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## India's Engagement with ASEAN: Beyond Trade in Goods

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Asia has experienced a surge of regional trade agreements (RTAs) in recent years particularly in East and Southeast Asia. Production across the region has become further integrated due to the institutionalisation of RTAs. The domain of integration now extends to South Asia with India and other South Asian economies connecting to East and Southeast Asia through formal trade arrangements. Proliferation of RTAs has revived the debate on multilateralism and regionalism. While most regional economies have adopted the multilateral framework of the World Trade Organization (WTO), their pursuit of RTAs have raised questions over whether they repose greater faith in regional trade networks. The Economics and Trade Policy research cluster at ISAS organised a workshop in Singapore on 20 October 2010 on 'Trade Policies in South Asia and Southeast Asia: Encouraging Regionalism?' It examined different aspects of the theme including comparative dimensions of trade frameworks, bilateral trade relations and country perspectives on regional trade. The papers are being brought out by ISAS as a working paper series. This paper is the fourth in that series.

### Abstract

*India has actively engaged the Association of Southeast Asian Nations (ASEAN), reaching a zenith with the signing of ASEAN-India Free Trade Agreement (AIFTA) on 13 August 2009. Further, India has plans for bilateral free trade agreements (FTA) with select ASEAN member nations. Broadly speaking, the comparative advantage of ASEAN member countries is in manufacturing, while that of India is in services. Hence both ASEAN and India can exploit their relative strengths. The paper will seek to look beyond trade in goods to flag*

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*other areas that might offer scope for broader engagement in the future. The paper argues that trade in services, security, the environment and infrastructure offer wider opportunities for collaboration between ASEAN and India.*

## **Introduction**

Since the early 1990s, the economic relationship between India and ASEAN has improved significantly. In 1992, India was admitted as a sectoral dialogue member of ASEAN and was granted the status of a full dialogue partner by December 1995. The year after, it became a member of the Asian Regional Forum (ARF). Subsequently, India was invited to be a member of the East Asian Summit in 2005.<sup>2</sup> The ties between the two entities have progressed substantively, providing a strong baseline for cooperation in various fields.

The 'Look East Policy' adopted by India in 1991, along with its liberalisation program and economic reforms, has become important not only with regard to trade flows in goods but also in the trade of services. At the beginning of 2010, the AIFTA came into effect promising greater bilateral trade.<sup>3</sup> The FTA only covered the trade in goods between the two parties with the prospect of liberalising regulations on more than 90 per cent of traded goods.<sup>4</sup> It is noteworthy, that the FTA will eventually include products such as crude and refined palm oil, coffee, tea, and black pepper, all of which are protected in their domestic markets. Tariffs on 4,000 products will be eliminated by 2016 at the earliest.<sup>5</sup> Tariffs on the highly sensitive products such as palm oil, coffee and tea will not be reduced until 2018. India will cut the tariffs on crude palm oil by 37.5 per cent and tariffs on refined palm oil by 45 per cent.<sup>6</sup> Also, concessions on sensitive products will be granted for a period of ten years.<sup>7</sup> The FTA will contribute towards the reduction of India's accumulated trade deficit with ASEAN.<sup>8</sup>

India now stands as ASEAN's fourth biggest trading partner and accounts for ten per cent of India's global trade.<sup>9</sup> The bilateral agreements that have emerged in the recent years demonstrate the extent of India's interest in engaging with Southeast Asia. In 2005, Singapore and India signed a Comprehensive Economic Cooperation Agreement (CECA)

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<sup>2</sup> Due to political differences, India had twice refused to become a dialogue partner with ASEAN (1975 and 1980). After the collapse of the USSR, the Indian economic crisis in 1990 and the success of the ASEAN development model, India changed its position.

<sup>3</sup> Bilateral trade meaning ASEAN as one entity conducts trade with India. In the following, single countries will be named when certain aspects only apply to them as countries, otherwise ASEAN will be treated as one entity in order to take account of its activities as one international player.

<sup>4</sup> See ASEAN, [www.aseansec.org](http://www.aseansec.org). Accessed on 22 March 2011.

<sup>5</sup> 'ASEAN-India Dialogue Relations', ASEAN, [www.aseansec.org/14802.htm](http://www.aseansec.org/14802.htm). Accessed on 22 March 2011.

<sup>6</sup> Shankari Sundararaman, 'India-ASEAN FTA: To be or not to be', *Deccan Chronicle* (14 April 2009), [www.deccanchronicle.com](http://www.deccanchronicle.com). Accessed on 12 October 2010.

<sup>7</sup> Amita Batra, 'India-ASEAN FTA: A Critique', *IPCS*, Issue Brief No.116 (September 2009).

<sup>8</sup> Suparna Karmakar, 'India-ASEAN Cooperation in Services: An Overview', *Indian Council for Research in International Economic Relations*, Working Paper No.176 (November 2005).

<sup>9</sup> Pranamita Baruah, 'India-ASEAN Scale New Frontier Following FTA', *Global Politician* (20 August 2009).

that included bilateral investment promotion, double taxation avoidance, air services and an FTA.<sup>10</sup> India has plans to sign individual FTAs with Brunei, Malaysia and Indonesia by the end of 2011.

India and ASEAN have different economic foci. While India's comparative advantage is in services, ASEAN, broadly speaking, has its strength in light manufacturing. The economic complementariness and the socio-cultural affiliation with the region offer an opportunity for deeper engagement. Mukul G. Asher et al. argued that India has not only proved to be a reliable partner but a co-investor of political and economic stability in the region. The imperative for stronger ties stems from the political and security environment, globalisation and its associated technological changes, and institutional foundations.<sup>11</sup>

Several scenarios are possible with regard to the emerging architecture, where ties between India and ASEAN member countries can be formalised. On one hand, India and ASEAN could allow the free hand of market forces to determine their trade volume without formally engaging in designed economic cooperation. Alternatively, India might become a member of the ASEAN+3 and transform this forum into an ASEAN+4. Conversely, rather than seeking an inclusion in a grouping that, by definition, does not include India, it would be more plausible to push for an ASEAN+6 which would yield the largest gains to India and East Asia in the form of an Asian Economic Community (AEC). The latter is often seen as the ultimate goal of Asian regional integration and perhaps it is in this context that India should attempt to play a role.

The following will discuss these possible future scenarios of Asian cooperation and integration. The first section will deal with the trade in services between India and ASEAN states as it was not included in the recently signed FTA. Since India is a service-based economy, it is fairly reasonable to take trade in services as a starting point for future ASEAN-Indian cooperation. This will be followed by a discussion on some of the broader issues of engagement with ASEAN. The issue of infrastructure development for example, will be discussed in the context of political and geostrategic considerations. An analysis of India's future role in the ASEAN integration process will be discussed

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<sup>10</sup> India also has trade agreements with Myanmar and Thailand.

<sup>11</sup> Mukul G. Asher, Rahul Sen and Sadhana Srivastava, 'ASEAN-India: Emerging Economic Opportunities', *Centre for Freedom and Development Studies* (May 2001), [www.cfdsindia.org/emergingeconomic.htm](http://www.cfdsindia.org/emergingeconomic.htm). Accessed on 22 March 2011.

## Trade in Services between India and ASEAN

ASEAN does not figure very prominently as India's trading partner. Hong Kong and Singapore are among the top 10 export destinations for India, while only Singapore ranks among the top ten as an importer. India accounts for barely three per cent of ASEAN's share of international trade.<sup>12</sup> In 2009, ASEAN accounted for nine per cent of India's total imports and 11 per cent of total exports.<sup>13</sup> However, it can be expected that growth in demand for ASEAN goods is likely to rise given India's increasing domestic demand, favourable demographics and rising domestic investments. India's recent growth trends are likely to continue in the future and hence evolving to become an important market for ASEAN goods. The recently signed FTA on goods will certainly boost trade between ASEAN and India.

