

## BIMSTEC Regional Integration: Prospects and Challenges<sup>1</sup>

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**Abstract.** The purpose of this paper is to explore the trade and investment potential under the ambit of regional cooperation comprising the seven contiguous countries of Bangladesh, India, Sri Lanka, Nepal, Bhutan, Thailand and Myanmar (BIMSTEC). The study addressed the latest update of BIMSTEC economic cooperation and then explored the economic impact of the regional integration. The potential economic impact of the BIMSTEC economic cooperation as well as BIMSTEC FTA could promote the growth for the region. One of the major findings of the paper is that a large part of BIMSTEC's trade has remained unrealized and the trade transaction cost is one of the major trading barriers prohibiting the growth of BIMSTEC intra-regional trade. The study reinforces that improvement in infrastructure and connectivity that leads to less trade transportation costs should be a necessary step in order to realize BIMSTEC's trade and investment potential. The paper concludes that liberalization of non-policy barriers will spur BIMSTEC's trade and economic cooperation.

**Keywords:** BIMSTEC, SAARC, Regional Integration, Trade, Economic Cooperation, GTAP Model.

### 1 Introduction

The Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC) is a supranational Free Trade Agreement (FTA) that started its journey through the Bangkok Declaration in 1997. The objective of regional integration is to accelerate growth through mutual cooperation in different areas of common interests by utilizing regional resources and geographical advantages. Unlike many other regional groupings, BIMSTEC is a sector-driven cooperative organization. Starting with six sectors—including trade, technology, energy, transport, tourism and fisheries—for sectoral cooperation in the late 1997, it expanded to embrace nine more

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sectors—including agriculture, public health, poverty alleviation, counter-terrorism, environment, culture, people to people contact and climate change [1].

In view of the above, the main research question in this paper is to explore the trade and investment potential under the ambit of regional cooperation of BIMSTEC. Rest part of the paper is organized as follows. Section 2 addresses the latest achievement of BIMSTEC economic cooperation. Section 3 explores the potential economic impact of the regional integration. Section 4 provides the major challenges of the BIMSTEC integration and finally conclusion and policy recommendation are briefed at the end.

## **2 Latest Achievement of BIMSTEC Negotiations**

As per agreed upon measures, the chairmanship of BIMSTEC rotates between the member countries. As of now, Nepal is chairing the organization since 2015 [2]. The BIMSTEC Trade Negotiating Committee (TNC) has held 20 sessions of negotiations. The negotiations are spread over the areas of (i) tariff concessions on trade in goods, (ii) customs cooperation, (iii) services and (iv) investments (v) Dispute Settlement Mechanism. There are four draft Agreements on Trade in Goods, Rules of Origin, Dispute settlement and Customs Matters have been agreed in different BIMSTEC TNC meetings and now waiting for sign the final agreements.

### **2.1 Tariff Reduction or Elimination under BIMSTEC**

The two avenues in which BIMSTEC countries shall reduce and/or eliminate its tariffs on originating goods of the other Party are fast track and normal track. The tariffs on the goods covered under the fast track as well as normal track shall be eliminated in equal annual installments with reference to their respective applied MFN tariff rates as of 1<sup>st</sup> August 2007 as the base rate.

### **2.2 Safeguard Measures**

According to the safeguard measures in place, BIMSTEC member nations are allowed to withdraw tariff concession for protectionism purposes, in case imports from free trade access from the FTA members cause significant harm to the domestic industries.

### **2.3 Rules of Origin**

Free trade agreements emphasize largely on Rules of Origin, and BIMSTEC is no different. The rules of origin for BIMSTEC are fairly modest. By 18<sup>th</sup> TNC meeting, held in June 2009, domestic value addition, regional cumulation, and product specific rules have been agreed upon between the member nations [6]. The product specific rules have been agreed upon for 147 products at HS 6 digit level.

### **3 Prospects for Economic Integration**

#### **3.1 Trade Scenario among BIMSTEC**

The member countries together had a staggering total export value of US\$ 606.6 billion, and an import value of US\$ 685.3 billion in 2014[7]. It is interesting to note that except for Thailand, all the other six member countries have a higher volume of imports than the export volume.

At the same time the intraregional trade was only US\$37 billion in 2014. However, the intraregional trade is significantly lower compared to many regional blocks. In 2014 intraregional trade among BIMSTEC countries was 2.86 % as against 7 % among the SAARC countries, 7.5 % among APTA and 16 % among South American Common Market (MERCOSUR) countries 29 % among ASEAN countries. Therefore, once PTAs and FTAs are negotiated and come into force, intraregional trade will grow much faster.

#### **3.2 Investment Cooperation to Strengthen Intraregional Investment**

Intraregional investment can be divided into two categories: Foreign Direct Investment (FDI) and Portfolio Investment. Investment flows are often strong indicators of investment commitments and cross-border trade cooperation trends. In the year 2000, FDI inflows reached about US\$8 billion in the BIMSTEC region, and kept increasing robustly till it hit its recent peak at US\$ 58 billion in 2008. Despite global slowdown of economic activities since then, BIMSTEC countries maintained an upwards trend over the annual FDI inflow values through 2000 to 2013 in the region.

