

EXPORT-IMPORT BANK OF INDIA

WORKING PAPER NO. 74

**INDO-SRI LANKA TRADE AND INVESTMENT RELATIONS:
CURRENT TRENDS AND PROSPECTS**

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EXECUTIVE SUMMARY

Sri Lanka's macroeconomic performance has continued to be progressive over the recent years, with real GDP growth remaining above 4 percent during 2014-2016. However, in 2017, the real GDP growth declined to 3.1 percent, owing mainly to negative growth rate of agricultural output in the first three quarters of the year. In absolute terms, nominal GDP and per capita income of Sri Lanka rose in 2017 to US\$ 87.4 billion and US\$ 4,065, respectively. The per capita income of Sri Lanka is higher than that of the other SAARC countries like Bangladesh, Bhutan, India, and Nepal. Average consumer price inflation, however, increased to 6.5 percent in 2017 compared to 3.8 percent in the previous year, owing to an increase in Value Added Tax (VAT) as well as an upward pressure on food prices due to fall in agricultural production. The Central Bank of Sri Lanka, in early 2017, decided to adopt a new, relatively market-driven framework for exchange rate management under the pressure to preserve sparse foreign exchange reserves. Sri Lanka's international reserves in 2017 represent an import cover of 3.7 months.

Sri Lanka is ranked 111th in terms of Ease of Doing Business in 2018 conducted by the World Bank and the International Finance Corporation. The government of Sri Lanka has been pursuing large-scale reconstruction and development projects in its efforts to spur growth in disadvantaged areas, develop small and medium enterprises and increase agricultural productivity. Sri Lanka has set its goal of "Vision 2025" with an aim to attain the status of an upper-middle income country by 2025 with a knowledge-based, highly competitive, social-market economy, by positioning Sri Lanka as an export-oriented economic hub at the centre of the Indian Ocean. Under this vision, Sri Lanka's target is to create one million new jobs, increase Foreign Direct Investments (FDI) to US\$ 5 billion per year and per capita income to US\$ 5,000 per year, and raise its exports two-fold to US\$ 20 billion per year, over the next three years.

International Trade of Sri Lanka

Ever since the liberalization of trade policy, Sri Lankan trade has been performing reasonably well. Over the decade, Sri Lanka's total trade increased from US\$ 19 billion in 2007 to US\$ 30 billion in 2016. The period witnessed increase in Sri Lanka's exports to US\$ 10.5 billion in 2016 from US\$ 7.7 billion recorded in 2007. Similarly, imports also increased to US\$ 19.5 billion in 2016 from US\$ 11.4 billion in 2007, mainly owing to higher imports of consumer and investment goods. The period also witnessed simultaneous widening of trade deficit owing to higher growth of imports.

Sri Lanka's exports as a percentage of GDP has been declining since 2011, from 16.2 percent to 12.7 percent in 2016. Similarly, imports as a percentage of GDP has also declined since 2011 from 31 percent of GDP to 23.6 percent of GDP in 2016. Further, a substantial proportion of Sri Lanka's exports have high import intensity. This is true especially in case of industrial exports which are reliant on imported inputs.

Composition of Sri Lanka's Merchandise Trade

According to data obtained from ITC, articles of apparel were the major export items of Sri Lanka, accounting for more than 40 percent of Sri Lanka's exports in 2016. Other major products in Sri Lanka's export basket during the same year comprised coffee, tea, mate and spices; rubber and articles; electrical machinery and equipment; and pearls, precious stones, metals and coins.

Mineral fuels, oils and their products continued to be the major imports of Sri Lanka in 2016, though its share declined from 23.5 percent of total imports in 2007 to 12 percent in 2016. Machinery and mechanical appliances, vehicles other than railway or tramway, electrical machinery and equipment, and knitted or crocheted fabric were the other major imports in 2016.

Direction of Sri Lanka's Merchandise Trade

India is the largest trading partner of Sri Lanka, though its share in Sri Lanka's total trade has decreased from 17.3 percent in 2007 to 15.2 percent in 2016. Other major trading partners of Sri Lanka in 2016 include China, the US, UK, UAE and Japan. A major shift in the recent years is a large improvement in the share of China in Sri Lanka's total trade from 5.1 percent in 2007 to 14.9 percent in 2016. The US and UK witnessed declining trends in their share over the decade, where as that of UAE and Japan marginally improved.

As a region, EU is the major export destination of Sri Lanka in 2016, with total exports from Sri Lanka amounting to US\$ 3.1 billion, increasing from US\$ 2.9 billion in 2007. As regards country-wise destination of exports, the US was the major export destination of Sri Lanka, accounting for 26.6 percent of Sri Lanka's total exports in 2016, followed by UK, India and Germany. Among the top destinations, there has been a gradual shift in Sri Lanka's export directions toward the US, India, UAE and China during the last decade as indicated by their rising shares.

India had traditionally been a major import source for Sri Lanka, contributing 24.4 percent of Sri Lanka's total imports in 2007. In 2016, China overtook India to become the major import source of Sri Lanka, with a 21.9 percent share in Sri Lanka's total imports, as against 19.6 percent share in the case of India. This is due to the sharp decline in imports of vehicles other than railway or tramway rolling stock and mineral fuels, oils and products from India. Other major import sources include UAE, Singapore, Japan, Malaysia and the US. Sri Lanka's imports from EU as a region increased from US\$ 1.4 billion in 2007 to US\$ 2.1 billion in 2016, though its share has decreased from 12.3 percent to 10.7 percent during the same period.

Concentration of Exports in Sri Lanka

Sri Lanka's merchandise exports are mainly concentrated on a few select set of products (apparel,

tea, and rubber), and are often targeted at a limited range of buyers, most of which are in developed country markets. For instance, 44 percent of Sri Lanka's exports are concentrated in three markets, the US, UK and India in 2016. Another critical aspect is that Sri Lanka's exports to leading Asian markets except for India continue to remain poor, and is mostly dependent on a few major Western markets. Similarly, 58 percent of Sri Lanka's exports are concentrated on three products, articles of apparel and clothing accessories, knitted or crocheted; articles of apparel and clothing accessories, not knitted or crocheted; and coffee, tea, maté and spices. However, these three top exports of Sri Lanka are not among the top ten products exported globally.

Foreign Direct Investment in Sri Lanka: Current Trends

There has been an increase in both inflow and outflow of Sri Lanka's Foreign Direct Investment (FDI) in 2016. Sri Lanka has been attracting investments in various industries such as apparel, construction, tourism and real estate. According to UNCTAD, FDI inflows into Sri Lanka registered a 32.1 percent rise in 2016, increasing to US\$ 898.1 million from US\$ 679.7 million in the previous year. Similarly, FDI outflows from Sri Lanka witnessed a four-fold increase to US\$ 236.8 million in 2016 from US\$ 54 million in 2015.

According to fDi Markets online database, the number of FDI projects in Sri Lanka increased from 15 in 2007 to 35 in 2016, resulting in increased total capital investment to US\$ 2.2 billion in 2016 from US\$ 541.8 million in 2007. Cumulative capital expenditure in Sri Lanka out of total 315 FDI projects during the decade stood at US\$ 17.4 billion, creating 66,720 jobs in the country. During 2007 to 2016, financial services were the largest sector to receive capital investment followed by hotel & tourism and warehousing & storage amounting to US\$ 2.6 billion, US\$ 2.5 billion and US\$ 2.1 billion, respectively. India is the largest investor in Sri Lanka during the period 2007-2016, with an investment of US\$ 5.3 billion

(30.7 percent of the total FDI). The other major investors during the last ten years are Hong Kong (accounting for 11.1 percent of total inward FDI received by Sri Lanka), followed by Germany (9.5 percent), China (5.4 percent), South Africa (5.2 percent) and UK (4.4 percent).

According to fDi Markets database, the number of outward FDI projects from Sri Lanka increased across the years, with a cumulative number of 72 projects during 2007-2016, and a capital expenditure amounting to US\$ 1.8 billion, creating 7,035 jobs in destination countries. In terms of sectors, financial services received maximum investment, with a share of 37.1 percent in total outward investment from Sri Lanka during the period 2007-2016. This was followed by transportation (29.9 percent share), hotel & tourism (7.9 percent), software & IT services (5.2 percent), textiles (5 percent) and food and tobacco sectors (4.9 percent). During 2007-2016, the major destinations of Sri Lanka's outward investment include India (33.4 percent of total outward investment by Sri Lanka), Oman (14.1 percent), Australia (13 percent), Maldives (12.6 percent), Hong Kong (4 percent) and Myanmar (4 percent).

Potential Sectors for Investment in Sri Lanka

According to the Board of Investment (BOI), Sri Lanka, Sri Lanka offers the following investment incentives to foster FDI in the country.

- Total foreign ownership is permitted across almost all areas of the economy.
- No restrictions on repatriation of earnings, fees, capital, and on forex transactions relating to current account payments.
- Safety of foreign investment is guaranteed by the constitution.
- Existence of a transparent and sophisticated legal and regulatory framework, covering all prerequisite business law enactments.
- Duty free (Customs Duty) import facility on plant, machinery & equipment during the project implementation period.

Target sectors actively promoted by Sri Lanka through BOI include:

- Export Oriented Manufacturing
- Export Oriented Services
- Tourism and Tourism Related Projects
- Infrastructure Projects
- Higher Education/Skill Development
- Value Added Strategic Projects
- Agriculture (Agro Processing, Fish Based Industry, Dairy) and
- Establishment of Industrial Estates, Special Economic Zones and Knowledge Cities.

India-Sri Lanka Bilateral Trade and Investment Relations

India's exports to Sri Lanka increased by a compound annual growth rate (CAGR) of 5.3 percent to US\$ 4.1 billion in 2016 from US\$ 2.6 billion in 2007. Similarly, India's imports from Sri Lanka increased by a CAGR of 4.1 percent to US\$ 0.6 billion in 2016 from US\$ 0.4 billion in 2007. India has maintained a trade surplus with Sri Lanka over the years, which stood at US\$ 3.5 billion in 2016, owing to India's size, population and rapidly emerging economy.

The major commodities exported by India to Sri Lanka during 2016 were vehicles other than railway or tramway accounting for 15.2 percent of the total exports, followed by aircraft, spacecraft and their parts; mineral fuels, oils and product of their distillation; ships, boat and floating structures; and cotton. A notable factor is that a number of products exported to Sri Lanka like aircraft, spacecraft and their parts; ships, boats and floating structures; salt, sulphur, earth and stones; knitted or crocheted fabrics; paper and its articles; and edible vegetables, roots and tuber have a significant share in India's

total exports to the world in 2016 thereby revealing the importance of Sri Lanka as an export destination for India. The major commodities imported from Sri Lanka in 2016 were coffee, tea and spices accounting for a share of 11.1 percent in total imports from Sri Lanka, followed by residue from food industry & animal fodder (8.3 percent), edible fruits and nuts (7.2 percent), mineral fuels, oils and product of their distillation (6.6 percent) and knitted or crocheted fabrics, and ships, boats and floating structures (5.7 percent each).

India Sri Lanka Free Trade Agreement (ISFTA)

India and Sri Lanka signed the India-Sri Lanka Free Trade Agreement (ISFTA) in December 1998, which has come into force in March 2000. The ISFTA covers only trade in goods. It provides either duty free access (zero duty) or duty preferences for products that are not under the Negative list. While India provides 4,227 Sri Lankan products duty free access to India, Sri Lanka provides 2,802 Indian products duty free access to its economy. In the negative list there are 431 products from India's side (garments, plastic products, rubber products etc), whereas 1,220 products from Sri Lanka's side (agricultural/livestock products, paper products, rubber products, electrical items etc) do not have any duty concession. They are excluded to protect the local industry. However, India has provided quotas on exports of tea, textiles and garments.

At present, the Economic and Technical Cooperation Agreement (ETCA) is being negotiated between the two countries as an extension over the ISFTA to widen the scope of trade, investment and technological cooperation. However, it would exclude movement of professional labour other than two sub-sectors – ship builders and IT professionals. The ETCA aims to boost cooperation in technical areas, scientific expertise and research among institutions, boost standard of goods and services to be able to compete in the global market and improve opportunities for manpower training and human resource development.

Bilateral Investment between India and Sri Lanka

India and Sri Lanka signed a Bilateral Investment Promotion and Protection Agreement on January 22, 1997, which came into force on February 13, 1998. According to data from the Ministry of Finance, Government of India (GOI) and the Reserve Bank of India (RBI), India's approved cumulative investments in Sri Lanka during April 1996 to March 2018 amounted to US\$ 1.5 billion.

According to fDi Markets database, India has emerged as the largest investor in Sri Lanka during 2007 to 2016 with US\$ 5.3 billion investment in 61 FDI projects, resulting in creation of 14,196 jobs. It accounts for 30.7 percent of total investments made in Sri Lanka during this period. Coal, oil and natural gas received the highest investment which amounted to US\$ 1.9 billion, followed by real estate (US\$ 1.2 billion), financial services (US\$ 0.6 billion), hotels & tourism (US\$ 0.5 billion) and automotive OEMs (US\$ 0.2 billion) during this period. Similarly, Sri Lanka has invested capital of amount US\$ 0.6 billion in 15 greenfield projects leading to creation of 1,555 jobs in India during 2007 to 2016. The major sectors in which Sri Lanka has invested are transportation (US\$ 360.6 million), financial services, textiles, and food and tobacco.

Potential Commodities for Enhancing Bilateral Trade with Sri Lanka

With a view to boosting bilateral trade relations with Sri Lanka, an important endeavor could be enhanced sourcing of Sri Lanka's imports from India, in which India has export capability and competitiveness. This would entail identification of potential items of India's exports, which would be based on the following analysis:

- Identification of major items of imports of Sri Lanka, and share of India in each product line of imports, based on 2-digit HS code
- Selection of potential items of India's exports to Sri Lanka, based on low share of India in Sri Lanka's import basket of major commodities; keeping in view India's global export capability,

as also Sri Lanka's demand for import of such commodities. This would further entail identification of potential export items to each market, up to the 6-digit HS code.

Based on the above criterion, potential items of exports from India to Sri Lanka identified at 2-digit HS Code classification would therefore include:

- Machinery and mechanical appliances (HS-84)
- Electrical machinery, equipment and their parts (HS-85)
- Pearls, precious stones and metals (HS-71)
- Special woven & tufted textile fabrics, lace, tapestries, and embroidery (HS-58)
- Aircraft, spacecraft and parts (HS-88)
- Optical, photographic, medical and surgical apparatus (HS-90)
- Cereals (HS-10)
- Dairy produce, eggs, honey and other edible products of animal origin (HS-04)
- Ships, boats and floating structures (HS-89)
- Man-made filaments and man-made textile materials (HS-54)
- Animal or vegetable fats and oils (HS-15)

Similarly, potential items of Sri Lanka's exports to India have been identified based on low share of Sri Lanka in India's imports, keeping in view Sri Lanka's global export capability, as also India's demand for import of such commodities. These would include:

- Mineral fuels, mineral oils and their distillation products (HS-27)
- Pearls, precious stones and metals (HS-71)
- Coffee, tea, maté and spices (HS-09)

Strategies for Improving Export Potential of Sri Lanka

Widening Export Base: Sri Lanka has a narrow export base, with exports being concentrated on few products and partners. The share of Sri Lanka's exports

in total global exports remained low at 0.07 percent in 2016 as compared to 0.06 percent in 2007. Because of the narrow export base, the country is exposed to large fluctuations in commodity prices. Currently, Sri Lankan economy focuses mostly on simple and unsophisticated products, with low share of high-tech exports. Sri Lanka's lack of export innovation and limited markets have restricted the export sector from reaching its full potential. The country should consider developing the export potential of other sectors. Export base should be expanded through a mix of strategies along with increased innovations in the sectors. New finance products along with interest rate subventions are also necessary for export development. Small and Medium Enterprises (SMEs) and non-traditional exporters need to be given a big push by providing export finance at a lower rate.

Product-Market Diversification: Sri Lankan exports are exposed to concentration risk where the demand conditions for select set of products and markets could have a significant bearing on the country's export performance. Diversification into new markets, new buyers as also new products is an imperative. For a wide market penetration, information on new markets, regulatory barriers in the countries etc. should be made easily available for the exporters. Exporters should also be provided support for new and niche product development which would give the country an edge in the international trade arena.

Strengthening Free Trade Agreements: There is also a need to strengthen and extend Sri Lanka's existing Free Trade Agreements (FTA). The World Bank has suggested that Sri Lanka should make progress on bilateral trade agreements while carefully evaluating the costs and benefits to the country, with special focus on non-tariff barriers and Mutual Recognition Agreements.¹ In the context of current lackluster export growth in the country, Sri Lanka could expand its trade with other developing countries, especially in Asia. This would enable the country to diversify

¹Enhancing competitiveness in Sri Lanka, World Bank, June 2016

its trade from Western developed economies, and reduce its vulnerabilities which emerge from adverse development in these economies. As South Asia is among the fastest growing regions in the world, Sri Lanka's FTAs with select Asian economies could play a major role here.

Strategies for Enhancing India-Sri Lanka Relationship

Geographical Diversification of Sri Lanka's Exports to India:

Sri Lankan exporters to India concentrate more on expansions into Tamil Nadu. It has been estimated that 40 percent of India's total trade with Sri Lanka takes place through Tamil Nadu, as a significant share of Sri Lankan exports to India enter through Chennai Port. This is at the expense of other trade-friendly South Indian states including Andhra Pradesh, Karnataka, Kerala, and Telangana.² Since trade through sea route is cheaper compared to other modes of transportation, and South India being home to six major sea ports of India along with other intermediate sea ports, the transshipment of cargos from Sri Lanka to various ports is easily possible at cheaper rates. An increased effective cooperation with the other Southern Indian states could pave way for integrating Sri Lankan manufacturing into various value chains present in the Indian manufacturing sector.

Cooperation to Formalize Informal Trade: Though no official figures are available for recent values of informal trade between both countries, various reports identify that there exists a large informal trade between India and Sri Lanka. The unofficial trade is carried out by both air and sea routes. The total informal trade between India and Sri Lanka is approximately 25-30 percent of the formal bilateral trade between both countries. Informal imports from India are around 40-45 percent of formal imports, while informal exports are around 25-30 percent of formal exports. Efforts should be

made to formalize this informal trade by means of trade and tariff liberalization, and relaxing the stringent government procedures, resulting in enhancement of formal bilateral trade between India and Sri Lanka. This also involves regular formal information exchange between both countries.

Setting up a Mechanism for Promoting Indian Investments in Sri Lanka:

Supported by its natural resources, investment incentives, educated work force and comparatively cheaper wages, Sri Lanka offers huge potential for investment for Indian investors in a number of sectors including tea, tourism, tyre manufacturing, manufacturing of vehicles, IT-enabled products and services, and infrastructure sector, among others. Sri Lanka is a beneficiary under GSP+ scheme of EU and also has FTAs with India, Iran and Pakistan. Sri Lanka signed a Comprehensive Economic Partnership Agreement with Singapore, and is currently negotiating FTA with China. It may not be necessary that Indian goods for exports are to be manufactured in India itself. India could leverage upon various FTAs of Sri Lanka and the GSP+ scheme and invest in Sri Lanka's potential sectors and products.

The government of India could set up an institutional mechanism/ framework in the lines of the Supporting India's Trade Preferences for Africa (SITA) project which would help to increase and diversify exports of Sri Lanka. Export diversification of Sri Lanka requires targeted intervention, and India could play a major role in improving the productive and export capacities of the country through investment, knowledge sharing and technology transfers. This would also improve capacities of Sri Lankan companies and Trade Support Institutions. This would further increase the trade between both countries, along with narrowing Sri Lanka's huge trade deficit with India.

²"Indo-Sri Lanka Economic Relations in Modi's India", speech by Dr. S. Narayan – former Finance Secretary, Ministry of Finance, India on 20 November 2017 at the Lakshman Kadirgamar Institute (LKI)

Cooperation in Capacity Development: An area of cooperation between India and Sri Lanka could be investing in capacity development. Sri Lankan exports generally lack innovation, and therefore need to increase Research and Development (R&D) spending to be more competitive. According to the World Bank, there are significant barriers holding back private creativity to realize the economic potential of Sri Lanka's relatively educated labor force. India could assist Sri Lanka in its efforts to increase R&D. Apart from investment, Indian institutions could share their expertise in the fields of export capability creation in the country, institutional strengthening and export development in the form of technical assistance and sharing of expertise through site visits. For instance, in the recent past Exim Bank has undertaken a consultancy assignment commissioned by the Commonwealth Secretariat to assist the Sri Lanka Export Credit Insurance Corporation (SLECIC) to review its operating policies and suggest new products while recommending measures to enhance the overall export financing framework in Sri Lanka,

and to create a framework for operationalising these recommendations.

Cooperation in SME Development: For economic growth to be inclusive, it is imperative to bring the SME sector into Sri Lanka's mainstream trade, so that the gains from trade go where they could make the biggest difference. SMEs in Sri Lanka account for 90 percent of the total number of enterprises, 45 percent of the total employment and contributes to 52 percent of the GDP of the country. The SME sector of Sri Lanka faces several problems like lack of technical know-how, shortage of long-term financial support, market link and research and development resulting in low participation in international trade. The National Policy Framework for Small Medium Enterprise (SME) Development 2016 of Sri Lanka recognizes the importance of cluster development. Under this cluster development approach, the entire value chain from input supply to processing and export will be supported and promoted. India could share its expertise on cluster development to the SMEs in Sri Lanka through various programmes.