ASEAN member states have signed the ASEAN Framework Agreement on Services (AFAS). They have made commitments in the fields of tourism, air-transport, business, construction, healthcare, information and communication technology (ICT), and telecommunication services. Of these, healthcare, tourism, travel and e-ASEAN<sup>14</sup> are considered to be the 'priority sectors' in which liberalisation should have been achieved by 2010, while the other service sectors shall be liberalised by 2020 at the latest.<sup>15</sup> There are two ways in which India can seek entry into the services markets of ASEAN. The first possibility is by taking advantage of the AFAS. This will require a formal agreement on services with ASEAN. The second, and more tedious process, is through bilateral negotiations with individual ASEAN countries. At any rate, India should formalise its links with ASEAN to encourage trade in services because of the huge potential that exists.

Two factors will drive the growth for trade in services. First, services play an increasingly important role in international trade. Second, India's economy is significantly based on services (seen in Figure 1). Consequently, one can expect India to be an important exporter of services to ASEAN, since the more developed economies in this region will be a source of demand for the services sector in India.

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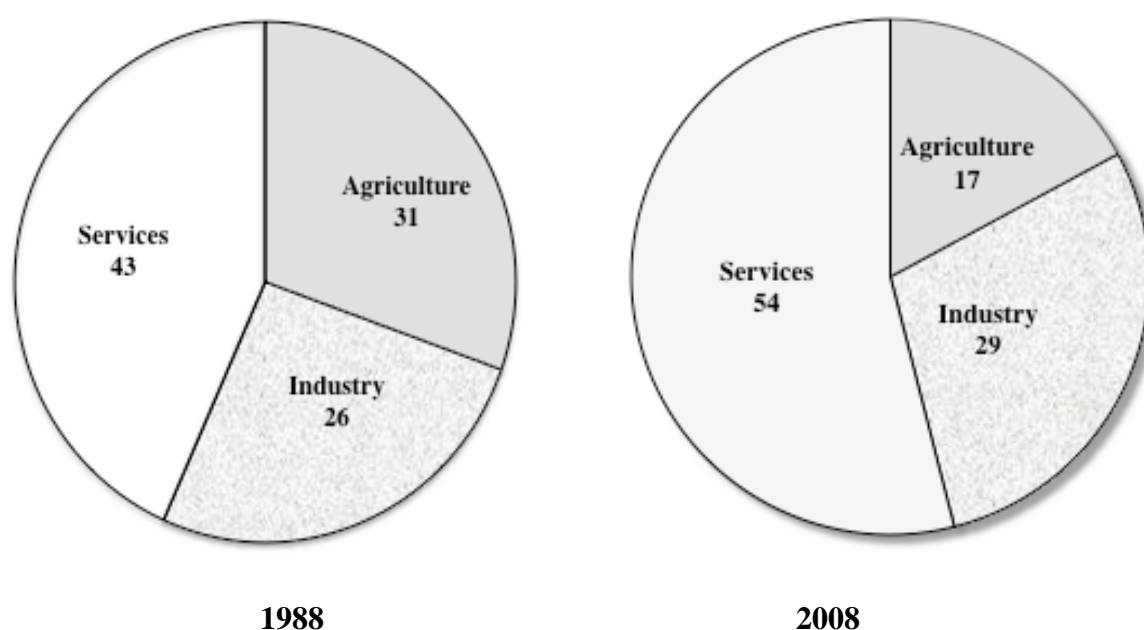
<sup>12</sup> Amita Batra, 'India-ASEAN FTA: A Critique', *IPCS*, Issue Brief No. 116 (September 2009).

<sup>13</sup> Rohini Malkani and Anushka Shah, 'India Macroscopic: India's Growing Labor Force – Boon or Bane?', *Monthly Monitor*, Citigroup Global Markets (23 July 2010).

<sup>14</sup> E-ASEAN is an initiative that is meant to facilitate and promote the growth of electronic commerce in the region.

<sup>15</sup> Suparna Karmakar, 'India-ASEAN Cooperation in Services: An Overview', *Indian Council for Research in International Economic Relations*, Working Paper No.176 (November 2005).

**Figure 1: India: Economic Contribution, By Sector**



**Source:** 'India at a Glance', *World Bank* (2009), [www.devdata.worldbank.org/AAG/ind\\_aag.pdf](http://www.devdata.worldbank.org/AAG/ind_aag.pdf). Accessed on 22 March 2011.

Among the WTO members, India is eleventh with regard to its share in world commercial services and ranks among the top export countries in financial services, telecommunications and information services, and construction, as well as the cultural, personal and recreational services. In addition, exports of commercial services in Asia have seen double-digit growth rates in the areas of commercial, transportation and travel over the past few years.<sup>16</sup>

In contrast to other countries, ASEAN states have been lukewarm in their demand for India's competitive advantage in services. Many developed countries have outsourced services, such as customer phone services or call centres, to India and have thereby kept their competitiveness. ASEAN states have not followed these trends yet. In part, this could be prompted by the stage of development of specific ASEAN economies. The less developed among them might not be in a position to have the demand for the services produced in India. Their stage of development has not matured sufficiently to embrace the outsourcing strategy. This reluctance can also be explained by the fact that some of the emerging economies have a better chance to be producers of services. For example, Malaysia has attracted outsourcing activities and therefore would not consider India as an outsourcing partner.

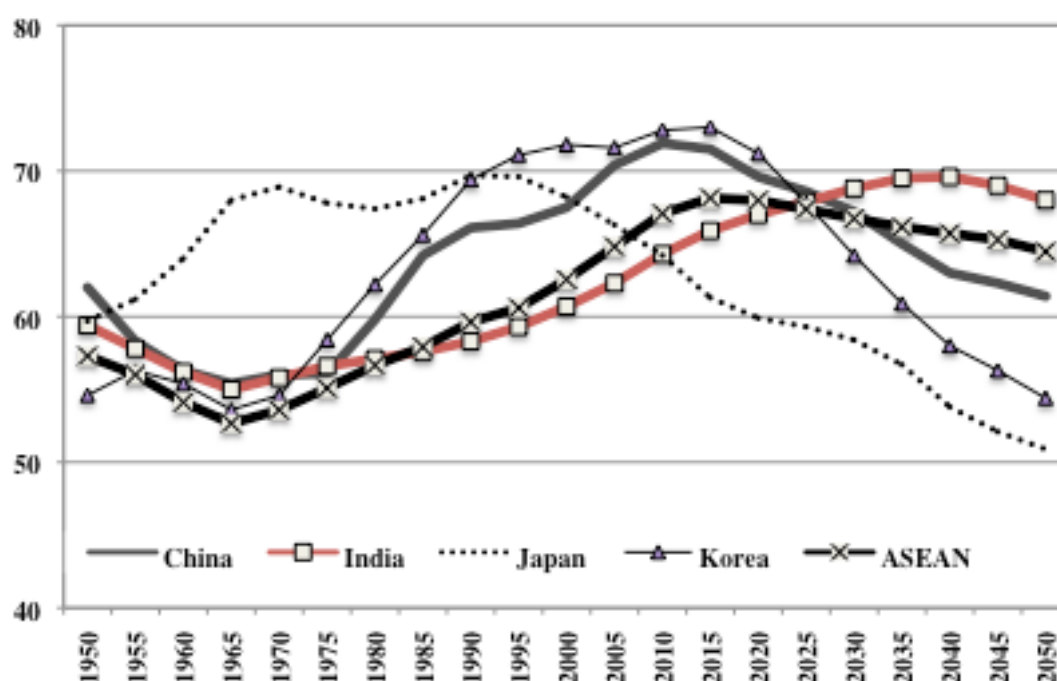
The above mentioned FTA between the two parties was only on goods and did not include services. This can either mean that services account for such a small share of bilateral trade

<sup>16</sup> 'International Trade Statistics 2010', *World Trade Organization*, [www.wto.org/english/res\\_e/statis\\_e/its2010\\_e/its10\\_toc\\_e.htm](http://www.wto.org/english/res_e/statis_e/its2010_e/its10_toc_e.htm). Accessed on 12 May 2011.

that the two parties did not see a necessity to include them. It could also mean that trade in services is sufficiently covered in the WTO General Agreement on Trade in Services (GATS). In the future, however, services might become a crucial part of trade between ASEAN and India.

