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Mapping and Analysis of South Asian Agricultural Trade Liberalization Effort

By

Parakrama Samaratunga*

Manoj Thibbotuwawa*

*Parakrama Samaratunga and *Manoj Thibbotuwawa are Research Fellow and Research Officer, Institute of Policy Studies (IPS), Sri Lanka, respectively. The views presented in this paper are those of the authors and do not necessarily reflect the views of IPS, ARTNeT members, partners and the United Nations. This study was conducted as part of the Asia-Pacific Research and Training Network on Trade (ARTNeT) initiative, aimed at building regional trade policy and facilitation research capacity in developing countries. This work was carried out with the aid of a grant from the International Development Research Centre (IDRC), Ottawa, Canada. The technical support of the United Nations Economic and Social Commission for Asia and the Pacific is gratefully acknowledged. Any remaining errors are the responsibility of the author. The authors may be contacted at parakrama@ips.lk and manoj@ips.lk

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Introduction

The South Asian Economies comprising Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan, and Sri Lanka (SAEs) represent 22 percent of world's population but they only account for just over 1 percent of world's trade. In 2003, agricultural trade in the SAEs amounted to US\$ 22 billion and it accounted for approximately 4 percent of world's agricultural trade and 23 percent of the regional trade. During the 1970s, SAEs had highly protected trade regimes supported by high tariffs, Non-Tariff Barriers (NTBs) and stringent controls on exchange. The rationale for protective policies was safeguarding domestic industries, improving the terms of trade, raising revenue, altering the income distribution and raising nutritional levels. During 1980s, the hitherto inward looking policies of SAEs took a marked shift towards outward looking policies. Economic policies were aimed at export-led industrialization as a means of achieving rapid economic growth. Moreover, SAEs by then had obtained memberships of various international organizations and various reforms were carried out to meet international obligations. The exchange rate regimes of many SAEs changed from fixed to managed float or free float and the restrictions on current account and capital accounts were substantially reduced. The trade policy changes emphasized on fewer trade restrictions and brought down tariff levels to a large extent especially in the case of Sri Lanka and in others, to some extent. During the late 1970s in Sri Lanka and in the late 1990s in other SAEs, the tariff structures were made simple and the number of tariff bands was reduced. The changes of the SAE's tariff structures and exchange rate regimes and relaxation of payment restrictions during the 1990s show that SAEs have moved towards greater openness in their trade.

All the SAEs, except Bhutan, are members of the WTO and under this multilateral trade agreement SAEs bound agricultural tariffs at considerably higher rates. During the first ten years (1995-2004) since the establishment of the WTO, the involvement of SAEs in regional trading arrangements has rapidly expanded (Table 1). The SAEs established the South Asian Association of Regional Cooperation (SAARC) in 1985. In 1993, the SAARC set up a regional cooperation in trade and initiated South Asian Preferential Trade Agreement (SAPTA). The SAEs envisage greater economic cooperation within member-countries by establishing a free trade area (SAFTA) by the year 2010, custom union by 2015 and economic union by 2020. The SAEs have also formed bilateral free-trade agreements; India-Sri Lanka, India-Nepal and Pakistan-Sri Lanka. Regional economic cooperation was fostered further with inter-regional agreements; Asia-Pacific Trade Agreement (APTA), Bay of Bengal Initiative for Multi-Sectorial Technical and economic Cooperation (BIMSTEC), India-Thailand, India-ASEAN, Indian Ocean Rim Association for Regional Co-operation (IORA-RC) among others.

Table 1: Preferential trading arrangements of South Asian countries

RTA= regional trade agreement; BTA= bilateral trade agreement

| Country | RTA | BTA (FTA / EPA) ¹ | Framework agreement ² | Proposed ³ |
|------------|---|---|---|--|
| Bangladesh | APTA (1976) SAPTA (1995) BIMSTEC (1997) | | Bangladesh-India (2006) Bangladesh-Morocco (2005) US-Bangladesh (2005) Sri Lanka-Bangladesh | Bangladesh-Nepal Bangladesh-Pakistan Bangladesh-Iran Bangladesh-Egypt |
| Bhutan | SAPTA (1995) BIMSTEC (1997) | India-Bhutan (2006) | | |
| India | APTA (1976) SAPTA (1995) BIMSTEC (1997) | India-Sri Lanka (2001) India-Mercosur PTA (2005) India-Nepal (1991) | ASEAN-India (2004) India-Afghanistan (2003) India-Bangladesh (2006) India-Singapore (2005) India-SACU (2004) India-Chile (2006) India-GCC (2006) India-Thailand (2004) | India-Malaysia India-Republic of Korea India-China India-Egypt |
| Nepal | BIMSTEC (1997) SAPTA (1995) | India-Nepal (1991) | | Bangladesh-Nepal |
| Pakistan | ECO(1985) and ECOTA (2003) SAPTA (1995) | Pakistan - Sri Lanka (2005) | China-Pakistan (April 2005) Sri Lanka – Pakistan (2005) | Bangladesh-Pakistan Pakistan-Malaysia Pakistan-GCC Pakistan-Afghanistan |
| Sri Lanka | APTA (1976) SAPTA (1995) BIMSTEC (1997) | Iran-Sri Lanka (25/11/04) Sri Lanka – Pakistan (2005) | Singapore-Sri Lanka US–Sri Lanka TIFA (2002) Sri Lanka - Egypt Sri Lanka - Bangladesh | Sri Lanka-Singapore |

