



Research Paper

## India's North East Frontier: Trade Gateway to East Asian Countries

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### Abstract

Transportation cost is a major determinant of trade between two partners. Estimation suggest transport cost constitute roughly around 10 per cent of the total trade cost. Better connectivity between production and consumption centres helps to substantially reduce the cost of traded goods and make them more competitive. This paper attempts to evaluate the effect of transport cost involved in the export of goods from North Eastern region to the neighbouring and East Asian countries. Significance of the North East (NE) region in terms of its geographical location and some of the important international transport arrangements has also been discussed. Attempts have also been made to assess the export potential of the region to cater the ASEAN market. The study argues to develop the NE region as an alternative route to cater export markets in the East Asian region. The analysis suggest that at least 50 per of the transport cost can be reduced using NE region as an alternative trade route.

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### I. Background and Introduction

Mode and cost of transport plays a vital role in efficiency of trade between two partners and consequently the economic integration (UNCTAD, 2003). Greater connectivity and developing of special routes for trade has historically been used as a tool to enhance trade at a cheaper rate. Better connectivity between production and consumption centres helps to substantially reduce the cost of traded goods and make them more affordable. A key determinant of trade competitiveness is the extent to how timely and cost-effectively export goods can be shipped from a factory, warehouse or port in the country of origin to destination markets (USAID, 2003). Reducing the distance of transportation for internationally traded goods not only lower their prices but also makes them more competitive.

Improved transport infrastructure enhances the trade between two nations which in turn deepen their economic integration. Various studies have also pointed out about the development international transport facility and cross-border transport infrastructure and associated regional economic integration (Fujimura, 2004). It is in this regard many countries, including Asian countries have come together to join hands to develop a number of alternative trade routes and deepen the economic integration. Great Asian Highway connecting 32 countries, garland highway, India-Myanmar-Thailand Trilateral Highway etc. are some of the examples of developing transport facilities through alternative routes to reduce trade cost and increase volume.

India is among the partners of developing the Great Asian Highway. A large part of India, mainly the North Eastern (NE) states will be connected through this Highway. It is expected that this route will drastically reduce the cost of transport of goods from the North East region to other parts of the country. This route will substantially reduce the road distance between India and ASEAN nations and in turn reduce the transportation cost. The reduced transportation cost will lead to reduction in the total export cost.

In order to deepen the economic integration with ASEAN nations, India has also taken a lot of steps. Region specific policies have been announced, preferential trading arrangement has been made, Trans-Border Growth Areas (TBGA) have been identified. Announcing Look East Policy in 1991 and entering into Free Trade Agreement (FTA) with ASEAN nations is considered as a major step by India to deepen the regional

integration<sup>1</sup>. The geographical position and various similarities of the region with ASEAN countries will help the NE region of India to play a crucial role in this regard. It is against the above backdrop, the current paper tries to analyse the role of improved transport facility in increasing trade between two partners and evaluates the measures undertaken by India to increase its trade volume with ASEAN nations in this regard. The study also compares the cost of transportation of goods to ASEAN countries through North Eastern states and through other traditionally used routes. In addition to that the study makes an attempt to evaluate the emergence of various concepts in the study of regional economic integration.

The study is organised in the following manner. Section II deals with survey of existing literature, section III describes the measures undertaken by India to increase its trade and deepen the economic integration with ASEAN nations. The same section also reflects India's trade relation with ASEAN countries. Section IV analyses how India can use North eastern region as alternative route for mercantile export to ASEAN countries. The final section concludes the study with policy suggestions.

## **II. Literature Review**

There has been steep increase in the international transport cost in recent times. Increasing transport cost has drawn attention of researchers and policymakers across the globe. (Hummels, 2007). As per a study conducted by the World Bank (2001), suggest that transport costs outweigh tariff barriers in 168 out of 216 countries that are U.S. trading partners. Various studies have also been conducted using empirical data and tried to suggest possible solution to reduce this cost. (Limao and Venables, 2001; Mico and Perez, 2002; Clark, Dollar and Mico, 2004; Egger, 2004; Combes and Lafourcade, 2005; Martinez-Zarzoso and Suarez-Burguet, 2005).

