

South Asian Regionalism in Times of Global Financial Crisis

Rahul Tripathi

The idea of regionalism in South Asia is nearly three decades old, with its institutionalization in the form of SAARC which remains its only formal manifestation. There have been, at the same time, less formalized interactions at the regional level where non-state actors have created associations guided by a certain complementarity of interests and convergence of goals. Given the historical and cultural unity of the subcontinent, one would have expected such initiatives, both formal and non-formal, to be a natural outcome of the desire to come together for collective good. In reality however, political and strategic divergence within the member countries has led to a scenario where regionalism as an idea has not achieved much.

At a time when the contemporary global political economy is undergoing unprecedented pangs and stresses, the idea of the 'collective' needs to be revisited not only at the regional level but also at the global level. This becomes all the more important in case of South Asia which has been facing numerous geopolitical and geo-economic stresses. On the one hand, it is home to one-fifth of the world's total population and nearly half of the world's poor – a statement that has become a cliché when it comes to analyzing South Asia's political economy and on the other, South Asia has been a witness to, both within and in the immediate neighbourhood, internecine political and ethnic conflicts. The current economic crisis may further aggravate political tensions, leading to chronic instability in the region. It is, therefore, imperative to explore whether the idea of regionalism can be revisited to locate some of the probable remedies to the present dilemma South Asia finds itself in.

Evolution of 'regional' in the midst of 'global'

It is not that the idea of regional cooperation against the backdrop of global turmoil has not been discussed in South Asia before. In fact, the early years of formalized regionalism in South Asia perhaps faced as much if not less turmoil both politically and economically. The early 1980s marked the beginning of the phase where the Cold War rivalry brought a dangerous conflict right next to the South Asian doorstep in the

form of Soviet intervention in Afghanistan and the consequent support of the United States to the Afghan Mujahideen with the intermediation of Pakistan. India saw the initiation of what was to become one of the many severe terror campaigns in Punjab in addition to the ongoing conflict in India's north-east and the Tamil militancy in Sri Lanka threatened to put the region among the global hotspots. Collectively, the region's economies continued to remain among the lower one-fourth on the global GDP scale. Intra-regional interaction among the countries of the region was at a minimum than what would be naturally anticipated due to historical connectivity.

Under these circumstances, the idea of SAARC took off in 1985 with rather over-guarded and cautious optimism. The following declaration of the first summit made a telling statement of the gravity that surrounded the region in both economic and political realms.

The Heads of State or Government expressed deep concern at the continuing crises in the global economy. They underscored that deteriorating economic and social conditions had seriously retarded developing countries. Sharply falling commodity prices, deterioration in the terms of trade, intensification of protectionist measures, spiralling debt burden and a decline in the flow of external resources, especially concessional assistance, had caused a serious setback to the economic development of the developing countries. These had been compounded by natural disasters and precarious world food security situation affecting developing countries. They also expressed concern over the diminishing capacity of international financial and technical institutions to respond effectively to the needs of the disadvantaged and poorer countries and regretted that the spirit of multilateral cooperation had begun to falter and weaken. This was particularly disturbing in the face of increased interdependence of developed and developing countries and the fact that economic revival of North was closely linked to economic progress in South. They believed that developments during the past decades had clearly demonstrated the structural imbalances and inequities inherent in the existing international economic system and its inadequacy to deal with problems of development.¹

¹ Declaration of the First SAARC Summit, Dhaka, 8 December 1985, www.saarc-sec.org

The political context was also alarming, particularly in view of the escalation of the nuclear arms race though the summit fell short of commenting on the tensions in the immediate neighbourhood. The caution was more than apparent as the Charter, while talking of 'promoting welfare' of the people of South Asia and 'contributing to mutual trust' made it imperative to avoid bilateral and contentious issues so that the spirit of regionalism does not get diluted by bilateral squabbling.² Moreover, the decision-making structures made it mandatory for decisions to be taken in a spirit of consensus.

