per cent to 15 per cent. Frankel (1997), taking a transaction cost perspective has emphasised ‘natural trade partners’, that includes countries that are geographically proximate, already trade substantially and have minimum cultural differences would be benefited from a free trade agreement.

A World Bank study also confirms that a free trade agreement does not significantly reduce trade between member and non-member countries (Pardo, Freund & Ornelas, 2009). Clausing (2001) studying the Canada-United States free trade agreement (CUSTA) also found that enhancement of efficiency was the usual norm of FTA. Chang & Winter (2002) studying MERCOSUR, however, found that integration hurts non-member countries though it is not an FTA but a customs union. Thus, there is always a passage for the positive welfare effect of an FTA mode of integration (ADB, 2002 & World Bank, 2005).

Molle (1991) pointed out that regional integration itself cannot be an objective but it serves and stimulates higher objectives. For instance, in a free trade area inter-relationship is exercised especially to rationalize the export performance of member countries. That calls to some extent for sacrifice of an individual country’s autonomy in economic policy-making that is aimed at discrimination. So, both costs and benefits are associated with regional integration. But possible sources of economic gain are a primary motivation for integration. El-Agraa (1989) pointed out that integration may explore the potential benefits of: specialization based on comparative advantages; larger market size creating a passage of economies of scale; increased competition forcing the attainment of economic efficiency that enhances the international bargaining strength of the member states. Moreover, benefits of integration also include savings in foreign exchange and transport costs. But participating countries often desire to increase their performance of economic activities while they are reluctant to sacrifice the autonomy of economic policy making.

Benefits of integration substantially depend on the tariff policies to the non-member states vis-a-vis members. Unilateral initiatives of tariff reduction on imports from non-participating countries will encourage more trade with non-member countries than members. And, tariff reduction through bilateral negotiation between member countries will stimulate trade in these two countries at the cost of other member countries. Studies (e.g. Ornelas, 2005a & 2005b) taking political motives into account point out that the contract-lock feature of integration will significantly reduce political lobbying for tariffs in import competing sectors that would make the sectors weaker.

Panagariya & Findlay (1996), however, pointed out that in a free trade area, members lobbying for greater external tariffs will raise protection against outsiders. In addition, if government welfare costs increase due to tariff revenue loss by the integration, that would motivate the reduction of external tariffs to recapture tariff revenue and economic efficiency (Freund, 2000 & Bond Raymond & Constantinos, 2004). Geenhuizen & Ratti (2001) pointed out that differences in culture, language, institutional divergence, level of technological development and religiosity might create greater psychic distance among members. A long list of non-preferential commodities, a lack of product diversity, equidistance of geographical location, political hegemony and mind-set may result in the integration being apparently dysfunctional.

4. SAFTA- past and present

Regional integration in the South Asia started relatively late compared with the other regions in the world. In December 1985, regional integration started first on the initiative of seven member countries: Bangladesh, India, Pakistan, Nepal, Bhutan, the Maldives, Myanmar and Sri Lanka through the formation of the South Asian Association of Regional Cooperation (SAARC). Later, in 2007, Afghanistan joined SAARC as the eighth member country.

The SAARC charter was signed with the aim of extending economic, social and cultural cooperation in order to accomplish peace and harmony. But the charter did not clearly purview provision for economic and trade cooperation. As such, in 1993 the South Asian Preferential Trade Agreement (SAPTA) was initiated by the founding members of SAARC to promote trade in the region, and that came into effect in 1995. SAPTA was formed with the aim of promoting trade in the region by reducing tariff and non-tariff barriers through negotiation. In addition it was decided that the three non-LDCs such as India, Pakistan and Sri Lanka would provide more favourable treatment for LDCs like; Bangladesh, Bhutan, the Maldives and Nepal.

Akanda (2011) pointed out that despite four rounds of dialogue on trade liberalization under SAPTA, trade in the region was increased minimally (Jayaraman & Choong, 2012). In the decade between 1995 and 2005, intraregional trade under SAPTA rose from 4.1 per cent to 5.0 per cent. Several issues, such as political animosity, distrust, a limited number of commodities for trade, stringent rules of origin and non-cooperation among member states were responsible for such a modest reflection of intraregional trade (Jhamb 2006; Panagaria, 2003 & Ali & Talukder 2010).