Kuwamori (2006) studied the role and impact of distance on transport cost using empirical data of Philippines import. The study conserved the time period between 1991 and 1996. Results of the study indicate that the impact of distance varies across commodity groups, but it is difficult to precisely determine the direction and the magnitude of this impact.

Geraci and Prewo (1977) estimated the transport cost equation for OECD countries and found that using only distance as a proxy for transport costs may result in underestimating the sensitivity of bilateral trade flows to transport costs. Hummels (1999) and Hummels (2001) estimated transport cost elasticity with respect to distance by transportation mode using U.S. import data. His results show that the distance coefficient of sea transport is higher than that of ocean transport.

Zarzoso and Lehmann D (2006) empirically investigated the Spanish exports to Poland and Turkey. Data for each of the 8,425 shipments exported as containerized cargo from the 51 Spanish provinces to Poland and Turkey in 2003 were investigated using the empirical model. The study analysed the relative importance of road and maritime transport costs in comparison with distance measures as determinants of trade flows. The main results of this investigation indicate that real distance is not a good proxy for transportation costs and identify the central variables influencing road and maritime transportation costs: for both modes, transport conditions are strong determinants, whereas efficiency and service quality are more important for maritime transport costs, and geographical distance is more important for road transport. Road and maritime transport costs are central explanatory factors of exports and they seem to deter trade to a greater extent than road or maritime transit time when endogeneity is considered.

Majority of the studies discussed above analysed the situation of US, EU and Latin American Countries. Only a handful of studies are available in economic literature emphasising the transport bottlenecks in India or in Asian economies. However, none of the studies have comprehensively suggested how to contain the increasing international transport cost. The study makes an attempt to bridge this gap in the research and suggest how India can utilise the North Eastern region as an alternative route to cater the export need of the East Asian markets.

## **Section III**

### **Indian Initiative: Why is NE so important?**

Government of India announced the Look East Policy during 1991 which focussed on the East Asian countries for close economic and commercial ties, increasing strategic and security cooperation and the

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<sup>1</sup> India entered into FTA with 10 member ASEAN nations during 2010. The agreement covers only goods. Dialogues to cover services and investment in the FTA are still under process.

emphasis of historic cultural and ideological links. India sought to create and expand regional markets for trade, investments and industrial development. The Look East Policy which was actively pursued by Atal Bihari Vajpayee and Manmohan Singh got bigger momentum during Narendra Modi government when he announced the up-gradation of Look East policy into Act East Policy during India-ASEAN Summit in Myanmar in November 2014<sup>2</sup>. Acting on the same line government also announced Neighbour First Policy. Through Neighbour First Policy the government attempts to increase its economics and political ties with its neighbour first.

The India and ASEAN signed the long awaited free trade agreement on 13<sup>th</sup> August 2009, which came into operation from 1<sup>st</sup> January 2010. Through this agreement India offered free movement of selected goods from the 10 member ASEAN countries into India. Similar agreements are also under negotiations between India and Asia Pacific Economic Council (APEC) and Regional Comprehensive Economic Partnership (RCEP). Along with these India is also engaged in many arrangements to enhance economic, political and cultural ties with its East Asian neighbours. BIMSTEC, Mekong Ganga Co-operation (MCG), BCIM etc. are some of the important examples.

Further, 'The Kaladan Multi-Modal Transit Transport Facility' connecting Indian ports on the eastern part and Sittwe port in Myanmar passing through a riverine transport corridor and road transport in Mizoram is expected to offer an alternate trade route to the North East (Sharma 2008). There is also a proposal under multilateral level to construct a 1,360 km Trilateral Highway from Moreh (Manipur, India) to Mae Sot (Thailand) through Bagan (Myanmar) targeted to be completed by 2016 (North East Vision 2020). Recently a feasibility study conducted by the Rail India Technical and Economic Services Ltd. on the proposed freight corridor, estimated the Jiribam-Imphal-Moreh rail link to cost US\$ 649 million (Bhattacharaya 2008).