1. ECONOMIC OVERVIEW OF SRI LANKA

Sri Lanka's economic growth has been gradually escalating over the recent years. Sri Lanka, which had been a predominantly rural-based economy has increasingly orientated towards services and manufacturing sectors. In fact, by 2017, services and industry accounted for 62 percent and 31 percent of Sri Lanka's GDP, respectively.

Sri Lanka's macroeconomic performance has continued to be progressive over the recent years, with real GDP growth remaining above 4 percent during 2014-2016. However, in 2017, the real GDP growth declined to 3.1 percent, owing mainly to negative growth rate of agricultural output in the first three quarters of the year. In absolute terms, nominal GDP and per capita income of Sri Lanka rose in 2017 to US\$ 87.4 billion and US\$ 4,065, respectively. The per capita income of Sri Lanka is higher than that of the other SAARC countries like Bangladesh, Bhutan, India, and Nepal. Average consumer price inflation, however, increased to 6.5 percent in 2017 compared to 3.8 percent in the previous year, owing to an increase in VAT (effective from November 2016) as well as an upward pressure on food prices due to fall in agricultural production (**Table 1.1**).

Sri Lanka is ranked 111th in terms of Ease of Doing Business in 2018 conducted by the World Bank and the International Finance Corporation. The Government of Sri Lanka has been pursuing large-scale reconstruction and development projects in its efforts to spur growth in disadvantaged areas, develop small and medium enterprises and increase agricultural productivity.

The Central Bank of Sri Lanka, in early 2017, decided to adopt a new, relatively market-driven framework for exchange rate management under the pressure to preserve sparse foreign exchange reserves. This has marked the beginning of gradually reducing interventions in foreign exchange markets. This policy change, together with an increased current-account deficit and a sizeable inflation differential with the US, has been one of the major drivers of the depreciation of the Sri Lankan rupee, which stood at SLR 152: US\$ 1 in 2017, as compared to SLR 146: US\$ 1 in 2016.

After two consecutive years of decline in foreign-exchange reserves caused by the Central Bank's attempts to stem depreciatory pressures on the currency, Sri Lanka's international reserves increased

Table 1.1: Macroeconomic Snapshot of Sri Lanka - Select Indicators

Indicators	2012	2013	2014	2015	2016	2017 ^p
Real GDP Growth (%)	9.1	3.4	5.0	5.0	4.5	3.1
Nominal GDP (US\$ bn)	68.4	74.3	79.3	80.5	81.6	87.4
GDP Per Capita (US\$)	3,351	3,610	3,821	3,842	3,857	4,065
Consumer Price Inflation (avg. % change)	7.5	6.9	3.2	0.9	3.8	6.5
Population (mn)	20.4	20.6	20.8	21.0	21.2	21.4
Current account balance (US\$ bn)	-4.0	-2.5	-2.0	-1.9	-1.9	-2.6 ^e
Current account balance (% of GDP)	-5.8	-3.4	-2.5	-2.4	-2.4	-3.0 ^e
International Reserves (US\$ bn)	7.1	7.5	8.2	7.3	6.0	7.5 ^e
Exchange Rate (SLRs: US\$, avg.)	127.6	129.1	130.6	136.0	146.0	152.0

Note: e: Estimates; p: Provisional estimates

Source: Department of Census & Statistics, Government of Sri Lanka; Central Bank of Sri Lanka; Economist Intelligence Unit

to an estimated US\$ 7.5 billion in 2017, from US\$ 6 billion in 2016, owing to the new policy shift towards a more market-driven framework for exchange rate management. Sri Lanka's international reserves in 2017 represent an import cover of 3.7 months.

Sri Lanka's Vision 2025³

Sri Lanka has set its goal of "Vision 2025" with an aim to attain the status of an upper-middle income country by 2025 with a knowledge-based, highly competitive, social-market economy, by positioning Sri Lanka as an export-oriented economic hub at the centre of the Indian Ocean. Under this vision, Sri Lanka's target is to create one million new jobs, increase FDI to US\$ 5 billion per year and per capita income to US\$ 5,000 per year, and raise its exports two-fold to US\$ 20 billion per year, over the next three years.

The Government of Sri Lanka's vision document has identified certain constraints to growth such as issues pertaining to public finance management, lack of product and concentration of exports, factor market constraints, weak property rights, lack of adequate infrastructure, inequitable access to finance, regulatory barriers that constrain investments, as well as institutional weaknesses, among others. The government is set to follow a new approach to growth,

which will be structured on a "knowledge-based, highly competitive, social market economy model", to foster and sustain successful institutions and policy, strong market structures, and a fairer society, whereby it aims to strengthen the drivers of growth and make growth more inclusive, create a strong and influential middle class towards an inclusive society, and introduce supportive legal reforms. The key focus areas to address the constraints and achieve the specified objectives are given as under:

- i. Strengthening Macroeconomic Framework
- ii. Strengthening Growth
- iii. Reforming Factor Markets
- iv. Improving Economic and Social Infrastructure
- v. Enhancing Technology and Digitalization
- vi. Improving Social Safety Nets
- vii. Promoting Food Security and Sustainable Development
- viii. Strengthening Governance and Accountability
- ix. Strengthening Coordination and Monitoring Implementation

The summarized particulars of various approaches and strategies enlisted in Sri Lanka's Vision 2025 are given in **Annexure**.

³"Vision 2025 – A Country Enriched", Prime Minister's Office of Sri Lanka, 2017

2. FOREIGN TRADE OF SRI LANKA

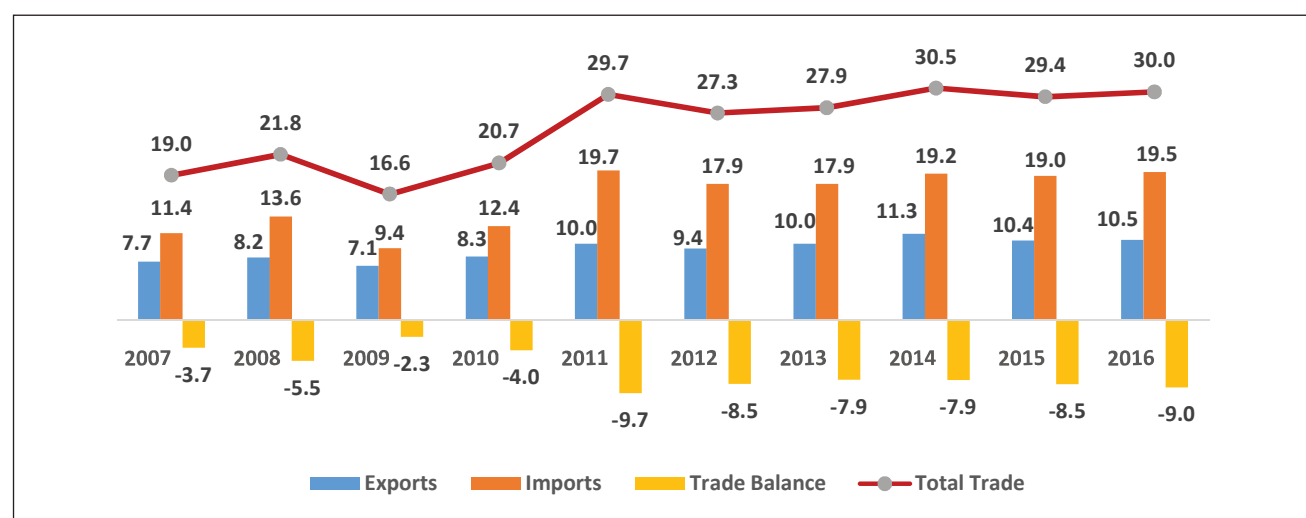
Sri Lanka was the first South Asian country to adopt liberalization policy, when it moved away from a protectionist trade policy to an export-oriented trade policy in 1977. This trade policy liberalisation initiative was followed by a series of additional policies in the next two decades including unification of the exchange rate, use of tariffs rather than quantitative restrictions to control imports, simplifications of the tariff structure, and removal of export taxes and controls. According to Central Bank of Sri Lanka (CBSL), the country's external trade policy is focused on achieving a higher integration with global markets, by encouraging external trade and international investments to leverage trade investment nexus. The government of Sri Lanka has recently adopted a New Trade Policy "to improve domestic productive capacity and trade performance, revitalize the nation's integration in global and regional markets, raise the living standards of the people and accelerate the nation's long-term economic growth rate"⁴.

International Trade of Sri Lanka

Ever since the liberalization of trade policy, Sri Lankan trade has been performing reasonably well. Over the decade, Sri Lanka's total trade increased from US\$ 19 billion in 2007 to US\$ 30 billion in 2016. The period witnessed increase in Sri Lanka's exports to US\$ 10.5 billion in 2016 from US\$ 7.7 billion recorded in 2007 (**Chart 2.1**). Sri Lanka's merchandise exports are highly concentrated within a select set of commodities and to select markets. In the recent past, Sri Lanka's exports were restricted by downward movement in commodity prices in the international market and modest economic recovery in Sri Lanka's major export destinations. Similarly, imports also increased to US\$ 19.5 billion in 2016 from US\$ 11.4 billion during the same period, mainly owing to higher imports of consumer and investment goods. The period also witnessed simultaneous widening of trade deficit owing to higher growth of imports.

Chart 2.1: Trends in Sri Lanka's Merchandise Trade

(US\$ billion)



Source: ITC Trade Map, derived from UN COMTRADE

⁴National Trade Policy, Ministry of Development Strategies & International Trade, Government of Sri Lanka, 2017

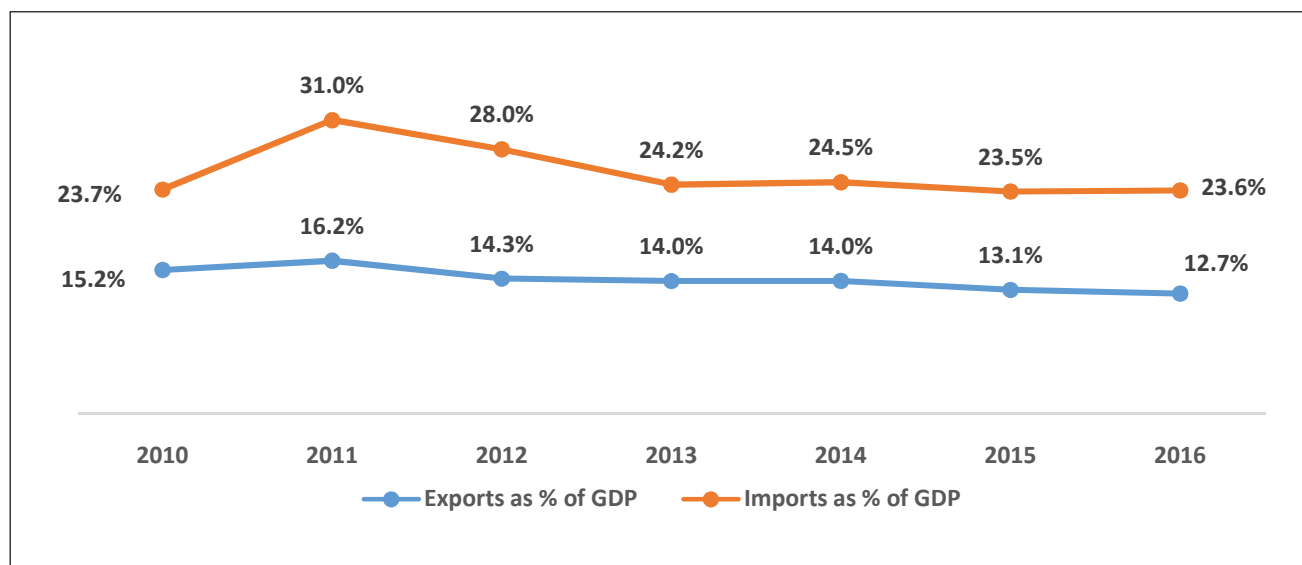
Export Propensity Index (export as a percentage of GDP) indicates the overall degree of reliance of domestic producers on foreign markets. It ranges from zero (with no exports) to 100 (with all domestic production exported). Sri Lanka's export propensity has been declining since 2011, from 16.2 percent to 12.7 percent in 2016 (**Chart 2.2**). Similarly, imports as a percentage of GDP has also declined since 2011 from 31 percent of GDP in 2011 to 23.6 percent of GDP in 2016. Further, a substantial proportion of Sri Lanka's exports have high import intensity. This is true especially in case of industrial exports which are reliant on imported inputs. According to a study by Verité Research,⁵ a major share of export value of garments, rubber products, petroleum products, and gems, diamonds and jewelry is accounted for by imported inputs. Intermediate imports account for 51.5 percent of all imports, and investment goods account for 26 percent of total imports of Sri Lanka in 2016.

Composition of Sri Lanka's Merchandise Trade

In this section, recent trends in composition of merchandise trade of Sri Lanka are analyzed using Harmonized System (HS) code at 2-digit level. During the last decade, Sri Lanka's export composition was dominated largely by apparel (HS Codes 61 and 62) and other traditional products like tea and rubber. In 2016, readymade garments (RMG) alone accounted for 43.6 percent of its global exports (**Table 2.1**).

Export of apparel (knit or crochet) to total exports, which accounted for 20.3 percent of the total exports in 2007, increased to 25.6 percent in 2016. Share of articles of apparel (not knit or crochet) to total exports has been declining from 20.7 percent in 2007 to 18 percent in 2016. Sri Lanka's coffee and rubber exports as a share of its overall exports has also witnessed a decline in the last decade. Retreaded or used tyre accounts for a major share of its rubber exports. Sri Lanka is the largest exporter of retreaded or used tyres in the world.

Chart 2.2: Exports and Imports of Sri Lanka as a Percent of GDP



Source: Central Bank of Sri Lanka and Exim India Calculations

⁵Sri Lanka: International Trade Performance and Prognosis, Vol.1. No. 1 November 2013, Verité Research

Table 2.1: Sri Lanka's Export Composition

HS Code	Product Label	2007		2016		CAGR (2007-2016, %)
		Value (US\$ mn)	% Share	Value (US\$ mn)	% Share	
61	Articles of apparel and clothing accessories, knitted or crocheted	1,553.0	20.3	2,703.0	25.6	6.4
62	Articles of apparel and clothing accessories, not knitted or crocheted	1,589.7	20.7	1,895.1	18.0	2.0
09	Coffee, tea, maté and spices	1,144.0	14.9	1,525.0	14.5	3.2
40	Rubber and articles	592.4	7.7	801.8	7.6	3.4
85	Electrical machinery and equipment and parts	254.2	3.3	241.8	2.3	-0.6
71	Pearls, precious stones, metals, coins	510.6	6.7	215.2	2.0	-9.2
08	Edible fruit and nuts	79.2	1.0	192.9	1.8	10.4
03	Fish and crustaceans and other aquatic invertebrates	170.6	2.2	182.4	1.7	0.7
21	Miscellaneous edible preparations	27.4	0.4	173.8	1.6	22.8
27	Mineral fuels, mineral oils and products of their distillation	2.2	0.03	163.6	1.6	61.4

Source: ITC Trade Map, derived from UN COMTRADE

A major recent boost to Sri Lankan exports is the reinstatement of the European Union (EU) Generalised System of Preferences Plus (GSP+) facility in May 2017, 7 years since its suspension. As a result, Sri Lankan exporters would again be able to export over 6,000 products duty free to the EU countries. The additional tariff advantage is expected to strengthen competitive position of the exports of Sri Lanka in EU. Apparel, processed food, seafood, toy products, porcelain and ceramic ware are some of the main sectors that will benefit under GSP+.

Mineral fuels, oils and their products continued to be the major imports of Sri Lanka in 2016, though its share declined from 23.5 percent of total imports in 2007 to 12 percent in 2016. Machinery and mechanical appliances, vehicles other than railway or tramway, electrical machinery and equipment, and knitted or crocheted fabric were the other major imports in 2016 (Table 2.2).

Direction of Sri Lanka's Merchandise Trade

India is the largest trading partner of Sri Lanka, though its share in Sri Lanka's total trade has decreased from 17.3 percent in 2007 to 15.2 percent in 2016. Other major trading partners of Sri Lanka in 2016 include China, the US, UK, UAE and Japan. A major shift in the recent years is a large improvement in the share of China in Sri Lanka's total trade from 5.1 percent in 2007 to 14.9 percent in 2016. The US and UK witnessed declining trends in their share over the decade, where as that of UAE and Japan marginally improved.

As a region, EU is the major export destination of Sri Lanka in 2016, with total exports from Sri Lanka amounting to US\$ 3.1 billion, increasing from US\$ 2.9 billion in 2007. Although Sri Lanka's total exports to EU has increased in value terms, its share has decreased from 37.6 percent in 2007 to

29.7 percent of total Sri Lankan exports in 2016. This could be partially attributed to the suspension of the GSP+ facility by the EU in 2010.

As regards country-wise destination of exports, the US was the major export destination of Sri Lanka, accounting for 26.6 percent of Sri Lanka's total exports in 2016, followed by UK, India and Germany. Among the top destinations, there has been a gradual shift in Sri Lanka's export directions toward the US, India, UAE and China during the last decade as indicated by their rising shares (**Table 2.3**).

India had traditionally been a major import source for Sri Lanka, contributing 24.4 percent of Sri Lanka's

total imports in 2007. In 2016, China overtook India to become the major import source of Sri Lanka, with a 21.9 percent share in Sri Lanka's total imports, as against 19.6 percent share in the case of India. This is due to the sharp decline in imports of vehicles other than railway or tramway rolling stock and mineral fuels, oils and products from India. Other major import sources include UAE, Singapore, Japan, Malaysia and the US (**Table 2.4**). Sri Lanka's imports from the EU as a region increased from US\$ 1.4 billion in 2007 to US\$ 2.1 billion in 2016, though its share has decreased from 12.3 percent to 10.7 percent during the same period.

Table 2.2: Sri Lanka's Import Composition

HS Code	Product Label	2007		2016		CAGR (2007-2016, %)
		Value (US\$ mn)	% Share	Value (US\$ mn)	% Share	
27	Mineral fuels, mineral oils and products of their distillation	2,680.8	23.5	2,333.7	12.0	-1.5
84	Machinery, mechanical appliances, boilers	831.7	7.3	1,750.2	9.0	8.6
87	Vehicles other than railway or tramway rolling stock	644.7	5.7	1,499.7	7.7	9.8
85	Electrical machinery and equipment and parts	743.0	6.5	1,375.8	7.1	7.1
60	Knitted or crocheted fabrics	463.8	4.1	797.1	4.1	6.2
39	Plastics and articles	407.8	3.6	710.1	3.6	6.4
52	Cotton	525.9	4.6	680.3	3.5	2.9
25	Salt, sulphur, stone, plastering materials, lime and cement	233.9	2.1	625.2	3.2	11.5
72	Iron and steel	333.5	2.9	597.6	3.1	6.7
71	Pearls, precious stones, metals, coins	283.3	2.5	514.2	2.6	6.9

Source: ITC Trade Map, derived from UN COMTRADE

Table 2.3: Major Export Destinations of Sri Lanka

Importers	2007		2016		CAGR (2007-2016, %)
	Value (US\$ mn)	% Share	Value (US\$ mn)	% Share	
USA	1,978.0	25.8	2,810.2	26.6	4.0
UK	1,017.2	13.3	1,045.1	9.9	0.3
India	515.8	6.7	753.5	7.1	4.3
Germany	438.0	5.7	509.9	4.8	1.7
Italy	391.8	5.1	428.9	4.1	1.0
Belgium	407.0	5.3	338.2	3.2	-2.0
UAE	209.9	2.7	292.9	2.8	3.8
China	35.6	0.5	215.5	2.0	22.2
Netherlands	151.0	2.0	208.3	2.0	3.6
Japan	161.5	2.1	203.8	1.9	2.6

Source: ITC Trade Map, derived from UN COMTRADE

Table 2.4: Major Import Sources of Sri Lanka

Importers	2007		2016		CAGR (2007-2016, %)
	Value (US\$ mn)	% Share	Value (US\$ mn)	% Share	
China	929.0	8.2	4,270.8	21.9	18.5
India	2,781.4	24.4	3,825.0	19.6	3.6
UAE	370.8	3.3	1,067.3	5.5	12.5
Singapore	1,106.9	9.7	1,030.3	5.3	-0.8
Japan	412.8	3.6	949.8	4.9	9.7
Malaysia	347.5	3.1	642.0	3.3	7.1
USA	255.3	2.2	540.0	2.8	8.7
Thailand	230.7	2.0	514.5	2.6	9.3
Taiwan	263.4	2.3	495.9	2.5	7.3
Hong Kong	724.2	6.4	465.9	2.4	-4.8

Source: ITC Trade Map, derived from UN COMTRADE

Sri Lanka's Trade Agreements and Arrangements⁶

According to the Asian Development Bank (ADB), agreements that have been signed and are in effect include:

- Asia-Pacific Trade Agreement
- India-Sri Lanka Free Trade Agreement
- Pakistan-Sri Lanka Free Trade Agreement
- South Asian Free Trade Area
- Sri Lanka-Iran Preferential Trade Agreement

Agreement that has been signed and not yet in effect includes:

- Comprehensive Economic Partnership Agreement between Singapore and Sri Lanka

Agreements for which negotiations have been launched include:

- Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC) Free Trade Area
- People's Republic of China-Sri Lanka Free Trade Agreement

Concentration of Exports in Sri Lanka

Sri Lanka has recorded impressive international trade performance over the last decade. Notwithstanding this, Sri Lanka's exports are heavily concentrated on a few select set of products (apparel, tea, and rubber), and are often targeted at a limited range of buyers, most of which are in developed country markets. For instance, 44 percent of Sri Lanka's exports are concentrated in three markets, the US, UK and India

in 2016. Another critical aspect is that Sri Lanka's exports to major Asian markets except for India continue to remain poor, and is mostly dependent on few major Western markets⁷. For instance, Japan is the third largest global market for apparels and accessories, which are the largest exports of Sri Lanka. But Japan accounts for just 1.9 percent of Sri Lanka's total exports and 0.97 percent of apparel exports in 2016.