Given these cautious steps at rooting regionalism in the initial years, the first phase can be regarded as a phase of reluctant regionalism where the grouping fell shy of taking a clear and consolidated position on any of the critical political-economic challenges within the region. Besides, there was a complete lack of movement on certain core areas of economic cooperation. This inertia on the core economic issues shifted gears in the early nineties with the initiation of discussion on two key issues which had hitherto been neglected, namely poverty alleviation and trade liberalization within the region. Consequent efforts led to the constitution of the first Independent Group on Poverty Alleviation that submitted its report in 1992 and the adoption of the declaration on South Asian Preferential Trade Agreement in 1995. The inherent limitations of these declarations notwithstanding, (IGPA Report remained a declaration of good intent and SAPTA led to a marginal expansion of intra-regional trade) SAARC continued to make projections for deeper and more meaningful interactions with the following agreements that were to follow: a) South Asian Free Trade Area (SAFTA), b) SAARC Development Fund and c) Treaty on Avoidance of Double Taxation. Furthermore, it was decided to adopt a collective position on international trade issues at multilateral fora. More recently, in a more meaningful twist to the whole idea of regionalism, SAARC emphasized on enhancing and reviving connectivity in the region as a way to strengthen physical and economic integration in the region as a precursor to the integration of the region with the world. It was, perhaps, for the first time that regionalism as a concept could be seen as a necessary adjunct to globalism.

One area where regionalism perhaps could have become a logical precursor to globalism was the one that undertook to take a collective position on global trade issues. SAARC economies, by and large, have faced similar trade and production complementarities which puts them on the same side of the fence at multilateral fora than perhaps at the regional level. This is especially the case with issues relating to

² Article I and X of SAARC Charter, www.saarc-sec.org

agricultural trade and access, textiles and movement of labour. It was, therefore, natural and necessary that SAARC countries collectively articulate their common concerns for them to be heard more strongly. While the spirit of the decision has sustained, the substance has often been found lacking, more so in the context of recent WTO negotiations. The unity of purpose expressed during pre-WTO meetings has often proved to be fragmented and short-lived. Besides, the prospects of a collective position on other matters of global economic concern have remained confined merely to the annual ministerial declarations rather than leading to concerted action. For instance, India has often joined hands with other sub-groups such as G20, BRIC, and IBSA. It is in this context that there is an urgent need to revisit the notion of regionalism to make it more meaningful in the specific context of the global economic crisis.

Present crisis and its impact on South Asia

It is pertinent to discern those elements of the contemporary economic crisis which have a specific implication for regional economies to be able to explore how regionalism can help in coping with them in a better way. First, the current crisis has been aggravated by greater interconnectedness of economies at the regional as well as the global level. The global financial and commodity markets are today much more interlinked than they were a decade ago when a similar crisis hit the emerging Asian economies. As a result, while the previous crisis could be localized and mitigated by intervention from multilateral agencies and countries which had, by and large remained unaffected, the current crisis may be far too pervasive and expansive to be localized. The very same institutions and agencies which came to the rescue last time are being viewed as both victims and perpetrators.

Second, the propensity of the present financial crisis to transform into that of the real sector has been much faster and the regional economies as a whole have had to bear the brunt. The collapse of the sub-prime loan market impacted the ability of banks to finance investment and trading scenarios which, in turn, deeply affected job prospects in developed as well as developing countries. The developing countries ostensibly have been hit doubly as not only have their prospective industrial plans suffered but also loss of jobs and rising food prices have precipitated social tensions in an unprecedented manner.

Though South Asia does not appear to have been as severely affected as perhaps the more open developing economies, the segregated effects on individual countries have been felt quite significantly. A recent World Bank report notes that the crisis hit the South Asian economies when

