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POLICY INSIGHTS

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BARRIERS BEYOND TARIFFS: SRI LANKA'S EXPORTS TO CHINA

Sri Lanka's forthcoming FTA with China has the potential to become the biggest bilateral trade deal for Sri Lanka in view of China's population and status as the world's second largest economy after the USA. Moreover, China is already Sri Lanka's second largest trading partner and second most significant source of imports.

The '*Study Group of China–Sri Lanka Free Trade Agreement*' identifies 9 potential products which would stand to benefit from a FTA with China. According to the feasibility estimates, liberalization of imports by China will increase exports from Sri Lanka by 30-112 per cent depending on the product in question. A study by IPS identifies 297 products with high trade potential to China; these products are currently not exported by Sri Lanka but are imported by China from elsewhere in the world, presenting new market opportunities for Sri Lankan exporters. Hence, tariff reductions under a FTA are expected to result in expansion of bilateral trade.

However, when tariffs are brought down through FTA negotiations, non-tariff measures (NTMs) can reduce the utilization of FTAs if they are not effectively dealt with. As experienced under the Indo-Lanka Free Trade Agreement (ILFTA), many Sri Lankan exporters have faced a multitude of difficulties in entering the Indian market due to the prevalence of NTMs – such as state taxes, standards, and administrative procedures, quotas, etc. – which were outside the scope of the Agreement. Hence, NTMs should be identified at the onset of trade negotiations and addressed along with tariff reductions/eliminations for FTAs to deliver the desired benefits.

In light of this, IPS conducted a study on '*Exporter's Perspective on Accessing Chinese Market under China-Sri Lanka FTA*' to identify constraints faced by Sri Lankan businesses in accessing the Chinese market including non-tariff measures, with the aim of providing recommendations for on-going FTA negotiations with China.

Methodology

The study focused on the sectors identified by the Joint-Feasibility Study as sectors with high trade potential; namely Tea, Textile and Clothing, Fish and Fisheries Products, Rubber and Rubber Products, Gems and Jewellery, Fruits and Vegetables, Coconut, and Machinery and Electronics. A total of 42 Key Informant Interviews (KIIs) were conducted covering a range of stakeholders including; exporters to China, Exporter Associations representing Sri Lanka's major export sectors to China, officials from Department of Commerce of Sri Lanka, Sri Lanka Standards Institute, Sri Lanka Tea Board and Export Development Board of Sri Lanka etc.

The findings from the KIIs were complemented by an analysis of NTMs through the World Bank WITS database.

Accessing The Chinese Market: Tariff And Non-tariff Measures

Both tariff and non-tariff measures are encountered by Sri Lankan companies when exporting to the Chinese market. Generally speaking, non-tariff measures seem to be more challenging than tariff barriers for agricultural exports, while the opposite is true for industrial exports.

NTMs are policy measures other than tariffs that can impact trade flows and include technical and non-technical measures affecting both imports and exports (Table 1). If NTMs are imposed by countries excessively beyond the specified measures to restrict imports from other countries, then they can be considered a Non-Tariff Barrier (NTB).

Challenges Faced By Agricultural Exporters To China

Agricultural exports (tea, fish and fisheries and fruits and vegetables) covered in the study are mostly burdened by NTMs, compared to tariffs (Table 2). The commonly cited problems faced by agricultural exporters to China are related to technical measures:

- High sanitary and phytosanitary (SPS) requirements compared to other export markets
- Lack of mutual recognition of standards and certificates
- Issues relating to quarantine and testing/certification
- Lack of transparency with regard to the food safety regulations
- Greater frequency of test reports and the levels/limits required in China compared to any other markets
- Lack of necessary testing facilities in Sri Lanka to meet testing and certification requirements applicable in China

Table 1: NTM Classification by Chapter

Imports		
Technical Measures	A -	Sanitary and Phytosanitary Measures
	B -	Technical Barriers to Trade
	C -	Pre-shipment Inspection and Other Formalities
Non-Technical Measure	D -	Contingent Trade-Protective measures
	E -	Non-automatic Licensing, Quotas, Prohibitions and Quantity Control Measures other than for SPS or TBT Reasons
	F -	Price-control Measures, including Additional Taxes and Charges
	G -	Finance Measures
	H -	Measures Affecting Competition
	I -	Trade-Related Investment Measures
	J -	Distribution Restrictions
	K -	Restrictions on Post-Sales Services
	L -	Subsidies M - Government Procurement Restrictions
	N -	Intellectual Property
	O -	Rules of Origin
Exports	P -	Export-Related Measures

Source:UNCTAD.