Source: APTIAD 2007

The SAEs, similar to other developing countries, had been taxing agricultural activities directly through tax polices and indirectly through economy-wide policies. The higher indirect distortions on agriculture were the result of over-valued exchange rates and the protection provided to the manufacturing sector (Kruger *et al.* 1988). Despite the changes in economic policies in 1980s and early 1990s protectionist policies did not change sufficiently and relatively higher tariff rates remained on agricultural commodities. Since

¹ It is difficult to classify BTAs precisely as distinction between an free trade agreement (FTA), economic partnership agreement (EPA) and framework agreement (FA) is often blurred and is often only distinguished by the name of the agreement itself.

² Years refer to when agreements were signed; not all of them are being implemented.

³ Includes a documented unilateral perspective.

agriculture sector is a very sensitive sector for SAEs, the changes in economic policies and the structures of the economies have not changed the socio-economic importance of it. The institutional developments related to trade in the South Asian region have paved way to some liberalization of agricultural trade.

This chapter maps the agricultural trade liberalization effort of the SAEs and it consists of four sections. The second section presents the nature of agricultural trade in the SAEs. The third section presents the agricultural policy changes and employs various approaches to measure the levels of agricultural trade liberalization. The fourth section presents institutional development that has led to agricultural trade liberalization of SAEs and the final section presents conclusions, based on the findings of the previous sections.

I. Agricultural Trade in South Asia

The structural changes during 1980s and 1990s placed non-agricultural sectors of the SAEs in the driving seat of economic growth. Nevertheless, the SAEs have achieved a considerable growth in agriculture during the past few decades as well. Though the shares of agriculture in national outputs have been declining, agriculture and agricultural trade still play a very important role in the SAEs (Table 2). The agriculture contributes to about 26 per cent of regional GDP (21 per cent in Maldives to 41 per cent in Nepal). Rural populations on average account for more than two thirds of regional population (64 per cent in Pakistan to 93 per cent in Bhutan). Nearly three quarters of the labour force in the region is involved in agriculture and the prevalence of poverty in the rural sector is very high. The percentage of population below poverty line ranges from 25 per cent (Sri Lanka) to 45 per cent (Nepal).

Table 2: Agriculture and South Asian Economies

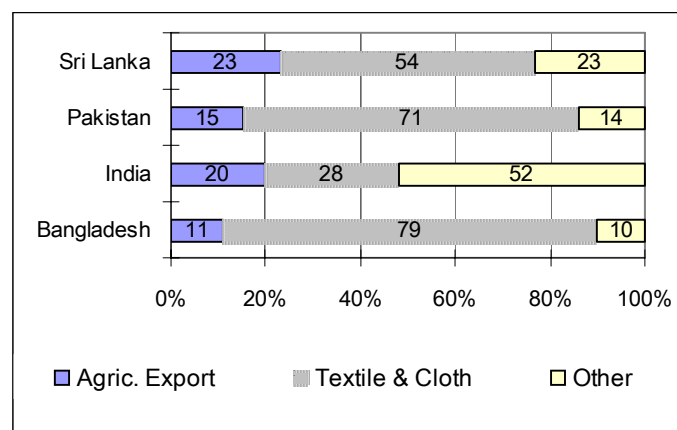
| | Bangladesh | India | Pakistan | Sri Lanka | Nepal | Maldives | Bhutan |
|--------------------------------------|-------------------|--------------|-----------------|------------------|--------------|-----------------|---------------|
| Population (million) | 128 | 998 | 135 | 19 | 22.9 | 0.3 | 0.8 |
| Population density (per sq. km) | 981 | 336 | 175 | 294 | 164 | 956 | 48 |
| Rural population (%) | 77 | 72 | 64 | 77 | 89 | 75 | 93 |
| Agriculture labor force (% of total) | 58 | 60 | 54 | 45 | 95 | 03 | 94 |
| GDP (US\$ billion) | 46 | 4477 | 58 | 16 | 5.0 | 0.3 | 0.4 |
| GDP per capita (US \$) | 362 | 450 | 508 | 814 | 220 | 1220 | 490 |
| Agriculture share of GDP (%) | 25 | 28 | 27 | 21 | 38 | 16 | 18 |

Note: Data represent 2004-05 for Bangladesh and India, 2002-03 for Pakistan, 2003-04 for Sri Lanka and Nepal. Source: World Bank (2004).