they had barely recovered from the trade shock due to increased global oil and food prices. Global food and oil crisis had severely impacted South Asia with the cumulative income loss ranging from 34 per cent of 2002 GDP for Maldives to 8 per cent for Bangladesh. Besides, current account deficits and fiscal imbalances worsened sharply and inflation surged high. Growth in South Asia declined from 8 per cent in 2007 to 6 per cent in 2008 and is projected to decline to 5 per cent in 2009 before recovering to 6 per cent in 2010.³ Another related study, while doing a more sectoral analysis of the fallout, highlights the impact on both the financial and real sector. While the financial sector is stated to be relatively protected, partly due to the limited opening of the sector and also because of stable macro-economic fundamentals in most of the regional economies, the real sector is the one likely to be affected more directly by way of declining export earnings, declining import prices, diminishing remittances and, finally, declining investment due to limited availability of private investment and reducing bank loan guarantees.⁴ Interestingly, the policy options available relate more to correcting domestic macroeconomic imbalances and greater institutional reforms to be done more at the level of individual economies, negating in a way, the efficacy of any collective action. In this context, the SAARC Ministerial Statement on the current crisis comes closer to the idea of collectively tackling the crisis but just falls short of clearly expounding the broad contours of any coordinated strategy.

In addressing this crisis, a well-coordinated regional approach is required considering the severe impact on the economies and the socio-economic development of the SAARC region. With strong economic foundations South Asia is well placed to strengthen intra-regional trade and economic development and contribute to global solutions to the crisis.

Special stimulus packages are needed for developing countries to cushion the impact of the crisis. Deepening and broadening regional and sub-regional economic links in the Asia Pacific and other regions is a necessity. Stimulus packages must also take into account the needs of developing economies and the need to sustain development and trade financing to enable the realisation

³ Impact of Global Financial Crisis on South Asia, 17 February 2009, www.siteresources.worldbank.org

⁴ Global Financial Crisis: Implications for South Asia, 21 October 2008, www.siteresources.worldbank.org

of the Millennium Development Goals and SAARC Development Goals unhindered. Developed countries should not resile into protectionism. Trade relations must also be allowed to develop naturally and the Doha Development Round must be concluded expeditiously.⁵

Regional way out?

The crisis has been attributed as much to contemporary financial malpractices as to the absence of regulatory mechanisms to oversee rogue transactions that eventually led to the crisis. The means to overcome, therefore, have to be at both at the protective as well as pre-emptive levels. There are, at the same time, issues relating to the global economic architecture which has often perpetuated systemic imbalances where developing countries have been at the receiving end of any crisis in international economic relations whether it is trade, investment, technology transfer or environment.

Managing the fallout of the crisis has been a predominant theme in distinct multilateral fora as it has been realized that there cannot be any individual-institutional or nation-centric efforts at countering the crisis which has acquired trans-regional and global proportions. There is a two-fold approach that is being visualized in comprehending and contextualizing the crisis. First, the nature of recovery can only be perceived to be spread over a certain period of time with no expectations of immediate return to normalcy. Given the declining rates of economic growth worldwide and the inability of global stock markets to pick up drastically, despite a year having passed, any revival will have to come from a sustained rather than one-off stimulus package. So there has to be a gestation period for recovery rather than manifestations of green shoots that keep emerging only to disappear the next day. Second, the spurt for revival will have to come as much from the major emerging economies like India, China and Brazil as from leading financial and manufacturing centres of the West. In essence, the remedy perceived is a collective one which will require coordinated action at revival, protection and pre-emption. Such a spurt on behalf of the emerging economies, however, will have to be based on an umbrella approach where, apart from becoming engines for global recovery, they could also act as magnets to pull the smaller and not so open economies of the region on the path of recovery and revival, a dual role, perhaps easier said than done but worth trying nevertheless.

⁵ SAARC Ministerial Statement on Global Economic Crisis, 28 February 2009, p.1, www.saarc-sec.org

Keeping in view the sustainability and collective nature of the efforts which are required to mitigate the crisis, the following areas where a regional rather than individual effort may appear to be more feasible for South Asia can be explored.

