Rise of China and India
Implications for the Asia Pacific

Edited by
AMITABH MATTOO
MALLIKA JOSEPH
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Australia India Institute

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FAROOQ SOBHAHN

NIHAL RODRIGO

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CHAPTER 11

Rise of China and India: Implications for Pakistan’s Economy and Environment

VAQAR AHMED

INTRODUCTION

Pakistan has borders with four countries out of which three happen to be giants in terms of land size, economy and population. These include China, India and United States (by virtue of being in Afghanistan since a decade). This has implied raised expectations from neighbours who at most times in history were not on congenial terms with each other and Pakistan was supposed to play a mediating role (Van Hollen 1980). There are proportions of elite in Pakistani society that are tilted towards US and others towards China. Similar skewed preferences are seen while formal institutions try to align themselves with one pole or the other. Such institutions primarily include the civil service and military (Shah 1997). A growing realization among these institutions is now about to make Pakistan more relevant to South Asia and offer Pakistan as an economic corridor in the region (Ahmed 2010, GoP 2008).

India has been a more recent entry into Pakistan’s favoured foreign policy priorities. A large part of the credit goes to the civil society organizations and business community which had the foresight to bring two traditional battlefield enemies together in the pursuit of boosting regional trade, investment and thereby address the common enemy of both countries i.e., poverty and widespread inequality. Pakistan’s recent grant of most favoured nation status to India for trading purposes and India’s readiness to allow foreign direct investment from Pakistan are both welcome moves, which however
remain incomplete due to pending issues of non-tariff barriers including movement of people (Hussain and Ahmed 2012).

Most country-specific simulations envisage this region to be on its course to becoming an interesting neighbourhood in terms of vast natural resources, large domestic demand, youth bulge (at least in South Asia), rising remittances and interests of Diaspora, and future prospects of increased regional trade which in turn can be a catalyst in maintaining stability and peace in the region. This is also visible through the two purely macroeconomic indicators exhibited in Figures 11.1 and 11.2 and demographic-cum-economic indicators exhibited in Figures 11.3 and 11.4.

The macroeconomic indicators explain that while Pakistan’s recent economic performance was well below that of China and India, the pattern of movement of real gross domestic product (GDP) growth was similar. This is particularly true for the decade of 2000s. Similar pattern is also observed in case of services sector growth in this region. The services sector growth represents the potential of a country to jump to advanced market structures, availability of sophisticated manpower, ability to build global linkages through transport, communication, banking and insurance channels. In 2011 Pakistan’s services sector contributed to over 50 per cent of GDP. Similar rise of services sub-sectors contributed to record high growth rates for India in the recent past.

This similarity of growth rates and sectoral distribution of growth (not intentionally brought about) now provides increased possibility for these countries to complement each other’s production structures given the similar population preferences. There is high movement of people migrating from rural to urban areas and it is the urban centres which are now becoming engines of national and sub-national growth. Also interesting to note is the phenomenon of convergence in urban population growth rates across the three countries. The other interesting feature is the similarity in movement of household consumption expenditure growth rates which now makes a compelling case for these countries to boost trade in complementarities. While Pakistan has faced a more volatile consumption pattern, however for the past two years the trend for these countries has been converging. The large population within these countries (and resultant
Figure 11.1: Economic Growth 1961–2011

Figure 11.2: Services Sector Growth 1971–2011
Figure 11.3: Urban Population 1960–2011

Figure 11.4: Household Consumption Expenditure Per Capita

Source: World Development Indicators.
domestic demand) to some extent have reduced the impact of global financial crisis on these economies (Ahmed and O'Donoghue 2010).

This paper tries to position Pakistan's opportunities and challenges amidst the rise of China and India as regional powers in Asia-Pacific and their global outreach particularly in economic spheres. While several strands in literature usually explain Pakistan's importance to both countries in terms of connectivity of China and India with Africa, Europe and Central Asia (Sachdeva 2006), this paper while recognizing the connectivity argument (in the next section) goes beyond such strategic simulations and also explains some short to medium term prospects whereby China and India can engage with Pakistan and vice versa. We then go on to explain that rising demand owing to economic and population growth may deteriorate environmental outlook which in turn can threaten the foreign policy relations. The scarce resource sharing (particularly water) between for example India and Pakistan will continue to be a concern. Similarly China's current structure of economic growth and its climatic costs (particularly with respect to construction activity in Xinxiang) may be an environmental threat to Pakistan as well. Such concerns have been highlighted under non-traditional security threats in this region (Ramay and Saleem 2012).

However, we also highlight in this paper the opportunity in case of energy sector whereby both India and Pakistan are now starting to think on possible ways in which cross-border energy trade can take place. Finally the paper will conclude with strong recommendations to base the future relations between these three countries on the pillars of sustainable development whereby growth processes in each country complement the efforts in other countries and South Asian region and China as a whole. The region will collectively need to realize that while economic growth will take centre-stage in order to absorb the growing labour force in the region, however, the equity and environmental concerns can no longer be ignored. Similarly it is also time where the world's 1st, 2nd and 5th biggest populations cannot continue to have closed borders for their youth and communities to interact. The movement of people (more important than just labour) should be a priority agenda for these countries to move forward.
CONNECTING PEOPLE AND PLACES

As Asia takes a centre-stage in the recovery from global financial crisis, emerging markets are innovating ways in which they can connect with each other and reap benefits of regionalism. Such endeavours are being seen in the form of Asian highway network, economic corridors in East and South Asia (Woodburn et al. 2008).