In these arrangements one common thing that one find is giving special emphasis to the North Eastern Region of India. The geographical locations of the region and the East Asian countries along with many other similarities have benefited the region to be a part of such growth initiatives. The North Eastern Region will play a significant role in the success of these international initiatives.

### **Significance of North East and ASEAN**

The North Eastern Region of India extends to north and east of the narrow Siliguri corridor and comprises Arunachal Pradesh, Assam, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim and Tripura. These eight States cover an area of 2,62,189 sq. km. constituting 7.98 per cent of the country's total geographical area and account for only around 3.79 per cent of the total population of the country (Census, 2001). The region contributes a little more than two per cent in India's total GDP. Assam is the largest state of North-East India representing 30 per cent of the region's geographical area, 68 per cent of its population, and 30 per cent of Northeast's net state domestic product (NSDP) (CUTS, 2010). The region has a long international boundary, about 96 per cent, with China and Bhutan in the north, Myanmar in the east, Nepal in the west and Bangladesh in the south and west.

Assam contributes more than 60% of the total GSDP of the region. This can be attributed to its relatively more developed infrastructure owing to its geographical advantage. Sikkim has the highest per capita Net State GDP in the region, while Mizoram has the highest literacy rate in the region. A close analysis of the industrialisation in NE region reveals that it laggard behind other states in the country. The limited industrialisation in the region is centred on a few natural resourced based industries such as natural oil and gas, coal, cement, tea, jute, paper, bamboo and cane based handicrafts and handloom industries and other forest based industries.

Even though NE region is endowed with huge potential to increase its export volume, the region lacks far behind in this regard. A number of studies have been conducted on the export potential of NE region and its role in facilitating trade with Asian countries (CUTS: 2010, RIS : 2011, Mukherjee: 2016, Bhattacharjee :2016). All these studies have stressed the greater role of the NE States in India's export to ASEAN region. Given the ethnic diversity of the north eastern region, ecological richness and cultural proximity with all the ASEAN partners the region will play the vital role in the initiative, once NE borders are opened up for trade under BCIM. It is also argued that the economic development of the land locked NE states can be addressed only through such strategic initiative involving the other nearby regions. Along with all these factors it is the geographical locations of the region, which makes it the centre point of the ASEAN. The NE region no longer is considered as a remote and backward zone; rather, it has been termed as "gateways of opportunities of international trade and commerce"<sup>3</sup>.

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<sup>2</sup>Details available at: <http://mea.gov.in/Speeches-Statements.htm?dtl/24143/Media+Statements+by+Prime+Minister+of+India+and+Prime+Minister+of+Vietnam+in+New+Delhi+October+28+2014>. Accessed on 15.02.2017

<sup>3</sup>Verghese B.G. (2004). "Borders matter more than boundaries from the North East looking out". *Man and Society: A Journal of North East Studies*, 1(1, spring)

Some have gone to the extent of referring this new 'strategic vision' could be a 'game-changer' for Asia, especially because it has the potential to bring together China, India, and Southeast Asia. The Vision Document of North East 2020 identified various characteristics of the region which can help to foster export from the region. Studies have also been conducted about the various features and factors which can help to fillip the export of various goods from this region to various East Asian countries (CUTS: 2010, Dubey: 2014). Some of these predominant factors and various proximities of the region with ASEAN member countries are-

(a) **Geographic Proximity:** With respect to geographic proximity, many researchers have argued and empirically demonstrated that it plays dominant role for countries to engage in international trade (Frankel and Romer 1999). The fact that countries or regions are far apart from each other may entail higher cost of transportation and communication which could otherwise be minimised if they are located at close proximity. All the NE states are located very closely with ASEAN countries. Trade route with lowest possible distance with ASEAN economies can only be developed from this region.

