

# Indo-Sri Lanka Free Trade Agreement: An Analysis of India's Merchandise Trade Performance

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## Abstract:

Sri Lanka has been India's biggest trade partner in the South Asia region. Both the nations have a history of robust trade relationship which has been further cemented by signing of Indo Sri Lanka Free Trade Agreement. The ISFTA provides duty-free access and duty preferences to goods, barring those which are on the Negative List. Bilateral trade between India and Sri Lanka has increased by around 9 times ever since the agreement came into effect in the year 2001. Total trade between the two countries was US\$ 6.2 billion in 2018-19, out of which India's exports to Sri Lanka were US\$ 4.7 billion and imports were US\$ 1.5 billion.

This paper is an attempt at quantitative analysis of the impact of FTA on India's trade with Sri Lanka both in terms of volume & commodity composition. For this purpose the analysis has been divided into two distinct time periods i.e Pre-FTA and Post- FTA period. Subsequently a comparison of performance during both the periods is undertaken before arriving at a conclusion as to the performance of the agreement.

## Keywords:

Bilateral Trade, ISLFA, HS Classification

## INTRODUCTION AND OBJECTIVE:

The Indo-Sri Lanka Free Trade Agreement (ISLFTA) signed in the year 1998 was a result of long years of wait for the benefits from regional trade integration process to kick in. It was also pushed further by India's strategy of using bilateral Trade agreements with its neighbors, as well as by Sri Lanka's attempt to enter in the largest market of the region. The agreement resulted in both the countries exchanging much deeper commitments than they did under SAPTA.

The agreement has given due consideration to Sri Lanka, the lesser developed partner and provides special and differential treatment to the country to help it gain additional market access, as well as allowing longer period for phasing out tariff restrictions. The measure has had a positive impact on not only bilateral trade between these two countries, but also cross-border flow of investment.

The objective of this study is to analyze the impact of Free Trade Agreement (FTA) on member nations. The study investigates the trade data over two distinctive periods i.e Pre FTA(1996-2000) and Post FTA i.e (2001-2016) for:

- a) The overall trend in the bilateral trade.
- b) The changing composition of trade.

## RESEARCH METHODOLOGY

For fulfilling the objectives, study covers the trade data of the member nations of each group over two periods namely Pre Free Trade Agreement (FTA) years and Post FTA years to analyze the trends and draw out the impact of each bilateral agreement within the Region's trade. Study has compared first trade data (export and import data) among nations; thereafter commodity wise analysis has also been done. Firstly study has analyzed the trade data from India to Sri Lanka and Sri Lanka to India in pre FTA and post FTA and tried to examine the

impact of FTA on trade volume. Similarly, commodity wise analysis has also been done to examine the impact of FTA on pre and post FTA volume of commodities. The study has also compared the trade data of sampled countries with the world data for the robustness.

The study is based on secondary data. Trade data has been collected through wide variety of sources viz., journals on international trade, yearbooks publishing. Statistical data viz. World Bank, UN, Unescap, IMF, WTO, UNCOMtrade etc. Different online data sources, web sites, text books, magazines have also explored. The study includes two major types of data sets extensively in the present study are-

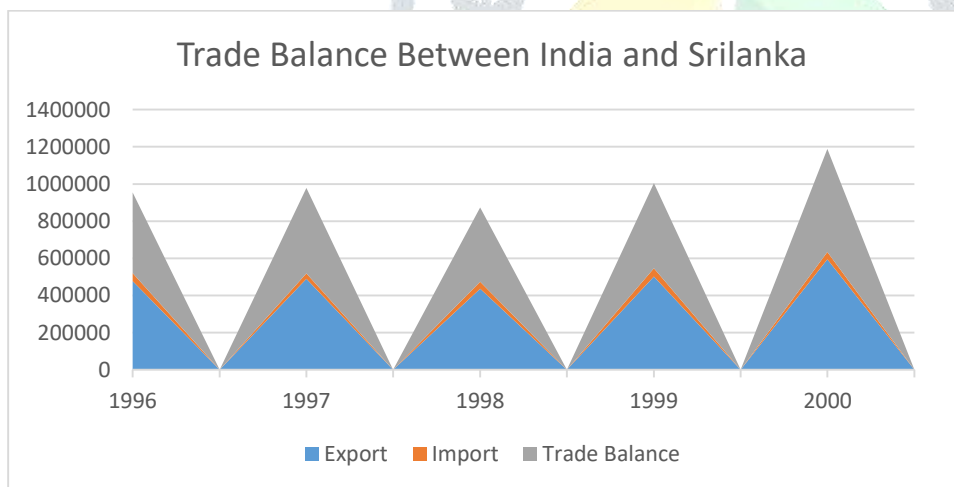
- a. Bi lateral Trade data
- b. Leading commodity group trade data.

