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Taking advantage of the Indo-Lanka Comprehensive Economic Partnership Agreement (CEPA)

Sri Lanka stands to benefit from early access to the large and growing Indian Services sector by engaging in CEPA.

Introduction

It is now 10 years since the Indo Lanka FTA was signed in 1998. During this period trade between the two countries reached new highs - India is now Sri Lanka's highest source of imports, 3rd highest export destination and the 5th highest source of FDI. Encouraged by the progress of the FTA, the two countries decided to deepen the agreement to include trade in services, investment and economic cooperation. Following the recommendations of the Joint Study Group report on the Indo-Lanka Comprehensive Economic Partnership Agreement (CEPA), negotiations began in May 2005. Thus far 10 rounds of technical level negotiations have been completed and the Agreement is expected to be signed sometime in mid 2008. This article will focus on the Trade in Services aspect of the CEPA and the potential opportunities available to the business community in Sri Lanka under this agreement.

What is Trade in Services?

Trade in services refers to the commercial exchange of services between countries. It is in essence similar to trade in goods in that it results in greater consumer choice and lower prices, increased competition and dynamism in markets and increased choice in sourcing services for business. However, trade in services occurs across 4 modes.

The liberalisation of trade in services refers to the removal of barriers that obstruct trade across these modes. Unlike trade in goods where taxes are the major barrier to trade, government regulations comprise the major barriers to trade in services. These include limitations on foreign investment in services, limits on number of foreign workers permitted, restrictions on remittances of salaries and profits of foreign establishments and so on.

The Indo-Lanka trade in services agreement under the CEPA will

result in the removal of certain barriers to trade in services between the two countries. The liberalisation of trade in services in the CEPA takes place according to a positive list, request-offer approach. Therefore, one country makes a request for liberalisation of a particular sector (for example liberalisation of all modes in construction services) in the other country. The liberalising country can then make a commitment according to its comfort levels - not necessarily acceding to the request. The IL CEPA also

FOUR MODES OF SERVICES SUPPLY:

Mode 1 (Cross border services) -

Where neither the consumer nor supplier of the service leaves their country (for instance, business process outsourcing, telemedicine)

Mode 2 (Consumption abroad) -

Where the consumer travels to the country of the supplier of services (travelling abroad to obtain education, health services or tourism)

Mode 3 (Commercial presence) -

Where the service supplier will establish through FDI in a foreign country (banks, hospitals, advertising firms)

Mode 4 (Movement of natural persons) -

Where individual service suppliers travel abroad on a temporary basis to work (doctors, accountants, IT professionals).

acknowledges the economic asymmetries between the two countries and full reciprocity from Sri Lanka is not expected.

What are the Export Opportunities under ILCEPA?

Given the slow progress of the WTO services negotiations, Sri Lanka stands to benefit from early access to the large and growing Indian services sector by engaging in the CEPA. As incomes increase at almost double digits annually, the demand for services will continue to expand in India. Furthermore, with economic growth wages in India have increased relative to those in Sri Lanka, and coupled with the effect of an appreciating Indian Rupee, services offered by Sri Lanka have become relatively competitive in the Indian market. Furthermore, access to the Indian market may



attract investment from 3rd parties into Sri Lanka, looking to export services to India through joint ventures with Sri Lankan firms.

In sectors such as accounting and book keeping, architecture, computer and related services, research and development services, travel agency and management consultancy, there is scope for export of services through mode 1 (and also mode 3). Such services are already supplied on a smaller scale to more developed nations therefore the potential is available. There are more sectors of potential when considering entering the Indian market through commercial presence. These include construction and engineering services, financial services (banking, insurance, leasing, and asset management), tourism and hospitality services. Many of these sectors have already seen Sri Lankan presence in India. Despite India strength in the IT sector certain Sri Lankan firms have been able to sell services in India (Interblocks sold internet banking solutions to Indian banks, Microimage provided Tamil SMS adoption to Airtel India). In tourism several major Sri Lankan firms such as John Keells and Jetwing have expressed interest in investing in the Indian

market whilst many smaller establishments have already been set up in Tamil Nadu. Sri Lanka construction industry too has recently shown interest in global ventures, particularly the Gulf market, therefore the potential exists to expand to India as well where construction is increasing at a rapid rate in both the residential and commercial markets.

.... And Import Opportunities?

Sri Lanka's services regime is largely liberal at the autonomous level. Therefore a commitment in the CEPA will legally lock-in the level of liberalisation committed to in the agreement (not necessarily the same as what is autonomously accorded). This will provide security and predictability to the investor - an important factor in terms of attracting investment to the country. In the past, increased foreign participation in Sri Lanka's services markets has had wide ranging benefits for business, consumers and overall economic efficiency. Examples of this include telecommunications and finance, where liberalisation resulting in competition led to significant improvements in service delivery, technology, consumer choice and prices. Similarly, Sri

Lanka stands to gain through increased foreign participation in sectors such as construction, higher education and health. An overall increase in competition in services that are inputs to business such as IT services, accountancy, marketing and distribution will help reduce costs of production and improve access to quality and skills. This applies to mode 4 as well, where Sri Lanka could consider making commitments in areas where performance constraining skill shortages exist in the country. However, as stressed earlier, large scale liberalisation need not occur at once, and can take place according to the country's requirements and comfort levels.

Challenges Ahead

Despite the benefits of liberalising trade in services there remain concerns, particularly with regard to the Indo-Lanka CEPA. The biggest concern is the fear of flooding by Indian professionals and firms. However this fear is misplaced since under the positive list approach, services liberalization can be controlled to the extent one is comfortable with. Another issue is pertaining to regulation - where some of the Sri Lankan regulatory authorities require more capacity to effectively regulate the activities of professionals working in the country. It should also be noted that despite getting market access in the Indian market, certain Sri Lankan firms have had difficulties in terms of excessive bureaucratic delays and hidden regulations that have made commercial operation problematic. These issues will need to be dealt with effectively in the CEPA and it is in the interest of Sri Lankan service suppliers to highlight such concerns to the relevant government authority engaging in negotiations.

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www.ips.lk

For more information please contact Tharanga Gunasekera Marketing Manager Coporate Banking on 0773633442 or email tharangagunasekera@hsbc.com.lk or visit our website www.hsbc.lk