Four LDCs, namely Bangladesh, Bhutan,

the Maldives and Nepal had a big trade deficit with India. That resulted in strong criticism of India as the dominant economy in the bloc. There was a lack of adequate willingness to rationalize the full potentials of SAPTA. To respond to the critics, India, at the ninth summit held in 2002, proposed to form the South Asian Economic Community (SAEC) by 2020. In line with that it was also decided to usher in a customs union by 2015. The proposed transition created an avenue for the South Asian Free Trade (SAFTA) agreement that was signed in 2004 and came into operation in January, 2006. In terms of population, SAFTA with 1.4 billion, which is more than 23 per cent of the total world population, is the largest of any economic bloc in the world. While the combined GDP of the 8 member countries is only 3 per cent of the world total GDP. India is the largest economy in the bloc, alone accounting for 80 per cent of the total GDP, 65 per cent of the exports and 67 per cent of the imports of SAFTA (Perera, 2009). A projection has been made that Bangladesh would be the supreme beneficiary of tariff concessions in the LDC category under SAFTA. Nepal and Bhutan have enjoyed duty free access to the Indian market for a long time and the Maldives trade is negligible, at least from India's perspective (World Bank, 2006).

SAFTA started with a mission to encourage intraregional trade by eliminating tariffs that impeded the free flow of goods between member countries in the region to zero per cent in different phases. A consensus was reached that Pakistan and India would reduce tariffs to zero per cent by 2012, Sri Lanka by 2013, and Bangladesh, Nepal, Bhutan, and the Maldives by 2015. Initially, all member states agreed to reduce tariffs to a maximum 5 per cent level under a ten year roadmap of a trade liberalization programme. Following that, by 2011 tariff rates on basic goods had been reduced from 6.1 per cent to 4 per cent; from 25 per cent to 9.5 per cent on intermediate goods and from 25 per cent to 18.3 per cent on finished products (Akanda, 2011). Moreover, the most sensitive issue is the number of commodities on the sensitive list that has been substantially reduced in 2012. And the special treatment for LDCs has been extended under SAFTA which started while SAPTA embarked on.

The foremost objective for formulating SAFTA was to enhance the trade opportunities of member countries in transport, engineering, technical products and information technology. The second objective was to initiate liberalization programmes in order to boost economic and foreign trade in the region. The third objective was to remove tariff and non-tariff barriers in order to ensure the free flow of goods and services. The fourth and final objective was to eliminate trade through illegal channels between India and other member states.

In line with these objectives, SAFTA has accomplished considerable success within a short span of time. But there is still a long way to go to establish it as a truly successful economic bloc. The following Table 3 shows that exports under SAFTA have witnessed considerable growth since trade liberalization programmes were adopted in 2006. Bangladesh, India and Pakistan have a substantial export share within the SAFTA region while the share of the Maldives and Sri Lanka was negligible.

Table 3: Export among SAFTA member countries (million US$)

Country	Bangladesh	India	Maldives	Pakistan	Sri Lanka	Total
2006	NA	NA	0.014	0.055	NA	0.069
2007	15.27	3.78	0	0.58	0.019	19.649
2008	98.32	8.98	0	31.8	0.041	139.141
2009	199.79	315.26	0	43.51	0.61	559.17
2010	236.71	276.93	0	56.12	0.52	570.28
2011	NA	NA	NA	NA	0.075	0.075
Total	550.09	604.95	0.014	132.06	1.26	1.29

Note: NA indicates that data is not available, data of Bhutan and Nepal is not available.
Source: SAARC Secretariat

It indicates that Bangladesh has room for putting more fruit into the export basket in the future. According to the projection of the SAARC secretariat, trade among SAFTA member countries by the end of 2011 reached around US$ 1.3 billion, which is still far away from its potential. That calls for identification of possible impediments in order to provide a deeper insight by the policy makers so that boosting of intraregional trade can be accomplished.

Chandra & Kumar (2008) have identified five critical issues that are responsible for poor intraregional trade in the SAARC region. First, the initiatives of trade liberalization by member states under SAFTA are not satisfactory compared to that under the WTO framework. Second, SAFTA entered into force in 2006 but LDCs were approved for concession up to 2015, thus preventing it from being fully operational until 2016. Third, trade of services has been completely excluded from SAFTA. Fourth, less strong initiatives regarding removal of nontariff barriers have been exhibited. And finally, stringent rules of origin, continuation of a long list of sensitive categories of products along with a limited number of commodities for tariff concession, have appeared as major impediments.