(b) **Ethnic Proximity:** This is a well recognise fact that the people of NE states share more proximity with their foreign neighbours than the mainstream Indian citizens. Their appearance, cultural events, festivals, food habits, traditional dress etc. finds similarity with many of the ASEAN countries.

(c) **Economic Complementarities:** Fundamentally, the economic complementarities originate from various participating member regions with different phases of development as well as asymmetric distribution of factor endowments. Economic complementarity may also take place due to asymmetry in terms of technology and the quality of human capital endowments available to each participating member in the growth zone. Asymmetric economic factor like labour, power, natural resources etc. in both the sides can complement the economic development of the region.

### **India's Relation with ASEAN Countries**

India and ASEAN nations share a good relation since very long. Various proximities in their culture, ethnicity etc. has helped them to be close to each other. But, unfortunately, the relationship remained lukewarm for the first four decades of India's independence due to the divergence in ideological outlook and security relationships during the Cold War. Relations were put back on track with the adoption of the "Look East Policy" by India in 1991 and ASEAN's strong desire to forge closer ties with India (Yong, 2005).

India and ASEAN became Sectoral Dialogue Partner in 1992, and subsequently full dialogue partner in 1995 focusing on cooperation in economic and development. The relation becomes stronger with signing of ASEAN India FTA (AIFTA) in 2009 which came into force in January 2010. Announcement of upgrading Look Act Policy into Act East Policy by Prime Minister Narendra Modi representing federal government of India shaped the relation even deeper.

Trade relationship between these partners can also be traced to a very old period. A vast variety of goods and services are being traded. The available data suggest that the trade between India and ASEAN which was also a major trading partner of India even before entering into FTA has increased many folds (Sikdar and Nag, 2011). It is also worth to mention here that, Singapore one of the members of ASEAN is also among the top trading partners of India. The ASEAN-India cooperation covers a wide area which includes Trade in goods, Trade & Investment, Science & Technology, Tourism, Human Resource Development, Transport & Infrastructure and Health & Pharmaceuticals.

Indian exports to ASEAN nations have increased more than 100 per cent between last 2 decades. During the same time period import from these nations have increased even steeper.

## **Section IV**

### **North East as Alternative Trade Route**

The NE region of India is not only blessed with abundant natural resources but also with significant and strategic location. The region has got 8 international boundaries covering around 5300 km<sup>4</sup>. The countries that connect the region are China, Myanmar, Bangladesh and Bhutan. Moreover, India is having close ties with all these countries both politically and economically. Trading activities also takes place through most of these borders (except China). The region was connected with Bangladesh through rail link even before independence. The inland water transportation facilities were also developed during the pre-independence period. Sizeable amount of goods used to be transported using the inland water routes. Land custom stations are also established in most of these borders. For overall economic and other development of the region special government agencies like North Eastern Council (NEC), North Eastern Development Finance Corporation Ltd (NEDFi), Ministry of Development for North Eastern Region (Doner) have been established.

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<sup>4</sup> Includes both land and water boundaries. Land boundaries covers around length of 4500 KM. See FICCI and PwC 2014 report.

In spite of having all the facilities and resources the region lags far behind the other parts of the country. Policy makers are also accused of neglecting the region for long<sup>5</sup>. The road transport system in the region is in abysmal condition. This situation is when road transport is the only mode of transportation for 7 out of 8 states in the region. Only Assam is connected with rail link and that too southern part of the state (Barak Valley) was included in the rail map very recently<sup>6</sup>. The inland water transport system has never drawn necessary attention from the government. Government never bothered to maintain or develop the existing water transport facilities of the pre-independence period in the region. Government announced Brahmaputra and Barak rivers as National Waterway, but no documentary evidence could be gathered which suggest up-gradation of the waterways in these two rivers.