India's age structure favours development for variable fields in the service sector. In contrast to the other major Asian nations, India's working population will increase rather than decrease for another 30 years (see Figure 2). Within ASEAN, only Cambodia and Laos have an increasing working population while the share of people aged 15 to 64 will decrease in all other ASEAN nations by 2020 (see Figure 3).<sup>17</sup> This trend will lead to increasing demand of services in ASEAN and India will prove to be a good partner to reduce and maybe even overcome this shortage. Additionally, ASEAN nations will face a lack of skilled labour, a factor that could be filled by India. Due to their enormous growth in the past years, economies like Malaysia, Singapore and Thailand face shortages in manpower at all skill levels.<sup>18</sup>

**Figure 2: Population Growth Trends: Age Group of 15-64**

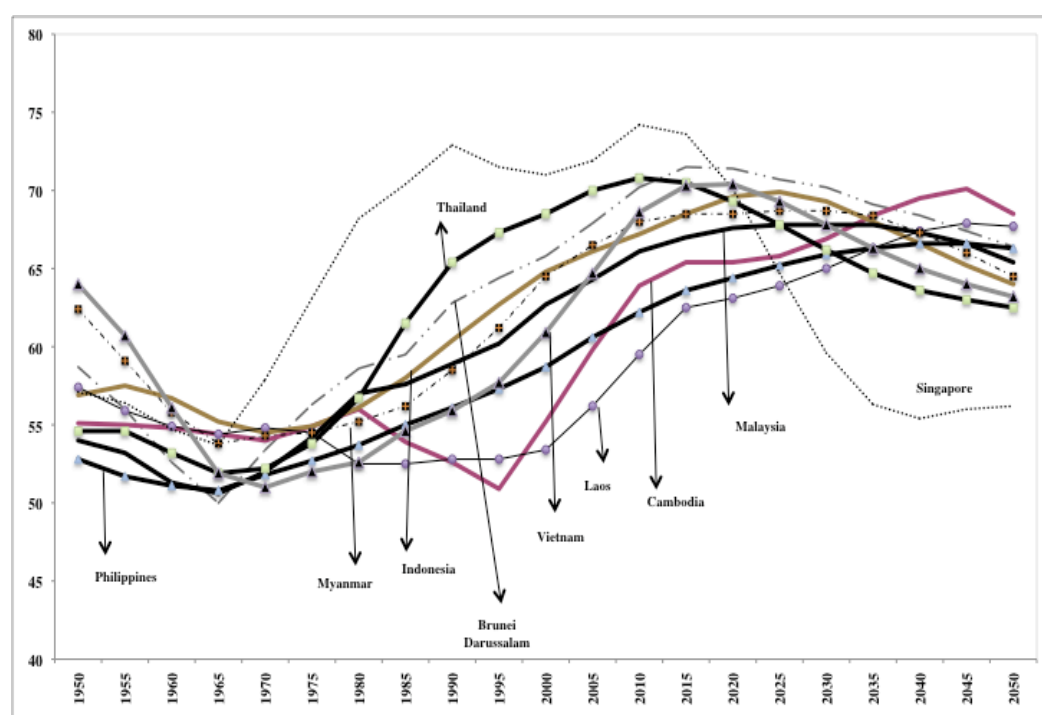


**Source:** United Nations, Population Division, <http://esa.un.org>. Accessed on 22 March 2011.

<sup>17</sup> See, United Nations, Population Division, <http://esa.un.org>. Accessed on 22 March 2011.

<sup>18</sup> Mukul G. Asher, Rahul Sen and Sadhana Srivastava, 'ASEAN-India: Emerging Economic Opportunities', Centre for Freedom and Development Studies (May 2001), [www.cfdsindia.org/emergingeconomic.htm](http://www.cfdsindia.org/emergingeconomic.htm). Accessed on 22 March 2011. Data for graphs from United Nations, Population Division.

**Figure 3: ASEAN Population: Age Group 15-64**



**Source:** United Nations, Population Division, <http://esa.un.org>. Accessed on 22 March 2011.

Although, the demographic outlook for India is very promising, its labour supply has to be planned and managed prudently. Even though India might have one of the largest labour markets on the world, India's Ministry of Labour warns that employment has to rise by at least 2.5 per cent per annum in order to match the growing labour force.<sup>19</sup> Even if India exports workers abroad, the domestic labour market still needs to grow at a considerable rate to keep pace with demographic trends. Considering a scenario in which India and ASEAN member countries liberalise not only trade in goods but also in services, it is likely that an agreement on labour mobility would be needed. Such an agreement might be viewed with circumspection by ASEAN states, due to the possible excess supply of labour originating from India. This might not be a concern in respect to skilled labour since, although, India is abundant in skilled manpower, some of the ASEAN countries have shortages. The situation will be more complex in reality since a free flow of the workforce could lead to imbalances in the labour market in the destination countries. Nonetheless, greater flexibility with regard to skilled labour will help ASEAN economies upgrade their production processes and move up the development ladder.

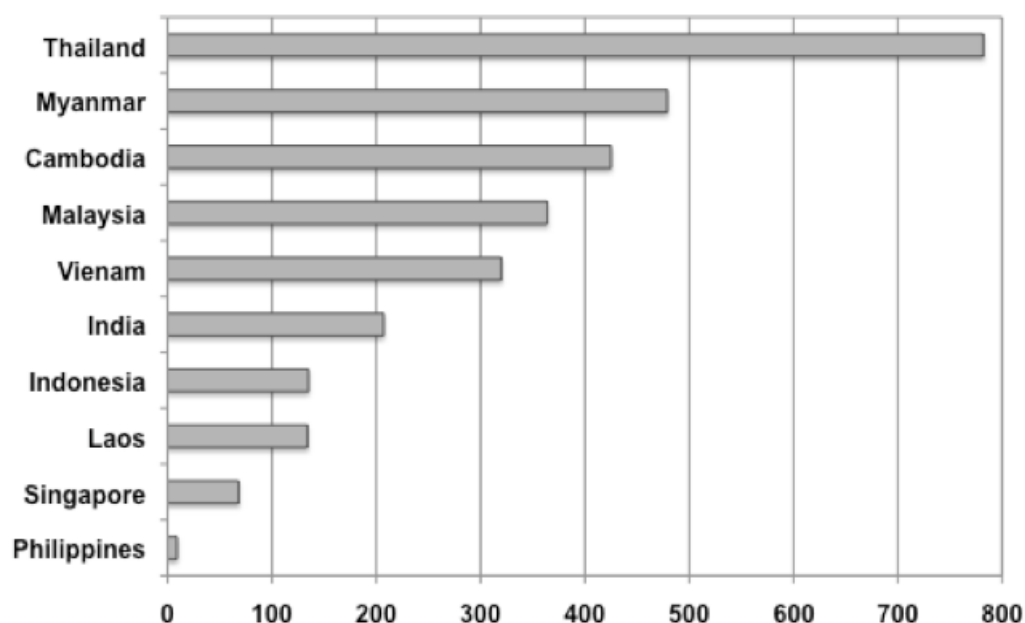
For ASEAN member countries, liberalising the movement of professionals and specialists across country borders is among the top priorities, since it would make it easier to provide high quality services. It is argued that India needs to engage on a bilateral basis with ASEAN

<sup>19</sup> Rohini Malkani and Anushka Shah, 'India Macroscopic: India's Growing Labor Force – Boon or Bane?', *Monthly Monitor, Citigroup Global Markets* (23 July 2010). Numbers based on a labour elasticity of 0.29 as was the average from the years 1994-2005 and a GDP growth of 9 per cent YoY (year on year).

member countries on services. This suggestion is made because the service sector integration within ASEAN has yet to be accomplished and ASEAN is relatively closed to foreign service providers that unless India and ASEAN sign an agreement on free movement on service providers.<sup>20</sup>

Within ASEAN, the ASEAN-5<sup>21</sup> economies have exported services in fields such as construction, healthcare, engineering, infrastructure development, and real estate services to name just a few. India's main exports to ASEAN regarding services are focused on software, technical education, audiovisual, finance and healthcare.<sup>22</sup> Healthcare is an area which holds much promise at various levels. As India has become internationally competitive in the production of pharmaceuticals, stronger cooperation with ASEAN states might increase India's export value in health products and healthcare systems in many ASEAN countries. A crucial aspect in this regard is the provision of affordable generic and other drugs for diseases such as HIV (human immunodeficiency virus) and AIDS (acquired immune deficient syndrome) in ASEAN states – as generic drugs are much cheaper than branded drugs and therefore a highly attractive import product.