5. Implications of SAFTA for Bangladesh

The export volume of Bangladesh with SAFTA member countries is expected to increase in future as all countries have reduced numbers of commodities in the sensitive categories (Table 4, Appendix). But trade with India will be extremely beneficial as the number of restricted category products has been reduced considerably over previous lists. And trade relationship with India and Pakistan is highly significant for several reasons, such as, Bangladesh has a recurring negative balance of trade with both countries. They are major sources of imports, and it is also their geographical proximity and cultural similarity that make them significant. Intraregional trade for Bangladesh is 15 per cent of its total trade, of which exports accounts for 95 per cent and imports 75 per cent, coming mainly from India and Pakistan in the SAFTA region. As a consequence a perennial trade deficit has been exhibited between Bangladesh and these two countries.

In this case SAFTA can play a significant role to reduce the trade gap, particularly with India. In 2011 Bangladesh was capable of reducing the gap down to 9 times which was 20 times in 2001 (Table 5, Appendix). Moreover, a survey reveals that trade via informal channels in Bangladesh with India is approximately equal to that of formal channels. That causes government revenue loss, security problems and raises political as well as social tension between the two nations (World Bank, 2006). To eliminate these problems through dialogue SAFTA can be an ideal platform.

According to Bhagwati & Panagariya (2006), the effect of bilateral trade on member states cannot always be assessed by the result of the balance of trade only. In line with the logic of a natural trading partner each country will form blocs with its neighbour (Frankel, Stein & Wei, 1995 & Frankel, 1997). As such, reducing the number of sensitive categories SAFTA has created a wider foray for the trade of a range of commodities among members. Thus a negative balance of trade might not be as harmful as estimated by several empirical studies. Because Bangladesh could import more raw materials, inputs, chemicals, accessories, machineries and technologies to support its key industries (Table 6, Appendix). If those are imported from distant sources that could be more costly, at least transportation costs and time are saved. This would enhance competitiveness of the country both in trading inside and outside the bloc.

The Economy Watch reports that trade across the borders of South Asian countries is only 5 per cent, which is very insignificant. India, Pakistan, Sri Lanka and Bangladesh are major players in the bloc. Interestingly all these four member countries are highly dependent on the EU market for the majority of their exporting, which is eventually making them competitors of each other abroad. That will create tremendous pressure on Bangladesh in the EU markets.

Despite this pressure Bangladesh would become more competitive in the EU markets at least for two reasons. First, under the revision of the sensitive list, which has been effective since 2012, India has approved the duty and quota free import of cotton, yarn, chemicals, machinery and accessories of garments and textiles. Second, in the wake of industrialization and the rapid economic development, these countries' labour costs have been increasing quickly wherein Bangladesh is still more competitive in the region. As readymade garments are the major export items of Bangladesh to the EU markets that would make it still more competitive. Because of low labour costs (on average a worker in Bangladesh earns $40 whereas in India that is $200), the duty free import of raw materials and accessories, and shorter movement times would certainly enhance its costs competitiveness. But at the same time, in order to put more fruits into the export basket, Bangladesh has to improve product quality, variety, novelty and diversity of product lines with more sophisticated products. Otherwise in the long run keeping up competitiveness will be challenging.

SAFTA has created a wider market space in the region for Bangladeshi products as all major trading partners have excluded almost 15-95% from the previous sensitive categories (Table 4, Appendix). In addition, India since 2011 has approved duty and quota free access to all items except tobacco and alcohol to SAARC LDCs including Bangladesh (BGMEA, 2013). The case of readymade garments will justify this argument. In 2001, just before the withdrawal of import licensing from textiles and garments, the Indian government imposed specific duties on garment commodities in order to protect domestic firms from low cost imports from LDCs. As such, RMG despite being a key export item for Bangladesh due to a high protection level (65.5%), market penetration was difficult as until 2003-04 total export was recorded as only $4.57 million (World Bank, 2006).