UN COMTRADE database has been mainly used for data analysis. HS 1996 classification is considered as we can get information regarding the trade pattern before the signing of the agreement. Looking at the time series data of both the countries, it was found that data for India is available for the complete time series (1996-2016). But as UN COMTRADE database is concerned, Sri Lanka's data is not available for the complete time period. Data for the years 1996-1998 are missing.

WITS data is used to assess the changing pattern of trade with respect to leading product categories as per HS6 classification.

## OVERVIEW OF BILATERAL TRADE:

The pre FTA trade from India to Sri Lanka shows a generic growth in India's exports to Sri Lanka through 1996 to 2000 with a slight decline in 1998. The Compounded Annual Growth Rate of exports in pre FTA period was 5.62%. Imports from Sri Lanka had a relatively inconsistent pattern however the overall Compounded Annual Growth Rate of imports has been negative at -1.78%.



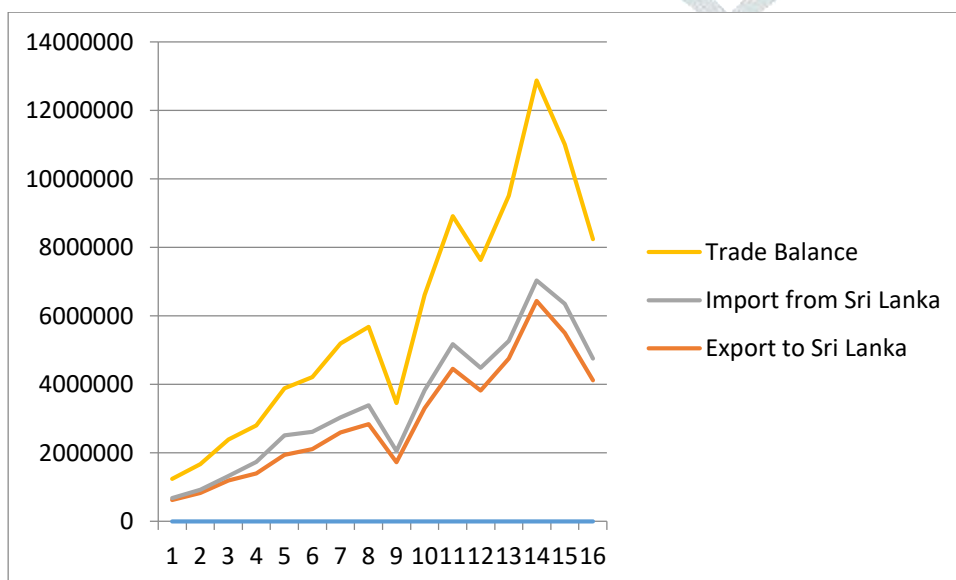
*PreFTA Trade Balance between India to Sri Lanka:*

Year	Export to Sri Lanka	Import from Sri Lanka	Trade Balance
<b>1996</b>	477369.4	42812.8	<b>434556.6</b>
<b>1997</b>	489329.6	30157.7	<b>459171.9</b>
<b>1998</b>	436957.1	37696.2	<b>399260.9</b>
<b>1999</b>	502183.6	44466.3	<b>457717.2</b>
<b>2000</b>	594165.4	39849.9	<b>554315.5</b>