**Figure 4: Prevalence of HIV per 100,000 Population, 2005**



**Source:** Author's calculations based on 'Global Report: UNAIDS Reports on the Global AIDS Epidemic 2010', *UNAIDS*, Annex 1 (2010), p.187.

<sup>20</sup> Suparna Karmakar, 'India-ASEAN Cooperation in Services: An Overview', *Indian Council for Research in International Economic Relations*, Working Paper No.176 (November 2005).

<sup>21</sup> ASEAN-5 consists of Philippines, Malaysia, Singapore, Indonesia and Thailand.

<sup>22</sup> Suparna Karmakar, 'India-ASEAN Cooperation in Services: An Overview', *Indian Council for Research in International Economic Relations*, Working Paper No.176 (November 2005).



As can be seen in Figure 4, the prevalence of HIV-AIDS is quite high in ASEAN countries and has likely increased since 2005.<sup>23</sup> Due to an aging population and the increasing spread of sexually transmitted diseases, healthcare costs are constantly rising in most ASEAN countries. With these factors in place, ASEAN states become more and more dependent on the import of drugs for these diseases. As living standards begin to evolve and improve, modern diseases such as diabetes and hypertension are also on the rise and need treatment. Thus, the import of drugs for these 'modern' diseases becomes even more important. There are two levels at which India can find its relevance within ASEAN member states. First, it can find a ready market for export and production of generic drugs for some of the lifestyle diseases that are increasing in numbers and importance. Second, it can venture into the supply of healthcare services.

Rahul Sen, et al., see great potential for a close cooperation between India and ASEAN states (such as Malaysia, the Philippines and Singapore) since these states have developed a comparative advantage in the field of electronic hardware production. India, with its focus on software development and applications, can explore opportunities in complementing the activities in these countries.<sup>24</sup> These complementarities can be developed in various directions. Malaysia's electronics sector is home to innumerable multinational corporations (MNCs). In the course of the development of the hardware industry, many local companies have benefited from the technology transfer and some of them have grown to become vendors to the MNCs. It is possible for Indian companies to gain access to markets through these firms. With the extension of technology and capital, it is possible for Indian companies to extend their reach into the hardware industry. The scope for entry into the Philippines could take a different track. The Philippines has a labour force that is relatively cheap, educated and fluent in English. Indian software companies could capitalise on these qualities to extend the operations of their companies and take advantage of the availability of the labour force in the Philippines and Malaysia.

Many of the countries in ASEAN have made GATS-plus commitments. Suparna Karmakar argues that they are likely to profit from even freer trade regimes than in those listed as priority sectors (air transport, business services, construction, financial services, maritime transport, telecommunication and tourism). As India has come to be the outsourcing hub in the region, most MNCs (and even smaller enterprises) have begun to heavily outsource not just their call centres and customer services but also back-end business process operations.<sup>25</sup> This includes services such as routine data-entry, crunching and handling, research and development activities, patent writing, financial portfolio analysis, medical transcriptions, payroll management, product design, accounting and book-keeping, processing of tax returns and insurance claims, and legal transcriptions.

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<sup>23</sup> The World Health Organization (WHO) has not included the Philippines, Brunei Darussalam, Japan, China and Korea are not listed, since prevalence is below 100 per 100,000 population.

<sup>24</sup> Rahul Sen, Mukul G. Asher and Ramkishan S. Rajan, 'ASEAN-India Economic Relations: Current Status and Future Prospects', *Institute of Southeast Asian Studies* (April 2004).

<sup>25</sup> *Ibid.*, p.15.

Despite the growing importance of information and communication technology, there are other services that are crucial to the future development of the economies of India and ASEAN and that offer mutual benefits as a consequence of greater cooperation. These fields include food security and energy. With regards to food security, India could support ASEAN countries in agricultural research and biotechnology. These areas of study have gained considerable importance over the past years, since improved methods in food production provide prospects of producing adequate amounts of food for populous states. By simply relying on traditional food production several states would most likely sooner or later face severe food supply shortages. However, benefits from cooperation in food related issues will not be one-sided since some ASEAN countries have attained expertise in fields such as deep-sea fishing (Thailand) and palm oil production (Indonesia and Malaysia). In the case of the latter, India is heavily dependent on palm oil and oleochemical for consumption purposes. Furthermore, the two parties could benefit from mutual cooperation in research and development, to engage in more value-added production activities.

With regard to energy, countries such as Indonesia, Malaysia and Brunei Darussalam provide prospects for mutually beneficial cooperation. This is possible in activities such as oil and gas exploitation and down-stream processing activities. Cooperation in the area of civilian nuclear power as a source of energy is another possible area for cooperation. Countries, such as Malaysia, are keen to explore the use of nuclear energy as an alternative source of energy and with India's expertise in this area it would be able to contribute. India's engagement in this field could help ASEAN achieve sustainability in energy supply. Various projects are being conducted in which India might support ASEAN nations, such as the Trans-ASEAN Gas Pipeline (TAGP) networks or the ASEAN Highway (AH) Network. Also, the Asia-Pacific Energy Cooperation (APEC) is a long-term project in which India can play an important role.

India's potential as a tourist destination is severely under-utilised. The target for visitors from ASEAN to India has been set to one million in 2010. Given that this number had only been 332,925 in 2008, this year's target will pose some challenges.<sup>26</sup> According to Sen, Asher and Ramkishen, India is neglected as a travel destination for ASEAN citizens due to the lack of an integrated approach that makes visiting India's vast geography and its diverse culture quite difficult.<sup>27</sup> It has been suggested that simplifications in the visa system could contribute to the growth of the tourist industry. Tourism to India has been mainly concentrated in metropolitan areas and tourists from East Asia only account for slightly above seven per cent of all tourists. Since India is highly interested in promoting development in rural areas, tourism could act as a suitable catalyst to direct investment to infrastructure in these areas. The

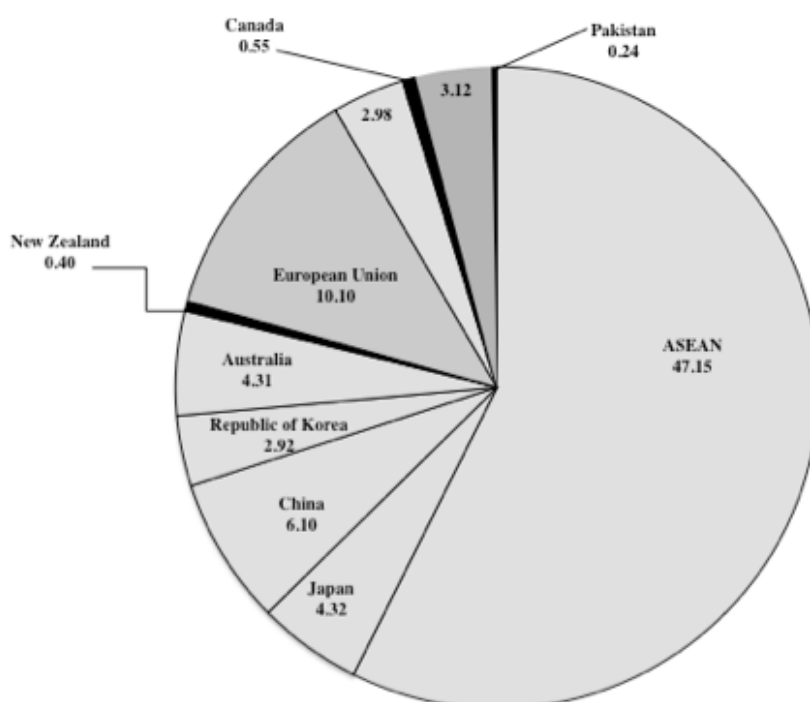
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<sup>26</sup> 'India Tourism Statistics 2009', *Government of India, Ministry of Tourism, Market Research Division*, <http://tourism.gov.in/statistics/Stat09-eng.pdf>. Accessed on 6 May 2010.

