INDO-SRI LANKA FREE TRADE AGREEMENT THE HYPE AND THE REALITY

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Since independence India and Sri Lanka have concluded three major treaties. They are the Srima-Shastri Pact (1964) (to resolve the citizenship question of the hill country Tamils who were brought from India to work in the plantations by the British), the Indo-Sri Lanka Peace Accord (1987) (to resolve the ethnic conflict in the Northern and Eastern provinces of Sri Lanka), and the Indo-Sri Lanka Free Trade Agreement (1998). The former two were political treaties and the latter an economic treaty. The Indo-Sri Lanka Free Trade Agreement was signed on December 28, 1998 and was supposed to have come into effect on March 01, 1999. Alas it came into operation only on March 01, 2000, typifying an ingrained characteristic of South Asia. Yet, at the operational level it has not come into force in Sri Lanka by mid-March (I have no idea about the Indian side), because according to the Customs they have not received the necessary authorization/instruction! However, the Customs is allowing the importers to clear their goods against a bank guarantee.

The Indo-Sri Lanka Free Trade Agreement consists of the Agreement and six Annexures–list of items entitled for 25% duty concessions by India [Annexure A para 1(b)], negative list of items of India (Annexure D-I), negative list of items of Sri Lanka (Annexure D-II), list of items entitled for 100% duty concession by India (Annexure-E), list of items entitled for 100% duty concessions by Sri Lanka (Annexure F-I), and list of items entitled for 50% duty concessions by Sri Lanka (Annexure F-II). The items which are not included in Annexure A para 1(b), Annexure D-I, or Annexure-E of India are entitled for 50% duty concession, though this list is not published.

'Free trade' is understood to be export and import of goods and services unhindered by tariff and non-tariff (for example, quantitative restrictions) barriers to trade. A necessary corollary to free trade in goods and services is the free movement of factors of production, particularly capital. The content of the Annexures of the FTA are summarized in the table.

	India		Sri Lanka	
	(Nos)	(%)	(Nos)	(%)
Negative List (no duty concession)	428	23.94	1183	49.48
25% duty concession	9	0.50	0	0
50% duty concession	-	-	889	37.18
100% duty concession	1351	75.56	319	13.34
Total	**1788**	**100.00**	**2391**	**100.00**

Accordingly, India has placed 428 items on their negative list and Sri Lanka has placed 1183 items on their negative list (normal rate of import duty is applicable to the goods in the negative lists). India has placed 9 items on their list entitled for 25% duty concession and Sri Lanka none. Sri Lanka has placed 889 items on their list entitled for 50% duty concession and India has not specified. Further, India has placed 1351 items and Sri Lanka has placed 319 items on their respective lists entitled for 100% duty concession. The items listed in the negative lists, 25% duty concession list, and the 50% duty concession list do not constitute 'free trade,' and only the items listed in the 100% duty concession lists constitute 'free trade.' Therefore, only 76% of the importable goods from Sri Lanka are entitled for 'free trade' in India, and a mere 13% of the importable goods from India are entitled for 'free trade' in Sri Lanka. The trade in goods entitled for 25% and 50% duty concessions are 'preferential trade' and not 'free trade' (some of these goods may be already covered by the South Asian Preferential Trade Agreement - SAPTA). Further, the trade in goods listed in the negative lists are neither 'preferential trade' nor 'free trade.' In the scenario of foregoing realities it is a misnomer to call this a 'Free Trade Agreement' (FTA).

The fact that India has placed only 24% of the total goods (428 out of 1788) in their negative list and the rest 76% (1351 items out of 1788) in the 'free trade' list may look very generous. However, it is not very much the number of goods, but the type of goods that matters here. For example, India has placed coconut and coconut products, natural rubber and rubber products, ready made garments and alcoholic spirits in its negative list [Annexure D-I], in which Sri Lanka seems to have comparative advantage over similar/same Indian products. Further, India has placed non-tariff barrier (quantitative restriction) to imports of tea and garments from Sri Lanka. A quota of 15 million kilograms of tea and 8 million pieces of garments per year are stipulated. However, in the context of prohibition on imports of agriculture produce and textiles and garments in India since independence these quotas seem to be a concession. Likewise, although the number of goods in the list entitled for 100% duty concession by India may seem to be impressive, Sri Lanka may not be in a position to exploit this concession fully due to resource and production constraints and price non-competitiveness vis-a-vis same/similar Indian products. Besides, the rules of origin clause (whereby at least 35% of the value added of the final product has to be in the country of export which is reduced to 25% if the inputs are from the import country) in the FTA may also preclude Sri Lanka's export of vast majority of goods included in the 100% duty concession list of India. Nevertheless, this (100% duty concession) may prompt greater foreign investment in Sri Lanka (including from India), over time, in order to penetrate the much larger Indian market. Ceramic and some rubber products are two notable Sri Lankan export goods that have potential to substantially exploit the 100% duty concession by India. During 1976-94 Sri Lanka exported 487 items to India (based on an item exported at least one year during the period), but bulk of it were traded irregularly and in very small values. Sri Lanka exported only a dozen major items to India regularly and in substantial values, mostly primary products and raw materials (Sarvananthan, forthcoming). In this scenario, the 1351 items granted duty free status by India may be an elusive export target for Sri Lanka to attain. Having said that, just because in the past Sri Lanka has managed to export only a handful of items regularly it does not mean that Sri Lanka cannot widen its exports to India in the future. Anyhow, it may be a long haul.