Source: World Integrated Trade Solution (WITS) database

The Post FTA exports have shown a continuously rising trend from 2000 to 2008. Major slowdown has been seen in the year of 2009, 2012 and in 2016. Although an insignificant decline (0.5%) in India's exports to Sri Lanka was seen in 2001 (ISFTA implemented from March 2000), it gathered momentum from 2002 to 2008. In 2002, the y-o-y growth rate for the same was 40% and 42% in the following year. The only year which registered a 40% y-o-y decline in India's exports to Sri Lanka was 2009 owed to the global economic downturn. The decline in exports from India to Sri Lanka in 2012 is largely due to steep increase in the excise duty imposed on the import of vehicles on two occasions during the year 2012 that has seriously affected the competitive advantage. The period has registered an overall Compounded Annual Growth Rate of exports of 13.4 %. Assuming the year 2001 as transition period to free trade agreement, FTA has boosted the India's export to Sri Lanka as the same is visible in the form of double digit growth(considering year 2000 as base year) in almost all the years post FTA.

The impact of FTA is more pronounced on India's import from Sri Lanka which saw a reversal in trend of negative growth in India's Import from Sri Lanka in pre FTA period. Post FTA period provided a quantum jump in India's import from Sri Lanka. The period saw a Compounded Annual Growth Rate in imports at 17.67%



*PreFTA Trade Balance between India to Sri Lanka:*

Year	Export to Sri Lanka	Import from Sri Lanka	Trade Balance
2001	621,480	55,036	566,444
2002	831,902	92,276	739,626
2003	1,195,088	123,128	1,071,960
2004	1,400,312	333,184	1,067,128
2005	1,939,282	568,495	1,370,787
2006	2,105,026	505,177	1,599,849
2007	2,594,192	441,365	2,152,827
2008	2,838,024	548,622	2,289,402
2009	1,724,637	328,803	1,395,834
2010	3,305,123	518,122	2,787,001
2011	4,452,043	717,983	3,734,060
2012	3,813,120	665,452	3,147,668
2013	4,753,967	515,295	4,238,672
2014	6,434,957	591,996	5,842,961
2015	5,501,015	848,782	4,652,233
2016	4,118,254	632,273	3,485,981

Source: World Integrated Trade Solution (WITS) database

**COMMODITY WISE ANALYSIS:**

The Pre FTA period shows an increasing trend of number of HS6 exported products on y-o-y basis. Similarly the Import trend is also on increase except in the year 1999 where the number of imported products declined from 291 to 257 due to economic crisis. However the number of exported products to Sri Lanka is more than the number of products imported from Sri Lanka in Pre FTA.

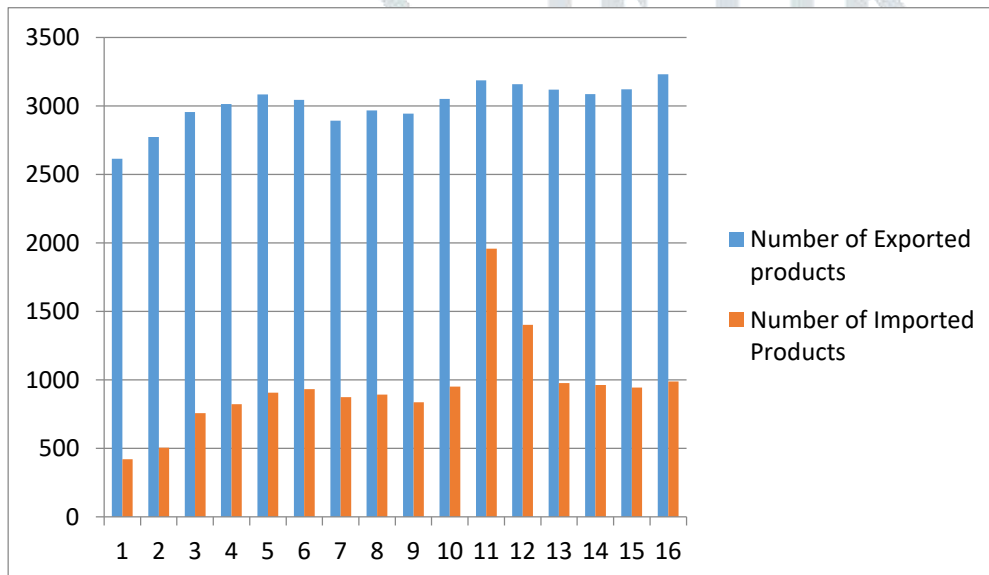


*Pre FTA No. of Products Exported/Imported*

Year	Number of Exported Products	Number of Imported Products
1996	1968	199
1997	2123	240
1998	2307	291
1999	2352	257
2000	2624	411