But the situation kept changing after the formation of SAFTA in 2006 following the reduction of the lists of sensitive categories and announcement of duty free and quota free access of 46 textile items in 2011. Under the preferential treatment Bangladeshi readymade garments (RMG), over time have become competitive with Indian domestic manufacturers. RMG exports in India reached $563.9 million in 2012-13 which represents a 123 per cent increase over the 2003-04 fiscal year. In addition, the former president of Bangladesh Garments Manufacturers and Exporters Association (BGMEA) has noted that due to cost competitiveness Bangladesh is creating a growing interest among Indian investors. Indian firms have already invested around $80 million in 35 garment factories in Bangladesh. That has unleashed an opportunity for Bangladesh to explore the third largest export destination for its garment commodities following the EU and the USA. As India has a total US$ 30 billion market for RMG of which US$ 450 million is in the middle class market wherein Bangladesh has core competency.

In addition to the RMG, pharmaceutical is another rising sector of the country which would be tremendously benefitted from SAFTA. Bangladesh as an LDC country enjoys a special treatment until 2015 on generic medicines under the agreement of trade-related aspects of intellectual property rights (TRIPS) of WTO. As India has improved much in the pharmaceuticals thus, the duty free import of chemicals and machineries from India can immensely help achieve the adequate competitive strengths essentially required for open market competition after 2015. The establishment of a reciprocal trade therefore would not hurt the counterpart (India) as long as Bangladesh will continue to import raw materials, inputs, machineries and accessories. Access to proximate sources of raw materials would increase productivity, improve lead time management capability by reducing raw materials and product movement time and result in a decline in production costs through economies of scale. And low transportation costs, cultural similarities along with preferential treatment would help raise competitiveness (El-Agraa, 1989).

Apart from that, Bangladesh can be the supreme beneficiary of SAFTA from spillover effects. Studies have indicated that when a major economy coexists beside smaller countries, spillover effects of the major economy's growth on the smaller economies is often high. Bhutan, the Maldives and Nepal are the nearest competitors of Bangladesh but have capacity constraints in terms of population, infrastructure and level of economic development. The next big force is Sri Lanka but it will not severely affect Bangladesh as it is fairly advanced in terms of level of education, infrastructure and economic progress. Thus Sri Lanka will capture more sophisticated parts of the value chain that to some extent will relieve the agony. Ding & Masha's (2012) study looks into how India's growth affects the growth of its immediate neighbors. The study concludes that the spillover effects of India's growth to other SAARC countries were positive, but at a low level. The findings of the study can be traced by the recent incremental trend of Indian companies' interest in investment in apparel, footwear, power plants, steel, coal, construction, and the automobile assembling sectors of Bangladesh.

Kojima (2000) explained the spillover effect by adopting the 'flying-geese-model' that further justifies that trade and investment led-growth can be rationalized by integration. It assumes that in the wake of industrialization low value adding upstream activities such as; manufacturing and assembling are likely to shift from advanced countries to less advanced countries. Now the question rises whether that would create a win-win situation for both partners engaged in trade. The Flying-geese type of development describes that both will be benefitted from the trade. Because advanced nations can leverage less advanced countries comparative advantages of low labour costs, that will stimulate the industrialization of the less advanced countries and consequently, create a market for the machinery and technologies of the more advanced countries.

Chandra & Kumar (2008) have pointed out that Least Developed Countries (LDCs) have the possibility of losing customs revenue by the progress of SAFTA. Recognizing the importance of the issue SAFTA keeps a provision of special treatment for LDCs in that they will be compensated by their developing countries' counterpart. So that LDCs can withstand the shock of tariff loss which otherwise may inspire them to trade more with non-members instead of members. Because of the export led growth strategy, constraints of land surface area, a huge population, the shortage of raw materials, machinery, technologies and capital items, imports are dominant over exports in the economy of Bangladesh. This has created a trade deficit with all member states of SAFTA except Sri Lanka. Therefore, being an import driven economy Bangladesh under the compensation scheme has managed the loss of tariffs.

Let's take a look at problems both at the regional and the country level that may diminish all potentials if adequate care is absent. SAFTA has created a platform to reduce tariff barriers through dialogue. Now the success of this nascent bloc is largely depending on to what extent members are willing to remove nontariff barriers. India being the dominant player should take the lead in making SAFTA an effective economic bloc. Both the Bangladeshi and Indian sides have pro and anti Indian sentiments and vice versa. Apart from that, Bangladesh has longstanding unsettled issues like; distribution of water, border conflicts, and the hydroelectric project on the river Borak. At the same time India accuses Bangladesh for instigating terrorism in its so called Seven Sisters in the North Eastern part.