Similarly, 58 percent of Sri Lanka's exports are concentrated in three products, articles of apparel and clothing accessories, knitted or crocheted; articles of apparel and clothing accessories, not knitted or crocheted; and coffee, tea, maté and spices. However, the country's top three exports are not among the top ten products exported globally. A detailed analysis of major export and import commodities and their respective top trading partners are given in **Table 2.5**.

Thus, Sri Lanka has a narrow export base, with highly concentrated exports. There is a huge merchandise trade deficit with exports accounting for nearly half the value of imports. Further, export to GDP ratio has had a declining trend. In order to mitigate export market risk, there is a need for product and market diversification in the existing export basket of Sri Lanka, which would pave way for export sustainability in the country. There is also a need to introduce policies and measures towards enhancing exports and harnessing the existing export potential of the country.

⁶ADB: Asia Regional Integration Centre, Tracking Asian Integration; <https://aric.adb.org/fta-country>

⁷Sri Lanka's Export Problem: Not Concentration, but Composition, August 2017, Verité Research

Table 2.5: Major Commodities Traded by Sri Lanka and its Major Trading Partners, 2016

Exports					Imports				
HS Code	Commodity	Exports (US\$ mn)	Major Export Destination for each Product	Share	HS Code	Commodity	Imports (US\$ mn)	Major Import Source for each Product	Share
All products	All products	10545.9	USA	26.6%	All products	All products	19500.8	China	21.9%
			UK	9.9%				India	19.6%
			India	7.1%				UAE	5.5%
			Germany	4.8%				Singapore	5.3%
			Italy	4.1%				Japan	4.9%
61	Articles of apparel and clothing accessories, knitted or crocheted	2703.0	USA	45.4%	27	Mineral fuels, mineral oils and products of their distillation	2333.7	UAE	30.5%
			UK	35.4%				Singapore	26.0%
			Italy	52.8%				India	16.5%
			Belgium	64.9%				South Africa	7.4%
			Germany	75.3%				China	6.7%
62	Articles of apparel and clothing accessories, not knitted or crocheted	1895.1	USA	46.2%	84	Machinery, mechanical appliances, boilers	1750.2	China	33.0%
			UK	20.6%				India	10.7%
			Italy	6.4%				Japan	7.3%
			Germany	4.3%				Germany	6.7%
			Belgium	2.9%				USA	5.3%
60	Coffee, tea, maté and spices	1525.0	Iran	10.1%	87	Vehicles other than railway or tramway rolling stock	1499.7	India	41.9%
			Russia	9.4%				Japan	39.2%
			Iraq	6.8%				China	8.2%
			Turkey	6.5%				Germany	3.1%
			UAE	5.0%				Thailand	2.2%
40	Rubber and articles	801.8	USA	30.8%	85	Electrical machinery and equipment and parts	1375.8	China	44.8%
			Germany	12.0%				India	10.7%
			Belgium	5.5%				Viet Nam	4.2%
			Italy	4.3%				Germany	4.2%
			UK	3.6%				USA	3.5%
85	Electrical machinery, equipment and parts	241.8	Switzerland	21.4%	60	Knitted or crocheted fabrics	797.1	China	33.6%
			India	13.7%				Taiwan	20.5%
			USA	5.8%				India	15.1%
			Germany	5.5%				Hong Kong	12.2%
			Hong Kong	5.5%				Italy	7.6%

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

3. FOREIGN DIRECT INVESTMENT IN SRI LANKA: CURRENT TRENDS AND OPPORTUNITIES

The role of Foreign Direct Investment (FDI) in enhancing export competitiveness, providing access to advanced technologies and know-how and economic development is well-recognized across the world. While a study by Information Handling Services⁸ ranked Sri Lanka among Asia Pacific's top 10 FDI hotspots, FDI in exports sector of the country is minimal and need to be strengthened.

Global headwinds along with significant policy risks had led to uncertainty among multinational enterprises leading to a loss in growth momentum of investment flows across the world in 2016. In the case of Sri Lanka, however, there was an increase in both inflow and outflow of FDI in 2016.

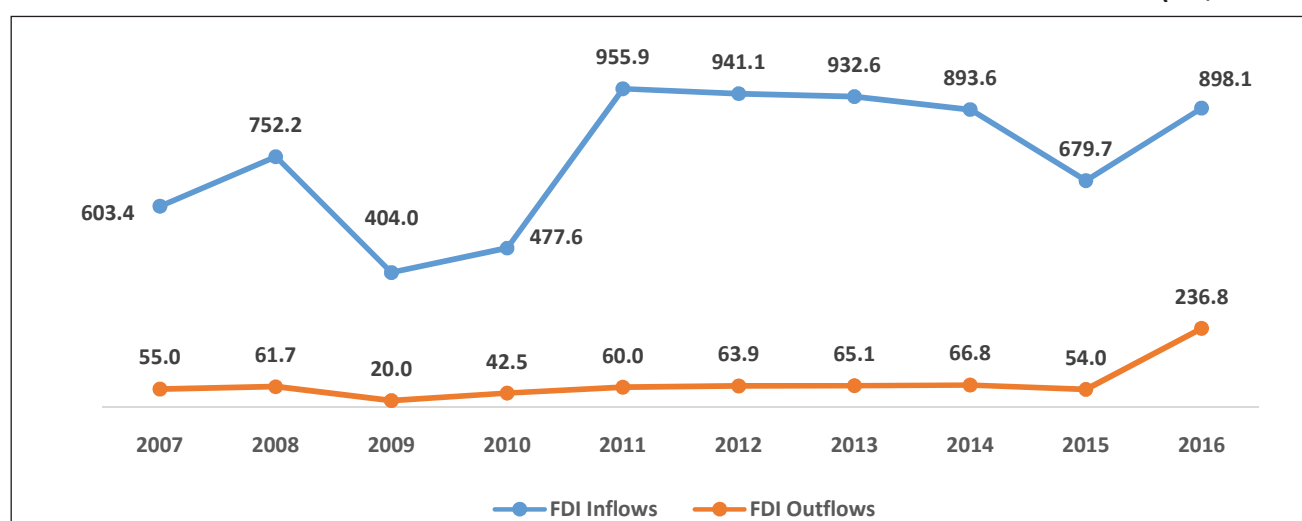
Sri Lanka has been attracting investments in various industries such as apparel, construction, tourism and real estate. According to UNCTAD, FDI inflows

into Sri Lanka registered a 32.1 percent rise in 2016, increasing to US\$ 898.1 million, from US\$ 679.7 million in the previous year. Similarly, FDI outflows from Sri Lanka witnessed a four-fold increase to US\$ 236.8 million in 2016 from US\$ 54 million in 2015 (**Chart 3.1**).

Table 3.1 shows the trends in foreign capital expenditure, number of FDI projects and jobs created by them in Sri Lanka as per fDi Markets online database. The number of FDI projects in Sri Lanka increased from 15 in 2007 to 35 in 2016, resulting in increased total capital investment to US\$ 2.2 billion in 2016 from US\$ 541.8 million in 2007. Cumulative capital expenditure in Sri Lanka out of total 315 FDI projects during the decade stood at US\$ 17.4 billion, creating 66,720 jobs in the country.

Chart 3.1: Trends in Sri Lanka's FDI Flows

(US\$ million)



Source: UNCTADStat and Exim India Analysis

⁸<http://news.ihsmarkit.com/press-release/economics-country-risk/emerging-markets-asia-pacific-offer-brightest-prospects-global-#.VxDORASaAnw.email>

Table 3.1: Trends in FDI Received by Sri Lanka during 2007-2016

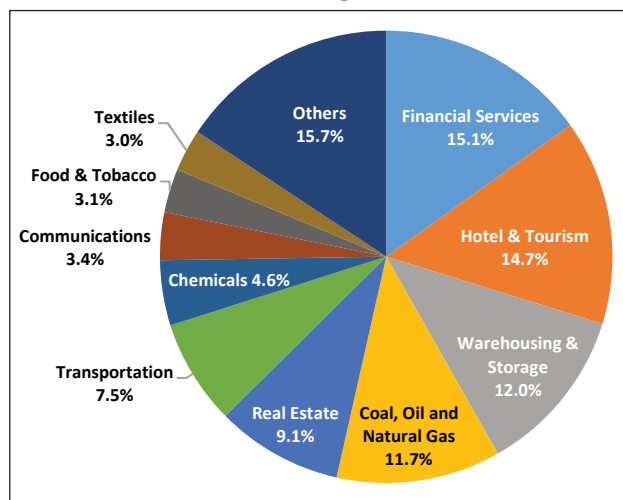
Year	No. of FDI Projects	Capital Expenditure (US\$ mn)	No. of Jobs Created
2007	15	541.8	2,906
2008	23	1,218.4	7,117
2009	23	2,224.7	8,574
2010	28	964.2	5,199
2011	49	3,837.5	10,044
2012	36	1,066.4	2,747
2013	39	2,195.6	11,044
2014	41	1,925.0	9,900
2015	26	1,153.2	5,013
2016	35	2,231.9	4,176
Total	315	17,358.6	66,720

Note: fDi Markets tracks crossborder investment in a new physical project or expansion of an existing investment which creates new jobs and capital investment. This data differs from official data on FDI flows as company can raise capital locally, phase their investment over a period of time, and can channel their investment through different countries for tax efficiency.

Source: fDi Markets online database

Major Sectors Attracting Investment in Sri Lanka

During 2007 to 2016, financial services is the largest sector to receive capital investment, followed by hotel & tourism and warehousing & storage amounting to US\$ 2.6 billion, US\$ 2.5 billion and US\$ 2.1 billion, respectively. **Chart 3.2** shows respective shares of the sectors attracting FDI in Sri Lanka. According to fDi Markets database, a major shift that occurred in 2016 is a large investment in coal, oil and natural gas sector which attracted US\$ 1.1 billion investment, contributing to 47 percent of total investment received in 2016. This is due to US\$ 1.1 billion investment by Indian Oil Corporation (IOC) in the city of Trincomalee (Eastern), Sri Lanka in 2016. Other sectors which witnessed an increase in investment in 2016 include hotel & tourism, warehousing & storage, financial services, food & tobacco and electronic components sectors.

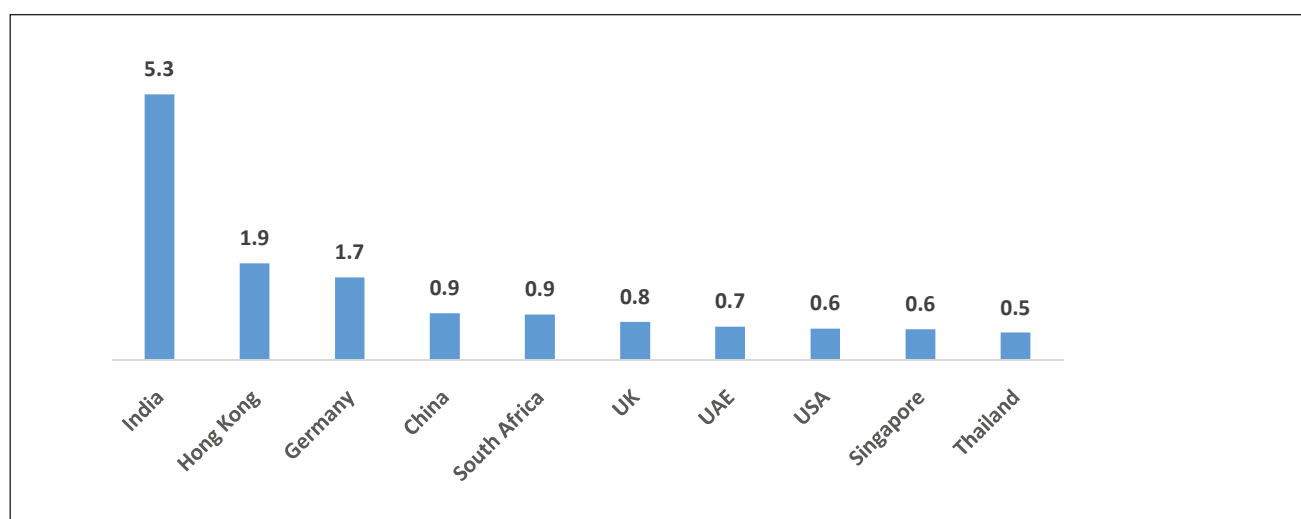
Chart 3.2: Major Sectors Attracting Investment in Sri Lanka during 2007-2016

Note: fDi Markets tracks crossborder investment in a new physical project or expansion of an existing investment which creates new jobs and capital investment. This data differs from official data on FDI flows as company can raise capital locally, phase their investment over a period of time, and can channel their investment through different countries for tax efficiency.

Source: fDi Markets online database

Chart 3.3: Major Investors in Sri Lanka during 2007-2016

(US\$ billion)



Note: fDi Markets tracks crossborder investment in a new physical project or expansion of an existing investment which creates new jobs and capital investment. This data differs from official data on FDI flows as company can raise capital locally, phase their investment over a period of time, and can channel their investment through different countries for tax efficiency.

Source: fDi Markets online database

Table 3.2: Trends in FDI Outflow from Sri Lanka during 2007-2016

Year	No. of FDI Projects	Capital Expenditure (US\$ mn)	No. of Jobs Created
2007	1	49.3	148
2008	3	33.5	203
2009	3	31.6	647
2010	3	63.6	136
2011	4	104.9	243
2012	21	739.7	1,697
2013	6	165.1	179
2014	8	85.1	415
2015	8	213.3	949
2016	15	275.9	2,418
Total	72	1,762.0	7,035

Note: fDi Markets tracks crossborder investment in a new physical project or expansion of an existing investment which creates new jobs and capital investment. This data differs from official data on FDI flows as company can raise capital locally, phase their investment over a period of time, and can channel their investment through different countries for tax efficiency.

Source: fDi Markets online database

Major Sources of Investment in Sri Lanka

The major investors in terms of FDI received in Sri Lanka during 2007 to 2016 are shown in **Chart 3.3**. India is the largest investor in Sri Lanka during the period 2007-

2016, with an investment size of US\$ 5.3 billion (30.7 percent of the total FDI). The other major investors during the last ten years are Hong Kong (accounting for 11.1 percent of total inward FDI received by

Sri Lanka), followed by Germany (9.5 percent), China (5.4 percent), South Africa (5.2 percent) and UK (4.4 percent). The top investors in 2016 include India, Hong Kong, Switzerland, Germany, Japan and China.

Outward Direct Investments from Sri Lanka

According to fDi Markets database, the number of outward FDI projects from Sri Lanka increased across the years, with a cumulative number of 72 projects during 2007-2016, and a capital expenditure amounting to US\$ 1.8 billion, creating 7,035 jobs in destination countries (**Table 3.2**).

In terms of sectors, financial services received maximum investment, with a share of 37.1 percent in total outward investment from Sri Lanka during the period 2007-2016. This was followed by transportation (29.9 percent share), hotel & tourism (7.9 percent), software & IT services (5.2 percent), textiles (5 percent) and food & tobacco sectors (4.9 percent). Similarly, in 2016 financial services received maximum investment, followed by ceramics & glass, textiles, food & tobacco and software & IT services sectors.

During 2007-2016, the major destinations of Sri Lanka's outward investment include India (33.4 percent of total outward investment by Sri Lanka), Oman (14.1 percent), Australia (13 percent), Maldives (12.6 percent), Hong Kong (4 percent) and Myanmar (4 percent). In 2016, however, Australia was the major investment destination of Sri Lanka with a total capital expenditure of US\$ 91.1 million (33.1 percent of total investment in 2016). Other major destinations during the year include Maldives, Haiti, UAE, Japan, Oman and India.

Investment Policy of Sri Lanka⁹

The Board of Investment Law (BOI Law): The Board of Investment Law No. 4 of 1978 and its amendments is the principal law applicable to foreign investments in Sri Lanka. Board of Investment (BOI), Sri Lanka is structured to function as the Central Facilitation point for investors and empowered to enter into

agreements with investors providing investment incentives of tax holidays, tax concessions and exemptions from customs duty & exchange control law.

Investment Incentives

Sri Lanka is located at the juncture of major global shipping routes which connect South Asia, Far East and the Pacific with Europe and the Americas. Geographically, Sri Lanka is strategically positioned next to India with close proximity to Southeast Asia and the Middle East. According to the BOI, in order to foster FDI in the country, Sri Lanka has the following investment incentives:

- Total foreign ownership is permitted across almost all areas of the economy.
- No restrictions on repatriation of earnings, fees, capital, and on forex transactions relating to current account payments.
- Safety of foreign investment is guaranteed by the constitution.
- Existence of a transparent and sophisticated legal and regulatory framework, covering all prerequisite business law enactments.
- Duty free (Customs Duty) import facility on plant, machinery & equipment during the project implementation period.

Sri Lanka also has bilateral investment protection agreements with 28 countries and double taxation avoidance agreements with 42 countries. It is also a founder member of the Multilateral Investment Guarantee Agency (MIGA), an investment guarantee agency of the World Bank. This provides a safeguard against expropriation and non-commercial risks. BOI has identified few target sectors for attracting investment in which Sri Lanka has strong foundation for growth and which are of national interest.

Exclusions and Limitations

According to the Exchange Control Provisions applicable for foreign investments, permission is

⁹Board of Investment, Sri Lanka

granted for the issue and transfer of shares in a company up to 100 percent of the issued capital of such company, to approved country funds, approved regional funds, corporate bodies incorporated outside Sri Lanka and individual residents outside Sri Lanka (inclusive of Sri Lankan residents outside Sri Lanka) subject to certain exclusions, limitations and conditions.

Exclusions: The above permission is not applicable in respect of shares of a company proposing to carry on any of the following businesses including pawn broking, retail trade with a capital of less than US\$ 1 million, and coastal fishing.

Limitations:

- a) Foreign investments in certain areas are approved only up to 40 percent of the issued capital of such company or a higher percentage of foreign investment when approval has been granted by the BOI only up to higher percentage. This is applicable for production of goods where Sri Lanka's exports are subject to internationally determined quota restrictions; growing and non-renewable primary processing of tea, rubber, coconut, cocoa, rice, sugar and spices; mining and primary processing of non-renewable national resources; timber based industries using local timber; deep sea fishing; mass communications; education; freight forwarding; travel agencies, and shipping agencies.
- b) In respect of the shares of a company carrying on or proposing to carry on any of the businesses in certain sectors will be granted permission only up to the percentage of the issued capital of the company for which percentage either general or special approval has been granted by the Government of Sri Lanka or any legal or administrative authority set up for the approval of foreign investment in such businesses. These include sectors such as air transportation; coastal shipping; large scale mechanized mining of gems; lotteries; and industrial enterprise in the Second Schedule of the Industrial Promotion Act, No. 46

of 1990, namely – any industry manufacturing arms, ammunitions, explosives, military vehicles and equipment, aircraft and other military hardware; any industry manufacturing poisons, narcotics, alcohols, dangerous drugs and toxic, hazardous or carcinogenic materials; and any industry producing currency, coins or security documents.

BOI Administered Export Processing Zones or Industrial Parks

Sri Lanka's export processing zones (EPZ) and industrial parks which were set up based on the country's zone development strategies have been a cornerstone in the industrial development and FDI inflows into the country. Various exemptions under Inland Revenue Law, Port & Airport Development levy Act, Value Added Tax Act and Strategic Development Project Act are available for BOI Approved Companies under EPZ. In addition, BOI provides duty free facilitation and exchange control exemptions for projects approved under BOI Law. The current list of EPZ and Industrial Parks in Sri Lanka administered by BOI is given below:

- Biyagama EPZ
- Colombo
- Horana EPZ
- Kandy Industrial Park
- Katunayake EPZ
- Koggala EPZ
- Malwatta EPZ
- Mawathagama EPZ
- Mirigama EPZ
- Mirijjawila EPZ
- Polgahawela EPZ
- Seethawaka EPZ
- Sooriyawewe
- Wathupitiwala EPZ

In addition to BOI administered zones, there are specialized sector specific privately owned industrial parks. These include:

- **Apparel and Related Industries:** MAS Fabric Park, Thulhiriya
- **IT / Knowledge Services:** Orion City IT Park, Colombo

Duty Free Facilitation: Companies signing an agreement with the BOI are entitled to obtain duty free facilities under Sec. 17 of BOI Law No. 4 of 1978. Companies that export more than 90 percent of goods produced (60 percent for apparel & ceramic) or services (with 70 percent turnover in convertible foreign currency), are entitled to be free of Customs Duty on capital goods and raw materials. Non-export oriented companies are entitled to import project related capital goods free of Customs Duty during the project implementation period. Prior to signing an agreement, the company should forward the list of items that it requires to set up and operate the project. These lists will be evaluated and approved by the Sector groups.

Exchange Control Regulation: Exchange Control exemption is granted for export-oriented projects under Sec. 17 of BOI Law and Strategic Development Projects. At present, a project is considered as an export oriented project only if it exports 90 percent of goods produced (60 percent for apparel & ceramic) or services (with 70 percent turnover in convertible foreign currency). Parts I, IA, II, III, IV V & VI of the Exchange Control Act are exempted for these companies and they are entitled to open and operate Foreign Currency Banking Unit (FCBU) account in any commercial bank in Sri Lanka.