<sup>27</sup> Rahul Sen, Mukul G. Asher and Ramkishen S. Rajan, 'ASEAN-India Economic Relations: Current Status and Future Prospects', *Institute of Southeast Asian Studies* (April 2004).

positive effects arising from an increase in tourism can only be realised if the Indian government boosts the promotion of visiting. It is also necessary to allocate more investment toward infrastructure in remote areas. Vice versa, India is not among the top origin countries of tourists travelling to ASEAN countries. The largest share of tourists visiting ASEAN states in 2009 originated from other ASEAN member countries (42 per cent), while only slightly more than three per cent originated from India (see Figure 5).<sup>28</sup>

**Figure 5: Tourists into ASEAN by Country of Origin**



**Source:** 'Tourism Statistics', *ASEAN Secretariat*, [www.aseansec.org/stat/Table29.pdf](http://www.aseansec.org/stat/Table29.pdf). Accessed on 6 May 2010.

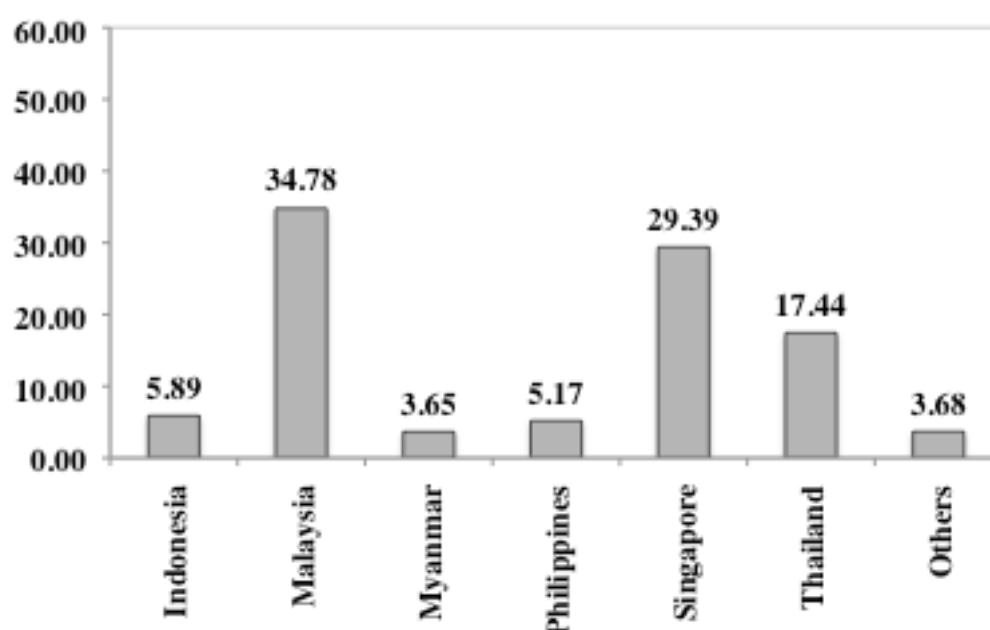
As an effort for improvement, India has opened up air travel for ASEAN carriers and granted them 21 direct connections as well as unlimited landing clearance in four metropolitan cities during peak travel months.<sup>29</sup> These changes are highly important since airfares between India and ASEAN were among the highest on a per air-mile basis and a higher competition of these routes will lower passengers' costs considerably and, thereby, raise India's attractiveness as a travel destination. The fact that the number of tourists to India has increased considerably over the past three years gives reason to expect further increases the more tourism is facilitated (see Figure 6).<sup>30</sup>

<sup>28</sup> 'Tourism Statistics', *ASEAN Secretariat*, [www.aseansec.org/stat/Table29.pdf](http://www.aseansec.org/stat/Table29.pdf). Accessed on 6 May 2010.

<sup>29</sup> Rupa Chanda and G. Sasidaran, 'Understanding India's Regional Initiatives within Asia', ISAS Working Paper No.48 (15 August 2008).

<sup>30</sup> Bureau of Immigration, India.

**Figure 6: Country-Wise Shares in Tourist Arrivals to India from Southeast Asia, 2008**



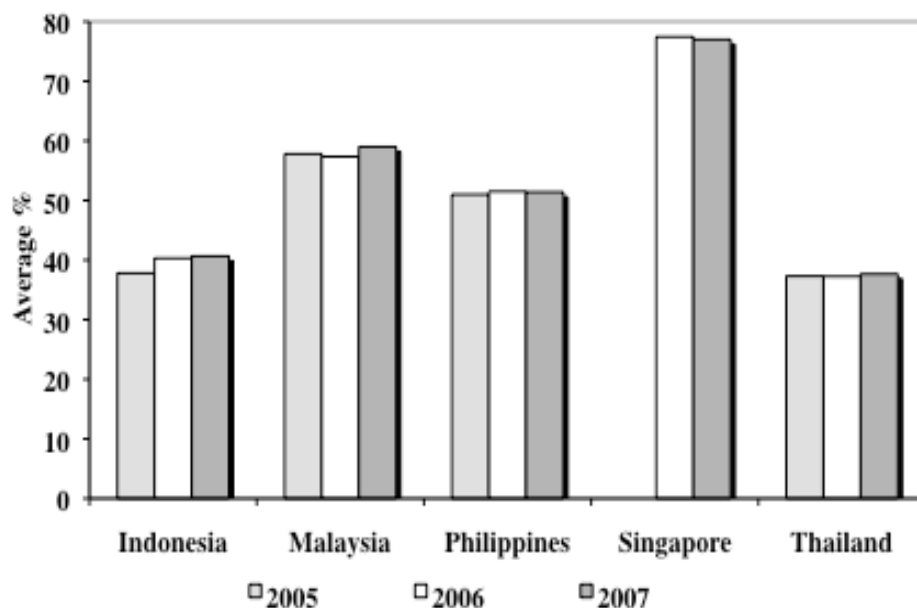
**Source:** 'India Tourism Statistics 2009', Government of India, Ministry of Tourism, Market Research Division, <http://tourism.gov.in/statistics/Stat09-eng.pdf>. Accessed on 12 May 2011.

De and Raychaudhury (2008) has also found a close correlation between the export in services and poverty reduction.<sup>31</sup> In his study, Raychaudhury found that a one per cent increase in service exports would result in a seven per cent increase in per capita income. Thus, by enhancing their cooperation in services, India and ASEAN members would be able to reduce poverty among the population and improve living standards. As the service sector accounted for about half the entire production in 2007-08 and provided about two-thirds of employment in India, enhancing cooperation in this field, therefore boosting these sectors will affect a large share of the population. In the ASEAN-5 states, employment in the service sector rose from 45 per cent to 53 per cent on average from 2005 to 2007(see Figure 7).<sup>32</sup>

<sup>31</sup> Prabir De and Ajitava Raychaudhury, 'Is India's Services Trade Pro-Poor? A Simultaneous Approach,' *Macao Regional Knowledge Hub*, Working Papers No.16 (December 2008).