The anti Indian groups in Bangladesh and the anti Bangladeshi groups in India keep a centrifugal pressure on their respective governments as part of their political game so that bilateral issues are not resolved. For instance, with the pressure of leftist political parties in West Bengal, problems with distribution of water of the Ganges and Tista rivers are not resolved. In the same way the anti Indian group in Bangladesh does not want India use the Chittagong seaport and its land for transhipment trade with the Seven Sisters. Moreover, Bangladesh has a problem with the Rohinga issue with Myanmar. On the other hand Pakistan is in conflict with India over the Kashmir issue. Political tension exists between India and Nepal with Maoist issues and between India and Sri Lanka with Tamil issues. If initiatives are not taken both at the country level and as a group to resolve these problems then SAFTA may fail to accomplish its full potential.

Most of the member countries have reached a bilateral trade agreement beyond the SAFTA. For instance, between Pakistan and Afghanistan and India and Sri Lanka there are bilateral agreements. And Nepal and Bhutan have a bilateral free trade agreement with India that gives duty-free access of products to the Indian market. With these agreements countries could be more interested to trade more with bilateral trade partners than with the other member countries of SAFTA. That may increase the possibility of trade diversion for Bangladesh.

Turning from the regional level to the country level, Bangladesh has an acute crisis of power, weak infrastructure and communication systems, inefficient port management, a bureaucratic mind-set in the public administration that increases the cost of doing business, business start up time and reduces competitiveness. These problems are hardly possible to solve with private level initiatives. Thus the government has to set policies keeping the long term benefits in mind of increasing electricity production, and improving the communication systems by furnishing all modes of transportation as well as enhancing bandwidth capacity to facilitate online communication. Further, there is a need to improve port management efficiency and above all the quality of service standards must be improved in all departments concerned so that the entire process can work faster.

Around 90 per cent of organizations are of small and medium size that lack sufficient capital and have limited access to external sources (e.g. banks and other financial institutions). As a consequence they cannot allocate sufficient budget for promotion and market research in order to explore market opportunities and threats. So the government has to promote Bangladeshi products both at the government to government (G2G) level and at the business to business (B2B) level by organizing and participating trade fairs.

Most companies are doing well because of their strong entrepreneurial dynamism but in many instances lack adequate formal education and training. Therefore businesses run on a trial and error process that results in the dying out of hundreds of prospective ventures at birth or in the growth stages. To overcome this problem, initiatives to establish a link among government-organizations-universities can be an ideal approach wherein government will take charge of developing infrastructure, and organizations in collaboration with the government and development partners will provide funding to the universities for research. The research output will remit back to the organizations for decision-making. That will ensure more informed decision-making and reduce the chance of die out and buy out.

6. Concluding comments

The study was taken with a broad research question in mind "Is Bangladesh a beneficiary of SAFTA". Empirical evidence suggest that the country can benefit from SAFTA as the bloc is gradually moving towards accomplishing the core objectives such as trade enhancement through liberalization, removal of tariff and non-tariff barriers through dialogue and elimination of trade via informal channels. The chance of being benefitted has increased for two reasons. First, most countries have reduced the number of items in the phase-II revision. Secondly, India as the major trade partner in the bloc has a long time trade deficit with Bangladesh, has significantly reduced the number of items from sensitive categories. Thus it will on the one hand creating a large regional market helping to minimize the trade gap and on the other contribute to enhance competitiveness of the domestic firms. However, beside the reduction of tariff barriers deliberate initiatives from both sides would be essentially required in order to leverage the benefits. Bureaucratic hurdles, the mind-set of the people and several bilateral conflicting issues should be immediately settled by concurrent initiatives at both the regional and the country level.

Apart from at the country level, Bangladesh needs profound improvement to mitigate electricity crises, management inefficiency, weak communication systems, financial constraints, institutional non-coordination, political instability and infrastructural problems. Industrial zones are nearby major metropolitan cities and that creates extreme pressure on the city life of migrant workers. This is making traffic congestion acute and killing a large portion of working hours and reducing productivity. In addition price inflation creates extra pressure on the cost of living that calls for the raising of wages and leads production costs higher. Thus the recent project of relocation of industries by establishing industrial parks in the countryside is expected to improve the situation.