Potential Sectors for Investment and Available Incentives

Target sectors actively promoted by Sri Lanka through BOI include:

- Export Oriented Manufacturing
- Export Oriented Services
- Tourism and Tourism Related Projects
- Infrastructure Projects
- Higher Education/Skill Development
- Value Added Strategic Projects
- Agriculture (Agro Processing, Fish-based Industry, Dairy)
- Establishment of Industrial Estates, Special Economic Zones, and Knowledge Cities

Export Oriented Manufacturing: Manufacturing is a key sector generating over 25 percent of Sri Lanka's industrial exports. The government of Sri Lanka has identified a wide range of targeted industrial sub-sectors to be promoted under the BOI to drive the economic development process of the country. A wide range of targeted industrial sub-sectors are promoted for investment including apparel industry; rubber based products – mainly solid tyers and surgical gloves; food processing industries – Prima Ceylon and high-tech manufacturing. In line with the new policy guidelines of the government, the manufacturing sector is to be promoted in three different segments where investment opportunities exist.

- a) *Export oriented sector to manufacture and export non-traditional goods* to generate foreign exchange earnings, employment, local value addition and the enhancement of industrial base is to be promoted by giving corporate tax exemptions. Customs duty exemptions will be granted for capital items and all other required items during the operational period of the project. Projects to be promoted under this category would include manufacturing and exports of all non-traditional products other than black tea in bulk, crepe rubber, sheet rubber, scrap rubber, coconut oil, desiccated coconut (other than desiccated coconut manufactured using continuous scale automated process technology and marketed with a quality guarantee), copra, fresh coconuts, and coconut fibre.
- b) *Newly targeted local market oriented sector* is to be promoted by granting the same tax exemptions given to export oriented manufacturers to encourage manufacturers which substitute the imported products. Customs duty exemptions will be granted for capital and construction items during the project implementation

period. Products that are to be promoted under this category include boats, pharmaceuticals, tyres and tubes, motor spare parts, furniture, ceramics, glassware of the mineral based products, cosmetic products, edible products manufactured out of the cultivated agricultural products, and construction materials. These products are permitted to be supplied for both local and export markets.

- c) *Projects under Strategic Development Project Act:* These include large scale projects which are of national interest and are likely to bring economic and social benefits supported by substantial inflow of foreign exchange, substantial employment which enhance the earning opportunities and envisaged transformation in terms of technology. Tax exemptions upto a maximum of 25 years and other exemptions of other levies would be granted by the State depending upon meeting the objectives referred above in the Act.

Investment opportunities exist in:

- Export oriented industries such as food processing, rubber based products, apparel, value added mineral based products, and ship & boats
- In the apparel sector opportunities exist for investment in apparel manufacturing, textile and fabric manufacturing, garment accessories, garment related services including garment washing, and textile testing, and screen printing.
- High end industries such as automobiles, electrical and electronics, and chemicals
- Import replacement industries such as pharmaceuticals, textile, dairy products, and fertilizer

Export Oriented Services: The government of Sri Lanka is planning to transform the country into a strategically important economic centre by developing five strategic hubs; a knowledge hub, a

commercial hub, a naval & maritime hub, an aviation hub, and an energy hub, taking the advantage of its strategic location & resources. In line with this decision, special emphasis is given for promoting investment in hub-related export service sectors where enormous opportunities are available for both foreign and local investors. The sub-sectors under export oriented services include shipping services, other marine services, printing services, management consulting services, aviation services, automation services, other export services, enterpot trading, and logistic services. Colombo and Hambantota Ports have been declared as Free Ports for further developing the shipping / trade related activities in Sri Lanka.

The BOI has been empowered to grant concessions for new investors in the following Hub-related activities in Free Ports and other designated areas.

- Entrepot trade involving import, minor processing and re-export
- Off-shore business where goods can be procured from one country or manufactured in one country and shipped to another country without bringing the same into Sri Lanka
- Providing front end services to clients abroad
- Headquarters operations of leading buyers for management of finance supply chain and billing operations
- Logistic services such as bonded warehouse or multi-country consolidation in Sri Lanka.

Investment opportunities also exist in establishment and operation of shopping malls that offer international branded products.

Tourism, Leisure and Related Projects: The tourism sector in Sri Lanka is experiencing an impressive growth both in terms of tourist arrivals and in foreign exchange revenues. The government of Sri Lanka has identified some key areas for tourism development and is promoting them for hotel and resort projects. These destinations are Kuchchaveli in Trincomalee

district on the north-eastern coast, Passikudah on the east coast, Kalpitiya on the north western coast consisting of 14 different islands, and Dedduwa near the river Madhu Ganga located close to Bentota on the south western coast. The Sri Lankan government is ensuring that the building blocks for economic growth are being developed simultaneously with major infrastructure projects such as expressways, airports and seaports. With the development of the underlying infrastructure by the government, Sri Lanka has become an attractive and increasingly accessible tourist destination in the recent years. Given these factors, there is a very strong opportunity for investment for construction and management of hotels, resorts, and leisure & entertainment complexes.

Infrastructure Projects: The country is currently involved in a massive infrastructure development drive to maintain a high and sustainable growth in the medium and long term. Timely development of economic infrastructure will help to increase economic efficiency while expanding the production capacity of the economy, facilitate productivity enhancement and reduction of regional disparity. The economic infrastructure development programme of the government is focused on all areas of infrastructure; development of roads, water supply and sanitation, ports and aviation, transport, housing and urban development, establishment of industrial zones, hospitals, and warehousing and logistic centres etc. The private sector is actively contributing towards the growth in various sub-sectors particularly with hotel and housing construction activities. Various sub-sectors which offer great opportunity for investment include housing and property development, shopping & office complex, mixed development projects, hospital services and medical services, warehousing & logistic services, exhibition centers, industrial parks and construction of highways and railways. Investment opportunities exist in construction and maintenance of:

- Northern expressway;
- Mixed Development complexes and other

commercial facilities in Colombo and other cities;

- Housing -Apartments;
- Export processing zones with state-of-the-art technology; and
- Warehousing and logistic centers etc.

Higher Education/Skill Development: Higher education is a major driver of economic development in Sri Lanka. In order to advance as a fast growing middle income country, it is critically important that Sri Lanka has the human capital needed to compete with the global knowledge economy. Sri Lanka needs a higher education system which can produce skilled, hardworking and enterprising graduates. Also, the country requires research and innovation capacity capable of promoting dynamic economic development. The knowledge hub initiative will help to develop Sri Lanka as a destination for investments in higher education and position the nation as a centre of excellence and regional hub for learning and innovation. The capacity of the state university system is limited, with not more than 20 percent of qualified students for university education are able to gain admissions to these Universities. Sri Lanka has targeted achievement of excellence in higher education by 2020, to become the most preferred country for higher education in the Asian subcontinent. Opportunities exist in:

- Establishment of Higher education institutes with appropriate programs in order to produce qualified personnel as sought by the Industries and services nationally and internationally; and
- Establishment and operation of IT software development, Knowledge Process Outsourcing / Business Process Outsourcing companies, IT and IT enabled services and IT Training Centers.

Value-added Strategic Projects: These include sectors such as power and energy, telecommunications and related services, ports development, distribution of petroleum related products such as LPG & LNG and recycling of waste. The island's Port Strategy are centred on six major ports in Colombo, Hambantota,

Galle, Trincomalee, Kankasanturai and Oluwil. The Government has given top priority to the development of Port infrastructure in recent years. Opportunities include:

- Developing & promoting *Non-conventional Energy sources* with improved technology;
- *Telecommunication* related services mainly to improve the quality by improving speed & coverage;
- *Maritime Sector*: Construction of new terminals, developing skills required for maritime industries, supporting logistic establishments, ship building and repairing industries, developing minor ports & connectivity, expanding related leisure activities, further research on exploring sea bed potential, marine support industries, rigging & offshore engineering, supply of spares, food, water and other goods, bunkering service, maintenance services, and transshipments services; and
- *Aviation Sector*: Improving aviation services to become a “location for aviation services” and improving airport facilities to become a good destination as well as a good transit point.

Agriculture: There are significant opportunities for investors in the agriculture sector both for the domestic market and for value added exports. The main focus of BOI is in terms of developing agricultural crops other than established traditional crops, like tea, rubber and coconut, particularly by enhancing domestic value addition. The government looks for specialised investment to improve productivity, level of technology innovation, access to international markets, use of quality seeds and planting materials and improve overall value addition. With diverse agro

zones for agro based industries and access to a large fishing area, Sri Lanka has much to offer for both local and foreign investors in agriculture sector including horticulture, livestock and fisheries sub-sectors.

Some of the opportunities in agriculture sector include:

- *Horticulture*: Sri Lanka aims to be recognized as one of the best horticulture producers in the world. In cut flower production, there are opportunities for investors who can bring in new hybrid varieties imported from overseas which can be used as mother plants and modernised with tissue culture technology. Similarly, opportunities are available to produce fruits and vegetables for the export market such as the Middle East, Japan etc.
- *Enhancing of value addition*: There are many areas in which value addition can be enhanced in the agro based sector. For example, Sri Lanka has been one of the largest exporters of spices. However, much of the exports has been in raw commodities form. The government encourages the induction of investors who can enhance the domestic value addition in Sri Lanka so that these items are exported in high value forms.
- *Fisheries*: Sri Lanka has considerable fisheries potential in offshore/deep sea, inland fisheries and aquaculture. The fisheries sector employs over 650,000 people directly and indirectly through related activities.
- *Livestock*: The livestock sector consists mainly of the dairy and poultry sub-sectors, which are considered as priority areas for growth, employment generation and increasing income of rural farmers.

4. INDIA-SRI LANKA BILATERAL TRADE AND INVESTMENT RELATIONS

India and Sri Lanka have been connected by a legacy of cultural, religious and linguistic ties since the pre-colonial era. Over the years, this has evolved into a political and commercial bond through cooperation in the fields of development, education, culture and defence. Sri Lanka has always been one of the priority destinations for Indian trade and investment given its geographical proximity, strategic location in the Indian Ocean and natural resources. Economic ties particularly increased during 1990s with liberalisation ushering in both the economies. In 1996, India replaced Japan as the largest source of imports of Sri Lanka accounting for 8-9 percent of its total imports.

India Sri Lanka Free Trade Agreement (ISFTA)¹⁰

In order to enhance bilateral trade between the two countries, India and Sri Lanka had signed the India-Sri Lanka Free Trade Agreement (ISFTA) in December 1998, which entered into force in March 2000. India's broader industrial base and its capability to meet Sri Lanka's import demand would provide Sri Lanka a greater market access, while helping Sri Lanka diversify its industrial base and raise its attraction as a favourable FDI destination on the basis of preferential access to the Indian market.

Rationale behind ISFTA

Existing trade agreements like Asia-Pacific Trade Agreement (APTA) and South Asian Preferential Trade Agreement (SAPTA) were based on positive list approach (commodity-to-commodity based negotiations) to tariff preferences. These concessions could not ensure free flow of traded goods to the desired extent. ISFTA on the contrary was based on a negative list approach and took into consideration asymmetric treatment (Sri Lanka's less diversified

industrial base and smaller economy). Therefore, all tariff lines apart from those listed in the negative list were subject to zero-duty or duty preferences at the end of implementation. In addition, special and differential treatment (SDT) is effectively built into the agreement to accommodate asymmetries between the two countries.

The role of South-South cooperation in promoting transfer of resources and technology through trade and investment is increasingly becoming important. When joint ventures are set up between two developing countries, the technology transfer have proved to be more cost-effective and suitable for the recipient country in terms of the factor endowment - raw material, labour and market conditions. The ISFTA was signed with the objective of increasing investment flows from India with successful adoptable technology transfer to Sri Lanka.

Although with liberalisation of both the economies, bilateral trade increased significantly in the mid-nineties but it failed to capture the large amount of informal trade carried out between India and Sri Lanka. High tariffs and inefficient procedures led to a flow of traded goods outside the official channel. ISFTA aimed at bringing this informal trade into the formal trading network by means of trade and tariff liberalization, which was expected to reduce high transaction costs and inefficiencies related to the trading process.

Tariff Concessions

The ISFTA covers only trade in goods. It provides either (i) duty free access (zero duty) or (ii) duty preferences for products that are not under the Negative list. While India provides 4,227 Sri Lankan products duty free access to India, Sri Lanka provides

¹⁰Handbook on Indo-Sri Lanka Free Trade Agreement, High Commissioner of India to Sri Lanka, March 2013

2,802 Indian products duty free access to its economy. In the negative list there are 431 products from India's side (garments, plastic products, rubber products etc), whereas 1,220 products from Sri Lanka's side (agricultural/livestock products, paper products, rubber products, electrical items etc) do not have any duty concession. They are excluded to protect the local industry. However, India has provided quotas on exports of tea, textiles and garments.

India provides duty free access to many product categories in almost all HS chapters, with the exception of HS Chapter 46 (manufactures of straw, of esparto or of other plaiting materials; basket-ware and wickerwork) and HS Chapters 50-63 covering textiles and textile articles. Sri Lanka also provides 100 percent duty concessions to Indian traders on a majority of product categories, excluding the following:

- HS 04 (Dairy produce; birds' eggs; natural honey; edible products of animal origin, not elsewhere specified or included);
- HS 06 (Live trees and other plants; bulbs, roots and the like; cut flowers and ornamental foliage);
- HS 09 (Coffee, tea, mate and spices);
- HS 16 - HS 24 (Prepared foodstuffs; beverages, spirits and vinegar; tobacco and manufactured tobacco substitutes);
- HS 46 (Manufactures of straw, of esparto or of other plaiting materials; basket-ware and wickerwork); and
- HS 64 (Footwear, gaiters and the like; parts of such articles).

Both India and Sri Lanka are also eligible for trade preferences under the South Asia Free Trade Agreement (SAFTA), which came into force in January 2006. SAFTA gives further preferences to both countries for certain category of products not covered under the ISFTA. The negative list for Sri Lanka with regard to India under SAFTA is 865, which is significantly higher than the 431 tariff lines in the

negative list under the ISFTA. On the other hand, the negative list for India with regard to Sri Lanka amounts to 1,065 tariff lines under the SAFTA, compared to the 1,220 tariff lines under the ISFTA. There are a total of 139 items in Sri Lanka's negative list under the ISFTA that do not feature in Sri Lanka's list under SAFTA. Duty free access under these items is, therefore, available to Indian exporters. India has also reduced the number of tariff lines under its negative list for SAFTA Non-Least Developed Contracting States (NDLCs) (Pakistan and Sri Lanka) by 264 items or 30 percent thereby providing the Sri Lankan exporters more access to Indian market.

Following are the commodities for which India offers quotas:

- **Tea:** 50 percent tariff preference on five tea items subject to a quota of 15 million kilograms per year.
- **Garments:** Garments covering Chapters 61 & 62 while remaining in the negative list, to be given 50 percent tariff concessions for 223 products on a fixed basis, subject to an annual restriction of eight million pieces. All eight million pieces would be allowed at zero duty with no fabric sourcing conditions.
- **Textiles:** A tariff reduction of 25 percent will be given for 528 textile items (Chapters 51-56, 58-60, & 63). Four Chapters under the textile sector remain in the negative list (Chapters 50, 57, 61 and 62). India has reduced 155 textile lines through a 30 percent reduction of its sensitive list under SAFTA.

The ISFTA has contributed towards more equitable and balanced growth of bilateral trade by narrowing the trade gap between the two countries in favour of Sri Lanka. Over 70 percent of Sri Lanka's exports have been undertaken under FTA preferences, compared to 30 percent of India's exports¹¹.

¹¹Handbook on Indo-Sri Lanka Free Trade Agreement, High Commissioner of India, March 2013

Comprehensive Economic Partnership Agreement

The success of the India-Sri Lanka Free Trade Agreement made both the countries keen for reaping the benefits of broader economic integration. The need for widening the ambit of the ISFTA to go beyond trade in goods and to include trade in services and investment was emphasized in the report of Joint Study Group¹². This would come under the Comprehensive Economic Partnership Agreement (CEPA). Negotiations for the CEPA began in 2005, and after three years of negotiations, the CEPA framework agreement was scheduled for signature by the two countries in parallel during the 15th South Asian Association for Regional Cooperation Summit in Colombo in July 2008. However, due to the reservations expressed by majority of Sri Lankan industrialists, the CEPA was not signed. The reservations expressed were due to the following reasons¹³–

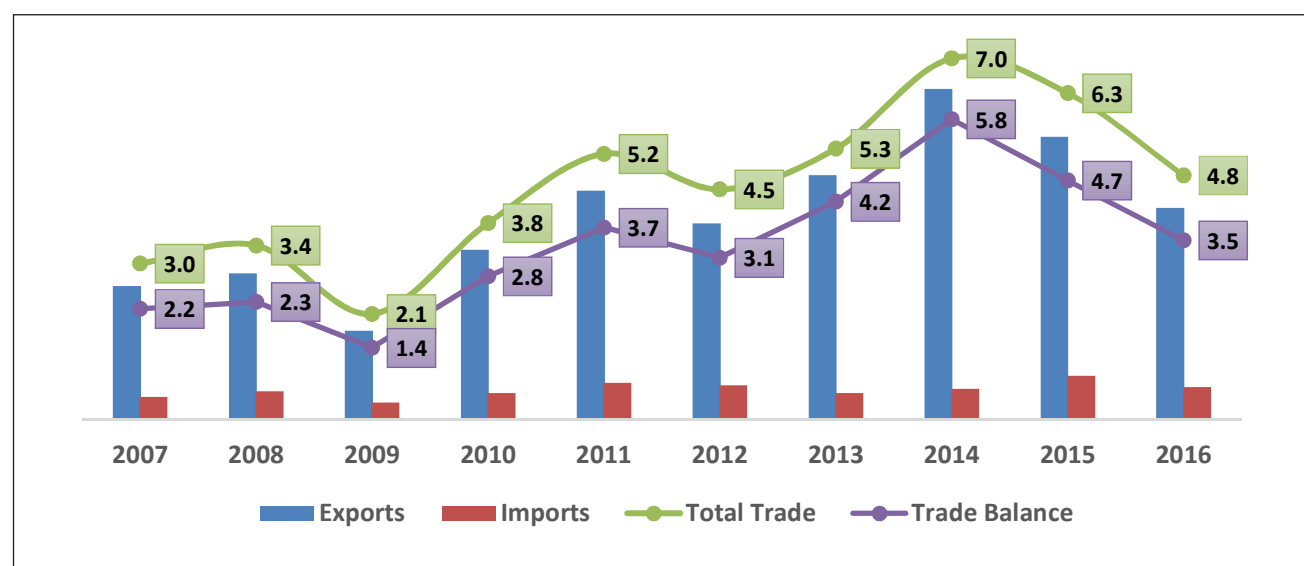
The first concern was largely related to the inclusion of trade in services, specifically the movement of natural persons (Mode 4) which was understood as a move toward free movement of labour between the two countries. Sri Lanka was concerned with the adverse impact of Indian labour's movement to the Sri Lanka's market.

Secondly, many of the Sri Lankan exporters were of the opinion that the non-tariff barriers in the Indian market were not taken into consideration in CEPA.

At present, the **Economic and Technical Cooperation Agreement (ETCA)**¹⁴ is being negotiated between the two countries as an extension over the ISFTA to widen the scope of trade, investment and technological cooperation. However, it would exclude movement of professional labour other than two sub-sectors – ship builders and IT professionals. The ETCA aims to boost cooperation in technical areas, scientific expertise and research among institutions, boost standard of

Chart 4.1: India's Trade with Sri Lanka

(US\$ billion)



Note: Bilateral trade figures in this chapter are considered with India being the reporting country and Sri Lanka being the partner and, thus, may not be comparable with corresponding data in other chapters.

Source: ITC Trade Map, derived from UN COMTRADE

¹²Joint Study Group on India Sri-Lanka Comprehensive Economic Partnership Agreement, October 2003

¹³The India–Sri Lanka Free Trade Agreement and the Proposed Comprehensive Economic Partnership Agreement: A Closer Look, Saman Kelegama, ADB Working Paper No. 458, February 2014

¹⁴The Economic and Technological Cooperation Agreement: Full steam ahead for India and Sri Lanka?, South Asia@ LSE, London School of Economics and Political Science Blog, 2016

Table 4.1: India's Major Exports to Sri Lanka

HS Code	Commodity	2007 (US\$ mn)	Share in Exports to Sri Lanka in 2007 (%)	2016 (US\$ mn)	Share in Exports to Sri Lanka in 2016 (%)	CAGR (%)	Share in India's Exports in 2016 (%)
	Total	2,594.2	100.0	4,118.3	100.0	5.3	1.6
87	Vehicles other than railway or tramway	253.0	9.8	627.8	15.2	10.6	4.2
88	Aircraft, spacecraft and their parts	92.0	3.5	415.5	10.1	18.2	13.7
27	Mineral fuels, oils and its products	971.1	37.4	373.5	9.1	-10.1	1.3
89	Ships, boats and floating structures	115.2	4.4	256.6	6.2	9.3	8.0
52	Cotton	117.6	4.5	243.4	5.9	8.4	3.9
30	Pharmaceutical products	77.0	3.0	198.7	4.8	11.1	1.5
84	Machinery and mechanical appliances	64.4	2.5	175.5	4.3	11.8	1.3
25	Salt, sulphur, earths and stones	9.6	0.4	172.9	4.2	37.9	9.5
85	Electrical machinery and equipment	33.6	1.3	123.6	3.0	15.6	1.5
60	Knitted or crocheted fabrics	28.2	1.1	113.7	2.8	16.8	42.8
09	Coffee, tea and spices	50.1	1.9	109.9	2.7	9.1	3.7
72	Iron and Steel	115.6	4.5	93.7	2.3	-2.3	1.5
39	Plastics and its articles	50.8	2.0	91.9	2.2	6.8	1.8
48	Paper and its articles	51.8	2.0	88.2	2.1	6.1	7.4
07	Edible vegetables, roots and tuber	46.3	1.8	83.5	2.0	6.8	7.2

Source: ITC Trade Map, derived from UN COMTRADE

goods and services to be able to compete in the global market and improve opportunities for manpower training and human resource development.