It is important to note that many BIMSTEC economies are relatively smaller to be able to undertake economic activities that could exploit substantial economies of scale. Economies of scale are better utilized in grander markets rising out of economic assimilation, and small countries have greater market penetration. Significant benefit can be derived by the BIMSTEC economies by adjoining and sharing the factors of production and the huge marketplace through preferential trading policies.

#### **3.3 The GTAP Model for Macroeconomic Analysis**

The most common modeling technique for estimating economic impacts of a trade agreement with economy-wide effects involves the Computable General Equilibrium (CGE) modeling framework of the Global Trade Analysis Project (GTAP). The general equilibrium model is thoroughly documented by Hertel in 1997 and in the GTAP database documentation [3]. It is a comparative static multi-regional CGE model.

In this paper, the static GTAP model is used. The static model has disadvantages relative to dynamic techniques, of not describing the time path, i.e. attention in the

analysis is concentrated on the end outcome rather than the transition [4]. The model's results may be very sensitive to the assumptions and data used. Almost all CGE exercises include a sensitivity analysis to obtain a range of results based on different assumptions or data.

### **3.3.1 Data and Country and Sectoral Aggregation**

The study makes use of Version 8 of the GTAP database which was released in 2012. The study has simulated all tariff elimination among BIMSTEC countries.

### **3.3.2 Analysis of the Simulation Results: Welfare and Macroeconomic Effects**

Based on the model simulations, this section reports the results that show the likely impacts on important macro-economic variables, economic welfare, industry outputs and exports. The effects of BIMSTEC FTA can be assessed at both the macro-economic and sectoral levels of analysis. Hossain, Sharif (2013) has examined the possible impacts of BIMSTEC FTA on its member countries using GTAP database and observed that BIMSTEC FTA will be welfare enhancing for all its members except Bangladesh. He also found that trading arrangement might generate employment for its members and creating employment opportunities for unskilled labor, BIMSTEC FTA can reduce poverty within the bloc. However, some differences have been identified in this research compared to the aforementioned study.

If the BIMSTEC countries completely eliminate import tariffs with each other, Thailand, India and Bangladesh are expected to experience welfare gain. The Sri Lanka and Nepal are expected to experience welfare loss. If we look at the allocative efficiency we can see that complete removal of all tariffs among BIMSTEC member countries that improve the allocative efficiency in all BIMSTEC countries.

## **4 Challenges facing the BIMSTEC Countries**

### **4.1 Connectivity and Infrastructure**

Infrastructure and connectivity are core elements of trade facilitation. Poor physical infrastructure—particularly the lack of telecommunication links, parking space, cold storage, accommodation facilities and power—is a major problem in the border station areas. BIMSTEC initiative will need to be geared to build the road, rail and air transport connectivity lack of which at present hinders deepening of trade and investment infrastructure. ASEAN could serve as a very good example for the BIMSTEC group members in this regard.

#### **4.2 Non-Tariff and Long Negative list**

As most of BIMSTEC members also member of SAFTA and APAT, the average tariff have been reduced. However, there are numerous non-tariff barriers that have to be removed. There are long negative list among BIMSTEC countries that need to be reduced within a specified timeframe in order to realize the trade potential. Harmonizations of standards, tariff elimination as well as dismantling of all para-tariff and non-tariff barriers are key for regional integration.

#### **4.3 Trade Facilitation**

World Bank's *Doing Business* report 2015 shows that establishment of a seamless system of cross-border movement of both cargo and people are major challenge for the BIMSTEC. For easing up cross-border movement and establishing greater connectivity the existing trans-border formalities, vehicular movement and customs procedures need to be simplified. Use of modern technology could play an important role in speeding up the procedures. A BIMSTEC visa could also be introduced to facilitate movement of people particularly for the investors and the businessmen.

### **5 Concluding Remarks**

This studies shows that if the BIMSTEC countries completely eliminate import tariffs with each other, Thailand, India and Bangladesh are expected to experience welfare gain. The Sri Lanka and Nepal are expected to experience welfare loss. There are three determining factors of equivalent variation i.e., allocative efficiency, terms of trade (TOT) effects and investment-saving (I-S) effects. If we look at the allocative efficiency we can see that complete removal of all tariffs among BIMSTEC member countries that improve the allocative efficiency in all BIMSTEC countries. The BIMSTEC FTA could enhance intra-regional trade as the simulations shown that export and import of all BIMSTEC countries would experience high growth.

Establishment of a seamless system of cross-border movement of both cargo and people is major challenge for the BIMSTEC. The BIMSTEC countries should work on Single Window facility that allows parties involved in trade and transport to lodge standardized information and documents with a single entry point to fulfill all import, export, and transit-related regulatory requirements. In the context of the current state of play, BIMSTEC remains one of the least connected regions in the world. BIMSTEC initiative will need to be geared to build the road, rail, port and air transport connectivity which at present hinders deepening of trade and investment infrastructure. Improving the state of connectivity within the region, and mobilizing the required resources to build the necessary infrastructure must be seen from the perspective of long term development strategy of BIMSTEC members.

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