6.1. Limitations of the study

This study, instead of taking industry specific evidence to assess gains, has broadly looked into the overall benefits that Bangladesh as a member country can leverage. Thus inferences drawn here might not be appropriate for many industries while viewing the same issue through a micro lens. Therefore adequate care must be taken in order for generalization of the findings and interpretation.

6.2. Future research direction

This study has taken the issue from the macro perspective but future research can be done to investigate the impact of SAFTA on industry specific issues. Future research can be done also to measure the impact of SAFTA from an investment perspective.

APPENDIX

Table 4: List of sensitive products

Member country	Number of products in the earlier sensitive lists	Number of products in the revised sensitive lists (Phase-II), effective from 1 January 2012
Afghanistan	1072	850 (22% reduction)
Bangladesh	1233 (LDCs) 1241 (NLDCs)	987 (LDCs) 20% reduction 993 (NLDCs) 20% reduction
Bhutan	150	150
India	480 (LDCs) 868 (NLDCs)	25 (LDCs) 95% reduction [695 (NLDCs)] 20% reduction
Maldives	681	152 (78% reduction)
Nepal	1257 (LDCs) 1295 (NLDCs)	998 (LDCs) 22% reduction 1036 (NLDCs) 20% reduction
Pakistan	1169	936 (20% reduction)
Sri Lanka	1042	[845 (LDCs)] 19% reduction 906 (NLDCs) 15% reduction

Source: SAARC secretariat

Table 5: Bilateral trade of Bangladesh with SAFTA member countries (value in million US$)

Country	2001-2002	2002-2003	2003-2004	2004-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2010-2011	Trade Scenario
Bhutan	1.57	1.57	2.93	4.65	1.52	1.40	1.35	0.61	2.24	3.12	Export
	3.52	2.74	3.35	8.50	11.68	9.98	13.73	12.12	11.98	18.58	Import
	1:2.50	**1:1.74**	**1:1.14**	**1:1.84**	**1:7.68**	**1:7.39**	**1:10.18**	**1:19.87**	**1:5.35**	**1:5.95**	**Trade Ratio**
India	50.28	84.08	89.27	144.19	241.96	289.43	358.08	274.26	304.62	512.51	Export
	1019.47	1352.64	1602.27	2042.06	1864.74	2268.11	3383.94	2863.19	3202.8	4560	Import
	1:20	**1:16**	**1:18**	**1:14**	**1:8**	**1:8**	**1:9**	**1:10**	**1:10.5**	**1:8.9**	**Trade Ratio**
Maldives	-------	-------	-------	0.48	0.02	0.27	0.08	0.14	0.74	0.93	Export
		-------	-------	0	0	0	0	0	0.86	1.44	Import
	---------	---------	---------	**0**	**0**	**0**	**0**	**0**	**1:1.16**	**1:1.55**	**Trade Ratio**
Nepal	2.92	3.29	2.55	4.74	4.55	0.848	6.70	8.78	8.78	10.84	Export
	3.34	5.54	4.12	1.71	2.69	5.96	52.95	68.73	43.14	48.46	Import
	1:1.14	**1:1.68**	**1:1.61**	**1:0.36**	**1:0.59**	**1:7.02**	**1:7.90**	**1:7.82**	**1:4.91**	**1:4.47**	**Trade Ratio**
Pakistan	28.60	31.51	45.11	64.09	57.74	61.06	71.01	76.21	77.67	86.79	Export
	67.32	92.08	112.62	139.46	149.87	188.00	238.97	280.37	323.7	669.3	Import
	1:2.35	**1:2.92**	**1:2.49**	**1:2.21**	**1:2.60**	**1:3.08**	**1:3.36**	**1:3.67**	**1:4.16**	**1:7.71**	**Trade Ratio**
Sri Lanka	2.07	3.76	10.35	11.11	13.25	14.82	19.32	18.67	23.74	34.73	Export
	6.10	7.98	9.82	10.29	10.86	16.37	15.26	18.57	22.76	27.57	Import
	1:2.94	**1:2.12**	**1:0.94**	**1:0.93**	**1:0.82**	**1:1.10**	**1:0.78**	**1:0.99**	**1:0.95**	**1:0.79**	**Trade Ratio**