Trends in Bilateral Trade

During 2001, Sri Lanka accounted for 1.4 percent of India's exports, which amount to US\$ 621.5 million. Over the years, exports have increased reaching US\$ 2.6 billion in 2007 and increased by a CAGR of 5.3 percent to US\$ 4.1 billion in 2016 in the last ten years.

India's imports from Sri Lanka increased from US\$ 55.0 million in 2001 to US\$ 0.4 billion in 2007. Imports have increased over the years peaking at US\$ 0.8 billion during 2015. During 2007 to 2016 imports from Sri Lanka have grown by a CAGR of 4.1 percent.

Total trade peaked during 2014 at US\$ 7 billion increasing from US\$ 3 billion in 2007. Total trade fell in 2015 and 2016 due to decline in export of mineral fuels, oils and product of distillation (**Chart 4.1**). India has maintained a trade surplus with Sri Lanka over the years, which stood at US\$ 3.5 billion in 2016, owing to its size, population and rapidly emerging economy.

Major Commodities Traded

India's exports to Sri Lanka during 2016 was dominated by vehicles other than railway or tramway, accounting for 15.2 percent of the total exports, followed by aircraft, spacecraft and their parts; mineral fuels, oils and product of their distillation; ships, boat and floating structures; and

Table 4.2: India's Major Imports from Sri Lanka

HS Code	Commodity	2007 (US\$ mn)	Share in Imports from Sri Lanka in 2007 (%)	2016 (US\$ mn)	Share in Imports from Sri Lanka in 2016 (%)	CAGR (%)	Share in India's Imports in 2016 (%)
	Total	441.4	100.0	632.3	100.0	4.1	0.2
09	Coffee, tea and spices	31.2	7.1	70.3	11.1	9.4	9.4
23	Residues from food industry & animal fodder	16.9	3.8	52.2	8.3	13.3	10.8
08	Edible fruits and nuts	0.9	0.2	45.3	7.2	54.6	1.6
27	Mineral fuels, oils and product of distillation	0.6	0.1	41.8	6.6	60.2	0.0
60	Knitted or crocheted fabrics	2.7	0.6	36.0	5.7	33.4	7.2
89	Ships, boats and floating structures	0.1	0.0	35.9	5.7	92.3	0.7
47	Pulp of wood or of other fibrous cellulosic material	13.2	3.0	34.3	5.4	11.2	2.1
39	Plastics and articles	3.3	0.7	22.7	3.6	23.9	0.2
84	Machinery and mechanical appliances	9.3	2.1	22.4	3.5	10.3	0.1
40	Rubber and articles	29.9	6.8	21.4	3.4	-3.6	0.7
85	Electrical machinery and equipment	42.9	9.7	20.7	3.3	-7.8	0.1
94	Furniture and stuffed furnishing	7.4	1.7	18.8	3.0	10.9	1.3
48	Paper and its articles	4.9	1.1	18.2	2.9	15.7	0.7
62	Articles of apparel and clothing, not knitted or crocheted	1.3	0.3	17.7	2.8	33.7	5.2
68	Articles of stone, plaster, cement & similar materials	15.6	3.5	16.1	2.6	0.4	2.1

Source: ITC Trade Map, derived from UN COMTRADE

cotton (**Table 4.1**). The share of vehicles other than railway and tramway have increased from 9.8 percent of total exports in 2007 to 15.2 percent in 2016 by CAGR of 10.6 percent. The shares of commodities such as aircraft and spacecraft parts; ships, boats and other floating structures; cotton; pharmaceutical products; machinery and mechanical appliances; salt, sulphur, earth and stones, and other commodities in exports to Sri Lanka have also increased during 2007 to 2016. The shares of mineral fuels, oil and product of their distillation and iron and steel have, however, fallen during the same period.

Another notable factor is that products exported to Sri Lanka like aircraft, spacecraft and parts; ships, boats and floating structures; salt, sulphur, earth and stones; knitted or crocheted fabrics; paper and its article; and edible vegetables, roots and tuber have a significant share in India's total exports to the world in 2016, thereby revealing the importance of Sri Lanka as an export destination for India. The CAGR for these commodities have increased during 2007 to 2016, except for mineral fuels, oils and their products, and iron and steel.

The major commodities imported from Sri Lanka include coffee, tea and spices, residue from food industry & animal fodder, edible fruits and nuts, mineral fuels, oils and product of their distillation, and knitted or crocheted fabrics, and ships, boats and floating structures, which together account for around 45 percent of India's imports from Sri Lanka in 2016. Share in imports from Sri Lanka have increased significantly during 2007 to 2016 for major commodities like coffee, tea and spices; edible fruits and nuts; mineral fuels, oils and product of their distillation; knitted and crocheted fabrics; ships, boats and floating structures and wood pulp (**Table 4.2**). The share of commodities like rubber and its articles,

electrical machinery and equipment, and articles of stone, cement and plaster in India's imports from Sri Lanka during 2007 to 2016, however declined Coffee, tea, spices; residue from food industry and animal fodder; knitted and crocheted fabrics; and apparel and clothing, not knitted or crocheted imported from Sri Lanka have significant share in India's import from the world in 2016, revealing Sri Lanka's importance as an import source. These commodities have also registered significant CAGR during 2007 to 2016, except for rubber and its articles, electrical machinery and equipment and articles of stone, plaster and cement.

Box 4.1: Informal Trade between Sri Lanka and India

According to a study carried out by ICRIER¹⁵, Indo-Sri Lanka informal trade is quite significant and amounted to US\$ 207 million during 2000-01. This would be roughly 30 percent of the total formal trade between the two countries in 2001. According to a survey conducted by the study, informal trade was found to be largely air-borne constituting 87 percent of total informal trade, the rest 13 percent being sea-borne informal trade. It was majorly unidirectional from India to Sri Lanka; informal export from India accounted for 89 percent of the total informal trade.

Informal traders/carriers mainly travel between Colombo and the three major cities of India namely Chennai, Tiruchirapalli and Thiruvananthapuram. In addition, goods are also procured from Delhi and Mumbai; mostly via Chennai. Chennai is the main centre for air-borne informal exports and imports, accounting for 85 percent of informal exports and 79 percent of informal imports.

The estimates on composition of air-borne informal trade show that textiles are the largest item constituting 57 percent of total air-borne informal exports, followed by electrical and mechanical items (20 percent). Other items exported informally were utensils, food items, electronic items, sports goods, brass items, medicines and agarbattis. Air-borne informal imports comprised largely of spices accounting for 37 percent of imports, followed by electronics (30 percent). The other items imported informally are cosmetics, cigarettes, liquor, ceramic and bags.

The estimates of composition of sea-borne informal trade show that electrical and mechanical items and grocery items accounted for 71 percent of sea-borne informal export to Sri Lanka. The other items exported informally by sea are utensils, chemicals and garments. The largest item imported informally by sea from Sri Lanka to India is electronics constituting 42 percent of sea-borne informal import, followed by spices, liquor, cigarettes and cosmetics.

On the import front, demand for third country goods was considered the most important factor influencing imports, due to difference in tariffs with the rest of the world prevailing in India and Sri Lanka. The Study also noted that in the context of the FTA, this implies that third country goods do not meet the requirements of rules of origin principles and are therefore traded informally from Sri Lanka to India. However, such trade is significantly lower than was witnessed in the early nineties when informal exports were roughly equal to informal imports. Lowering of tariffs has led to a reduction in informal imports of third country goods in recent years.

¹⁵India's Informal Trade with Sri Lanka, Nisha Taneja, Indian Council for Research on International Economic Relations (ICRIER) Working Paper No. 82, April 2002

India-Sri Lanka Trade in the context of SAARC¹⁶

The South Asian Association for Regional Cooperation (SAARC) Preferential Trading Arrangement (SAPTA) was signed in April 1993 and came into force in December 1995 with the objective of promoting mutual trade and economic cooperation among the member countries through exchange of concessions. However, with a relatively slower progress under SAPTA, the two governments decided to enter into a bilateral agreement to increase the mutual benefits

of free trade¹⁷. As a result of such arrangement, trade between India-Sri Lanka has witnessed significant increase. However, there is a need to further enhance India-Sri Lanka's trade in order to catch up with the pace of India's trading activities with other SAARC countries such as Bangladesh and Nepal. In fact, during the period 2007-2016, Sri Lanka's position has declined from being the top trading partner in the SAARC region in 2007 to the third largest trading partner after Bangladesh and Nepal in 2016 (Table 4.3 and 4.4).

Table 4.3: India's Trade with SAARC Nations in 2007

(US\$ million)

Country	Export	Import	Total Trade	Trade Balance
Afghanistan	218.5	76.1	294.6	142.4
Bangladesh	2,063.8	233.3	2,297.1	1830.5
Bhutan	70.8	202.1	272.9	-131.3
Maldives	79.7	3.6	83.3	76.1
Nepal	1,237.1	469.8	1,706.9	767.3
Pakistan	1,584.3	286.7	1,871.0	1297.6
<i>Sri Lanka</i>	<i>2,594.2</i>	<i>441.4</i>	<i>3,035.6</i>	<i>2,152.8</i>
SAARC	7848.4	1713	9561.4	6135.4

Source: ITC Trade Map, derived from UN COMTRADE

Table 4.4: India's Trade with SAARC Nations in 2016

(US\$ million)

Country	Export	Import	Total Trade	Trade Balance
Afghanistan	473.0	282.3	755.3	190.7
Bangladesh	5,668.8	677.1	6,345.9	4,991.7
Bhutan	374.2	127.3	501.5	246.9
Maldives	180.2	6.3	186.5	173.9
Nepal	4,526.2	385.3	4,911.5	4,140.9
Pakistan	1,592.6	461.1	2,053.7	1,131.5
<i>Sri Lanka</i>	<i>4,118.3</i>	<i>632.3</i>	<i>4,750.6</i>	<i>3,486.0</i>
SAARC	16,933.3	2,571.7	19,505	14,361.6

Source: ITC Trade Map, derived from UN COMTRADE

¹⁶The South Asian Association for Regional Cooperation (SAARC) was established with the signing of the SAARC Charter in Dhaka on 8 December 1985. SAARC comprise eight Member States: Afghanistan, Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka. (SAARC Secretariat)

¹⁷India-Sri Lanka Bilateral Free Trade Agreement: Six Years Performance and Beyond, Saman Kelegama, Indra Nath Mukherji, RIS, February 2007

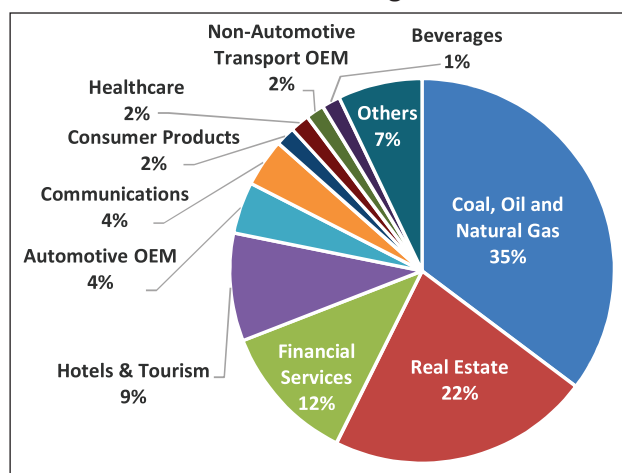
Bilateral Investment between India and Sri Lanka

India and Sri Lanka signed a Bilateral Investment Promotion and Protection Agreement on January 22, 1997, which came into force on February 13, 1998. According to data from the Ministry of Finance, Government of India (GOI) and the RBI, India's approved cumulative investments in Sri Lanka during April 1996 to March 2018 amounted to US\$ 1.5 billion¹⁸.

The RBI data on overseas direct investments only captures the approved overseas investments rather than actual flow of funds and the ultimate destination of fund flows; and this could lead to distorted picture of the extent of the linkages between India and the rest of the world in terms of actual outward investments. To overcome this limitation, and to get a more meaningful understanding on the trends in Indian overseas investments, this study has drawn upon the data collated by the Financial Times through its online database tracking cross-border greenfield investment, viz. fDi Markets, which provides real-time monitoring of investment projects and capital investment to track and profile companies investing overseas.

According to fDi Markets database, India has emerged as the largest investor in Sri Lanka during 2007 to 2016, with an investment of US\$ 5.3 billion in 61 FDI projects, resulting in creation of 14,196 jobs. It accounts for 30.7 percent of total investments made in Sri Lanka during this period. Coal, oil and natural gas received the highest investment which amounted to US\$ 1.9 billion, followed by real estate (US\$ 1.2 billion), financial services (US\$ 0.6 billion), hotels & tourism (US\$ 0.5 billion) and automotive OEMs

Chart 4.2: Major Sectors Attracting Indian Investment in Sri Lanka during 2007-2016



Note: fDi Markets tracks crossborder investment in a new physical project or expansion of an existing investment which creates new jobs and capital investment. This data differs from official data on FDI flows as company can raise capital locally, phase their investment over a period of time, and can channel their investment through different countries for tax efficiency.

Source: fDi Markets online database

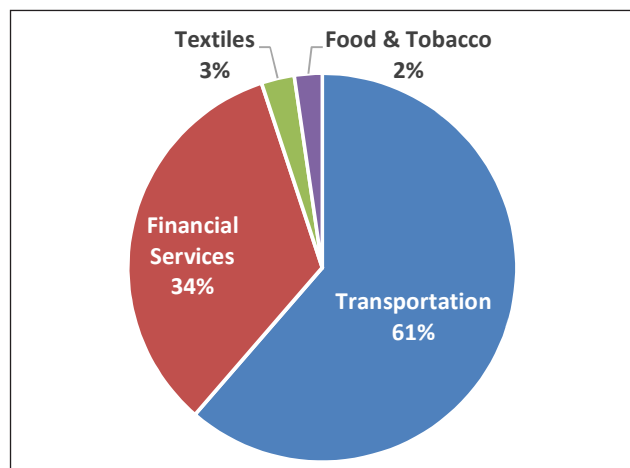
(US\$ 0.2 billion) during this period. **Chart 4.2** shows the major sectors attracting Indian investments in Sri Lanka along with their respective shares during the same period.

Some of the Indian companies that have invested in Sri Lanka include Indian Oil Corporation (IOC), NTPC Ltd. (National Thermal Power), Mahindra & Mahindra (M&M), ITC, Bharti Airtel, Mfar Hotels & Resorts, Life Insurance Corporation of India Ltd. (LIC), MRF Lanka, TVS Group, Ashok Leyland, UltraTech Cements, Ambuja Cement, CEAT, Aditya Birla Group, L&T, SSN Logistics etc¹⁹. Some Indian banks present in Sri Lanka include State Bank of India (SBI), Indian Overseas Bank (IOB), Indian Bank, ICICI Bank and

¹⁸Approved Overseas Direct Investment implies RBI Approvals for Overseas Direct Investment in Equity, Loan and Guarantees

¹⁹fDi Markets

Chart 4.3: Major Sectors Attracting Sri Lankan Investment in India during 2007-2016



Note: fDi Markets tracks crossborder investment in a new physical project or expansion of an existing investment which creates new jobs and capital investment. This data differs from official data on FDI flows as company can raise capital locally, phase their investment over a period of time, and can channel their investment through different countries for tax efficiency.

Source: fDi Markets online database

Axis Bank²⁰. Lanka LIC, a subsidiary of LIC of India, is also operating in Sri Lanka in the insurance sector.

According to Ministry of Commerce and Industry, GOI, during April 2000 to December 2017, India's total foreign direct investment inflows from Sri Lanka amounted to US\$ 73.6 million.

According to fDi markets database, Sri Lanka has invested capital of amount US\$ 0.6 billion in 15 greenfield projects leading to creation of 1,555 jobs in India during 2007 to 2016. The major sectors in which Sri Lanka has invested are transportation (US\$ 360.6 million), financial services, textiles, food and tobacco. The respective shares of these sectors are shown in **Chart 4.3**. Some of the Sri Lankan companies investing in India are CL Synergy, Bank of Ceylon, Fashion 365 Retail, Apexaura, Kandurata Umbrella Industries and Odel. Bank of Ceylon is operating in India with its services limited only to commercial operations and catering primarily to Sri Lankans.

²⁰India Sri Lanka Foreign Relations, MEA, GoI

5. POTENTIAL FOR ENHANCING INDIA'S TRADE WITH SRI LANKA

As highlighted in the previous chapter, bilateral trade relations between India and Sri Lanka have witnessed a significant rise in recent years, having risen from US\$ 3.0 billion in 2007 to US\$ 4.8 billion in 2016.

Although India is Sri Lanka's second largest import source, there still exists considerable untapped potential for Indian exporters in Sri Lanka's diversified market. This section attempts to identify such potential items of exports from India to Sri Lanka so as to enhance bilateral trade relations, based on an analysis of Sri Lanka's top imports, India's share in Sri Lanka's imports, and India's global export capability. The identification of potential items of India's exports is based on the following criteria:

- Identification of major items in Sri Lanka's import basket, and share of India in each product line of imports, based on 2-digit HS commodity code; and
- Selection of potential items of India's exports based on low share of India in Sri Lanka's import basket of major commodities, keeping in view India's global export capability. This would entail identification of potential export items under each 2-digit HS code, up to the 6-digit HS commodity code.

As can be seen in **Table 5.1**, India's share in Sri Lanka's imports of the identified commodities is marginal, thus, highlighting the potential to enhance these exports to Sri Lanka, in light of the demand in the country, and also India's global export capability. These potential items of India's exports to Sri Lanka would include:

- Machinery and mechanical appliances (HS-84)
- Electrical machinery, equipment and parts (HS-85)

- Pearls, precious stones and metals (HS-71)
- Special woven & tufted textile fabrics, lace, tapestries, and embroidery (HS-58)
- Aircraft, spacecraft and parts (HS-88)
- Optical, photographic, medical and surgical apparatus (HS-90)
- Cereals (HS-10)
- Dairy produce, eggs, honey and other edible products of animal origin (HS-04)
- Ships, boats and floating structures (HS-89)
- Man-made filaments and man-made textile materials (HS-54)
- Animal or vegetable fats and oils (HS-15)

Based on the above analysis, potential items of export to Sri Lanka, under each of the above identified categories, up to the 6-digit HS code, are analysed below.

Machinery and Mechanical Appliances (HS-84)

Sri Lanka's total import of machinery and mechanical appliances has more than doubled over the past decade, from US\$ 831.7 million in 2007 to US\$ 1,750.2 million in 2016, with majority of the imports being sourced from China, which accounted for a share of 33 percent of Sri Lanka's total imports of the commodity in 2016 (**Table 5.2**).

Machinery and mechanical appliances constitute India's 3rd largest global exports in 2016, amounting to US\$ 13.6 billion, with a share of 5.2 percent in India's total exports to the world, highlighting high global export capability of India for this commodity. India has the potential to further enhance export of these items to Sri Lanka, keeping in view Sri Lanka's high demand for these commodities. With a view to increasing India's exports to Sri Lanka, potential items for exports at 6-digit HS commodity code have been identified and presented in **Table 5.3**.

Table 5.1: Potential Items of Exports from India to Sri Lanka, 2016

HS Code	Product Label	Sri Lanka's Imports from World (US\$ mn)	Sri Lanka's Imports from India (US\$ mn)	% Share of India in Sri Lanka's Total Imports	India's Exports to World (US\$ mn)
84	Machinery and mechanical appliances	1,750.2	187.9	10.7	13,557.5
85	Electrical machinery, equipment and parts	1,375.8	147.6	10.7	8,217.9
71	Pearls, precious stones and metals	514.2	10.6	2.1	42,290.7
58	Special woven & tufted textile fabrics, lace, tapestries, and embroidery	315.2	15.8	5.0	361.2
88	Aircraft, spacecraft and parts	298.8	0.2	0.1	3,025.8
90	Optical, photographic, medical and surgical apparatus	288.3	21.2	7.4	2,649.6
10	Cereals	259.4	9.5	3.6	5,554.8
04	Dairy produce, eggs, honey and other edible products of animal origin	250.3	1.3	0.5	279.7
89	Ships, boats and floating structures	226.6	0.5	0.2	3,221.9
54	Man-made filaments and man-made textile materials	199.6	16.4	8.2	1,925.4
15	Animal or vegetable fats and oils	130.1	4.0	3.1	843.8

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Table 5.2: Sri Lanka's Major Sources of Imports of Machinery and Mechanical Appliances (HS-84)

Partner Country	2007		2016	
	Value (US\$ mn)	% Share	Value (US\$ mn)	% Share
World	831.7	100.0	1,750.2	100.0
China	89.9	10.8	577.6	33.0
India	78.9	9.5	187.9	10.7
Japan	64.2	7.7	128.6	7.3
Germany	76.2	9.2	117.7	6.7
USA	51.4	6.2	93.1	5.3
Singapore	175.8	21.1	77.5	4.4
Malaysia	21.1	2.5	73.7	4.2
Italy	36.6	4.4	71.0	4.1
Thailand	13.5	1.6	53.4	3.1
UK	33.7	4.1	48.7	2.8

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Table 5.3: Machinery and Mechanical Appliances (HS-84) – Potential Exports to Sri Lanka

HS Code	Product Label	Sri Lanka's Imports from World 2016 (US\$ mn)	Sri Lanka's Imports from India 2016 (US\$ mn)	India's Share in Sri Lanka's Imports (%)	India's Exports to World 2016 (US\$ mn)
847130	Data-processing machines, automatic, portable, weighing <= 10 kg	82.6	-	-	18.9
848180	Appliances for pipes, boiler shells (excluding pressure-reducing valves)	46.3	4.0	9.0	707.1
842952	Self-propelled mechanical shovels, excavators and shovel loaders	43.9	2.0	5.0	146.8
842810	Lifts and skip hoists	26.4	0.6	2.0	13.9
847141	Data-processing machines, automatic	24.9	0.1	1.0	11.4
844399	Parts and accessories of printers, copying machines and facsimile machines	24.2	0.7	3.0	21.8
842951	Self-propelled front-end shovel loaders	21.8	2.0	9.0	36.3
841370	Centrifugal pumps, power-driven (excluding those of subheading 8413.11 and 8413.19)	20.6	1.3	6.0	229.2

Note: '-' indicates not available/negligible

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Electrical Machinery, Equipment and Parts (HS-85)

Sri Lanka's total imports of electrical machinery and equipment have also nearly doubled over the past decade, from US\$ 742.9 million in 2007 to US\$ 1,375.8 million in 2016, indicating an increasing import demand for the commodity. Nearly half of the imports of electrical machinery and equipment have been sourced from China (**Table 5.4**).