In June 2012 Pakistan’s railways authorities participated in Economic Cooperation Organization’s (ECO) meeting. Iran, Pakistan and Turkey vowed to bolster rail links in the coming months and perhaps the most interest lies in the recommencement of Islamabad–İstanbul (via Tehran) cargo service. Pakistan’s business community has been pressing for such a link for a long time now and they also participated in the meeting in order to ensure that such a service is punctual and regular.

Similarly in 2011 Pakistan’s government officials led by the president visited China for discussing the rail and road links through Pakistan which could give Chinese freight access to the Arabian Sea and from there onwards to Middle East and Europe. China has since long shown its interest in the development of Gwadar port in Balochistan province of Pakistan and also to make investment in improving Pakistan’s rail and road networks that will link Chinese border with Gwadar port (Haider 2005). The Chinese government is of the view that the road and rail link between Gwadar–Khunjarab–Urumqi can save Chinese merchandise seven trading days if compared with the current route from Shanghai and Malacca Straits. In quantitative terms Chinese merchandise from Urumqi through Gwadar going up to Dubai and London becomes 4,300 miles shorter. Similarly while the distance from Dubai to Shanghai via Indian Ocean is 9,000 miles, the distance from Dubai to Khunjarab is 3,300 miles.

The Planning Commission of Pakistan despite a current volatile security advisory in Balochistan has expedited the road sector projects in the province. These include work on the 193 km Gwadar–Turbat–Hoshab, 453 km Hoshab–Panjgur–Naag–Basima–Sorab, 414 km Hoshab–Awaran–Khuzdar, 110 km Basima–Khuzdar, and 242 km Khuzdar–Shahdadkot (Planning Commission 2012). Since
July 2011 Pakistan China Business Forum has been active in organizing business promotion fares in Kashgar in order to sensitize the wider Chinese business community regarding the developments on Pakistan side which may benefit China. Rayaan Air, a Pakistani Charter Airline has also started a 90 minutes Islamabad–Kashgar cargo flight.

In Pakistan the private sector from China has been active for some time now and according to the 2011 data there were almost 13,000 Chinese working in 120 enterprises in Pakistan. China also agreed to manage the operations at Gwadar Port once the agreement with Singapore Port Authority expired. Pakistan plans to seek further assistance from China in order to equip Gwadar Port for receipt, dispatch and processing of crude oil, gas, and liquefied natural gas for onwards shipment to South-East Asia and the far-East. However actual on-ground implementation of this detailed plan is now awaiting peace and stability in Balochistan.

During the China–Eurasia Expo 2011 it was also realized by the Chinese and Pakistani governments that in order to maintain and increase the trade flow, the existing Karakoram Highway that links the two countries needs to be upgraded. China has already agreed to support the 411 km Havelian–Khunjrab railroad inside Pakistan, and establishment of fibre optic link across the border is at the feasibility stage.

Sadly due to the past baggage of political insecurity, the progress with India is much more recent and at a much lesser pace if compared with China. For India, lets take the case of Thar Express—a rail passage which links Sindh with Rajasthan. Despite both governments investing heavily into this cross border rail link since 2006, it is usual for this train to see delays and operational inefficiencies making it irrelevant for the business community. There are vast numbers of businesses that are envisaged to gain from this link. These are mainly Sindh-based concerns that intend to trade with Maharashtra and Gujarat and currently use the Mumbai–Karachi sea route. A more efficient rail link here will allow cargo to reach dry ports in under 24 hours and at less than half the cost. Similarly the World Bank also noted that it costs US $550 (at 2006 prices) to ship merchandise container from Mumbai to Karachi versus
US $325 if the same container is sent through Delhi–Wagah (WB 2004, Ahmed et al. 2010).

Another case that may be considered is that of Wagah–Attari road link. This link has repeatedly been reported to suffer from increased instances of warehouse inadequacies and corruption by border staff on both sides thereby preventing the use of this route. According to the Associated Chambers of Commerce and Industry of India, even the slightest operational reforms at this border can increase the value of trade up to US $8 billion. The facilitation reforms for improving connectivity have been reiterated at several forums which include: transforming cross-border infrastructure from just trade corridors to comprehensive economic corridors, provision of fast track lanes for goods in transit, set up SAARC (South Asian Association For Regional Cooperation) single window for customs, promote multimodal transport so that rail can be promoted while road sector complements the trade and passenger activity, simplification and harmonization of trade procedures through ICT-enabled measures (including certifications, licensing and lab testing reports), enhance trading hours from existing 5 to 12 hours at the Wagah gate, and adopt open-sky policy.