Source: UNComtrade database

Post FTA the number of commodities exported to Sri Lanka is continuously increasing from the year 2001 to 2016 except in the year of 2007, 2008 and 2009. Number of imported products from Sri Lanka was less than export. Number of products imported from Sri Lanka has also increased from the year 2001 to 2006, while decreased from 2007 to 2009 indicating an overall decline in the trade. A steep rise has also been noticed in the import in the year 2011, after that it is continuously decreasing.

*Post FTA No. of Products Exported/Imported*

Year	Number of Exported products	Number of Imported Products
2001	2614	422
2002	2774	506
2003	2954	757
2004	3014	823
2005	3084	906
2006	3045	932
2007	2893	875
2008	2966	893
2009	2943	836
2010	3052	952
2011	3186	1959

2012	3158	1401
2013	3118	976
2014	3087	963
2015	3120	944
2016	3230	989

Source: UNComtrade database

## DETAILED COMMODITY ANALYSIS

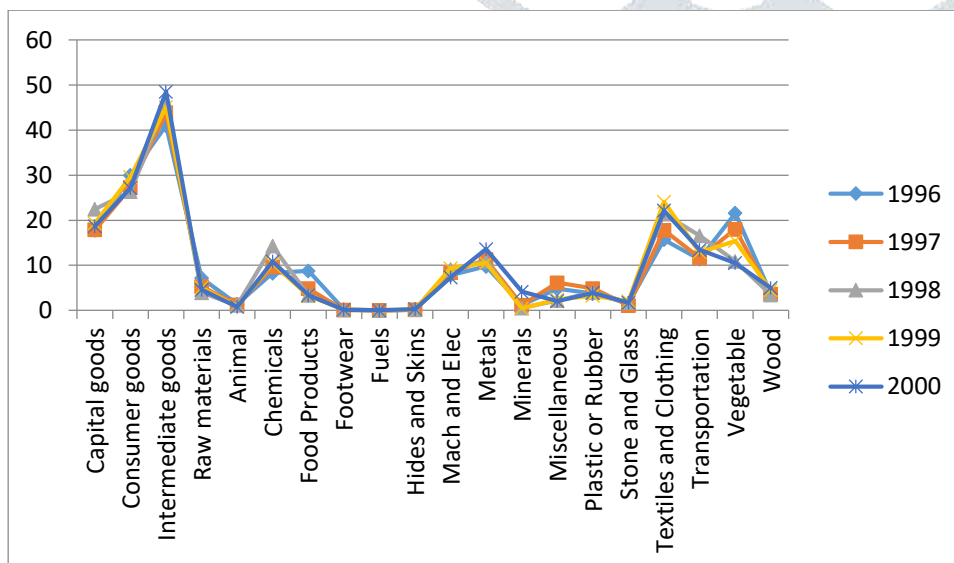
### Pre FTA Exports

The commodity wise trade data volume in percentage on year-on-year(y-o-y) basis during pre FTA has been analyzed. In case of capital goods y-o-y trade volume percentage has increased from 3.13% in 1997 to 14.3% in 2000 except in the year 1999 when major financial crisis was going on. Annual cumulative Growth Rate (ACGR) of capital goods exported to Sri Lanka was 6.93%

Consumer goods y-o-y trade volume percentage has increased from 5.07% in 1997 to 20.74% in 2000 except in the year 1998. Annual cumulative Growth Rate (ACGR) of consumer goods exported to Sri Lanka was 3.32%. In the same way all the commodity has been analyzed and author has found that ACGR of fuels is highest (49.33%), after that minerals (43.91%), hides and skin (22.49%) is high. Analysis has also found that textile and clothing (15.15%) and chemicals (12.99%) have also reported high ACGR. Y-o-Y basis high growth has been reported on fuels which increase form 28% in 1997 to 128% in 2000 to Sri Lanka. Another interesting fact has been noted in the case of minerals y-o-y basis export percentage was nil in 1997 while this has increased to 918% in 2000.