The SAEs have reported a favorable economic growth during past few decades, but, these developments seem to have a lesser effect on their rural sector. Rural poverty and income inequality have increased in Bangladesh and Sri Lanka (World Bank, 2004). This may be partly due to the decline in importance of agricultural sector in SAEs due to their non-agricultural sectors being placed in the driving seat of economic growth. This decline of

importance of agriculture has resulted in greater inequality and poverty since a larger share of population is living in rural areas and is involved mainly in agricultural activities for their livelihood. This becomes further evident when changes in the share of merchandize exports are considered. Bangladesh, Pakistan and Sri Lanka depend more on a narrow base of manufactured exports, textile and clothes and some other manufactured exports (Figure 1).

Figure 1. Share of Merchandize Exports (%) 1995-1999



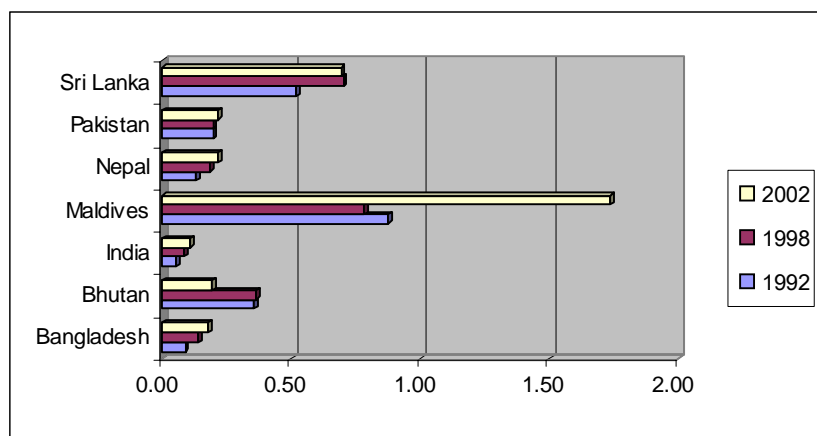
Source: Anderson (2002)

In order to obtain desirable benefits from liberal trade, the SAEs have given more emphasis to achieve macroeconomic stability. In addition to tariff protection, exchange rate policies and monetary and fiscal policies are employed to obtain direct and indirect protection for importables and exportables. During late 1990s, appreciation of real exchange rates was observed in Sri Lanka and Bangladesh and it has eroded the price incentives that generated through exchange rate depreciation (Karunagoda *et al.*, 2003; World Bank, 2004). Consequently, these SAEs have taken certain protective measures, such as increase of para-tariffs, to avoid undesirable impacts of economy wide effects.

The Agricultural Tradability Index (ATI), the ratio of total agricultural imports and exports to agricultural GDP, measures the changes in the economy with respect to agricultural trade. It also indicates how vulnerable a country is to liberalization of agricultural trade (Valdes and McCalla, 1999). All SAEs, except Bhutan, show increased shares of agricultural trade in their economies. The ATI also indicates that Maldives and Sri Lanka are more open to agricultural trade while India is the least open country in the South Asia (Figure 2).

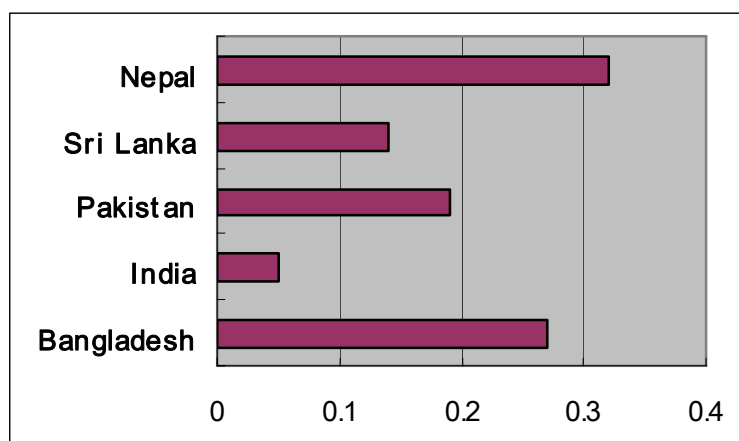
The Food Import Capacity (FIC), the ratio of the value of food imports to that of total non-food exports, measures the capacity of a country to finance food imports by non-food exports (Figure 3.) (Wilson 2002). A low ratio indicates relative low food imports (India) or relatively higher non-food sector exports (Sri Lanka). The net agricultural export index is positive for net exporters and it is negative for net importers. Among SAEs, only India and Sri Lanka are net agricultural exporters while others are net agricultural importers (Figure 4). The changes in net agricultural export index show that Bangladesh and Pakistan have moved from net exporter to net importer status while India has moved from net importer to net exporter status over time.