Strengthening regional monitoring capacity

South Asia, at present, does not really have a regional institutional mechanism to analyze and comprehend the crisis that has engulfed the region, perhaps because regional cooperation in the financial spheres has been rather segmented and episodic. The regional body that comes closest to performing this role is SAARCFINANCE, a network of finance secretaries and governors of the central banks of the member countries which was approved in principle in 1998 and got official recognition by SAARC in 2002. As stated in the objectives of the mechanism, issues relating to global financial developments and their implications for South Asian economies are very much on the agenda but the role remains discursive rather than policy prescriptive.⁶ Another similar opportunity is provided by the annual meetings of central banks under the auspices of the Asian Clearing Union (ACU) which was established in 1975 as a regional clearing and payments facility and had with it the explicit mandate of fostering greater monetary cooperation among member countries. Its members include Bangladesh, India, Pakistan, Nepal, Pakistan, Sri Lanka, Iran, Myanmar and of late Bhutan, thereby giving it a SAARC Plus character. The ACU, in its nearly three and a half decades' existence, could not go beyond the traditional role of a clearing facility with a very limited focus on payments and can hardly be considered as a mechanism that provides greater policy prescriptive advice on the issues of global monetary and financial instability and how the region could cope with them.⁷

One may wonder whether, from a theoretical point of view, such institutional mechanisms orchestrated through formalised bureaucratic structures can at all be effective in pre-empting and prognosticating if a regional financial crisis of the kind that has a contagion effect does strike South Asia. There may, in fact, be a point in the argument that such mechanisms can only be effective to the extent that the larger forces of regional cooperation and integration shape them. In this regard,

⁶ SAARC Finance has become the latest in the series of exchanges on financial matters and has a rotating chair within the Secretariat. For details see www.rbi.org.in

⁷ Rahul Tripathi, *Monetary and Payments Cooperation in South Asia* (New Delhi: Concept Publishers, 2010).

SAARC's role has not been very encouraging and despite being recognized officially, such structures act as mini SAARC bodies in letter and spirit.

The need, therefore, would be to transform the role of such bodies from a mere recommendatory to more implementation oriented where the mechanism is not only able to measure the magnitude and extent of a crisis once it erupts but is also able to put in place some concrete measures which would be enforced as per the mandate received from the apex SAARC body. For instance, now that it has been established that the recent financial crisis was more an outcome of unregulated investments in mortgage transactions, SAARCFINACE could set in place immediately the nature and level of exposure the South Asian financial sector may have with regard to such global transactions and may put a cap on the degree to which such exposure is sustainable. Or SAARC could also think of putting in place a more harmonized system of payments settlements so that some kind of early warning systems could be put in place to identify spurious transactions which may ultimately aggravate the crisis. A small yet significant step in this direction has already been taken with the creation of SAARC Payments Initiative (SPI). To its credit, the SPI has already undertaken a number of action-oriented activities. It may also:

- carry out a stocktaking exercise of the Payment and Settlement System (PSS) in the region on a comparable basis to understand the current status of the PSS in each member country;
- assess the volume of cross-border remittance payments in member countries;
- set up a National Payment Council (NPC)/Committee in each member country, where such a committee does not currently exist; and
- conduct conferences and seminars, publish SAARC Payments Bulletins and launch a website to convey developments in the PSS in the region and its future endeavours.⁸

The SPI, however, will need a greater mandate and teeth to be able to expand its role as a monitoring body towards which, at present, there are no signs of moving. Until the time one is able to conceive a regional regulatory body in SAARC, which could oversee the trends in financial volatility, a modification of the existing SAARCFINANACE mechanism would be in order.

⁸ For details see www.saarcpay.lk

Strengthening regional financing facility

The second, yet equally significant area where regional capacity to withstand and overcome a financial crisis could be more of a post-crisis management mechanism of building a regional reserve facility that could enable the member countries facing the brunt of the crisis to meet temporary liquidity requirements. Creation of regional reserve mechanisms to face regional crises has been a prominent theme in recent regional cooperation literature, particularly after the Asian financial crisis of the 1990s but it has evoked mix responses, particularly from global funding agencies. The Annual Economic and Social Survey of Asia and Pacific 2008, titled *Sustaining Growth and Sharing Prosperity*, written against the backdrop of the sub-prime crisis, points to the need for improving regional cooperation to prevent and react to such a crisis. It cites the example of ASEAN Plus Three proposal of pooling together their foreign exchange reserves to meet the crisis and states that converting the system of bilateral currency swaps to a multilateral pool will increase the speed and ease of response. It also seeks to expand the mandate to other countries and emphasizes the greater sharing of information about portfolio flows and collaborating in regulatory activities.⁹