On the other hand, lower growth in the export has been reported in the case of miscellaneous i.e. 31.29% (1997) to 1.05% and animals, vegetables, stones and glasses, mechanical and electrical, footwear etc. Negative growth in terms of ACGR has been reported in chemicals (-12.99%), raw materials (-5.59%), animals (-8.89%), food products (-16.91%) and in case of vegetables (-11.76%).

India's export to Sri Lanka as a percentage of total exports



Source: Author's computation based on WITS data

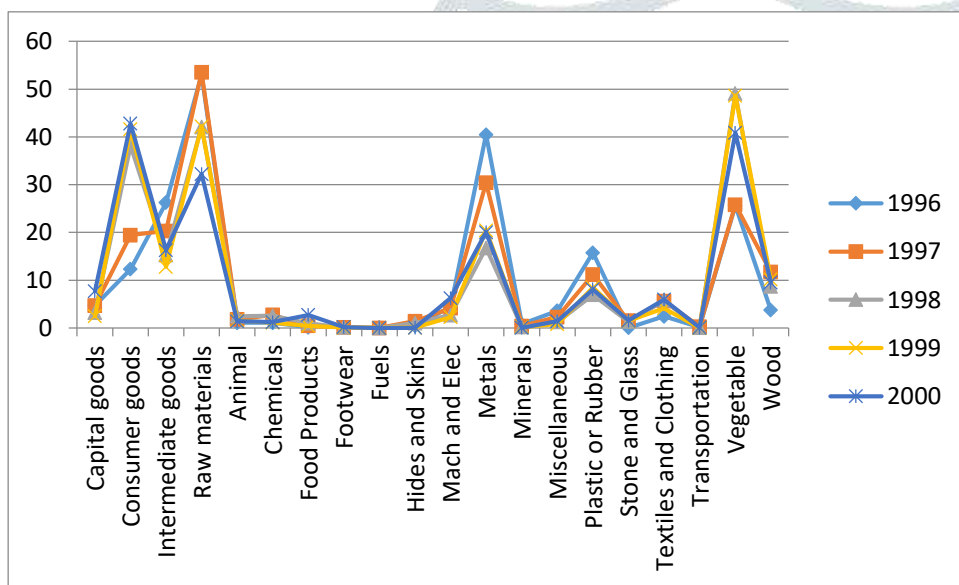
## Pre FTA Imports

Volume of import from Sri Lanka was less in comparison to export. Higher growth on y-o-y basis has been reported in case of capital goods, raw materials, food products, foot-wears, mechanical and electrical, transportation and textile and clothing.

Lower growth in import on y-o-y basis has been reported in case of consumer goods, raw materials, animals, chemicals, fuels, hides and skins, metals, minerals, vegetables and woods. World-wide high growth in import has been reported in capital goods, raw materials, fuels, mechanical & electrical and textiles and clothing.

High ACGR in case of import from Sri Lanka has been reported in the commodities of consumer goods (34.08%), food products (99.66%), footwear (195.69%), stones and glasses (133.46%). Lower ACGR has found in fuels (-75.74%), hides and skins (-39.89%), minerals (-57.65%), miscellaneous (-1.89%) and transportation (-21.06%).