On the rail infrastructure side both India and Pakistan have not moved forward despite more lucrative routes which are either a possibility or have been operational in the past before Partition of both countries (Taneja 2006). From Rajasthan (India) one can see two prospective rail links into Sindh (Pakistan). First is Jaisalmer in Rajasthan which is at 217 km from Rohri in Pakistan and second is Anupgarh in Rajasthan which is 200 km from Multan. Both districts have shorter distance to Pakistan given that within Pakistan the current route i.e. Karachi–Rohri is 478 km. From East Punjab (India) there are also two unused tracks that were operational before partition. First is Ganda Singh Wala–Hussainiwala route which opens into Firozpur district in India and has rail and road linkages with Pakistan’s Punjab border and this route was operational until 1970 for bringing tradable items on both sides particularly agricultural products. Second is Indian terminal of Fazilka which was historically connected by rail to Bahawalnagar and Bahawalpur via Mandi Sadiqganj. The distance between Fazilka and Mandi
Sadiqganj is only 150 km and this was also the rail route which used to go through Bhatinda and connect Delhi (India) with Karachi (Pakistan). Given that Bhatinda hosts Hindustan Petroleum Corporation’s oil refinery therefore it has the potential of becoming a key supplier of petroleum products to Pakistan.

Ultimately the above-mentioned routes are of strategic importance to India as well. Given that India’s current trade with Common-wealth of Independent States (CIS) suffers due to poor connectivity it has shown interest after signing of Afghanistan–Pakistan Transit Trade Agreement, to open Munabhao–Khokhrapar land route. Recent talks between the two countries also indicate Indian Punjab’s desire to export agricultural products to Iran via Pakistan. The CIS region is important for India from the viewpoint of oil and gas linkages as well in order to meet its future needs. From the trade point of view the Federation of Indian Export Organization has expressed interests in exporting pharmaceuticals, engineering, petroleum, wood and furniture products and IT services to CIS. Further this also fits well with the ‘New Silk Road’ Strategy (also backed by US) whereby Turkmenistan, Afghanistan, Pakistan and India (TAPI) have been talking about gas pipelines. The US feels that once it exits from Afghanistan such initiatives could be guarantors of peace and stability in the region. Already Uzbek and Turkmen powerhouses are providing electricity to Afghanistan and rail links are being constructed between Afghanistan, Turkmenistan and Kazakhstan—in fact, the rail link from the Uzbek border to Mazar-e-Sharif in Afghanistan has already been completed.

The US Silk Road Strategy Act also tries to build bridges with the ongoing thinking of EU, China and India. So while EU has been contemplating Transport Corridor for Europe, the Caucasus and Asia (TRACECA), China is pursuing Chinese Eurasia Land Bridge that links China, Russia and Europe via Kazakhstan. China will also play an important role in post-US exit Afghanistan through the Shanghai Cooperation Organization (SCO) and its linkages with Pakistan. Similarly India is pursuing International North South Transport Corridor with Iran and Russia. While all these initiatives are at different stages of implementation the regional security situation in this region will continue to draw a question
mark on these efforts. Unless all regional players come forward on
a collective vision of connecting South Asia, China and CIS and
beyond, such strategies remain mere permutations (CAPF 2012).
Within the connectivity debate it is interesting to note the growth
of ICT and related communication services in South Asia. The
mobile telephony has become accessible in this part of the world
even to individuals earning less than US $2 per day. However,
there are two issues that prevent the benefits of such widespread
ICT access. First is weak cross-border linkages e.g. India and
Pakistan not allowing roaming facility for home country service
providers and second is national, e.g. applications for phones are
not catering to the needs of poorest of the poor—the largest number
of whom now live in South Asia.

While connectivity between places is important it needs to be
recognized that connectivity between people has also gained
importance with the rise of social media. Now in order to com-
municate with each other the people of India and Pakistan do not
need to go through the restrictive visa regimes (that have to some ex-
tent been relaxed after the 2012 meeting between foreign ministers
of both countries) and they are seen to be part of several channels
through social media where they discuss cross-border and trans-
South Asia activities and prospects. In fact, it was the deregulation
of media (and its pressure thereafter on national governments),
social media growth, business to business interaction and youth
organizations on both sides that have successfully led to bring both
countries closer in foreign policy terms.

The rise of civil society organizations in South Asia also requires
special mention. Several civil society led initiatives were instru-
mental in breaking the ice between these two arch rivals, particularly
the most recent ones such as movement of peace termed ‘Aman Ki
Asha’ led by two media groups of India and Pakistan. Similarly the
series of South Asia Economic Summits led by five civil society
think tanks is now being termed as South Asian Davos following
the tradition of World Economic Forum in Davos. This summit is
an annual feature and brings together political and business com-
munities along with members of think tanks, academia, media
and lawyers. Both India and Pakistan also have some of the largest
diaspora numbers spread outside of their countries. They were also proactive in sensitizing the international community about the need to bring these two neighbours closer for regional prosperity.  

PROSPECTS OF ECONOMIC CORRIDORS

Despite the recent successes in trade diplomacy Pakistan’s government as well as the business community has been slow in reaping the benefits of increased regionalism. Trade with India and overall South Asia is abysmally low. However China after the 2005 free trade agreement with Pakistan became a major source of merchandise import to Pakistan. This section looks at the potential for Pakistan not just to increase trade flows with neighbours but also develop a trade-investment nexus (Srinivasan 2006).