<sup>32</sup> World Bank. For Singapore, no data was available for 2005.

**Figure 7: Employment in Services**



**Source:** Author's chart created using *World Databank*, <http://databank.worldbank.org>. Accessed on 12 May 2011.

As incomes rise, household consumption will also be boosted. Thus, the Indian economy will face an upswing accompanied by more investment and consumption that in turn will spur even more demand. However, Raychaudhury also finds that while poverty decreases, the unemployment rate and inequality will increase, due to the fact that most service exporters are situated in metropolitan areas. Within the urban areas, inequality will rise as service exporters are able to gain large profits and pay higher wages while other enterprises might not be able to follow this trend. Regional disparities have increased over the past several years and if India and ASEAN enhance their cooperation in services these disparities are likely to increase further. The Indian government should strengthen investment in rural areas to avoid these disparities from becoming too large. Additional education and advanced vocational training programs could help to prepare workers for these possible challenges.

Even though India has enormous potential for trade in services, Malkani and Shah mention several factors that could hinder a smooth development in service.<sup>33</sup> The growing Indian population will face a geographical mismatch in the upcoming years as the work force will continue to grow – the Indian population is expected to hit roughly 1.35 billion by 2015 – but the share of skilled workers will decline and the concentration will be in agriculture and the unorganised sector. These facts underline that the Indian government will need to broaden investment into human capital and the development of remote regions in order to exploit the full potential of closer cooperation with ASEAN states.

<sup>33</sup> The following arguments are cited from Rohini Malkani and Anushka Shah, 'India Macroscopic: India's Growing Labor Force - Boon or Bane?', *Monthly Monitor, Citigroup Global Markets* (23 July 2010).

The agreement recently signed by India and ASEAN states only covers trade in goods and there is little doubt that it will be followed by one in services. Taking into account the discussion of possible benefits from enhanced cooperation in services it is only natural that the Indian Commerce and Industry Minister, Anand Sharma, in a meeting with the Singaporean Trade Minister, Lim Hng Kiang, in early July 2010, called for an agreement on services and investment.<sup>34</sup> This call did not come unexpectedly as in January 2010, ASEAN deputy Secretary-General said that the first agreement was not the end of the road but instead an agreement on services in trade should also be completed later that year.<sup>35</sup> Prospects for such an agreement seem quite possible at the moment and chances are quite high that it will be signed in the near future.

### **Other Areas of Engagement**

Areas such as security, the environment and infrastructure do not directly impinge upon trade in services, yet they cannot be ignored. First, these issues, although peripheral to trade and economic cooperation, hold the potential to be constraining factors if not addressed constructively. Second, security and infrastructure provide the foundation for effective trade in goods and services. Third, there are economic opportunities that can emerge through activities in these areas, especially with respect to environment and infrastructure.

The 1,600 km border shared by Myanmar and India is a useful example of the intersection between security and economic spillovers. The recently signed FTA (the AIFTA) will most likely boost regional trade in this border region and, therefore, contribute to the development of India's northern provinces. However, this will not be possible unless the underlying security issues are effectively managed. James R. Roulngul argues that unless the infrastructure, communication, industries and agriculture throughout India's northeast have to be developed first before trade relations can flourish.<sup>36</sup> Since the region is rich in resources and is of strategic importance, the development of infrastructure is a necessary component of any development process. While this region is a possible route through which India's engagement with ASEAN can progress, a precondition for this is the satisfactory development of the north-eastern states in India. Amita Batra argues that India's northeast can only optimally profit from the AIFTA when it is 'lifted out of its current economic equilibrium first.'<sup>37</sup> Chanda and Sasidaran point out that China has gained influence in Myanmar and the AIFTA can, perhaps, be used as a platform to foster those India-Myanmar ties. The full benefits of the AIFTA cannot be reaped unless India maintains a secure border with Myanmar but it also has to manage China's early engagement with Myanmar.

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<sup>34</sup> 'India for early investment, services pact with ASEAN', *The Economic Times* (10 July 2010).

<sup>35</sup> Veeramalla Anjaiah, 'India, ASEAN must "enhance connectivity" to reap benefits', *The Jakarta Post* (23 January 2010).

<sup>36</sup> James R. Roulngul, 'India-ASEAN FTA: Implications for India's Northeast', <http://www.articlesbase.com/authors/james-r-roulmgul/82285>. Accessed on 8 October 2010.

<sup>37</sup> Amita Batra, 'India-ASEAN FTA: A Critique', *IPCS*, Issue Brief No. 116 (September 2009).

There are at least two points of entry for India to penetrate into the Southeast Asian market. One point would be through ASEAN member states that surround the Straits of Malacca. The states that are clustered around this area include the older ASEAN members, which are the more developed economies. The other strategic point is via Myanmar. Myanmar has the possibility of being a very important market in the long-term, after it opens up more freely to trade and gains a more stable political structure, viewed in this perspective connectivity and ties with Myanmar become significant.

The creation of infrastructures is an excellent instrument through which India can engage with ASEAN, while also laying the foundation for further economic relations. The building of the Trilateral Highway Project (THP) linking India and Thailand through Myanmar is a good example of India's engagement in Southeast Asia. The project was first launched under the Mekong Ganga Cooperation and was later incorporated into The Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (known as BIMSTEC). Several problems have hindered the completion of this project. They include financial restrictions which have prevented central parts of the highway from being constructed. Besides, issues along the Indian-ASEAN border such as illegal trade, drug trafficking and insurgencies continue to hamper cooperation. But other considerations weigh over purely economic figures. China claims that the region of Kachin as its own and it has a strong influence there. Further, completing the highway might also flood the area with Chinese goods and weapons. These concerns go against India's security interests and would contribute to a reluctance to proceed with the construction of the highway, notwithstanding the undeniable economic advantages. However, as India is Myanmar's second largest export market accounting for 12.3 per cent of its total exports,<sup>38</sup> its interest to broaden economic ties should be pronounced.

However, the THP combines India's economic interests with strategic objectives. The THP will encourage the economic development of India's north-eastern states and it will secure trade routes that will create a link with the western part of Southeast Asia. By strengthening infrastructure links with Myanmar, India will ultimately be able to gain easier access by land to Thailand. It will also contain China's rising influence in that region. As Pate argues, the completion of this project is crucial for the realisation of India's 'Look East Policy' while a failure will very likely be interpreted as a failure of the Indian-Asian integration.<sup>39</sup> Apart from the completion of the highway, a closer cooperation between ASEAN and India will show their interest in the peaceful management of future power balance in Asia.<sup>40</sup>

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<sup>38</sup> Thailand is the most important export market and accounts for 52 per cent of Myanmar's total exports. See, *CIA World Factbook* (2010), [www.cia.gov/library/publications/the-world-factbook/geos/bm.html](http://www.cia.gov/library/publications/the-world-factbook/geos/bm.html). Accessed on 12 May 2011.

<sup>39</sup> Tanvi Pate, 'India-Myanmar-Thailand Highway', *IPCS*, Article No. 3115 (6 May 2010).

<sup>40</sup> Prashanth Parameswaran, 'Strengthening ASEAN-India Relations in the 21<sup>st</sup> Century', *Project 2049 Institute*, (27 May 2010).

Roulngul argues that the AIFTA will not be able to achieve its goals unless this region is developed and becomes the centre of Indian-ASEAN trade. Although, it might be true that India's north-east will not become the 'gateway' of trade unless the region is developed with a stable infrastructure, such an argument misplaces the importance of that part of the region; and it might be an exaggeration to perceive it as being the centre of Indian-ASEAN trade. Trade has long been conducted through seaports and it will most likely continue to be done in that way. Indeed, trade will expand with lower tariff rates and with the removal of other trade barriers. The development of the northeast will provide additional trading routes but will not displace trade through seaports or airports.