On the other hand, Sri Lanka's inclusion of 49% of the total goods (1183 out of 2391) in the negative list and a mere 13% in the 'free trade' list is abysmal to say the least. Some of the goods included in Sri Lanka's negative list may be defended on the grounds of protecting indigenous small and medium scale agricultural and industrial producers, but some of them are ludicrous and/or not in the best interest of the domestic consumers. Let us look at a few examples of the latter case. The rationale for including wheat and wheat flour (Annexure D-II, p19&20) in the negative list is intriguing, because this is entirely an import item and an essential commodity. Bulk of the wheat imports by Sri Lanka is from America under the PL480 agreement. Besides, the import of wheat is monopolized by the state-owned Co-operative Wholesale Establishment (CWE), and the processing into wheat flour is monopolized by Prima Ceylon Ltd (a Singaporean multinational company). According to a study undertaken by the USAID in early-1990s, CWE was making considerable amount of loss in wheat import, processing and wholesale marketing operations. In these circumstances, it is hard to understand the inclusion of wheat and wheat flour in the negative list of Sri Lanka. Further, the inclusion of fish and fish products (p4-8), milk and dairy products (p8&9), motor vehicles and parts, bicycles (p81-84), tooth brushes, ball point pens, pencils (p88), combs, hair slides and hair pins (p89) in Sri Lanka's negative list does not seem to be well thought-out. For example, due to the civil war fish catch in Sri Lanka has drastically declined in the past two decades and imports from India are necessary to meet local demand for this essential commodity. Moreover, domestic milk and dairy production falls far short of the local requirement. Therefore, duty free access (or at least a duty concession) to Indian fish and fish products, and milk and dairy products would have gone a long way to meet the nutritional requirements of Sri Lankan consumers. Further, duty free access or duty concession to imports of motor vehicles and parts, and bicycles from India would have benefited consumers in Sri Lanka by lowering transport costs. Finally, tooth brushes, ball point pens, pencils, combs, hair slides and hair pins are mass consumption wage goods, and therefore the inclusion of these items in the negative list does not seem to be in the best interest of consumers.

It is not only that the number of items accorded 'free trade' status by Sri Lanka is paltry, but also the composition seems not worth mentioning. The list of 319 items entitled for 100% duty concession by Sri Lanka overwhelmingly comprises chemical and chemical products, and medicinal products (antibiotics, vitamins, etc) (Annexure F-I).

The FTA mentions that India would phase out tariffs within 3 years (except for the items in Annexure A para 1(b)), and that Sri Lanka would phase out tariffs within 3 years for items entitled for 50% duty concession at the moment (Annexure F-II) and within 8 years for the rest of the items (except the items in its negative list). The respective negative lists will stay intact even after the proposed phasing out of tariffs over time. Although India claims to have removed all non-tariff barriers to imports from Sri Lanka, the above mentioned quotas for tea and garment imports from Sri Lanka nullifies this claim.

In sum this is hardly a 'Free Trade Agreement,' and India and Sri Lanka have to go a long way to achieve that goal. Besides, no FTA will be effective without provision for unhindered movement of capital, especially in the Indo-Sri Lanka case (see Sarvananthan, forthcoming). Therefore, India and Sri Lanka should work towards this goal as well. It seems that the Indo-Sri Lanka Free Trade Agreement was a hastily concluded treaty, because India was perhaps feeling the pinch of American economic sanctions in the aftermath of nuclear tests undertaken in May 1998 and therefore was looking for alternative export markets, and Sri Lanka was perhaps pushed into the treaty to be in the good books of India due to politico-military considerations connected to the protracted civil war in Sri Lanka.

At the outset it was mentioned about three major treaties between India and Sri Lanka in the past four decades–'Pact,' 'Accord' and 'Agreement'. The 'Pact' was never fully implemented, the fate of the 'Accord' is all too well known, and now I do not see much prospect for the 'Agreement' either in respect of fulfilling its objectives. To me, only a partial success of the 'Pact' and 'Accord' stems from the fact that the primary stakeholders of these treaties were only marginally incorporated in the policy-making process. Similarly, I do not think that the main stakeholders of the FTA were incorporated in this policy-making endeavour. It is high time India and Sri Lanka undertake a genuine soul-searching of their policy-making process. ■

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