PAKISTAN TRADE PATTERNS WITH NEIGHBOURS

Pakistan has seen overall positive changes in growth rates of its exports. However, not much success has been met in neighbouring markets. While exports to China showed a change from 5.7 per cent growth rate in 2009 to 6.6 per cent growth rate of exports in 2011, the growth rate of exports destined to India during the same time declined from 1.3 to 1.1 per cent (Table 11.1). To some extent Pakistan’s own supply side constraints also played an important role in curtailing progress towards export diversification and sophistication (Planning Commission 2011).

Pakistan’s key exports to China include cotton, leather, plastics, fisheries, cement, mineral fuels, organic chemicals, copper, and

<table>
<thead>
<tr>
<th>Year</th>
<th>Pakistan Exports to China (US $ million)</th>
<th>Pakistan's Exports to India (US $ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2009</td>
<td>1995.7</td>
<td>470.6</td>
</tr>
<tr>
<td>2010</td>
<td>2871.8</td>
<td>549.9</td>
</tr>
<tr>
<td>2011</td>
<td>3357.9</td>
<td>545.7</td>
</tr>
</tbody>
</table>

Source: UN Comtrade.
textile made-up. Din et al. (2009) predict that due to the size of Chinese economy the balance of trade will remain tilted towards China however as a result of China–Pakistan free trade agreement, change in production structures in Pakistan is expected which can result in lower prices for Pakistani consumers, greater variety and improved quality (given the intensity of competition), and increased incentives for innovation. The main exports to India include cement (and related material), dry and processed food, cotton, organic and inorganic chemicals, leather, and copper.

The easing of trade restrictions (at least the tariff related barriers) has allowed importing sectors to benefit more in turn not only boosting the producer’s surplus (Pakistan’s exports having substantial imported content) but also benefiting the consumers in most cases. The imports from China and India show an overall increase over the past few years (although remaining volatile with India). China today occupies over 25 per cent share in Pakistan’s overall imports.

The key imports from China include electrical and electronic equipment, machinery and boilers, fertilizers, organic chemicals, steel, plastics and rubber. The imports from India include organic chemicals, cotton, vegetables, plastics, tea, chemicals and sugar. Despite high trade barriers in past the exchange of merchandise between India and Pakistan continued in the form of informal trade. The informally traded items traditionally included cloth, pharmaceuticals, textile machinery, livestock and cosmetics. These items constituted almost 80 per cent of informally traded goods whose value in 2005 stood around US $534 million (Khan et al. 2007).

Pakistan and India being members of SAARC are also signatories in South Asia Free Trade Agreement (SAFTA). The progress on this agreement has been slow up till now and the current improvement in political relations of India and Pakistan (two largest countries in SAARC) provide an opportunity to push SAFTA forward. Estimates reveal that through a full implementation of SAFTA (and supplementary reforms to address non-tariff barriers) both countries could increase their bilateral trade by 79 per cent (Baroncelli 2007). A South Asia-wide report explains that sourcing the key South Asian imports from within the region (instead of importing them from
TABLE 11.2: PAKISTAN’S IMPORTS FROM CHINA AND INDIA

(US $ million)

<table>
<thead>
<tr>
<th>Year</th>
<th>Pakistan’s Imports from China</th>
<th>Pakistan’s Imports from India</th>
<th>% of Imports from China</th>
<th>% of Imports from India</th>
</tr>
</thead>
<tbody>
<tr>
<td>2009</td>
<td>7,559.5</td>
<td>2,160.8</td>
<td>23.9</td>
<td>6.8</td>
</tr>
<tr>
<td>2010</td>
<td>10,495.4</td>
<td>3,119.8</td>
<td>28.0</td>
<td>8.3</td>
</tr>
<tr>
<td>2011</td>
<td>12,941.3</td>
<td>3,214.7</td>
<td>29.7</td>
<td>7.4</td>
</tr>
</tbody>
</table>

Source: UN Comtrade.

outside) can lead to a gain of US $2 billion to South Asian consumers (Chatterjee and George 2012).

Within South Asia the dream of a free flow of trade activity remains unfulfilled unless the proposed trade corridors are geared up as comprehensive economic corridors which should in turn involve overland connectivity for example between countries such as Afghanistan, Pakistan and India. The ports in South Asia will also require connectivity which is time and resource efficient. An open sky policy for aviation sector will be required and new routes for cargo and passenger still need to be explored (Prabir De 2012).

One of the key opportunities on which Pakistan is currently missing out is the potential of trade in services with China. Given a large English speaking labour force China has long expressed its interest in having government level negotiations whereby Pakistanis with professional degrees can practice in China. Although this cooperation has taken off in education sector where we see Pakistani students and teachers actively visiting China, however, the progress is still awaited in the rest of the services sub-sectors particularly banking, transportation and communications.