Electrical machinery and equipment form India's 9th largest global exports in 2016, amounting to US\$ 8.2 billion, with a share of 3.2 percent in India's total exports to the world, highlighting India's global export capability of this commodity. Keeping in view high demand of the commodity in Sri Lanka, and given India's export capability, the potential items for enhancing such exports (at 6-digit HS code) have been identified and presented in **Table 5.5**.

Pearls, Precious Stones and Metals (HS-71)

Sri Lanka's total import of pearls, precious stones and metals has nearly doubled over the past decade, from US\$ 283.3 million in 2007 to US\$ 514.2 million in 2016, with major import sources being Switzerland, UAE, Singapore, Israel and Belgium (**Table 5.6**).

Pearls, precious stones and metals (HS-71) form India's largest global exports in 2016, amounting to US\$ 42.3 billion, with a share of 16.3 percent in India's total exports to the world. However, India's share in Sri Lanka's global imports of this commodity stands at a meagre 2.1 percent in 2016, highlighting the potential to further export these items to Sri Lanka. With a view to increasing India's exports of pearls, precious stones and metals to Sri Lanka, potential items for exports at 6-digit HS commodity code have been identified and presented in **Table 5.7**.

Table 5.4: Sri Lanka's Major Sources of Imports of Electrical Machinery, Equipment and Parts (HS-85)

Partner Country	2007		2016	
	Value (US\$ mn)	% Share	Value (US\$ mn)	% Share
World	742.9	100.0	1,375.8	100.0
China	117.2	15.8	616.4	44.8
India	40.1	5.4	147.6	10.7
Vietnam	2.2	0.3	58.1	4.2
Germany	19.5	2.6	57.5	4.2
USA	41.6	5.6	48.6	3.5
Hong Kong	104.1	14.0	46.2	3.4
Japan	18.8	2.5	44.9	3.3
Singapore	83.6	11.3	42.1	3.1
Switzerland	27.4	3.7	38.9	2.8
Malaysia	15.2	2.0	37.8	2.7

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Table 5.5: Electrical Machinery, Equipment and Parts (HS-85) - Potential Exports to Sri Lanka

HS Code	Product Label	Sri Lanka's Imports from World 2016 (US\$ mn)	Sri Lanka's Imports from India 2016 (US\$ mn)	India's Share in Sri Lanka's Imports (%)	India's Exports to World 2016 (US\$ mn)
851712	Telephones for cellular networks, mobile telephones or for other wireless networks	241.9	3.2	1.0	235.7
851762	Machines for the reception, conversion and transmission or regeneration of voice/ images	140.5	0.6	-	182.9
852872	Reception apparatus for colour television	87.6	23.5	27.0	27.4
850440	Static converters	38.2	3.5	9.0	526.6
850213	Generating sets with compression-ignition, internal combustion piston engine, diesel or semi-diesel	34.9	14.5	41.0	71.1
853400	Printed circuits	26.9	0.1	-	127.7
850300	Parts suitable for use solely or principally with electric motors and generators	25.6	7.9	31.0	225.9
851770	Parts of telephone sets, telephones for cellular networks or for other wireless networks	24.4	2.1	9.0	475.7
853710	Boards, cabinets and similar combinations of apparatus for electric control or the distribution	22.0	3.7	17.0	352.0

Note: '-' indicates not available/negligible

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Table 5.6: Sri Lanka's Major Sources of Imports of Pearls, Precious Stones & Metals (HS-71)

Partner Country	2007		2016	
	Value (US\$ mn)	% Share	Value (US\$ mn)	% Share
World	283.3	100.0	514.2	100.0
Switzerland	5.9	2.1	151.7	29.5
UAE	3.5	1.2	146.7	28.5
Singapore	5.3	1.9	91.7	17.8
Israel	34.8	12.3	67.5	13.1
Belgium	180.4	63.7	17.9	3.5
India	3.0	1.1	10.6	2.1
Slovakia	-	-	9.8	1.9
Hong Kong	4.7	1.7	3.8	0.7
Thailand	2.9	1.0	3.2	0.6
China	0.3	0.1	3.1	0.6

Note: '-' indicates not available/negligible

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Table 5.7: Pearls, Precious Stones & Metals (HS-71) – Potential Exports to Sri Lanka

HS Code	Product Label	Sri Lanka's Imports from World 2016 (US\$ mn)	Sri Lanka's Imports from India 2016 (US\$ mn)	India's Share in Sri Lanka's Imports (%)	India's Exports to World 2016 (US\$ mn)
710812	Gold, including gold plated with platinum	374.8	-	-	4,329.6
710239	Diamonds excluding industrial diamonds (worked, but unmounted/ unset)	54.2	4.7	8.8	22,440.7
710231	Non-industrial diamonds (unworked)	52.1	3.7	7.1	1,576.1
710391	Rubies, sapphires and emeralds (unmounted/ unstrung)	6.6	0.1	1.5	255.7
711319	Articles of jewellery of precious metal other than silver	3.9	0.4	9.2	9,205.9
711790	Imitation jewellery (excluding that of base metal)	2.2	0.4	19.9	128.3
711719	Imitation jewellery of base metal	1.6	0.6	38.6	83.4

Note: '-' indicates not available/negligible

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Special Woven & Tufted Textile Fabrics, Lace, Tapestries and Embroidery (HS-58)

As can be noted from **Table 5.8**, there has been a steady rise in Sri Lanka's total imports of special woven & tufted textile fabrics, lace, tapestries and embroidery, which has increased by more than

two-fold over the past decade from US\$ 142 million in 2007 to US\$ 315.2 million in 2016. However, majority of these imports have been sourced from China, with a share of 33.2 percent in Sri Lanka's imports of the commodity in 2016, followed by Hong Kong, South Korea, and Italy.

On the other hand, over the past decade, India's share in Sri Lanka's imports of the commodity witnessed marginal increase from 2.9 percent in 2007 to 5 percent in 2016. In order to further increase India's exports to Sri Lanka, considering India's export capability of the commodity, the potential items for exports at 6-digit HS commodity code have been identified and presented in **Table 5.9**.

Aircraft, Spacecraft and Parts (HS-88)

Sri Lanka has witnessed more than ten-folds growth in imports of aircraft, spacecraft and their parts over the past decade, which has increased from US\$ 20.5 million in 2007 to US\$ 298.9 million in 2016. France is the largest source of Sri Lanka's imports of this commodity, with a share of

Table 5.8: Sri Lanka's Major Sources of Imports of Special Woven & Tufted Textile Fabrics, Lace, Tapestries and Embroidery (HS-58)

Partner Country	2007		2016	
	Value (US\$ mn)	% Share	Value (US\$ mn)	% Share
World	142.0	100.0	315.2	100.0
China	13.4	9.5	104.6	33.2
Hong Kong	49.7	35.0	91.3	29.0
Republic of Korea	3.5	2.4	25.1	8.0
Italy	22.6	15.9	19.5	6.2
Taiwan	10.4	7.3	18.3	5.8
India	4.2	2.9	15.8	5.0
Indonesia	0.9	0.7	8.6	2.7
Thailand	7.2	5.1	7.3	2.3
USA	2.4	1.7	4.7	1.5
Japan	0.6	0.4	2.9	0.9
Germany	3.5	2.5	2.7	0.9

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Table 5.9: Special Woven & Tufted Textile Fabrics, Lace, Tapestries and Embroidery (HS-58)- Potential Export to Sri Lanka

HS Code	Product Label	Sri Lanka's Imports from World 2016 (US\$ mn)	Sri Lanka's Imports from India 2016 (US\$ mn)	India's Share in Sri Lanka's Imports (%)	India's Exports to World 2016 (US\$ mn)
580429	Mechanically made lace (excluding that of man-made fibres)	97.3	0.9	0.9	10.7
580620	Narrow woven fabrics of textile materials	91.1	6.0	6.6	17.5
580410	Tulles and other net fabrics	29.4	2.9	9.9	8.8
580710	Labels, badges and similar articles of textile materials	17.6	0.9	5.1	6.5
580632	Narrow woven fabrics of man-made fibres	13.0	0.1	0.6	9.7

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

53.5 percent in Sri Lanka's imports, followed by UK, which has a share of 40.3 percent in Sri Lanka's imports (**Table 5.10**).

While India's global exports of aircraft, spacecraft and their parts stood at US\$ 3 billion in 2016, which indicates high global export competency of Indian exporters, India's share in Sri Lanka's imports of the

commodity continued to remain meagre over the past decade, accounting for a share of 0.1 percent in 2016. To capture the untapped market for this commodity in Sri Lanka based on export capabilities of India, the potential items for exports at 6-digit HS commodity code have been identified and presented in **Table 5.11**.

Table 5.10: Sri Lanka's Major Sources of Imports of Aircraft, Spacecraft and Parts (HS-88)

Partner Country	2007		2016	
	Value (US\$ mn)	% Share	Value (US\$ mn)	% Share
World	20.5	100.0	298.8	100.0
France	6.0	29.4	159.8	53.5
UK	1.5	7.2	120.5	40.3
USA	1.1	5.6	10.1	3.4
Germany	4.6	22.4	2.7	0.9
China	0.7	3.2	2.3	0.8
Singapore	3.8	18.7	0.9	0.3
Turkey	-	-	0.4	0.1
Hong Kong	0.4	1.8	0.4	0.1
Saudi Arabia	-	-	0.3	0.1
Netherlands	0.2	1.0	0.2	0.1
India	-	-	0.2	0.1

Note: '-' indicates not available/negligible

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Table 5.11: Aircraft, Spacecraft and Parts (HS-88) -Potential Export Items to Sri Lanka

HS Code	Product Label	Sri Lanka's Imports from World 2016 (US\$ mn)	Sri Lanka's Imports from India 2016 (US\$ mn)	India's Share in Sri Lanka's Imports (%)	India's Exports to World 2016 (US\$ mn)
880240	Aeroplanes and other powered aircraft of an unladen weight of more than 15000 kg (excluding helicopters)	265.8	-	-	727.4
880330	Parts of aeroplanes or helicopters (excluding those for gliders)	29.2	0.2	0.5	1660.2
880211	Helicopters of an unladen weight of 2000 kg or lesser	1.6	-	-	1.6
880390	Parts of aircraft and spacecraft	0.7	-	1.5	288.5
580632	Narrow woven fabrics of man-made fibres	13.0	0.1	0.6	9.7

Note: '-' indicates not available/negligible

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Optical, Photographic, Medical and Surgical Apparatus (HS-90)

Sri Lanka's total imports of optical, photographic, medical and surgical apparatus has increased by nearly three-folds over the past decade from US\$ 97.1 million in 2007 to US\$ 288.3 million in 2016, with major import sources being the US, China, Germany and Japan (Table 5.12).

India's global exports of optical, photographic,

medical & surgical apparatus amounted to US\$ 2.6 billion in 2016. However, over the past decade, India's share in Sri Lanka's imports of the commodity has significantly declined from 13 percent in 2007 to 7.4 percent in 2016. In order to boost India's exports to Sri Lanka, considering India's global export capability of the commodity, the potential items for exports at 6-digit HS commodity code have been identified and presented in Table 5.13.

Table 5.12: Sri Lanka's Major Sources of Imports of Optical, Photographic, Medical and Surgical Apparatus (HS-90)

Partner Country	2007		2016	
	Value (US\$ mn)	% Share	Value (US\$ mn)	% Share
World	97.1	100.0	288.3	100.0
USA	4.3	4.5	54.3	18.8
China	9.2	9.4	42.9	14.9
Germany	12.0	12.4	33.4	11.6
Japan	10.4	10.7	31.3	10.8
India	12.7	13.0	21.2	7.4
UK	4.4	4.6	18.0	6.3
France	1.8	1.8	13.6	4.7
Ireland	0.1	0.1	8.9	3.1
Switzerland	7.0	7.2	7.7	2.7
Singapore	16.1	16.5	7.7	2.7

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Table 5.13: Optical, Photographic, Medical and Surgical Apparatus (HS-90) – Potential Export Items to Sri Lanka

HS Code	Product Label	Sri Lanka's Imports from World 2016 (US\$ mn)	Sri Lanka's Imports from India 2016 (US\$ mn)	India's Share in Sri Lanka's Imports (%)	India's Exports to World 2016 (US\$ mn)
901890	Instruments/ appliances used in medical, surgical or veterinary sciences	50.6	3.4	6.7	186.3
903289	Regulating/ controlling instruments and apparatus (excluding hydraulic or pneumatic, manostats)	19.9	3.4	17.2	239.9
902190	Articles and appliances worn, carried, or implanted in the body	14.8	1.7	11.3	10.0

902139	Artificial parts of the body (excluding artificial teeth and dental fittings)	13.5	0.4	2.8	36.7
903180	Instruments, appliances and machines for measuring or checking	11.3	0.8	7.5	73.3
902214	Apparatus based on the use of X-rays, for medical, surgical or veterinary uses	11.0	0.1	0.9	38.1
902780	Instruments and apparatus for physical or chemical analysis, or for measuring or checking viscosity	10.7	0.6	5.7	25.7
901839	Needles, catheters, cannulae used for medical, surgical, dental or veterinary purposes	7.9	0.9	11.6	211.6
902830	Electricity supply or production meters, incl. calibrating meters	7.8	0.5	6.6	98.0
902110	Orthopaedic or fracture appliances	6.2	1.6	25.5	27.6
903300	Parts and accessories for machines, appliances, instruments or other apparatus	6.0	0.5	8.5	83.8
901819	Electro-diagnostic apparatus, incl. apparatus for functional exploratory examination	5.0	-	0.1	45.3

Note: '-' indicates not available/negligible

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Cereals (HS-10)

Nearly half of Sri Lanka's imports of cereals are sourced from Canada, which has a share of 47.1 percent in Sri Lanka's imports of cereal in 2016, followed by Russia, which has a share of 20.6 percent (**Table 5.14**). Other major sources of imports of cereals for Sri Lanka include Australia (8.6 percent), the US (6.5 percent) and Germany (4.5 percent).

While cereals form India's 11th largest exports in 2016, amounting to US\$ 5.6 billion, India's share in Sri Lanka's imports of cereals has considerably declined over the past decade, from 15.8 percent in 2007 to 3.6 percent in 2016. As recorded by ITC, Sri Lanka has levied a high ad valorem tariff as high as 18 percent on cereals, which could be one of the probable reasons for a low share of the commodity in India's exports. With a view to enhance exports of cereal to Sri Lanka

in line with India's export capabilities, the potential items for exports at 6-digit HS commodity code have been identified and presented in **Table 5.15**.

Dairy Produce, Eggs, Honey and Other Edible Products of Animal Origin (HS-04)

Sri Lanka's imports of dairy produce, eggs, honey and other edible products of animal origin has grown significantly over the past decade from US\$ 186 million in 2007 to US\$ 250.3 million in 2016. However, majority of imports of this commodity are sourced from New Zealand, which has a share of 73 percent in Sri Lanka's imports of the commodity in 2016, followed by Australia, which has a share of 17 percent (**Table 5.16**).

Both in absolute as well as in relative terms, Sri Lanka's imports of the commodity from India has

Table 5.14: Sri Lanka's Major Sources of Imports of Cereals (HS-10)

Partner Country	2007		2016	
	Value (US\$ mn)	% Share	Value (US\$ mn)	% Share
World	264.1	100.0	259.4	100.0
Canada	166.7	63.1	122.1	47.1
Russia	-	-	53.6	20.6
Australia	0.7	0.3	22.3	8.6
USA	27.2	10.3	16.9	6.5
Germany	-	-	11.7	4.5
Pakistan	12.7	4.8	10.1	3.9
India	41.8	15.8	9.5	3.6
Thailand	1.4	0.5	4.3	1.7
China	6.0	2.3	2.9	1.1
Romania	-	-	2.8	1.1

Note: '-' indicates not available/negligible

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Table 5.15: Cereals (HS-10)- Potential Export Items to Sri Lanka

HS Code	Product Label	Sri Lanka's Imports from World 2016 (US\$ mn)	Sri Lanka's Imports from India 2016 (US\$ mn)	India's Share in Sri Lanka's Imports (%)	India's Exports to World 2016 (US\$ mn)
100199	Wheat and meslin (excluding seed for sowing and durum wheat)	230.2	0.7	0.3	47.5
100630	Semi-milled or wholly milled rice	12.5	2.7	21.4	5,057.6
100590	Maize (excluding seed for sowing)	10.8	4.8	44.1	106.3
100510	Maize seed for sowing	4.1	-	0.1	26.4
580632	Narrow woven fabrics of man-made fibres	13.0	0.1	0.6	9.7

Note: '-' indicates not available/negligible

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

declined over the past decade, from US\$ 1.7 million in 2007 to US\$ 1.3 million in 2016, with India's share declining from 0.9 percent in 2007 to 0.5 percent in 2016. As recorded by ITC, Sri Lanka has levied a high ad valorem tariff equivalent to 36 percent on dairy products, which could be one of the probable

reasons for a low share of the commodity in India's exports. Some of the potential items (at 6-digit HS code) for enhancing India's exports and capture the untapped market for this commodity in Sri Lanka have been identified and presented in **Table 5.17**.

Table 5.16: Sri Lanka's Major Sources of Imports of Dairy Produce, Eggs, Honey and Other Edible Products of Animal Origin (HS-04)

Partner Country	2007		2016	
	Value (US\$ mn)	% Share	Value (US\$ mn)	% Share
World	186.0	100.0	250.3	100.0
New Zealand	149.1	80.1	182.8	73.0
Australia	19.7	10.6	42.7	17.0
USA	2.1	1.1	10.4	4.1
Austria	1.7	0.9	7.0	2.8
Belgium	-	-	1.6	0.6
Denmark	-	-	1.4	0.6
India	1.7	0.9	1.3	0.5
Canada	0.9	0.5	0.6	0.2
Poland	-	-	539	0.2
UK	160	0.1	469	0.2

Note: '-' indicates not available/negligible

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Table 5.17: Dairy Produce, Eggs, Honey and Other Edible Products of Animal Origin (HS-04) – Potential Export Items to Sri Lanka

HS Code	Product Label	Sri Lanka's Imports from World 2016 (US\$ mn)	Sri Lanka's Imports from India 2016 (US\$ mn)	India's Share in Sri Lanka's Imports (%)	India's Exports to World 2016 (US\$ mn)
40210	Milk and cream in solid forms of a fat content by weight less than 1.5%	19.2	-	-	50.9
40630	Processed cheese (not grated or powdered)	8.8	0.3	3.8	4.5
40510	Butter (excluding dehydrated butter and ghee)	3.7	-	-	6.6

Note: '-' indicates not available/negligible

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Ships, Boats and Floating Structures (HS-89)

As is evident from **Table 5.18**, Sri Lanka's total imports of ships, boats and floating structures have increased by more than eighty times over the past decade from US\$ 2.8 million in 2007 to US\$ 226.6 million in 2016. It is noteworthy that China's share in Sri Lanka's import of the commodity has significantly amplified from 1.3 percent in 2007 to 98.4 percent

in 2016, thus making China the single largest import source of ships, boats and floating structures for Sri Lanka.

On the other hand, while India's global exports of ships, boats and floating structures amounted to US\$ 3.2 billion in 2016, India's share in Sri Lanka's imports of the commodity stood at a meagre 0.2 percent in 2016. In order to boost India's exports to

Sri Lanka, in view of India's global export capability, the potential items for exports at 6-digit HS commodity code have been identified and presented in **Table 5.19**.

Man-Made Filaments and Man-Made Textile Materials (HS-54)

The imports of man-made filaments and man-made textile materials by Sri Lanka has more than doubled in the past decade, from US\$ 96.5 million in 2007 to US\$ 199.6 million in 2016, indicating a high demand for the commodity in Sri Lanka. Nearly one-third of these imports are

sourced from China, which has a share of 31.8 percent in Sri Lanka's imports of this commodity in 2016, followed by Taiwan, which has a share of 8.7 percent (**Table 5.20**).