Table 2: Constraints Faced Accessing the Chinese Market

	Sector	Technical Measures: SPS	Technical Measures: TBT	Pre-shipment Inspection & Other Formalities	Non-technical Measures	Prevalence of High Tariff Barriers	Other
Agriculture	Tea	√	√		√		
	Fish & Fisheries	√	√		√		
	Fruits & Vegetables	√	√				√
Non-agricultural	Rubber & Rubber Products					√	√
	Textiles & Apparel		√			√	√
	Gems & Jewellery					√	

For example, tea exports to China are subjected to rare-earth content testing, which is unique to China and not a requirement in other export markets. Moreover, the exact particulars of this standard are not clear to the exporter. It is also revealed that testing for rare-earth content is problematic as the available testing facilities in Sri Lanka are insufficient. The current laboratories can only specify if rare-earth content is present or not in tea, but the levels of rare-earth cannot be determined as *per se* Chinese requirements. Moreover, China does not recognize testing and certificates issued by Sri Lanka, while testing in China is considered to be time-consuming and complex by exporters.

In the case of fish exports, while other markets require shrimp exporters to obtain an antibiotic test report for one pond in a shrimp farm, antibiotic reports for China have to be provided for each and every pond in a farm. Meanwhile, obtaining quarantine requirements for exports of fruits and vegetables are stated to be extremely cumbersome and time-consuming, involving a lengthy government approval process. For example, it took Sri Lanka nearly three years to obtain quarantine certification to export bananas to a few ports in China. It is important to note that the interviews revealed that tariffs were less problematic compared to meeting NTMs when exporting to China.

Challenges Faced By Industrial Exporters To China

In comparison to agricultural exports, tariffs are reported to be more challenging for industrial exporters covered in the study (textile and apparel products, rubber and rubber products and gems and jewellery).

Currently, China provides duty free access under several FTAs to a number of countries which Sri Lanka directly competes. For example, textiles and apparels are subject to an MFN rate of 16% when entering the Chinese market, while under the China-ASEAN FTA, imports from Indonesia, Malaysia, Philippines, Cambodia, Myanmar, Vietnam and Thailand have duty free access to China. Although Sri Lanka has preferential access to the Chinese market under the Asia Pacific Trade Agreement (APTA), the margin of preference offered does not provide a competitive advantage to Sri Lankan exporters. Rubber and rubber products are subjected to duties ranging from 15-30%, similar to gems and jewellery (0-5% on gems, 10.75% on base metals, and 17.5-30% on jewellery) compared to duty-free access provided by China to ASEAN members.

According to the interviews with industrial exporters to China, highlighted NTMs related mainly to the textile and apparel sector and specifically to China-specific testing requirements, and lack of necessary facilities in Sri Lanka to undertake China-specific tests.

Although testing standards of apparel and textile of China are mostly in par with EU and USA standards, China independently tests garments at two points: port of entry and the market. This particular test is called China testing or GB testing (GB stands for *Guobiao* in Chinese or National Standard). SGS (world's leading inspection, verification, testing and certification company) performs this test according to China's National General Safety Technical Code for Textile Products, also known as GB 18401. The code ensures product quality and safety and applies to apparel, decorative and home textiles, which are produced and/or sold in Chinese market. Random method of GB testing has caused high degree of uncertainty among garment exporters to China since the entire consignment can be recalled or fined at the market even if it is cleared at the point of entry. Fines charged and penalties imposed for any non-compliant product are extremely high and a number of such incidences have been reported in the recent past.

Another cause of concern is the requisition of more detailed test reports for textile and garment imports compared to other markets For instance, it is mandatory to provide a composition test report to China even for 100% cotton fabric, whereas EU and USA only need this particular test carried out for blended/ mixed fabrics. This requirement in turn results in higher costs of testing compared to other export markets. Nonetheless, tariff barriers were perceived to be high across industrial products as the margin of preferences offered under APTA is limited and do not provide a competitive advantage to Sri Lanka compared to its ASEAN competitors

Recommendations For Negotiations

Sri Lankan exporters face both tariff barriers and non-tariff measures when entering the Chinese market. A FTA, which does not address NTMs, may not be sufficient in delivering the expected trade gains for Sri Lanka. Therefore, it is imperative for China-Sri Lanka trade negotiations to simultaneously address both tariff barriers and NTMs. Given that the agreement with China is going to be a comprehensive one, SPS/TBT issues will be taken into account during the negotiations. Some of the key issues to figure in negotiations, include but are not limited to;

- Addressing NTMs in addition to tariff concessions as a priority
- Striking Mutual Recognition Agreements (MRAs) on standards
- Setting up Chinese accredited testing laboratories in Sri Lanka
- Enhancing capacities and efficiencies of testing laboratories in the country which China may consider assisting under the umbrella of economic and technical cooperation
- Ensuring the availability of all trade-related documents/ regulations/ information in English
- Strengthening relationships/co-ordination with related Chinese state authorities

This Policy Insight is based on findings from the IPS study, "Exporters' Perceptions on Accessing the Chinese Market under China-Sri Lanka FTA" by researchers, Janaka Wijayasiri, Dharshani Premaratne, Nipuni Perera.

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