INVESTMENT PROSPECTS WITH CHINA AND INDIA

The idea of engaging China in Pakistan for direct investment has been around for some time. Various Chinese projects have met success in Pakistan and currently there are 13,000 Chinese in Pakistan either working under joint ventures or government level public sector investment cooperation. The Trade Development Authority
of Pakistan (TDAP) declared 2012 as ‘Focus China Year’. The level of Chinese investment in Pakistan according to 2011 data stood around US $25 billion. At the government level, Pakistan has been extending space to Chinese authorities for investments in energy, mining, engineering, chemicals and IT sectors. However we see in Table 11.3 that there are other sectors too where Pakistan can benefit from China’s economies of scale. China has large stock of FDI (in various countries) in sectors such as transport, warehousing, construction and finance.

Pakistan and China already have a Joint Investment Company established with help from China Development Bank. The Industrial and Commercial Bank of China has also opened branches in Islamabad and Karachi. China has also allowed use of yuan in cross-border trade settlement. A currency swap arrangement is now under review.

For Pakistan to engage China in future foreign direct investment (FDI), domestic regulatory outlook and market openness demands attention. For example in case of energy sector, Chinese investors

### TABLE 11.3: GLOBAL STOCK OF FOREIGN DIRECT INVESTMENT BY CHINA (2010)

<table>
<thead>
<tr>
<th>Item</th>
<th>US $ million (2010)</th>
<th>% Change since 2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>Services (multi)</td>
<td>3,229.7</td>
<td>113</td>
</tr>
<tr>
<td>Community, social and personal service activities</td>
<td>1,479.3</td>
<td>12</td>
</tr>
<tr>
<td>Health and social services</td>
<td>36.2</td>
<td>213</td>
</tr>
<tr>
<td>Education</td>
<td>23.9</td>
<td>17</td>
</tr>
<tr>
<td>Business activities</td>
<td>1,16,885.8</td>
<td>37</td>
</tr>
<tr>
<td>Finance</td>
<td>55,253.2</td>
<td>23</td>
</tr>
<tr>
<td>Transport, storage and communications</td>
<td>23,187.8</td>
<td>26</td>
</tr>
<tr>
<td>Hotels and restaurants</td>
<td>4,49.9</td>
<td>81</td>
</tr>
<tr>
<td>Wholesale and retail trade</td>
<td>42,006.5</td>
<td>19</td>
</tr>
<tr>
<td>Construction</td>
<td>6,173.3</td>
<td>52</td>
</tr>
<tr>
<td>Electricity, gas and water</td>
<td>3,410.7</td>
<td>36</td>
</tr>
<tr>
<td>Unspecified secondary</td>
<td>17,801.7</td>
<td>36</td>
</tr>
<tr>
<td>Mining and quarrying</td>
<td>44,660.6</td>
<td>40</td>
</tr>
<tr>
<td>Agriculture and hunting</td>
<td>2,612.1</td>
<td>33</td>
</tr>
</tbody>
</table>

*Source: International Trade Centre.*
complained that while they see substantial prospects in electricity generation for a population of over 180 million people, the pricing structure is not aligned with market forces. While investment in generation is allowed the transmission is controlled by the government at a price which is set by the government which will imply a higher payback period on investment even under times of high domestic economic growth. Recently the Planning Commission has provided a checklist of such market impediments to National Economic Council (Planning Commission 2011).

Similarly the two regulatory bodies National Electric Power Regulatory Authority (NEPRA) and Oil and Gas Regulatory Authority (OGRA) require reform as recently they have been subject to supreme courts observations due to actions which were not as per standard operating procedures. Further transparency is required in the decisions undertaken by both these regulatory bodies. Another example is the import of energy raw material which is mainly oil and petroleum products in Pakistan. This import is not only controlled with a strict regime of statutory regulatory orders, it is usually made by civil servants who do not have experience in reading fluctuations in market activity and end up procuring oil in future time period at a much higher price.

Regarding prospects of Indian investment in Pakistan it is now encouraging to see that India has lifted ban on its natives to invest in Pakistan. In a meeting of Pakistan–India Business Council, investors from India showed interest in investing $20 billion in mining, energy, petroleum, and infrastructure. At the Nuclear Security Summit in March 2012 India formally offered Pakistan 5000 MW electricity through Wagah–Attari border. Several leading Indian concerns have also expressed their interest in the Thar Coal project in Sindh province of Pakistan. The Coal based electricity generation is already underway in Rajasthan which shares border with Sindh.

A more recent development has been India's decision to allow FDI from Pakistan. The Indian Department of Industrial Policy and Promotion earlier this year sent proposal to Ministry of Finance for carrying out the necessary changes in Foreign Exchange Management Act of India to allow FDI from Pakistan. The actual realization
of this decision can take three possible forms. One may be a joint venture between the entities from both sides, the second can be an investment into a complementary sub-activity and third may be an investment that competes with the current production in India. It is likely that in the initial phase the first two options will be practised given that there are still enough procedural measures which will prevent any competitor from Pakistan.

Pakistani businessmen have since long been keen to invest in India given the sheer size of the market next door. Muslim Commercial Bank in July 2012 had submitted a proposal to Central Bank in Pakistan for opening three branches in India (Amritsar, Delhi and Mumbai). Other sectors in which Pakistani businessmen have shown interest include cement, chemicals and pharmaceuticals.