### India' Import from Sri Lanka as a percentage of total imports



Source: Author's computation based on WITS data

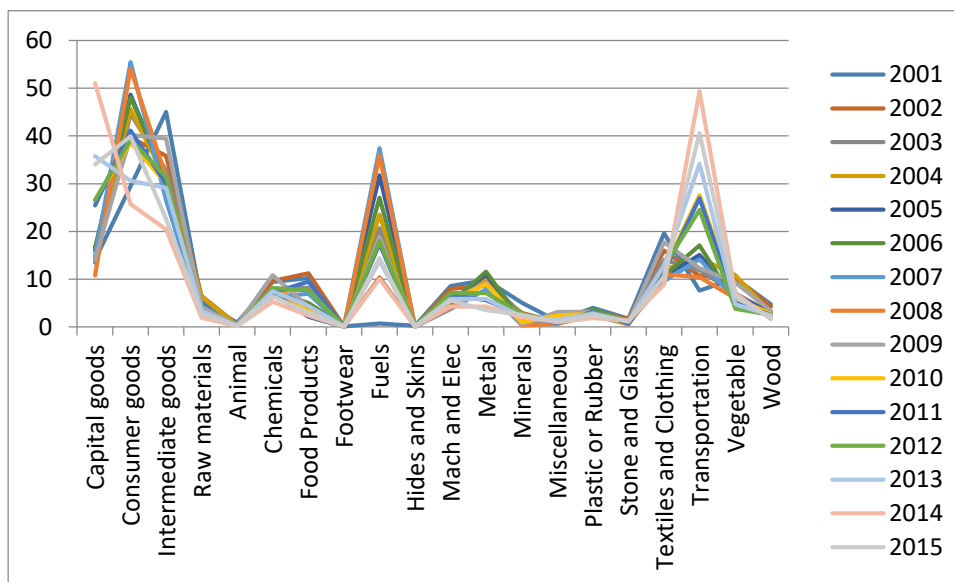
## Post FTA Exports

Trade volume is very fluctuating from the year 2001 to 2016, major fluctuation has been observed in the period of 2007 to 2009. FTA helped in increasing % export of capital goods to Sri Lanka. This happened despite the share of capital goods in India's export basket decreased in post FTA era. Although post FTA export of consumer goods to Sri Lanka increased % but did not alter India's export basket composition. Thus, the export growth to Sri Lanka and world were in the same range. No visible impact of export of intermediate goods to Sri Lanka is seen. Although there has been % increase in export of raw material to Sri Lanka in FTA but its % growth in comparison to export to world was less. Thus, there was no impact of FTA on export of raw material to Sri Lanka. Though % growth of export to Sri Lanka substantially increased in post FTA era but lagged behind the % growth of export of animal to world. Thus, the increase in export of animal to Sri Lanka could be assigned to overall % increase of export of animal to world by India. Although growth of export of food product to Sri Lanka increased in post FTA era, but it was far behind overall % growth of export of food products to world. No advantage to India in regard to export. In case of footwear India is in advantageous position from the world. Post FTA fuels export to Sri Lanka has increased by 32.12% while to the world only 18.34%. In case of

hides and skin post FTA reduction has been seen in the export. There has been substantial increase in % growth of export of machinery and electrical goods to Sri Lanka in post FTA but it remained below the % growth of export to world. Thus, no impact of FTA on export.

FTA has helped in increasing export of miscellaneous commodity to Sri Lanka. The % growth of export of Plastic & Rubber to Sri Lanka increased in post FTA era but lagged behind corresponding % growth export to world. Thus, no impact of FTA on India. In case of stones and glasses India is in the advantageous position. In textile and clothing export has been decreased while in the case of transportation export has increased. Post FTA no visible impact has been observed in the vegetables as export to Sri Lanka and worldwide it is same. Interesting fact has been seen in case of export of woods, worldwide export of woods has increased while to Sri Lanka has decreased.