The air transport system is also tells no different story. The data suggest deterioration of the air connectivity in the region since 1970. A study conducted by FICCI and PwC reports that number of airports reduced from 17 during 1970 to 11 recently. No regular flight is available to most parts of the region. Guwahati the biggest city and the capital of Assam and gateway to enter the region is an exception. The city is privileged to have an international airport and well connected with other parts of the country. A few international flights also fly from this airport to the neighbouring countries like Bhutan, Nepal etc. However, it is not clear from the available data weather cargo flights operate from this airport.

The condition of the road and water transport system connecting the neighbouring countries are also far from satisfactory level. Not even a single road connecting any of the international borders (be it state or national highway) are maintained. There is no wonder about the very small amount of mercantile trade takes place through these borders. The transport facility and cost which is a major determinant of trade is definitely behind this small size of trade. The transport facilities of the region are in abysmal condition even when the region occupies a significant location in many of the international trade route development arrangements (discussed in the earlier section). Despite realising the potential of NE region, government has never taken any well planned action to develop the trade routes and increase the trade volumes through and from this region. This is the scenario in a situation when India's trade values are constantly increasing with these neighbouring countries including other East Asian countries. But despite the region's geographical and cultural proximity to these countries, the share of NE India in the total trade has been consistently hovering in the range of 1 to 2% while contributing only 5% of the total exports to Bangladesh, Myanmar and Bhutan (FICCI and PwC, 2014). In addition to that the data also suggest that many of the majorly exported items to these countries are abundantly grown in the region. The trade potential of the region is added up further by India's FTA with SAARC and ASEAN (all of the neighbouring countries of the region are members of either of these economic blocks). Due to lack of proper transport arrangements, many of the products grown in the region like tea, bamboo based handicraft item, handloom items, processed fish, rice, etc. are exported to the East Asian countries using other trades routes rather than using the nearby borders<sup>7</sup>. This argument is supported by Ministry of Commerce and Industry data which disclose that around 95 per cent of the export to Bangladesh, Bhutan and Myanmar from the region rely on other route rather than NE region. This is not only increasing the cost of the export but also leading to a huge loss to the exchequer of the region. This is also to be noted that poor transport facilities act as a major deterrent to both trade facilitation agreement and ease of doing business index. Developing NE region as an efficient route to export to cater East Asian markets will reduce the transport cost, which in turn will lead to reduced export cost and make Indian goods more competitive. Further, this will also bring economic prosperity in the long neglected region. The significant benefit of developing NE region as an alternative route to trade can be better understand from the following tables which represents the comparison of the transportation cost through different channels.

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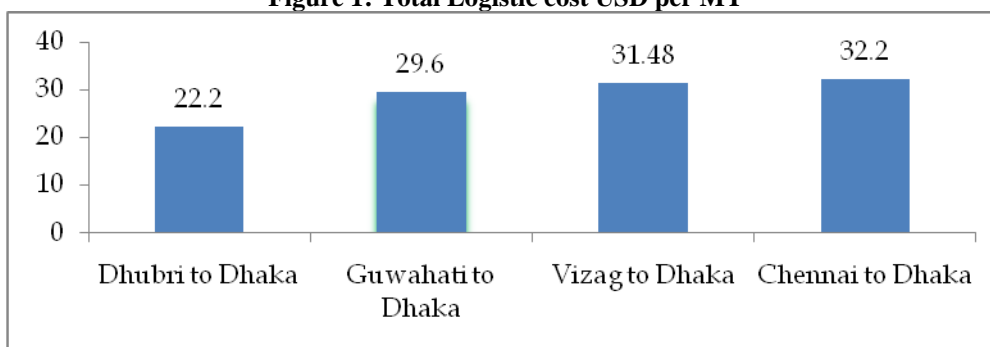
<sup>5</sup> Bibhu Prasad Routray (2003) (Neglected Northeast: Whose Responsibility? Institute for Conflict Management. Available at <http://www.ipcs.org/article/terrorism-in-northeast/neglected-northeast-whose-responsibility-1145.html>

<sup>6</sup> During 2016 January the old meter gauge lines were converted into broad gauge line. The conversation works are under way to connect Tripura.