With regard to security issues, especially ASEAN members bordering the Malacca Straits, have a growing common interest in securing the sea trade routes, reducing piracy and fighting terrorism. As an example, Singapore and Malaysia have signed maritime security treaties with India, these being the two states that have invested the most in India.<sup>41</sup> Thus, along with Indonesia and the Philippines, these ASEAN countries have the strongest interest in ensuring that trade along the Straits of Malacca can function without disruption. India's interest in this regard was demonstrated by its naval forward presence of joint operations and compatibility with Southeast Asian navies.

A crucial aspect of India's engagement with ASEAN can be accomplished through initiatives to close the development gap among the less developed Southeast Asian states. In particular, India can take part in helping ASEAN members such as Cambodia, Myanmar, Laos or Vietnam (CMLV states) to catch-up and close the development gap with 'older' ASEAN members. India has undertaken efforts to improve living conditions in Indochina. This functional cooperation includes human resource development, science and technology, health and pharmaceuticals, transport and infrastructure, information and communication technology, agriculture, energy and people-to-people exchanges. These initiatives are funded by the ASEAN-India Fund (AIF).<sup>42</sup> For example, it financed the establishment of entrepreneurship development centres (EDC) and Centres for English Language Training (CELT) and granted credits especially to the poorer CLV (Cambodia, Laos and Vietnam) ASEAN member countries. In general, the cooperation is conducted under the framework of the ASEAN-Indian Partnership for Peace, Progress and Shared Prosperity adopted in November 2004.

According to Trewin, it is essential for less-developed ASEAN members to receive substantial capacity building in infrastructure and establish institutions in order to successfully join in the liberalisation process. It would be in India's favour to contribute to the process of capacity building. Yet, it may not be practical to expect India to support ASEAN's capacity building, since India had a per capita GDP of 46,116 (approximately

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<sup>41</sup> Rupa Chanda and G. Sasidaran, 'Understanding India's Regional Initiatives within Asia', ISAS Working Paper No.48 (15 August 2008).

<sup>42</sup> 'ASEAN-India Dialogue Relations', *ASEAN*, [www.aseansec.org/14802.htm](http://www.aseansec.org/14802.htm). Accessed on 22 March 2011.



US\$980) in 2008.<sup>43</sup> This figure is much lower than the average per capita GDP in ASEAN, which amounts to US\$6,565.21.<sup>44</sup> Comparing the per capita GDP across ASEAN countries and India, India ranks among the lower income countries. Notwithstanding this fact, attempts should be made, where possible to contribute towards the capacity-building process of ASEAN, particularly of those who are at the lower stages of development. The CLMV countries are prime targets for such capacity-building efforts.

In the light of India's technical expertise, it is possible for it to cooperate in the areas of natural disaster forecasting and relief. As was seen in 2004, when the tsunami hit Indonesia, joint action eased the burden on India. Since most ASEAN members have large shares of their population living along coastlines and depending on agriculture and fishing, natural disasters can easily wipe out the livelihoods of these people. Rising sea levels, tropical storms, droughts and heat waves can deteriorate agricultural production in India and ASEAN states substantially. Thus, the two parties could benefit from concerted preventive measures and enhanced environmental protection. Such actions will also be favourable to the tourist sector since rising sea temperature causes, for example damage to diving sites and thereby hinders tourists from spending their holidays in the region. By initiating joint action against climate change this will reduce the number of natural catastrophes. It will also ensure that agricultural production is sustained and maintaining a sufficient supply of food.

Although not directly linked to the AIFTA, Rupa and Sasidaran argue that India has a strategic interest in fostering relations with Japan as it could support Japan in securing trade routes through the Indian Ocean. This route is important for Japan, as its trade flows and energy supply follow this path. In return, India needs Japan's support in order to lift international restrictions on civil nuclear trade with India.<sup>45</sup> Another noteworthy point is that India's own need for energy is also constantly increasing and has led India to enter negotiations with most parts of the world including the European Union (EU), the United States (US), energy-rich African states, Latin America and the Gulf region. In a certain sense, Japan's cooperation will help India explore the nuclear option for its energy needs in the long-run. Quite clearly, both Japan and India have an economic interest in ASEAN. This suggests, as we will be discussed in what follows, that an architecture that involves both countries may be to the mutual benefit of the region.

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<sup>43</sup> According to the exchange rate of 20 July 2010.

<sup>44</sup> The CIA *World Factbook* and *Asian Development Bank*. When calculated as the total GDP of ASEAN divided by its total population, the per capita GDP is only US\$2,582.64. This substantial difference is due to the comparatively high per capita income in Singapore contrasting the low per capita incomes in most other ASEAN countries.

<sup>45</sup> Rupa Chanda and G. Sasidaran, 'Understanding India's Regional Initiatives within Asia', ISAS Working Paper No.48 (15 August 2008).

## **Future Prospects of ASEAN Integration**

The AIFTA has obvious advantages for India because it can now import products from ASEAN more cheaply than before. Furthermore, India can diversify trade ties and enlarge its export market by an additional 600 million consumers, thereby reducing its dependence on the EU and the US as delivery markets. As ASEAN started engaging in international trade earlier than India, they are much more integrated into the world economy. India has enhanced its activities toward more integration and engagement in global trade and ASEAN could serve as a multiplying force for India to catch up. Concerning trade agreements, India only recently began to pursue bilateral negotiations, as it had to follow up on the international trend towards regionalisation. ASEAN also profits for a trade agreement with India as it can serve the extensive Indian demand.

However, there are not only economic but also political aspects to the AIFTA. Firstly, ASEAN wants to attain more bargaining power on the international stage. In the past years, ASEAN signed FTAs not only with India, but also with China, South Korea and Japan (November 2007). Thereby, ASEAN has managed to strengthen its ties with all of the major powers in the region. As the US hegemony diminishes these are the powers that will determine the change in the global power distribution.

For ASEAN, it is important not to be marginalised by the four large powers surrounding it. By signing FTAs with all four major regional powers, ASEAN is able to ensure that it will not be left out regardless of which of the four countries assume leadership over the region. Additionally, China has increasingly gained influence in Asia over the past decades. Thus, ASEAN has to counterbalance this growing influence by strengthening its ties with India. This action seems necessary since not only economic ties but also socio-cultural ties are strong with China as many overseas Chinese live and work in Southeast Asia<sup>46</sup>. India does not enjoy the same advantage since the Indian diaspora, as Asher et al. argue, does not enjoy a strong political position and has thus not had much influence on Indian-ASEAN relations and investment flows. Rather there seems to be a trend of emigrating professionals and specialists of Indian origin especially from countries such as Singapore and Malaysia.<sup>47</sup>

The implementation of India's 'Look East Policy' has coincided with China's rise and growing global influence. This policy has also taken shape at a time when Southeast Asia has emerged as a vibrant market. As India is geographically located to the west of the Asian region, it could be legitimately concerned that it would be excluded from the benefits of a dynamic market. Although, relatively, ASEAN countries are small India would not want to be 'left out' of the integration process. This brings into question the mechanism through

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<sup>46</sup> With more than 28 million Chinese living on Southeast Asia, that accounts for 70 per cent of all overseas Chinese.

<sup>47</sup> Mukul G. Asher, Rahul Sen and Sadhana Srivastava, 'ASEAN-India: Emerging Economic Opportunities', *Centre for Freedom and Development Studies* (May 2001), [www.cpsindia.org/emergingeconomic.htm](http://www.cpsindia.org/emergingeconomic.htm). Accessed on 22 March 2011.

which India can engage with ASEAN.