#### *India's Export to Sri Lanka as a percentage of total exports*



Source: Author's computation based on WITS data

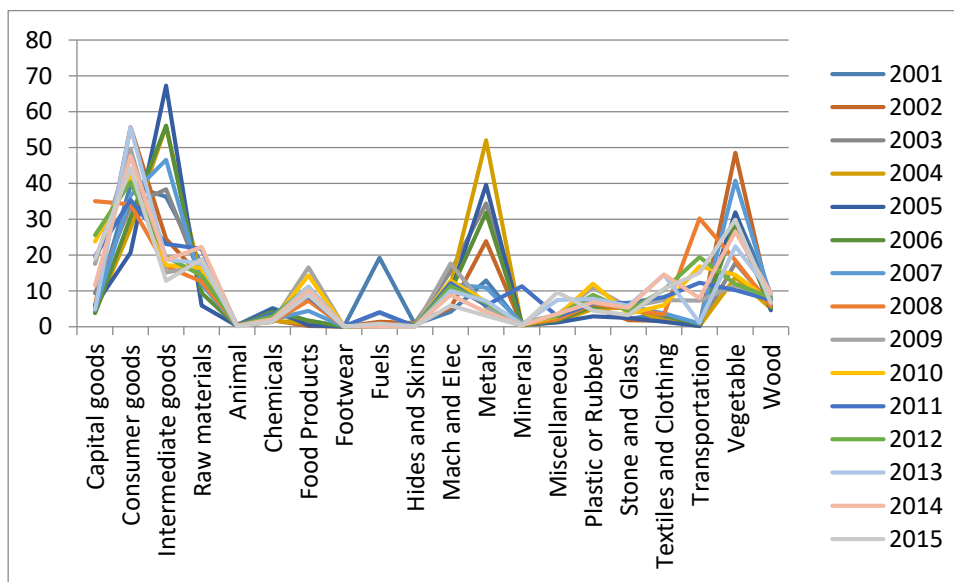
#### **Post FTA Imports**

FTA helped in increasing % import of capital goods from Sri Lanka from 10.69% to 22.27%. While import from Sri Lanka of consumer goods declined substantially in post FTA but import from world increased substantially. Import of intermediate goods from Sri Lanka substantially increased in post FTA era. So, is the import from world. It can therefore be concluded that since India imported more intermediate goods as a whole, the increase of import from Sri Lanka cannot be assigned to FTA. There has been significant growth on import of raw material from Sri Lanka. This has happened despite the fact that import of raw material from world decreased almost by half. Thus, FTA helped Sri Lanka in increasing export of raw material to India. While, there is marginal increase in growth of import of animal from Sri Lanka, there has been substantial reduction in import of animal from world. Thus, it is situation advantage to Sri Lanka. However, import of chemicals from Sri Lanka increased substantially but, this is on account of corresponding increase of import of chemicals from world. Though there has been substantial reduction in % growth of import of food products from Sri Lanka yet it was far more above the % growth of import of food products from world. There has been reduction in % growth of import of footwear from Sri Lanka. Despite the fact India's import of footwear from world many fold increased. Thus, indicating a negative impact for Sri Lanka.



Although there has been an increase in import of fuel from Sri Lanka in post FTA era. It is in consonance with % growth of import from world. Thus, there is no impact of FTA either on export or import. There has been check in negative growth of import of hides & skins in post FTA. There seems to be no impact of FTA either on India or Sri Lanka. Growth in import of Machinery & electrical from Sri Lanka has been witnessed in post FTA era, but there had been corresponding % growth in import from world so no impact on import from Sri Lanka. There was substantial increase in % growth of import of metals from Sri Lanka in post FTA but lagged behind % growth of import from world, so, no impact on import. In case of plastic and rubber no impact of FTA has been observed. There has been substantial decrease in import % growth of Stones & Glass in post FTA era. Thus it is advantage India. In case of textile & clothing and transportation impact of FTA has been observed. No visible impact of FTA on vegetables and woods has been observed.

#### *India's Import from Sri Lanka as a percentage of total imports*



Source: Author's computation based on WITS data

#### **Conclusion:**

It would be safe to conclude that the ISLFTA had a significant bearing on India's trade with Sri Lanka both in terms of value and the number of commodities traded. Post FTA saw a significant jump in the value of exports which recorded a Compounded Annual Growth Rate of 13.4% as compared to just 5.62% in the pre- FTA period. The impact is more pronounced on India's import from Sri Lanka which saw a complete reversal of negative growth in the Pre FTA period to a positive figure of Compounded Annual Growth Rate of 17.67%. The post FTA period also saw a steady rise in the number of HS6 commodities exported and Imported.

A detailed commodity wise analysis brings forth many interesting inferences with respect to each category. In case of Capital goods in the first 10 years of FTA there was no change in percentage composition but from 2010 onwards there has been substantial increase in percentage of capital goods in the India's Export Composition. While consumer goods saw a visible increase in both Export as well as import post FTA, raw materials saw a declining trend on both the aspects. In case of intermediate goods FTA gave a favorable result to Sri Lanka with CAGR being more pronounced for Imports as compared to exports. Chemicals too saw a more or less same growth in both exports as well as imports. Fuel too showed a positive trend in both exports & imports post FTA however Exports showed a more favorable result.

Hence while in terms of value and number of commodities traded FTA has pushed up India's trade with Sri Lanka, however not much alteration has been seen in case of commodity composition. The structural composition has more or less remained the same wherein most of the commodity groups have benefitted.

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