South Asia will not exactly need to reinvent the wheel if and when it decides to opt for a similar arrangement for the South Asian region as some rudimentary structures already exist. As part of the ACU, the member countries already have been taking part in an ACU SWAP facility and the inbuilt period of two monthly settlements which has acted as a kind of financial mechanism that also acts as a short term credit for member countries.¹⁰ So far, the ambit of this facility has been merely to make up for intra-regional settlements and has not been expanded to a reserve facility that meets larger shortfalls. The other regional credit arrangements in South Asia have been more in the form of developmental financing, the most prominent of them being the South Asian Development Fund (SADF). SADF was created in 1996, merging the SAARC Fund for Regional Projects (SFRP) and the SAARC Regional Fund. Its prime objectives were to support industrial development, poverty alleviation, protection of environment, institutional/human resource development and promotion of social and infrastructure development projects in South Asia. The fund started with a resource base of 5 million dollars (contributed on pro rata basis by SAARC Member States) and till its closure in June 2008, had funds amounting to

⁹ *Economic and Social Survey of Asia and the Pacific 2008: Sustaining Growth and Sharing Prosperity* (Bangkok: UNESCAP, 2008), p.23.

¹⁰ See www.asianclearingunion.org

approximately 7 million dollars.¹¹ Perhaps a facility which could complement both the liquidity requirement and developmental financing with appropriate participation of both the private and public sector could help in creating an enhanced regional facility in South Asia.

Redesigning regional cooperation architecture

Having articulated two areas where regional efforts may help to counter the adverse fallout of the financial crisis, the third area is a more fundamental one which calls for a reconsideration of the principles and premises for regionalism in South Asia. As stated at the beginning of the paper, regionalism in South Asia has been a good idea but a bad practice by any standards of regional interaction. While the regional structures created out of SAARC have been impressive, the regional spirit emanating from it has been less to write home about. Given the manner in which the financial meltdown has affected people (rather than the state), either by way of loss of jobs, income and assets, it is quite apparent that unless a regional cooperation model that emphasizes cooperation and touches upon lives of people rather than remaining an agency of state interaction is adopted, it would not make a meaningful impact. There is, therefore, a strong case for revisiting the institutional structures of cooperation as that will imbibe a greater urgency for creating a regional apparatus so essential for accomplishing the first two measures that have been pointed out.¹² One would, therefore, look forward to a 'SAARC from below' based on people-centric ideas where the state plays the role of mediator and facilitator for regional interaction.¹³ Such people centricity becomes all the more necessary as South Asia will continue to seek greater integration with the rest of the world and movement of people will be the key element through which such linkage will be strengthened.

Conclusion

Even though South Asia appears to be coping with the adverse fallout of the financial meltdown and the region appears poised towards a relatively stable growth in the coming years, there are important lessons to be learnt in the policy and prescription with regard to how the regional approach could help South Asia in mitigating such crises. While it is apparent that political factors have been too deeply entrenched in the region to make economic regionalism viable, there is still enough basis in

¹¹ See www.saarc-sec.org

¹² Kishore C. Dash, *Regionalism in South Asia: Negotiating cooperation, institutional structures* (Oxford: Routledge, 2008).

¹³ Rahul Tripathi, 'Reorienting the Regional discourse on South Asia : Vision for a People's SAARC', *South Asian Survey*, vol.13, no.2, September 2006, p.323.

South Asia to rediscover and redefine the existing cooperation structures to make them more meaningful and constructive in enabling the region to meet the impending external crises which may not necessarily be of the region's own creation. As South Asia continues to seek integration with the rest of the world, it needs a regional cushion which may provide it the necessary capacity to cope with adverse fallouts of financial crises. Regionalism as an idea, therefore, may still provide the necessary stabilizing influence in its specific and general manifestations, if appropriately nurtured.