Source: Developed by the author based on data compiled from Dhaka Chamber of Commerce

Table 6: Five major trading partners of SAFTA member countries (percentage of total export and import)

Partner→ Reporter↓		Rank-1	Rank-2	Rank-3	Rank-4	Rank-5
Bangladesh	Exports	European Union (51.2)	United States(25.7)	India (4.0)	Canada (3.5)	China (1.7)
	Imports	China (15.6)	India (13.2)	European Union (9.79)	Kuwait (7.2)	Indonesia (5.1)
India	Exports	European Union (20.5)	UAE(14.4)	United States (10.8)	China (5.9)	Hong Kong (4.0)
	Imports	European Union (14.4)	China (11.5)	UAE (7.4)	United States (6.0)	Saudi Arabia (5.4)
Pakistan	Exports	European Union (24.6)	United States (18.3)	UAE (8.8)	Afghanistan (7.8)	China (5.7)
	Imports	European Union (16.1)	China (12.0)	Saudi Arabia (11.1)	UAE (10.6)	Kuwait (5.7)
Sri Lanka	Exports	European Union (36.9)	United States (23.1)	India (5.1)	UAE (3.1)	Russian Federation (2.7)
	Imports	India (20.7)	European Union (12.8)	Singapore (11.7)	Iran (8.8)	China (8.1)
Nepal	Exports	India (63.5)	European Union (11.1)	United States (7.1)	Bangladesh (6.9)	China (2.7)
	Imports	India (56.8)	China (11.2)	European Union(5.4)	Saudi Arabia (3.0)	Indonesia (2.9)
Bhutan	Exports	....	....	....	....	....
	Imports	....	....	....	....	....
Maldives	Exports	Thailand (49.0)	European Union (31.0)	Sri Lanka (9.5)	Japan (2.9)	Iran (2.9)
	Imports	Singapore (21.3)	UAE (18.0)	European Union (11.5)	India (10.4)	Malaysia (7.7)
Myanmar	Exports	....	....	....	....	....
	Imports	Singapore(22.9)	Japan (13.5)	Korea (12.5)	Malaysia (12.7)	China (10.7)

Note: Bhutan's trade data are not available in the database. Export data of Myanmar are not found in the database.

Source: World Trade Report (October, 2010)

Table 7: Major export and import items from SAFTA member countries

Country	Export items	Import items
Bhutan	Knitwear, Melamine, Woven Garments, Biscuits, Jute Manufacture, Footwear.	Live animals, Vegetables Products, Mineral Products, Prepared food stuffs,, beverages, Plastic and articles thereof, Boilers Machinery and mechanical appliances.
India	Chemical fertilizer, Pharmaceutical products and other chemical products, Raw jute, Frozen Food, Agri-products, Jute goods, Woven garments and Knitwear.	All types of cotton, cotton yarn/thread and cotton fabrics, Cereals, Mineral fuels, mineral oils and products of their distillation, bituminous substances and mineral waxes, Boilers, machinery and mechanical appliances, parts thereof, Vehicles other than railway or tramway-rolling stock and parts and accessories thereof, Iron and Steel, Residues and waste from the food industries, prepared animal fodder, Edible vegetables and certain roots and tubers, Plastic and rubber, Man-made staple fibres, Organic Chemicals, Electrical machinery and equipment, Aluminium and article thereof, Paper & paper board.
Maldives	---	--
Nepal	Pharmaceutical Products, Fertilizer, Textile and Textile article, Electrical machinery and equipment	Edible Vegetable and certain roots and tubers, Residues and waste from food industries.
Pakistan	Raw jute, Tea, Chemical Products, Agree-products, Jute goods.	Cotton, Cereals, Sugar and sugar confectionery, Manmade filament, Manmade staple fibres, Special woven, Knitted or crocheted fabrics, Machinery and mechanical appliances, Chemical products.
Sri Lanka	Chemical products, Jute goods, Agri-products, Knitwear, Woven garments.	Chemicals Products, Plastic and plastic products, Rubber and rubber products, Cotton, Man-made filament, Transport equipment, electric and machinery equipment.

Note: data of the Maldives was not accessible
Source: Extracted from the database of Dhaka Chambers of Commerce Industries

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