Having discussed trade and investment implications for Pakistan we also need to discuss the aid channel through which Pakistan benefits from China. The public and publicly guaranteed medium and long-term debt from China was around US $2.7 billion in end-March 2012 (GoP 2012). In terms of foreign loans China has been relatively more accessible to Pakistan (compared with other bilateral sources) and the term structure of these loans has been somewhat relaxed. For example, in 2007 an interest rate of 3 per cent was charged over an amortization term of fifteen years. However, in 2011 loans were contracted at 2 per cent over an amortization term of 20 years. There has also been an increase in grants received from China. From US $6 million in 2003 the grant size of China increased to US $49 million in 2007 and US $249.5 million in 2011.

COOPERATION IN WATER RESOURCES

Pakistan has reached a situation in water sector that many call an ‘emergency in waiting’. A report by Woodrow Wilson Centre explains that Pakistan could face widespread shortages in another 25 years (Kugelman and Hathaway 2009). The current water management practices have come under criticism due to the neglect of authorities in responding to structural constraints. The piped water supply to almost 65 per cent of the population is irregular
and on occasions not potable. The access is with 35 per cent of population for 3–6 hours daily (mostly in case of large cities). Irrigation practices also remain primitive and account for 90 per cent of overall water use in the country. Pakistan consumes 75 per cent of its water resources compared to 34 per cent in neighbouring India.

The geo-politics of water scarcity and governance is equally important. Pakistan is facing the threat of future water scarcity due to China and India building dams over rivers that flow into Pakistan. Indus River which originates from China and passes through India before coming into Pakistan is regarded as the life-line of Pakistan’s agriculture production. This river now faces an anticipated shortfall given China’s newly-built dam in Tibet at Seng-Ali. Pakistan for its own future hydropower needs had planned to build dams in Daimer and Bunji on river Indus. However, given such anticipated shortfalls in water flow the financiers of these infrastructure plans inside Pakistan are not very sure about the precise future flows of river Indus and its hydropower potential. In September 2012 World Bank announced that it was backing out on its commitment to finance the Daimer-Bhasha Dam which some say is also due to India claiming that this dam comes in Gilgit-Baltistan which is a disputed territory between the two neighbours.

India will also continue to dam its Himalayan rivers given its current and future energy requirements. A series of projects on Jhelum and Chenab rivers have been planned by India. Both these rivers are sources of water for agricultural lands in Pakistan’s Punjab province. The Indian argument has been that these dams will not be used for storage, however, India accepts that they will delay the flow of water into Pakistan. This over the longer term also threatens the current cropping patterns.

Pakistan has turned to the international court in order to protect its water rights. It has already complained about the dam in Gurez valley terming it illegal as per international water laws. While the court has halted any permanent work, however, India continues tunnelling and related activities. The foreign policy relations of both countries are also being tested due to the dispute over Baglihar
and Kishanganga dams in India which Pakistan believes is a deviation from the Indus Water Basin Treaty of 1960 (Figure 11.5). Similarly Pakistan has also raised concerns with Indian authorities on Nimoo-Bazgo Dam.

Given that China and India have their own differences on water sharing therefore going forward China, India and Pakistan need to collectively work on how best to protect and share the scarce water resources. The shrinking Himalayan glaciers are also expected to cut the flow of Indus by 8 per cent over the next four decades. Examples such as ‘Good Water Neighbours’ which is a project to raise awareness of the water sharing problems of Palestinians, Jordanians and Israelis provide a good starting point for dialogue and future action. There is a strong case for Track-II efforts (dialogue led by civil society) which may compliment the Track-I efforts (government-level negotiations) on this subject. Launching joint dam ventures such as the one between India and Bhutan known as Tala Hydroelectricity Project is also a good example of regional cooperation.

![Map of South Asia showing the Indus River Basin and key countries involved in water sharing.](image)

*Source: The Economist.*

*Figure 11.5: Baglihar and Kishanganga Dams Built by India*
REGIONAL SOLUTIONS FOR ENERGY SCARCITY

The supply of energy will continue to remain a critical ingredient in kick starting economic growth in Pakistan which currently hovers around 3 per cent. In this context Pakistan has been engaging with China for its foreign investment needs in the energy sector. In August 2011 both countries held the first Pakistan–China Joint Energy Working Group meeting. During the meeting 19 new energy projects were offered to Chinese companies. China is ahead of the curve when it comes to renewable energy technologies, solar panels, and wind turbines. Given Pakistan’s potential in renewable energy such as hydro, wind and solar there is a need to further broaden the current rounds of discussions between the two countries.

The on-going hydropower projects in collaboration with China include Bunji Dam in Skardu (with capacity of 7200 MW electricity), Taunsa hydroelectric power project in Punjab (with capacity of 120 MW electricity), Kohala hydropower project in Muzaffarabad (with capacity of 1100 MW electricity) and Karot hydropower project (with capacity of 720 MW electricity). In wind and solar power projects China has offered support for 50 MW wind power project in Jhampir (Sindh province) and has in principle agreed to support 300 MW solar power projects in Pakistan. The stalled Ghazi–Barotha Hydropower Project is also expected now to be completed by the Chinese government. China and Pakistan have also been cooperating in civilian nuclear energy and there are plans to expand this programme.