With regard to the prospects of future integration in the region, a more fundamental question is that of ASEAN's future integration. It must be recognised that the ASEAN Secretariat is not a decision-making body. Indeed, ASEAN functions on the basis of a loose cooperation among member states. Since these states have different levels of development and varying degrees of engagement with China, there are some issues where they have common challenges. The effects of China's investment in the high-speed train running from Kunming, China to Singapore cannot be discounted. While connectivity will be improved between China and ASEAN, the threat of an excess supply of Chinese goods will be an issue to be confronted. Also, the undervaluation of the Chinese yuan against the US dollar hampers the competitiveness of the less-developed ASEAN states such as Cambodia and Laos, presenting ASEAN and the US with a common challenge. Thus, the US and ASEAN have a common interest in pressuring the Chinese government to revalue the yuan. States such as Malaysia and Indonesia are no less susceptible to the effects of an undervalued yuan. A revaluation might also help to improve the trade balance of states as Indonesia with China that changed from a surplus in 2003 to a trade deficit in 2008 because China rose up the value chain unexpectedly fast and is increasingly attracting FDI away from Southeast Asia.<sup>48</sup> These issues present an argument for a more consolidated common position in ASEAN. They also point to the need for an approach that has a wider cooperative framework.

The ASEAN+6 approach provides the basis for a broader degree of involvement in the region. This will allow ASEAN to pursue its objectives while also drawing upon the resources of New Zealand, Australia and India. The +6 approach includes all the major players in Asia, but the same concerns that plague ASEAN+4 cannot be discarded. As long as ASEAN itself does not follow a common approach, enhance regulatory frameworks and create tighter integration among its own members, it will be difficult to conceptualise its cooperation with six powerful economies. Nevertheless, this framework offers the best opportunity for responding to future challenges, without forsaking the opportunities that abound.

The foreign ministers of the ten ASEAN member states have been discussing an expansion of the East Asian Summit to include Russia and the US States. This move offers the possibility of counteracting the rising Chinese influence in the region. The engagement of the US and Russia in regional affairs would significantly increase the importance of the East Asian Summit. Such an expansion would provide for an ASEAN+8 framework, but as Daly argues, it would perfectly fit into the ASEAN strategy, 'remain independent, keep linking up, build off from existing points of agreement, remain pragmatic.'<sup>49</sup> Daly even argues that the consultative body of ASEAN+8 might be the only chance to fill the strategic and power

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<sup>48</sup> Sean Daly, 'Obama's ASEAN Policy Looks Auspicious', *Policy Innovations* (19 May 2010), [www.policyinnovations.org/ideas/commentary/data/000189](http://www.policyinnovations.org/ideas/commentary/data/000189). Accessed on 15 September 2010.

<sup>49</sup> *Ibid.*

vacuum created after the end of the Cold War in South China Sea. In May 2010, a US trade representative had also named the ASEAN states to be the most important destination for US direct investment, with the investment being three times larger than that in China and ten times that in India. Also, the US seeks a transpacific agreement to further foster relations with Asia in the upcoming years.<sup>50</sup>

Asher, Sen and Srivastava argue that India should approach ASEAN in two ways. On the one hand, it should enhance its cooperation with ASEAN as an organisation. On the other, it should seek further bilateral and country-specific engagement with ASEAN's members. The reason for this two-track approach is that ASEAN as an organisation was not granted much authority and hence decisions and agreements signed by ASEAN might not result in the close cooperation envisaged in the beginning. This fact might provide an answer to why India continues to seek bilateral FTAs with ASEAN members despite the fact that the AIFTA has come into effect in January 2010. However, they conclude that the potential of bilateral cooperation between India and ASEAN states will not be fully realised as long as far-reaching political commitments are not made, especially in Thailand and the Philippines.<sup>51</sup>

According to Batra, the best route to follow for India is via an ASEAN+1 alignment first. As this has been put into place in form of the AIFTA one could argue that the next step lies in the formation of ASEAN+4. However, the question arises whether the creation of the AIFTA or its completion – which is set for 2016 – should be seen as the point after which the creation of ASEAN+4 seems appropriate. When following an ASEAN+1 alignment India should enhance its already existing cooperation with ASEAN members in initiatives such as the Mekong-Ganga Cooperation Initiative on tourism, culture and development. This approach would give India the chance to improve its relations with the subregions of ASEAN and might gain support for projects on broader scale. At a more practical and immediate level, India can realise these goals by organising more visits of high-level politicians and representatives to and from India and by providing substantial scholarships to students and research fellows to strengthen sentiment of common cultural heritage. Certainly, increasing the trade volume with ASEAN subregions is also a fundamental part of enhancing cooperation.

Also, domestic reforms are needed to maintain current growth rates in the future but implementing such reforms will demand many resources and will delay negotiations on cooperation. Along these reforms are changes in the bloated, inefficient and corrupt Indian bureaucracy, infrastructure investment and institutional fixes to enhance competitiveness and boost export resilience. Last but not least, grassroots connections between Indian and ASEAN citizens must be strengthened to ground cooperation and relations not just on

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<sup>50</sup> Lalit K. Jha, 'US FDI: ASEAN beats China and India', *Rediff* (4 May 2010), <http://business.rediff.com/report/2010/may/04/us-fdi-asean-beats-china-and-india.htm>. Accessed on 22 March 2011.

<sup>51</sup> Mukul G. Asher, Rahul Sen and Sadhana Srivastava, 'ASEAN-India: Emerging Economic Opportunities', *Centre for Freedom and Development Studies* (May 2001), [www.cpsindia.org/emergingeconomic.htm](http://www.cpsindia.org/emergingeconomic.htm). Accessed on 22 March 2011.

agreements signed by the governments but also on the will and support of the people. Partnerships of universities, businesses and art institutions are needed to boost mutual understanding.

On the part of ASEAN, it might show its goodwill towards India by supporting India's request of membership in the APEC in the APEC convention in November 2010 or allowing India to join the Chiang Mai Initiative Multilateralisation (CMIM) Agreement.<sup>52</sup> Since India's as well as ASEAN's interests are related to maritime security issues – be it securing the Malacca trade routes, securing sea-related food production or managing China's rising naval build-up – this area would be an ideal issue to start with.

## **Concluding Remarks**

This paper has tried to explore the future prospects of Indian-ASEAN relations. The agreement on trade in goods that came into effect at the beginning of 2010 was possibly a starting point in this respect. The next stage in India's economic relations will be to seek completion of an agreement on trade in services. This is an area in which India's contribution to the region can be fully realised. Even though services prove to be a very good starting point to enhance cooperation further, there are several political as well as organisational obstacles that have to be resolved before India and ASEAN can take their cooperation to the next level.

On the one hand, an agreement on services trade would be well advised, since it might help to overcome the bias in benefits from the current agreement towards ASEAN states. On the other hand, ASEAN states need to come to terms with the direction in which ASEAN integration will precede. If this question remains unsolved, it is unlikely that ASEAN states will be able to represent themselves as one body in global negotiations. Nevertheless, given their different levels of development, India will have to engage with the states with due consideration to their economic conditions.

In addition to the possibilities that India can find within the services sectors of the respective ASEAN member states, there are other areas for cooperation. These areas include capacity building and the improvement of connectivity through infrastructure development. India's technical expertise can also be extended to ASEAN by cooperating in disaster forecasting and management. Indeed, India's engagement with ASEAN should be comprehensive and wide-ranging. Nevertheless, the question of how this involvement will be executed depends on the framework that is selected. The two options that are possible are ASEAN+4 and ASEAN+6. Since there are political barriers that may have to be overcome in accessing these regional

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<sup>52</sup> Prashanth Parameswaran, 'Strengthening ASEAN-India Relations in the 21<sup>st</sup> Century', *Project 2049 Institute*, (27 May 2010). This agreement came into effect in March 2010 and membership is restricted to ASEAN+3, thus far.

architectures, it would be to India's benefit to initiate its engagement with ASEAN member states on a bilateral basis. This will give India the opportunity to build a firm basis for involvement with ASEAN regardless of the framework that eventually emerges.

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