Figure 2. Agricultural Tradability Index (ATI) 1992, 1998 and 2002



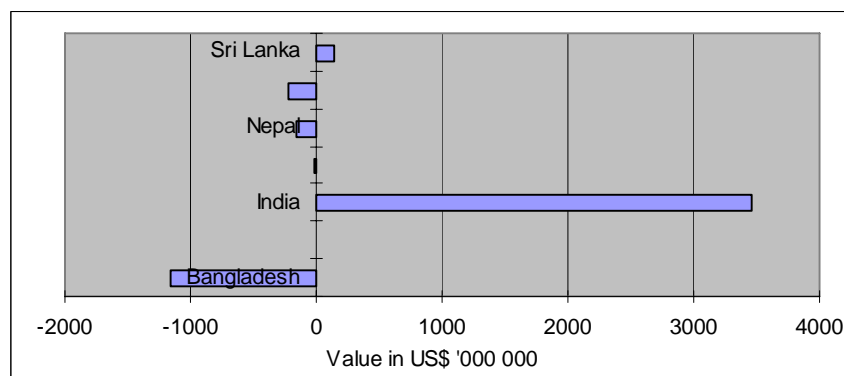
Note: $ATI = (Agriculture\ Imports + Agriculture\ Exports) / Agriculture\ GDP$.
Source : authors calculations

Figure 3. Food Import Capacity Index (FICI)



Note: $FICI = Value\ of\ food\ imports / Value\ of\ total\ non-food\ exports$.
Source: Wilson 2002

Figure 4. Agricultural Net Export Index (ANEI) (2002)



Note: $ANEI = Agriculture\ Exports - Agriculture\ Imports$ (Bhutan = -3)
Source: authors calculations

A. Export specialization in agricultural products

Trade theory suggests that trade between countries is basically driven by the comparative advantages and differences in technology, economies of scale or tastes and in some circumstances by strategic trade policies. Prospects for trade expansion are likely to be poor for countries that share a comparative advantage in similar products. The comparative advantage for SAEs is estimated for the agricultural commodities/commodity groups using an index of Revealed Comparative Advantage⁴ (RCA) (Balassa, 1965) (Table 3). The concept of RCA is based on the assumption that the pattern of commodity trade reflects relative costs and differences in non-price factors. The index of RCA for a product is defined as the ratio of the share of a country's exports to its share in world exports. A RCA value greater than one indicates export specialization in that commodity or commodity group. The RCA for some product categories show that SAEs have wide differences in export specialization and thus, there is a potential for promotion of intra-regional trade. However, similarity of export specialization observed in some product categories may pose a major constraint on agricultural trade development in the region. India has RCA in a wide variety of agricultural goods and it indicates the presence of higher potential for India to benefit under more liberal trade environment. Agricultural products of Bangladesh show RCA in limited product categories but higher protection levels of Bangladesh limit the potential for trade expansion. India and Pakistan show RCA in cereals and sugar but both these commodity groups are in the sensitive list of Sri Lanka.

Table 3: Export Indices of Revealed Comparative Advantage (RCA): Agricultural Products

| Product | Bangladesh | | | | India | | | | Maldives | | | |
|---------------------------------|------------|------|------|------|-------|------|------|------|----------|------|------|------|
| | 1995 | 1998 | 2001 | 2004 | 1995 | 1998 | 2001 | 2004 | 1995 | 1998 | 2001 | 2004 |
| Live animals | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Meat | 0 | 0 | 0 | 0 | 1 | 1 | 1 | 1 | 0 | 0 | 0 | 0 |
| Fish and Crustaceans | 10 | 7 | 8 | 12 | 3 | 0 | 4 | 3 | 78 | 87 | 74 | 74 |
| Dairy products | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Coffee, Tea, Cocoa, Spices | 2 | 1 | 1 | 1 | 5 | 6 | 5 | 3 | 0 | 0 | 0 | 0 |
| Cut flowers and foliages | 0 | 0 | 0 | 1 | 1 | 1 | 1 | 1 | 0 | 0 | 0 | 0 |
| Vegetables and fruits | 0 | 0 | 0 | 0 | 2 | 2 | 2 | 2 | 0 | 0 | 0 | 0 |
| Cereals and cereal preparations | 0 | 0 | 0 | 0 | 4 | 4 | 3 | 0 | 0 | 0 | 0 | 0 |
| Oil seeds | 0 | 0 | 0 | 0 | 2 | 1 | 2 | 2 | 0 | 0 | 0 | 0 |
| Tobacco & tobacco | 0 | 0 | 0 | 0 | 1 | 1 | 1 | 1 | 0 | 0 | 0 | 0 |

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