Despite being the third largest import source for the commodity, India's share in Sri Lanka's imports has considerably declined over the past decade, from 10.3 percent in 2007 to 8.2 percent in 2016. With a view to enhance exports of the commodity to Sri Lanka in line with India's export capabilities, the potential items for exports at 6-digit HS commodity code have been identified and presented in **Table 5.21**.

Table 5.18: Sri Lanka's Major Sources of Imports of Ships, Boats and Floating Structures (HS-89)

Partner Country	2007		2016	
	Value (US\$ '000)	% Share	Value (US\$ '000)	% Share
World	2,788	100.0	226,622	100.0
China	35.0	1.3	223,067	98.4
Finland	-	-	856	0.4
India	11.0	0.4	530	0.2
USA	133.0	4.8	470	0.2
France	125.0	4.5	451	0.2
Canada	-	-	219	0.1
Vietnam	-	-	215	0.1
UK	31.0	1.1	198	0.1
Japan	15.0	0.5	129	0.1
Mexico	-	-	91	-

Note: '-' indicates not available/negligible

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Table 5.19: Ships, Boats and Floating Structures (HS-89) – Potential Export Items to Sri Lanka

HS Code	Product Label	Sri Lanka's Imports from World 2016 (US\$ mn)	Sri Lanka's Imports from India 2016 (US\$ mn)	India's Share in Sri Lanka's Imports (%)	India's Exports to World 2016 (US\$ mn)
890510	Dredgers	219.7	-	-	184.2
890190	Vessels for the transport of goods & persons	4.1	-	-	229.1

Note: '-' indicates not available/negligible

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Table 5.20: Sri Lanka's Major Sources of Imports of Man-Made Filaments and Man-Made Textile Materials (HS-54)

Partner Country	2007		2016	
	Value (US\$ mn)	% Share	Value (US\$ mn)	% Share
World	96.5	100.0	199.6	100.0
China	9.7	10.1	63.5	31.8
Taiwan	9.8	10.1	17.5	8.7
India	9.9	10.3	16.4	8.2
Hong Kong	7.0	7.3	15.1	7.6
Italy	5.7	5.9	14.2	7.1
USA	7.5	7.8	14.2	7.1
Republic of Korea	6.6	6.8	9.5	4.7
Singapore	7.3	7.5	7.5	3.8
Japan	0.7	0.7	6.8	3.4
Vietnam	0.6	0.6	6.7	3.3

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Table 5.21: Man-Made Filaments and Man-Made Textile Materials (HS-54) – Potential Export Items to Sri Lanka

HS Code	Product Label	Sri Lanka's Imports from World 2016 (US\$ mn)	Sri Lanka's Imports from India 2016 (US\$ mn)	India's Share in Sri Lanka's Imports (%)	India's Exports to World 2016 (US\$ mn)
540233	Textured filament yarn of polyester (excluding that put up for retail sale)	16.9	3.6	22	713.6

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Animal or Vegetable Fats and Oils (HS-15)

Sri Lanka's imports of animal or vegetable fats and oils are sourced from Malaysia, which has a share of 79.9 percent in Sri Lanka's imports of the commodity in 2016, followed by Indonesia, which has a share of 5.3 percent (**Table 5.22**).

On the other hand, Sri Lanka's imports of the commodity from India has declined over the past decade, from US\$ 14.5 million in 2007 to US\$ 4 million in 2016, with India's share declining from 7.7

percent in 2007 to 3.1 percent in 2016. As recorded by ITC, Sri Lanka has levied a high ad valorem tariff equivalent to 38 percent on animal or vegetable fats and oils, which could be one of the probable reasons for a low share of the commodity in India's exports. In line with India's export capability, the potential items (at 6-digit HS code) for enhancing India's exports to capture the untapped market for this commodity in Sri Lanka have been identified and presented in **Table 5.23**.

Table 5.22: Sri Lanka's Major Sources of Imports of Animal or Vegetable Fats and Oils (HS-15)

Partner Country	2007		2016	
	Value (US\$ mn)	% Share	Value (US\$ mn)	% Share
World	189.3	100.0	130.1	100.0
Malaysia	33.7	17.8	103.9	79.9
Indonesia	37.2	19.6	6.9	5.3
Turkey	-	-	5.2	4.0
India	14.5	7.7	4.0	3.1
UK	0.3	0.2	2.4	1.9
South Africa	0.2	0.1	2.4	1.9
Australia	3.7	1.9	1.0	0.8

Note: '-' indicates not available/negligible

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Table 5.23: Animal or Vegetable Fats and Oils (HS-15) – Potential Export Items to Sri Lanka

HS Code	Product Label	Sri Lanka's Imports from World 2016 (US\$ mn)	Sri Lanka's Imports from India 2016 (US\$ mn)	India's Share in Sri Lanka's Imports (%)	India's Exports to World 2016 (US\$ mn)
151800	Animal or vegetable fats and oils and their fractions (boiled, oxidised, dehydrated/ sulphurised)	8.2	-	0.2	27.3
151620	Vegetable fats and oils and their fractions, (partly or wholly hydrogenated, inter-esterified)	6.5	-	0.3	56.2
151790	Edible mixtures or preparations of animal or vegetable fats or oils	6.4	0.1	2.1	3.6
150420	Fats and oils of fish and their fractions	1.8	-	0.9	11.6

Note: '-' indicates not available/negligible

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Potential for Enhancing Sri Lanka's Exports to India

The previous section highlighted potential for enhancing India's exports to Sri Lanka for tapping the untapped markets for Indian exporters. With a view to enhancing overall bilateral trade with Sri Lanka, this section attempts to identify potential items of exports from Sri Lanka to India, based on an analysis of Sri Lanka's top exports, India's share in Sri Lanka's exports, and India's global import demand. The criteria for identification of potential items of

Sri Lanka's exports to India is broadly similar to the previous analysis and is given as under:

- Identification of major items in Sri Lanka's export basket, and share of India in each product line of exports, based on 2-digit HS commodity code; and
- Selection of potential items of Sri Lanka's exports based on low share of India in Sri Lanka's export basket of major commodities, keeping in view India's global import demand & Sri Lanka's

export capability. This would entail identification of potential items for Sri Lanka's exports under each 2-digit HS code, up to the 6-digit HS commodity code.

Table 5.24 depicts India's share in Sri Lanka's exports of the identified commodities, which is marginal, therefore, highlighting the potential to enhance these exports from Sri Lanka, in light of the demand in India, and also Sri Lanka's export capability. These potential items of Sri Lanka's exports to India would include:

- Mineral fuels, mineral oils and distillation products (HS-27)
- Pearls, precious stones and metals (HS-71)
- Coffee, tea, maté and spices (HS-09).

Mineral Fuels, Mineral Oils and Distillation Products

Mineral fuels, mineral oils and distillation products

form India's largest imports, amounting to US\$ 89.3 billion in 2016 and accounting for 25 percent of India's total imports from the world during the same year. India's major sources of imports of this commodity include Saudi Arabia, Iraq, UAE, Nigeria and Iran.

Sri Lanka's exports of mineral fuels stood at US\$ 163.6 million in 2016, which majorly gets exported to UAE and Singapore. India's share in Sri Lanka's total exports stood at 9.3 percent in 2016. There exists potential to enhance exports of certain specific commodities under the mineral fuels category, in view of Sri Lanka's export capability and India's capacity to absorb such exports. Such potential items of exports (at 6-digit HS code) have been identified and presented in **Table 5.25**.

Table 5.24: Potential Items of Exports from Sri Lanka to India, 2016

HS Code	Product Label	Sri Lanka's Exports to World (US\$ mn)	Sri Lanka's Exports to India (US\$ mn)	% Share of India in Sri Lanka's Total Exports	India's Imports from World (US\$ mn)
27	Mineral fuels, mineral oils and distillation products	163.6	15.2	9.3	89,308.8
71	Pearls, precious stones and metals	215.2	3.5	1.6	48,129.7
09	Coffee, tea, maté and spices	1,525.0	69.6	4.6	747.4

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Table 5.25: Mineral Fuels, Mineral Oils and Distillation Products (HS-27)- Potential Items of Exports to India

HS Code	Product Label	Sri Lanka's Exports to World 2016 (US\$ mn)	Sri Lanka's Exports to India 2016 (US\$ mn)	% Share of India in Sri Lanka's Total Exports	India's Imports from World 2016 (US\$ mn)
271019	Medium oils and preparations of petroleum or bituminous minerals	158.2	15.2	10.0	2,233.7

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Pearls, Precious Stones and Metals (HS-71)

Pearls, precious stones and metals constitute India's second largest imported commodities, with a share of 13.5 percent in India's total imports in 2016. India's major sources of imports of this commodity include Switzerland, UAE, Hong Kong and Belgium.

At the same time, pearls, precious stones and metals form the 6th largest exports for Sri Lanka, which is majorly exported to Israel, Hong Kong, the US, Switzerland and Belgium. India's share in Sri Lanka's exports of this commodity, however, stood at a meagre 1.6 percent, thus, highlighting the potential to expand exports of the commodity from Sri Lanka. In view of India's capacity to absorb such commodities due to its high import demand, a list of such identified potential items for exports from Sri Lanka (at 6-digit HS code) are presented in **Table 5.26**.

Coffee, Tea, Maté and Spices (HS-09)

India's total imports of coffee, tea, mate and spices stood at US\$ 747.4 million in 2016, which are majorly imported from Vietnam, with a share of 27.9 percent of India's total imports of this commodity. Sri Lanka is India's second largest import source, with a share of 9.4 percent of India's total imports of the commodity.

At the same time, coffee, tea, mate and spices form the 3rd largest exports for Sri Lanka, amounting to US\$ 1.5 billion in 2016, with a share of 14.5 percent in Sri Lanka's total exports to the world. This commodity is majorly exported to Iran, Russia, Iraq, Turkey and UAE, with India's share in Sri Lanka's exports of this commodity being only 4.6 percent, thus, highlighting the potential to expand the exports from Sri Lanka, in view of Sri Lanka's global export capability and India's high import demand of the commodity. A list of identified potential items for exports from Sri Lanka (at 6-digit HS code) are presented in **Table 5.27**.

Table 5.26: Pearls, Precious Stones and Metals (HS-71) - Potential Items of Exports to India

HS Code	Product Label	Sri Lanka's Exports to World 2016 (US\$ mn)	Sri Lanka's Exports to India 2016 (US\$ mn)	% Share of India in Sri Lanka's Total Exports	India's Imports from World 2016 (US\$ mn)
710239	Diamonds worked, but unmounted/ unset (excluding industrial diamonds)	85.1	0.1	-	2,453.6
710391	Rubies, sapphires and emeralds, worked, but unstrung /unmounted	79.3	2.2	3.0	1,421.9
710231	Non-industrial diamonds, unworked (excluding industrial diamonds)	19.0	0.1	1.0	16,455.7
711319	Articles of jewellery of precious metal other than silver and their parts	12.9	0.4	3.0	300.9

Note: '-' indicates not available/negligible

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

Table 5.27: Coffee, Tea, Maté and Spices (HS-09) - Potential Items of Exports to India

HS Code	Product Label	Sri Lanka's Exports to World 2016 (US\$ mn)	Sri Lanka's Exports to India 2016 (US\$ mn)	% Share of India in Sri Lanka's Total Exports	India's Imports from World 2016 (US\$ mn)
090411	Pepper of the genus Piper	68.1	47.5	70.0	183.2
090710	Whole fruit and stems of Cloves	12.8	4.7	36.0	141.5

Source: ITC Trade Map, derived from UN COMTRADE and Exim India Analysis

6. KEY OBSERVATIONS AND THE WAY FORWARD

As highlighted in the previous chapters, India and Sri Lanka have enjoyed a strong socio-economic relationship, which has strengthened over the years. As around 80 percent of world trade are carried by sea, Sri Lanka's role in the nautical corridor between the East and West is of importance not only from a geostrategic perspective, as well as from maritime economics and security perspectives. Sri Lanka has a unique geo-strategic advantage, as it is located at the crossroads of major shipping routes connecting South Asia, the Far East and the Pacific with Europe and the Americas. The East-West shipping route passes just six to ten nautical miles south of Sri Lanka. More than 60,000 ships navigates through this route annually carrying two-thirds of global petroleum supply and half of all containerized cargo²¹. Supported by its strategic location, Sri Lanka could play a greater role as a global export hub. India being a major partner of Sri Lanka could support in this endeavor of Sri Lanka.

Challenges hindering Export Potential of Sri Lanka

Low Export Base: Sri Lanka has a narrow export base, with exports being concentrated on few products and partners. The share of Sri Lanka's exports in total global exports remained low at 0.07 percent in 2016 as compared to 0.06 percent in 2007. Because of the narrow export base, the country is exposed to large fluctuations in commodity prices. Sri Lanka's lack of export innovation and limited markets have restricted the export sector from reaching its full potential. Inadequate production base to produce for domestic or export markets is another major factor hindering export development of the country.

As Sri Lanka has a low degree of export commodity composition, it could consider developing the export potential of other sectors, so as to further benefit from

an export-led growth process. Currently, Sri Lankan economy focus mostly on simple and unsophisticated products, with low share of high-tech exports. Export base, hence, should be expanded through a mix of strategies along with increased innovations in the sector. New finance products along with interest rate subventions are also necessary for export development. SMEs and non-traditional exporters need to be given a big push by providing export finance at a lower rate.

The current import tax system of the country remains highly protectionist and complex, deterring long term financial commitments in production and trade to some extent. This needs to be corrected and FDI in tradable sectors should be actively promoted. Hence, there is a strong case for providing time-bound tax holidays and investment tax allowances beyond the tax-holiday period for export-oriented investors in Sri Lanka.

Product-Market Concentration: Sri Lankan exports are exposed to concentration risk where the demand conditions for select set of products and markets could have a significant bearing on the country's export performance. Being a small island nation, sustained growth and development in Sri Lanka requires growth and diversification of exports. Diversification into new markets, new buyers as also new products is an imperative. Sri Lankan exports are yet to penetrate many foreign markets. For a wide market penetration, information on new markets, regulatory barriers in the countries etc. should be made easily available for the exporters. Exporters should also be provided support for new and niche product development which would give the country an edge in the international trade arena.

²¹'Sri Lanka's Role in the Indian Ocean and the Changing Global Dynamic' Speech by Dr Harsha de Silva, Deputy Minister for Foreign Affairs, Sri Lanka at the Institute of South Asian Studies, National University of Singapore on January 9, 2017

Strengthening Free Trade Agreements: There is also a need to strengthen and extend Sri Lanka's existing FTAs. The World Bank has suggested that Sri Lanka should make progress on bilateral trade agreements while carefully evaluating the costs and benefits to the country, with special focus on non-tariff barriers and Mutual Recognition Agreements.²² In the context of current lackluster export growth in the country, Sri Lanka could expand its trade with other developing countries, especially in Asia. This would enable the country to diversify its trade from Western developed economies, and reduce its vulnerabilities which emerge from adverse development in these economies. As South Asia is among the fastest growing regions in the world, Sri Lanka's FTAs with select Asian economies could play a major role here.

Sri Lanka should leverage various opportunities provided by these regional synergies emerging out of FTAs. While negotiating for new FTAs and further discussions on existing FTAs, the country need to address various issues which are prevalent in its current FTAs. For instance, ongoing trade negotiations between India and Sri Lanka need to address various non-tariff barriers. The India-Sri Lanka Economic Technology Cooperation Agreement (ETCA) once signed is expected to enhance the scope of existing FTA between both countries by facilitating freer movement of goods and services with special emphasis on cooperation in the development of technology and in investments. Thus, Sri Lanka should make maximum use of its existing PTAs and FTAs, while forming FTAs with other major countries should be a priority area.

Enhancing India-Sri Lanka Relationship

Some of the key focus areas and imperatives for strengthening India's engagements with Sri Lanka are highlighted below:

Geographical Concentration in Sri Lanka's Exports to India: Sri Lankan exporters and businesses exporting to India have kept their geographical focus too narrow. They concentrate more on expansions into Tamil Nadu, partially due to strong historical socio-economic ties between Sri Lanka and Tamil Nadu. It has been estimated that 40 percent of India's total trade with Sri Lanka takes place through Tamil Nadu, as a significant share of Sri Lankan exports to India enter through Chennai Port. This is at the expense of other trade-friendly South Indian states including Andhra Pradesh, Karnataka, Kerala, and Telangana.²³

Trade through sea route is cheaper compared to other modes of transportation. Since South India has six major sea ports of India including the Chennai Port, Ennore Port, and Tuticorin Port in Tamil Nadu, the Visakhapatnam Port in Andhra Pradesh, the New Mangalore Port in Karnataka, and the Cochin Port in Kerala, along with other intermediate sea ports, the transshipment of cargos from Sri Lanka to various ports is easily possible at cheaper rates. An increased effective cooperation with the other Southern Indian states could pave way for integrating Sri Lankan manufacturing into various value chains present in the Indian manufacturing sector. There is immense potential to enhance India's trade relations with Sri Lanka, and in the process to correct the trade imbalance existing between both countries.

Cooperation to Formalize Informal Trade: Though no official figures are available for recent values of informal trade between both countries, various reports identify that there exists a large informal trade taking place between India and Sri Lanka. The unofficial trade is carried out by both air and sea routes. Air-borne trade takes place mostly through air passengers and sea-borne takes place in the form of boat trade through ports. The total informal trade between India and Sri Lanka is approximately 25-30

²²Enhancing competitiveness in Sri Lanka, World Bank, June 2016

²³"Indo-Sri Lanka Economic Relations in Modi's India", speech by Dr. S. Narayan – former Finance Secretary, Ministry of Finance, India on 20 November 2017 at the Lakshman Kadirgamar Institute (LKI)

percent of the formal bilateral trade between both countries. Informal imports from India are around 40-45 percent of formal imports, while informal exports are around 25-30 percent of formal exports²⁴.

Sri Lankan goods including automobile spare parts, construction materials, cement, spices, electronic items and commodities such as cosmetics, cigarettes, liquor, and ceramic are mostly involved in this informal trade. Indian goods include mostly textile products, electrical and mechanical items, apparatus, food items, electronic items, sports goods, brass items and medicines. According to Directorate of Revenue Intelligence, India, a lot of gold and silver has also been smuggled from Sri Lanka to India. Efforts should be made to formalize this informal trade by means of trade and tariff liberalization, and relaxing the stringent government procedures, resulting in enhancement of formal bilateral trade between India and Sri Lanka. This also involves regular formal information exchange between both countries.

Setting up a Mechanism for Promoting Indian Investments in Sri Lanka: Supported by its natural resources, investment incentives, educated work force and comparatively cheaper wages, Sri Lanka offers huge potential for investment for Indian investors in a number of sectors including tea, tourism, tyre manufacturing, manufacturing of vehicles, IT-enabled products and services, and infrastructure sector, among others. Sri Lanka is a beneficiary under GSP+ scheme of EU and also has FTAs with India, Iran and Pakistan. Sri Lanka signed a Comprehensive Economic Partnership Agreement with Singapore, and is currently negotiating FTA with China. It may not be necessary that Indian goods for exports are to be manufactured in India itself. India could leverage upon various FTAs of Sri Lanka and the GSP+ scheme and invest in Sri Lanka's potential

sectors and products.

The United Kingdom of Great Britain and Northern Ireland's Department for International Development (DFID) has set up the Supporting India's Trade Preferences for Africa (SITA) project with the aim of increasing value of business transactions between India and five African countries, namely Ethiopia, Kenya, Rwanda, Tanzania and Uganda. Its goal is to promote exports from these five East African countries to India through investment and skills transfer from the Indian side. Currently, Sri Lanka's exports are concentrated on a few commodities and countries. The government of India could set up a similar institutional mechanism/ framework in the lines of SITA project in Sri Lanka which would increase and diversify exports of Sri Lanka. Export diversification of Sri Lanka requires targeted intervention, and India could play a major role in improving the productive and export capacities of the country through investment, knowledge sharing and technology transfers. This would also improve capacities of Sri Lankan companies and Trade Support Institutions. This would further increase the trade between both countries, along with narrowing Sri Lanka's huge trade deficit with India. It may be set up in such a way that it need not be binding for Sri Lanka to export such products hence developed to India itself, but to any other markets where it has a comparative advantage. This proposal is also in line with the strategy of attracting more export-oriented FDI to enable exports which are enshrined in the Government of Sri Lanka's Vision 2025.

Cooperation in Capacity Development: An area of cooperation between India and Sri Lanka could be investing in capacity development. Sri Lankan exports generally lack innovation, and therefore need to

²⁴Legal Cross-Border Trade vs. Illegal Cross-Border Trade: Promoting Sustainable Regional Cooperation in South Asia through Transnational Trade, Muthukuda Arachchige Dona Shiroma Jeeva Shirajanie Niriella, Asian Journal of Humanities and Social Sciences (AJHSS), Volume 2, Issue 4, November, 2014

increase R&D spending to be more competitive. According to the World Bank, there are significant barriers holding back private creativity to realize the economic potential of Sri Lanka's relatively educated labor force. India could assist Sri Lanka in its efforts to increase R&D. Apart from investment, Indian institutions could share their expertise in the fields of export capability creation in the country, institutional strengthening and export development in the form of technical assistance and sharing of expertise through site visits. For instance, in the recent past Exim India has undertaken a consultancy assignment commissioned by the Commonwealth Secretariat to assist the Sri Lanka Export Credit Insurance Corporation to review its operating policies and suggest new products while recommending measures to enhance the overall export financing framework in Sri Lanka, and to create a framework for operationalising these recommendations.