Pakistan also has one of the largest coal reserves in the world. While China and India meet 80 and 75 per cent of their needs respectively from coal, Pakistan’s share of coal in electricity production remains negligible. Indian firms already operating in Rajasthan have expressed their interest towards joint ventures in exploring the potential of Thar Coal in Sindh province of Pakistan. The economies of scale for these Indian firms will be natural given the proximity benefits.

With India, the proposed portfolio of energy projects (being considered at the government level) is in fact larger in scale, however, fragile geo-strategic situation in the region is preventing progress
on-ground. The first is the US $7 billion Iran–Pakistan–India gas pipeline project which seems stalled on two accounts. First India believes that the pipeline passes through the volatile regions of Pakistan (in Balochistan province) and therefore a correct assessment regarding certainty of supply, transport and transit fee cannot be made at this stage. Second US has been piling pressure on India and Pakistan not to go ahead with this project given the on-going sanctions on Iran. However, after a recent follow up by Iranian prime minister with his counterpart in India and pressure by Indian Parliamentary Panel on this subject there are hopes that the three countries may go ahead with this project.

The second proposed project is US $7.6 billion TAPI gas pipeline (1,700 km) and all four countries have now managed to settle the transit fee issue. Through this project Pakistan and India are expected to receive in the beginning 1.365 billion cubic ft of gas per day (bcfd) and Afghanistan will receive 0.5 bcfd. The gas price structure will be reviewed with Turkmenistan every five years. More recently Bangladesh has expressed the desire to join the TAPI project. The success of this project too hinges upon stability in Afghanistan.

The cooperation between India and Pakistan in the energy sector need not wait for the materialization of above mentioned mega and transnational projects. Both countries have recently been contemplating electricity trade (as mentioned above). The government of Indian Punjab province has recently shown the intent of exporting surplus electricity to Pakistan by 2013. Many have termed prospective energy trade between the two countries as a stronger form of confidence building measure (Pandian 2005).

ENVIRONMENTAL THREAT

It comes as no surprise that high levels of production activity in Pakistan’s eastern neighbourhoods and spread of military waste in Afghanistan have all collectively contributed in deterioration of climatic conditions. These have resulted in faster glacial melt, repeated instances of country-wide flooding, changing cropping patterns and uncertain overall ecological impacts.

There are fifty-two glacial lakes in Pakistan which have been
classified as potentially dangerous and there have been recent instances of glacial lake outburst floods (GLOF). The glaciers in Pakistan are receding at an average rate of 40 to 60 m per decade (Gardelle et al. 2012). Among the more recent phenomena in Pakistan are urban flooding, cyclones and coastal flooding, water crises and droughts.

Environment is a shared heritage and all citizens in a region contribute to the good or bad interventions in the region.

Table 11.4 exhibits the select environmental indicators for the three countries. China and India show to a large extent relatively poor performance. There are 86 and 76 bird species threatened in China and India respectively. Both countries have some of the highest rates of reliance on coal for electricity production. This reliance is not expected to come down in near future given the high growth rate of urban population in both countries. These statistics have implications for the region which should not be forgotten in the race to achieve higher economic growth and export levels.

The unfortunate aspect is that the governments in China, India and Pakistan have been alerted about the unsustainability of their production processes since a long time ago. Rijal (1999) while studying the energy use patterns in these countries explained that supply and demand patterns of energy in the mountain areas around Himalaya are unsustainable. There is continued preference given to low quality energy forms which are also subsidized by the governments and there is lack of institutional framework for promoting decentralized renewable energy technology.

In February 2012, Sustainable Development Policy Institute hosted the Track-II dialogue between India and Pakistan on Climate Change. Amongst the various recommendations it was strongly felt that:

(a) adaptation strategies must be designed keeping in view the shared ecosystems in the region, such as mountains, glaciers, rivers and monsoon systems as well as the common interest of countries and prevention of conflict;

(b) the relevant decisions adopted by SAARC summits on climate change, especially those pertaining to food security and disaster
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<td>CO₂ emissions (kg per PPP $ of GDP)</td>
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<td>Population in the largest city (% of urban population)</td>
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*Note* (*): The data on Methane and Nitrous Oxide emissions is for 2010 (last available year).

*Source*: World Development Indicators.
risk reduction should be implemented through enhanced cooperation and removal of impediments;
(c) SAARC should carry out a feasibility study on the establishment of a green climate fund for South Asia; and
(d) Establish ‘Climate Policy Coordination Group’ comprising policy makers of the two countries to harmonize positions at international fora.

We have in our earlier text explained the economic (trade and connectivity) benefits to Pakistan in the event of greater regional integration. However, it is important at this stage to take inventory of the environmental cost of integration in the traditional sense. This should then allow us to think towards regional integration in a manner which adheres to the principles of sustainable development.