<sup>7</sup> This information is based on our interaction with exporters, Land custom officers in the region.



Figure 1: Total Logistic cost USD per MT



Source: FICCI and PwC

The data reflects the total cost of transporting goods to Dhaka is around 50 per cent higher using the Vizag or Chennai routes. This cost will become even higher after adding the domestic transportation cost from Guwahati to Vizag or Chennai. In addition the transporters are also subject to various other taxes levied by states on interstate transportation. It is pertinent here to mention that the distance between Guwahati and Chennai is approximately 2630 Km via NH 16 and it takes more than 75-85 hours for a container to reach Chennai port. While the same container takes around 60-70 hours to cover the approximate distance of 1820 Km via NH 16 and 26 to reach Vizag port.

The data in the figure above clearly suggest that transportation of goods from the two different points of North East viz. Dhubri and Guwahati are highly cheaper as compared to Vizag and Chennai ports. Furthermore, the expected transportation time will also be less than 50 per cent than that of other two ports. It is worth here to mention that time consumed during the transportation of goods play a crucial role, mainly in case of perishable items. And many of the goods produced and exported from NE region are perishable in nature. On the basis of the above evidence it can be argued that goods produced in NE region should follow the regional border points to export to neighbouring countries instead of using Vizag and Chennai ports. This will not only save a lot of time bur also significantly reduce the total export cost.

## Section V

### Conclusion and way forward

Transportation cost is a major determinant of trade between two partners. Estimation suggest transport cost constitute roughly around 10 per cent of the total trade cost. Better connectivity between production and consumption centre helps to substantially reduce the cost of traded goods and make them more competitive. It has been observed in the study that even after having a lot of potential and geographical advantage the region lacks far behind than the other parts of the country. North Eastern region is a stakeholder in many of the international economic arrangement like BCIM, MCG, GMS, and Trans Asian Highway etc. In spite of all these the region has absence of satisfactory transport facility of any mode. Either of the rail, road or water transport facility is adequate to cater domestic requirement leave aside international requirement. The roads connecting the international borders are also found to be the victim of negligence. The inland water transport system has never drawn necessary attention from the government. Forget developing new inland water transport, Government has even failed to maintain the existing water transport facilities of the pre-independence period of the region. Similar story was also noticed in case of Air Transport System. The number of airports reduced from 17 during 1970 to 11 recently. No regular flight is available to most parts of the region.

Even though the transport system of the region is abysmal condition, we still believe in the potential of the region to become an export hub for the East Asian countries. Developing the region as an alternative route to cater export markets in the East Asian region will reduce the transport cost, which in turn will lead to reduced export cost and make Indian goods more competitive. Further, this will also bring economic prosperity in the long neglected region. The analyses suggest that at least 50 per of the transport cost can be reduced using NE region as an alternative trade route. Developing the region as an alternative trade route can be done through expansion of roads between the following routes.

- ✓ Bangkok – Mandalay – Moreh – Imphal – Silchar – Karimganj – Sylhet
- ✓ Guwahati – Dawki – Jamalpur – Dhaka – Petrapole – Kolkata
- ✓ Aizwal – Silchar – Agartala – Sabroom – Chittagong

Similarly proposed railway links from Mandalay-Imphal-Jiribam-Silchar-Agartala-Dhaka should be operationalized without delay. The Agartala – Sabroom line should also be developed soon. Railway lines should also be expanded to other parts of the region very soon and expedite the on-going expansion of railway links in the region.

Inland water transport should also develop. Inland water terminals should also develop nearby international borders. The policy makers should also understand the urgent need of the development of the air transport system of the region. Abandoned airports should be made operationalized soon.

A detailed research on how to develop these transport facilities can further add to this study.

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