Cooperation in SME Development: For economic growth to be inclusive, it is imperative to bring the SME sector into the Sri Lanka's mainstream trade, so that the gains from trade go where they could make the biggest difference. SMEs are vital as a vehicle to create jobs and therefore ensure more participation of the poor in economic development. SMEs in Sri Lanka account for 90 percent of the total number of enterprises, 45 percent of the total employment and contributes to 52 percent of the GDP of the country²⁵. The National Policy Framework for Small and Medium Enterprise (SME) Development 2016 of Sri Lanka recognizes the importance of cluster development. Under this cluster development approach, the entire value chain from input supply to processing and export will be supported and promoted. India could share its expertise on cluster development to the SMEs in Sri Lanka through various programmes.

²⁵National Policy Framework for Small Medium Enterprises (SMEs) Development, Ministry of Industry and Commerce, Sri Lanka, May 2016

7. EXPORT-IMPORT BANK OF INDIA IN SRI LANKA

As the apex financial institution in India for financing, promoting and facilitating India's international trade and investments, Export-Import Bank of India (Exim India)'s vision has evolved from financing, facilitating and promoting trade and investment to a conscious and systematic effort at creating export capabilities. Since Exim India commenced operations in 1982, the developing and least developed countries have always been a focus area, and thus formed a critical component of Exim India's strategy to promote and support South-South cooperation, trade and investment. Exim India's commitment towards building relationships and fostering cooperation among southern countries is reflected in the various activities and programmes which Exim India has set in place. Exim India operates a comprehensive range of financing, advisory and support programmes to promote and facilitate India's trade and investment.

A. Financing Programmes

(i) Lines of Credit

Exim India is the implementing agency for extending Lines of Credit (LOCs) under Government of India (GOI)'s India Development and Economic Assistance Scheme (IDEAS). To promote bilateral and regional commercial relations, Exim India extends LOCs to governments, parastatal organizations, financial institutions, commercial banks and regional development banks to support export of eligible goods on deferred payment terms. As on March 31, 2018, Exim India, at the behest of and on behalf of the Government of India, has extended a total of 7 operative LOCs to Sri Lanka, amounting to US\$ 1.43 billion (**Table 7.1**). An LOC of US\$ 150 million to Ceylon Petroleum Corporation, Sri Lanka has been fully repaid.

Table 7.1: Operative LOCs extended by Exim India to Sri Lanka

Sector and Purpose of Lines of Credit	Amount (US\$ million)
Purchase of equipment/supplies from India	100.0
Rehabilitation of Colombo-Matara Railway line	100.0
Upgradation of Southern Railway corridor from Colombo to Matara	67.4
Track Laying by IRCON - 92 km Ommanthai- Pallai of Northern Railway (US\$ 185.35 mn), Track Laying by IRCON - 60 km Madhu Church-Tallaimannar Sector (US\$ 149.74 mn) and Track Laying on Medawachchiya Madhu Railway Line (US\$ 81.31 mn)	416.4
Track laying on the Pallai-Kankesanthurai railway line (US\$ 149.34 mn), Setting up of signaling and telecommunications systems for the Northern railway line (US\$ 86.52 mn), and Other projects as may be approved by GOI (US\$ 146.51 mn)	382.4
For financing procurement of rolling stock for Sri Lankan Railways (US\$ 177 mn); Up-gradation of railway tracks (Maho-Anuradhapura-Omanthai or any other sector) (US\$ 136 mn), and Utilisation of balance amount, if any, as may be agreed to between Borrower (GOSL) and GOI	318.0
Rehabilitation of Kankesanthurai Harbour	45.3
Total Operative LOCs to Sri Lanka	1,429.5

Source: Exim India

(ii) Supporting Project Exports

Exim India plays a pivotal role in promoting and financing Indian companies in execution of projects. Towards this end, the institution extends funded and non-funded facilities for overseas industrial turnkey projects, civil construction contracts, supplies as well as technical and consultancy service contracts. These projects, in turn, facilitate and support infrastructure development in host countries, thereby contributing to the overall development process in the region. A number project contracts were secured and executed by Indian exporters in Sri Lanka with financing from Exim India in sectors such as railway line construction, civil, mechanical & engineering works, and ship building, among others.

(iii) Buyers Credit Under National Export Insurance Account (NEIA)

In order to provide further impetus to project exports from India on medium-or long-term basis, especially in the infrastructure sector, Buyer's Credit under National Export Insurance Account (BC-NEIA) was introduced in April 2011. Under this programme, Exim India facilitates project exports from India by way of extending credit facility to overseas sovereign governments and government-owned entities for import of goods and services from India on deferred credit terms. Indian exporters can obtain payment of eligible value from Exim India, without recourse to them, against negotiation of shipping documents. NEIA is a Trust, set up by Ministry of Commerce and administered by ECGC Ltd. As on March 31, 2018, Exim India sanctioned an aggregate amount of US\$ 441.4 million for 4 projects in Sri Lanka valued at US\$ 529.6 billion under BC-NEIA. The projects supported include:

- Supply, erection and commissioning of a 30 MLD Water Treatment Plant and distribution to 9 reservoirs across the Dambulla region;
- Supply of Two Offshore Patrol Vessels;
- Plant and design-build contract for civil, mechanical and engineering works for the

Aluthgama, Mathugama and Agalawatta Integrated Water Supply Project; and

- Design - Build Contract for Civil and Mechanical & Engineering Works for Polgahawela, Pothuhera and Alawwa Integrated Water Supply Project.

(iv) Finance for Joint ventures

With a view to support Indian companies in their endeavour to globalise their operations, Exim India operates a programme to support overseas investments by Indian companies through joint ventures (JVs) and wholly owned subsidiaries (WOS). Such supports include loans and guarantees, equity finance and in select cases direct participation in equity along with Indian promoter, to set up such ventures overseas. As on March 31, 2018, Exim India has provided finance to seven Indian companies for setting up ventures in Sri Lanka in pharmaceuticals, textiles/garments, ferrous metals & metal processing, telecommunications, and agro & food processing sectors, among others, with a sanctioned amount of ₹ 218.3 crores.

B. Asian Exim Banks Forum

With a view to enhance cooperation and forge a stronger linkage among its member institutions, the Asian Exim Bank's Forum (AEBF), a grouping of Asian Exim Banks, was conceived and initiated by Exim India in 1996. The Forum meets every year since its inception at an Annual event hosted by the member institutions in rotation. The Annual meetings serve as a forum for discussing a wide range of issues focused on fostering common understanding as well as exchanging and sharing information. Together, the endeavour is to meet the challenges faced by the Export Credit Agencies in the region and explore possible areas for further regional cooperation. Sri Lanka Export Credit Insurance Corporation (SLECIC) has attended meetings of the AEBF as an Observer.

C. Global Procurement Consultants Ltd.

Exim India has taken the initiative of setting up of Global Procurement Consultants Ltd. (GPCL),

in partnership with leading consultancy firms in India, for providing procurement related services to multilateral agencies such as the World Bank and Asian Development Bank. GPCL has undertaken a number of assignments in South Asia including an independent procurement review of the World Bank funded transport sector projects in Sri Lanka.

D. Research Studies

Exim India carries out research on areas related to bilateral trade and investment, sector/ product/ country and regional studies, as also policy issues related to the external sector with a view to enhancing competitiveness of Indian exporters. The published research studies related to Sri Lanka include:

- BIMSTEC Initiative: A Study of India's Trade and Investment Potential with Select Asian Countries
- Potential for Enhancing Intra-SAARC Trade: A Brief Analysis

E. Exim India: Experience Sharing

Exim India is well positioned to share its experience and expertise in the fields of capacity creation, institutional strengthening, export development and export capability creation. The Bank is, thus, well placed to provide a range of technical assistance in these fields. Exim India was commissioned by the Commonwealth Secretariat London, to assist the SLECIC to review its operating policies and suggest new products while recommending measures to enhance the overall export financing framework in Sri Lanka. The assignment was conducted in two phases. In the first phase, Exim India made a number of recommendations to strengthen the export credit institutional structure in Sri Lanka and enhancing its trade competitiveness by facilitating greater flow of export credit and broadening the export base of the country. The second phase involved creating a framework for operationalising the recommendations made by the Bank as part of the earlier assignment.

F. Marketing Advisory Services

Exim India plays a promotional role and seeks to create and enhance export capabilities and international competitiveness of Indian companies through its Marketing Advisory Services. The Bank provides assistance to Indian firms in their globalisation efforts by locating overseas distributor(s)/ buyer(s) / partner(s) for their products and services. Exim India also assists in identification of overseas opportunities for setting up plants or projects or for acquisition of companies overseas. A few cases where Indian exporters could foray into Sri Lankan markets with the support of Exim India is given below.

- A contract was signed between Kolkata based GPT Infra Pvt. Ltd. and National Housing Development Authority, Sri Lanka, for construction of low cost housing condominiums.
- Rajkot-based Antilla Propack signed an agreement for supplying laminated tubes and bottles to a Sri Lankan importer.
- A Gurgaon based company, Coslight India Ltd signed an agreement to supply lithium batteries to a telecom company in Sri Lanka.

G. Representative Office

Exim India has a representative office in Singapore, which seeks to establish and maintain relationships with multilateral agencies, regional development institutions, trade and investment promotion bodies, international banks, chambers of commerce, government departments and institutions and identify areas of cooperation in Sri Lanka, along with that in other countries in the region. The representative office also plays a role in facilitating India's economic cooperation with Sri Lanka, while keeping close coordination with Indian Missions in the region. The office projects Bank's capabilities in financing India's international trade and investment, as also keeps the Bank abreast of the developments in the economic and banking/ financial sectors in Sri Lanka.

Annexure:

Sri Lanka's Vision 2025: Goals, Approaches and Strategies

Goals	Approaches	Strategies
Strengthening Macroeconomic Framework	Three-pronged approach: 1 Fiscal consolidation 2 Price stability 3 Market based competitive exchange rate	<ol style="list-style-type: none"> 1 Broaden tax base to ensure tax revenue of 16 percent of GDP and rationalizing tax system by minimizing exemptions, tax holidays & special rates; 2 Rationalise government expenditure with mandatory binding targets for fiscal deficits and government debt levels; 3 Fiscal reforms to achieve medium to long-term targets for macroeconomic stability and an improved investor climate; 4 Liability management strategies to bring down debt (both domestic and foreign) to GDP ratio under 70 percent by 2020; 5 Prioritise capital expenditure outlays for development with a comprehensive Public Investment Programme (PIP); 6 Encourage improved domestic supply and distribution networks, and allow imports of food products and essential commodities at reasonable costs to address short term price fluctuations; 7 Move towards a flexible inflation targeting regime for medium and long term price stability; and 8 Allow the exchange rate to be market-determined.
Strengthening Growth	<ol style="list-style-type: none"> 1 Empower the private sector and accordingly incentivize domestic and private investments 2 Revamp trade policy to enable export-driven economy 3 Services expansion 	<ol style="list-style-type: none"> 1. Establish a 'Single Window' for new business registration to streamline procedures and improve investment climate; 2. Stipulate a standardised package of incentives with clear eligibility criteria for investors; Incentives to be linked directly to physical investments made in the form of capital allowances, with appropriately designed incentives for those in high technology and innovative industries; 3. Formulate clear Public-Private-Partnerships (PPP) policy with well-defined legal, regulatory and institutional framework to attract private players. Potential areas for expanding new PPPs include health care, leisure, tourism, education, ports and aviation; 4. Integrate SMEs into the formal sector by establishing hard and soft infrastructure frameworks to help them improve brand value, and access credit and new markets; 5. New Trade Policy, to attract more export-oriented FDI, improve trade logistics, make customs procedures transparent and quicker, and boost firms' abilities to compete in global markets; 6. Phase-out para-tariffs and simplify the tariff system;

		<ol style="list-style-type: none"> 7 Develop programmes to mitigate harmful effects on domestic firms and workers, including training and capacity building activities and trade cost adjustment compensatory finance programmes; 8 Enhance access to trade finance by strengthening the Sri Lanka Export Credit Insurance Corporation (SLECIC); 9 Encourage export-diversification into services; 10 Expand port infrastructure and related services to position Sri Lanka as a global logistics hub; 11 Develop tourism by establishing a conducive institutional framework for SMEs in the tourism industry & encouraging the private sector to attract tourists from new markets and to offer new products; and 12 Liberalise access to sea and air services to facilitate the tourism industry.
Reforming Factor Markets	<ol style="list-style-type: none"> 1 Land Reforms 2 Labour Market Reforms 3 Capital Market Reforms 	<ol style="list-style-type: none"> 1 Make changes to land tenure restrictions associated with alienated lands, offer clear transferable titles, and remove barriers to competitive real estate markets; 2 Establish major economic development zones and mega projects of urban development; 3 Improve land administration and modernise land management; 4 Facilitate increased female labour force participation through improving employee benefits as well as improving access to tertiary education and vocational training; 5 Encourage the private sector to conduct skill development programmes to improve labour productivity; 6 Balance policies to promote out-migration with domestic labour market needs; 7 Revise immigration policies to facilitate obtaining services of first and latter generation migrant Sri Lankans; 8 Formalise sectors of vulnerable employment by standardising occupations with internationally accepted certifications and licensing; 9 Reforms to improve financial market's legal and regulatory frameworks, infrastructure and institutions; and 10 Fast-track amendments to the Securities and Exchange Commission (SEC) Act and the Demutualisation Bill, and broaden regulatory provisions for the trading of derivatives and commodities to facilitate penetration of investment products to larger customer base.
Improving Economic and Social Infrastructure	<ol style="list-style-type: none"> 1 Provision and improvement of social goods such as education, skills development and healthcare 	<ol style="list-style-type: none"> 1 Making 13 years of education available to all and reforming education administrative procedures by establishing school boards and inspectorate; 2 Increasing access to tertiary education using a PPP model to have international universities in the country, improving R&D and links to global industries for practical training;

	<p>2 Inclusive growth through infrastructural development, technology optimization and digitalization</p>	<p>3 Expand opportunities for vocational training with private sector support;</p> <p>4 Restructure curricula for strengthening entrepreneurial capabilities;</p> <p>5 Strengthen the curative and preventive primary health care delivery system to treat Non Communicable Diseases (NCDs) and support programmes for combating Chronic Kidney Disease (CKDu);</p> <p>6 Review alcohol taxation policies to reduce alcohol consumption;</p> <p>7 Develop an electronic medical information management system;</p> <p>8 Expand access to emergency pre-hospital medical care, with basic and advanced life support;</p> <p>9 Increase investment in logistics, with a focus on infrastructure, especially road and rail networks;</p> <p>10 Establish economic corridors to facilitate industrial development, especially in the south western and north eastern regions, along secondary corridors for agro-based industries & tourism;</p> <p>11 Improve access to pipe borne water supply facilities in underserved urban areas and rural and estate areas with the help of PPPs;</p> <p>12 Encourage vertical housing projects to meet demand for urban low income and middle class affordable housing;</p> <p>13 Extensively improve the public transport system, establish multi-modal transport centres with park and ride facilities, electrify the existing railway system and construct new rail tracks; and</p> <p>14 Encourage the Build-Operate-Transfer model in small to medium scale infrastructure projects across the country.</p>
Enhancing Technology and Digitalization	<p>1 Encourage the use of digital and other emergent technologies</p> <p>2 Enhance the digital ecosystems</p>	<p>1 Encouraging the transfer of appropriate foreign technologies into Sri Lanka and promoting private sector investment in digital technology & ICT industry through incentives to support emerging industries and improve market access for start-ups;</p> <p>2 Integrating ICT literacy into school curricula in order to move towards a digitally empowered economy;</p> <p>3 Increasing free Wi-Fi provisions and incentives provided to widen internet access;</p> <p>4 Increasing digitalisation of Government operations and continuing the national digital identity initiative;</p> <p>5 Strengthening ICT based marketing interfaces for domestic producers to access a larger global market;</p> <p>6 Encouraging innovations in mobile payment systems and peer-to-peer lending platforms with necessary oversight to facilitate growing penetration mobile devices;</p>

		<ol style="list-style-type: none"> 7 Strengthening the National Intellectual Property Office to effectively manage registration exploitation, regulation and resolution; and 8 Strengthening the legal framework for electronic transactions to enhance the e-commerce legislative framework & cyber security.
Improving Social Safety Nets	<ol style="list-style-type: none"> 1 Provide necessary support to the poor and vulnerable 	<ol style="list-style-type: none"> 1 Establish an integrated, efficient social protection system to minimise programme duplications, beneficiary overlaps and reduce administrative costs; 2 Initiate a contributory pension benefit scheme for all workers; 3 Improve targeting for the Samurdhi programme for re-emphasising livelihood development and microfinance components to enable income generation; and 4 Improve access to public services, education, and employment opportunities for the differently abled by improving basic infrastructure facilities to make them independent and self-reliant.
Promoting Food Security and Sustainable Development	<ol style="list-style-type: none"> 1 Agricultural reforms to address food security 2 Create inclusive growth by developing underserved districts 3 Prioritize environmental protection and disaster management, and energy security 	<ol style="list-style-type: none"> 1 Facilitate efficiency in agricultural markets through a National Food Production Programme, establishing agricultural megazones, and strengthening value chain development; 2 Promote private sector participation and PPPs to modernise the agriculture sector, introduce modern value chains, and agriculture mega zones; 3 Expedite the proposed Agriculture Sector Modernisation Project and introduce incentive for SME agribusinesses to invest in commercial agriculture and value chains; 4 Exploring new niche markets, promoting value addition in tea for re-export, and private sector entrepreneurship in rubber, coconut and sugar production; 5 Helping smallholders improve production and processing to take advantage of global market opportunities and also offer short-term price support for sudden global commodity glut or collapse in price; 6 Credit facilities for encouraging investment in value addition and development of milk-based products, poultry and fisheries sectors; 7 Promote Smallholder Agribusiness Partnership (SAP) project to enhance competitiveness, by establishing public-private-producer-partnerships (4Ps) in agribusiness; 8 Introduce national level policy action on food quality and permitted fertilizer levels to ensure sufficient availability of organic products; 9 Establish a new development bank using existing financial institutions, to support long-term project-based development financing and enhance access to finance, particularly in the SME sector;

		<ol style="list-style-type: none"> 10 Undertake key development projects including Ruhuna Development Area, Trincomalee Economic Development Area, Wayamba Special Economic Development Area, and Rajarata Development among others; 11 Implement a comprehensive District Development Plan for all five districts in the Northern Province for resolving issues related to resettlement, re-building damaged infrastructure, facilitating livelihoods, community needs and drinking water; 12 Address rural infrastructure development such as building bridges, town development, small and medium size irrigation and potable water supply facilities in Uva province; 13 Establish regional technology centres to assist SMEs in identifying products in demand, target markets and opportunities to advertise online; 14 Implement strategies for financial inclusion by providing access to finance and financial literacy in rural areas, especially for the growth of the SME sector; 15 Establish a National Disaster Reserve Fund for financing post-disaster reconstruction to resettle those living in landslide prone areas; 16 Promoting sustainable use of oceanic and marine resources, organic agricultural practices, climate resilient green technology, and clean renewable energy; 17 Develop environment-friendly transport sector to promote energy efficient vehicles that will reduce fuel consumption; 18 Introduce a green financing strategy to encourage banks and other financial institutions to invest actively in green projects; 19 Phasing out single use polythene and using tax incentives to encourage citizens to practice waste management methods; 20 Implement waste to energy projects through PPP; 21 Increase overall power generation, access, and storage by implementing long-term generation expansion plans 22 Provide incentives for non-conventional renewable energy (NCRE) technologies, such as small hydros, wind power, and solar projects; 23 Implementation of formula-based pricing for dealing with energy products to minimise effects of global energy price fluctuations;
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		<p>24 Provide incentives for energy efficient imports, especially motor vehicles, bulbs, and electrical equipment and promote green construction methods and energy efficient industrial processes; and</p> <p>25 Develop the downstream petroleum industry-related infrastructure to regulate imports, exports, distribution and marketing of petroleum products.</p>
Strengthening Governance and Accountability	<p>1 Strengthen the rule of law</p> <p>2 Fight corruption</p> <p>3 Ensure democratic freedom</p>	<p>1 Strengthening policies of good governance by incorporating elements of constitutional reform, economic policy changes, improved governance, and transitional justice;</p> <p>2 Strengthening ongoing reconciliation efforts to ensure the rights of all citizens and uphold and strengthen citizens' Right to Information; and</p> <p>3 Implementation of the Grama Rajya (GR) concept to address gaps in people's participation in Government and development.</p>
Strengthening Coordination and Monitoring Implementation	<p>1 Coordinating for effective implementation of policies and projects</p>	<p>1 Implementation of a consistent and predictable economic policy framework;</p> <p>2 Strengthening the framework and capacity for monitoring and evaluation; and</p> <p>3 Utilizing digitalisation to support coordination and monitoring.</p>

Source: "Vision 2025 – A Country Enriched", Prime Minister's Office of Sri Lanka, 2017

About Exim Bank's Working Paper Series

As part of its endeavour in enriching the knowledge of Indian exporters and thereby to enhance their competitiveness, Exim Bank periodically conducts research studies. These research studies are broadly categorized into three segments, viz. sector studies, country studies and macro-economic related analysis. These studies are published in the form of Occasional Papers, Working Papers and Books. The research papers that are brought out in the form of Working Papers are done with swift analysis and data collation from various sources. The research papers under the series provide an analytical overview on various trade and investment related issues.

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