As China and India both on occasions have shown interest in using Pakistan’s rail and road network for transit this in turn is bound to increase traffic density. If Pakistan also agrees to accommodate the increased Chinese freight destined for Gwadar Port for onward distribution to Europe and Africa this in turn should imply increased investment in transportation infrastructure. Up till now at the government level there has not been much contemplation regarding the environmental consequences of this substantial civil work. Similar considerations will apply if activity through Afghanistan–Pakistan Transit Trade Agreement expands and India makes use of this transit. An additional reflection on the expansion at Gwadar Port relates to the threat to marine activity that must be accounted for once such investments are initiated. A related issue is that of the environmental implications of Pakistan being used as an energy corridor.

At the product specific level this paper identifies the key exports and imports that Pakistan enjoys with China and India. However, an environmental appraisal is desired ex-ante which should allow us to see the implications as the production increases in the event of favourable regional integration (particularly in case of backward industrial linkages with sub-sectors). We know from current scientific literature that the compliance of environmental laws at the
agricultural and industrial level remains very poor in all three countries. Hence the reason for again reiterating a joint environmental forum that can highlight and suggest a way forward on sustainable regional integration. At the SAARC level this has been a longstanding recommendation that originated from the Male Declaration that was issued at the 5th SAARC Summit.

The urgency of the above-mentioned problem magnifies when one looks at the projected health impacts of environmental deterioration in the region. Khwaja et al. (2012) while explaining the existing situation of air pollution in South Asia demand a legally binding agreement that can strengthen the framework for air pollution reduction at the regional level.

Similarly Khan et al. (1999) had given a comprehensive plan whereby capacities for trade can be built across the region in a manner that ensures sustainable development. Authors had proposed that at the sectoral level environmental standards such as ISO 14000 can ensure efficiencies in the production processes. Second these standards have built-in quality controls that can in fact help in retaining and expanding export markets. Third and a consequence of the above two points—cleaner environment will help the macroeconomy once the health care costs decrease and health-related productivity losses are redeemed. Fourth the incidence of environmental deterioration on the poorest of the poor can in turn be decreased through compliance with standards. It is this segment of the population that is most vulnerable to climate change. Finally the authors have proven for the case of textile and leather that costs of mitigating environmental damage are modest (contrary to the views forwarded earlier).

CONCLUSION

While Pakistan has engaged China and India bilaterally in trade, investment, connectivity and infrastructure related cooperation, however, the same level of cooperation is still missing in social sectors. Given that these three countries put together make the largest single cluster of population in the world, collective regional solutions for climate change, food security, health and education
will go a long way in cementing the relations between these countries, not just at the state level but also at people to people interactions.

There is a need to advocate responsible regional economic growth. With China and India both having over 70 per cent of their electricity needs met by coal and the rising levels of air pollution in South Asia, Pakistan is going to be on the receiving end when it comes to negative externalities arising out of regional economic growth. Pakistan in its bilateral relationship with both countries needs to take up the issue of black carbon that is received from India and China and adversely affects Pakistan. The back-to-back floods since 2010 and instances of changing weather patterns in Pakistan have far-reaching effects on national exchequer and nation's productivity. This issue becomes all the more important with China's plans to invest US $100 billion during the next five years towards infrastructure needs of the Xinjiang province neighbouring Pakistan. The black carbon emitting from this construction activity is bound to exacerbate vulnerability of natural disasters in northern areas of Pakistan.

For deeper integration between these three countries it will be important to identify the cross-border clusters based on comparative advantages. In case of China–Pakistan this will imply that Pakistan should see this as an opportunity to align the economic activities (goods and labour market) with bordering regions in China. Similarly with investment and trade barriers coming down it is an opportunity for Sialkot and Gujranwala cluster in Pakistan's Punjab province to discover supply chain linkages with Indian Punjab. The business community will have to be more active in their cross-border interaction with their counterparts and national governments may play the facilitatory role. In case of India and Pakistan this may imply easing the visa regime for businessmen on both sides. For this to happen, comprehensive economic corridors need to be envisaged which should not only look at the business angle but also people to people interaction in the spheres of culture, education and sports.
NOTES

1. Deputy Executive Director, Sustainable Development Policy Institute. Email: vaqar@sdpi.org. The author acknowledges comments by the anonymous referee and Mahmood Khwaja, Senior Advisor, Sustainable Development Policy Institute.

2. We use the term ‘favoured’, as India has always been in the priority list however, the bilateral relations have remained bitter in the past.

3. The EXIM Bank of China is reported to have completed feasibility of financing Faisalabad–Karachi–Gwadar motorway project in May 2011 (weblink: http://ow.ly/f0hWe, accessed on 4 November 2012).


5. Currently bulk of trade traffic is through the Wagah–Attari border.


7. The CIS region consist of republics of former Soviet Union, except the three Baltic states, i.e. Estonia, Latvia and Lithuania.

8. Indian government is of the view that sending goods via Bandar Abbas Port in Iran to Russia will cut the cost by over 40 per cent.

9. See commentary by Lahore University of Management Sciences (Pakistan) and LIRNEasia (Sri Lanka) http://ow.ly/f34Je (weblink accessed on 6 November 2012).

10. For example the efforts of Pakistan–India & UK Friendship Forum at the House of Lords (UK) http://ow.ly/f37u0 (weblink accessed on 6 November 2012).


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