

Importance of FTAs for Market Access and Development

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FTAs Galore

- FTAs became popular due to two reasons: (a) multilateral trade liberalization as determined by the WTO coming to a standstill; and (b) some of the large regional groupings with regional trade agreements (RTAs) finding it difficult to come to an agreement on the speed of liberalization
- The WTO website shows that the number of regional trade agreements now amount to 387 out of which 90% came into operation after the late 1990s
- More than 35% of the global trade now flows via RTAs

Key Advantages

- More market access to exports
- A smaller country can reap economies of scale and thereby improve competitiveness of exports
- Diversification of export market without relying too much on a few markets
- Giving the best deal to the consumers from cheaper imports that are not produced in the domestic market
- Ability to protect production sectors that should not face competition through a negative list

More on Advantages

- Easier to reach an agreement when negotiations are confined to two parties
- Dispute settlement also becomes easier when it is among two parties
- An FTA can trigger better trade facilitation and other trade-related reforms in both partner countries
- More trade can trigger investment flows between the two countries
- FTAs can assist getting linked to supply chains that are key components of modern large scale production networks

Wrong Approaches to FTAs

- Myth1: “That the sole objective of an FTA should be to reduce the trade deficit between the two countries” – this is outdated thinking. The objective of the FTA should be to give the best deal to both producers and consumers of the two countries and work out a “win-win” situation. In this process, there is a possibility of the trade deficit sometimes widening between the two countries
- Myth2: “In a FTA between a large and a small country, the permanent beneficiary will be the big country” -- not the case. In such FTAs, Special and Differential Treatment (SDT) is build in favour of the smaller country in the FTA to ensure that the smaller country gains while it operates at its comfort level in the FTA

What is Special & Differential Treatment ?

- Larger Negative List for the smaller country
- More duty free openings at the start of the FTA by the larger country
- Longer tariff phasing out period for the smaller country
- More favourable rules of origin for the smaller country
- Large revenue earning import sectors for the small country may be kept in the negative list
- Etc.

Concerns on Market Access

- Non-tariff barriers can dilute better market access with low tariffs
- Smaller country will not have the supply capacity to fully exploit the advantages of preferential tariffs
- Market intelligence for new products in demand which are exportable may be lacking
- Rules of origin can be misused by free riders to gain market access

Addressing Market Access Issues

- The removal of NTBs should be automatic with the tariff preferences and should be a binding commitment
- Go for joint ventures with buy-back arrangements to overcome supply constraints, if immediate increasing of supply capacity is problematic
- Have Sri Lankan embassies with market intelligence experts/professionals so that they could sensitize local chambers on market niches, demand patterns, etc.
- Have close monitoring of under invoicing of imports for fulfillment of rules of origin, so that the fly-by-night investors do not exploit the FTA and give it a bad name

Safeguarding Local Industries

- Negative list can be prepared with due consultation with the industries/agriculture
- Protection and revenue may govern the preparation of the negative list
- It will be prudent to get the anti-dumping legislation in place before embarking on the FTA with China given the fact that there has been special emphasis on some import substitution industries

Opening up to the Partner

- Cheap machinery, vital inputs to production, etc., could be part of the duty free list for importation from the partner country
- Such imports can increase the competitiveness of our exports as well as import substitutes to compete more effectively in the global and domestic markets, respectively
- Consumer durables not produced in Sri Lanka should be encouraged at a lower duty to give the best deal to the consumers

Regulatory Framework of the FTA

- Working out SDT with the liberalization list, negative list, ROO, etc.
- FTA design should be to maximize trade creation and minimize trade diversion and basically create new trade
- Dispute Settlement Mechanism with equal representation from both parties and working with simple majority decision
- Nodal points with Chambers of both countries (Department of Commerce in both countries will be the official focal points) for ironing out problems that emerge from time to time
- Anti-dumping legislation in Sri Lanka must come back to the discussion forum

FTA and Development

- Once market access issues, safeguarding local industries, and regulatory framework are sorted out, an FTA can be an important contributor to enhance production and consumer welfare and thereby contribute to the overall economic development of a country
- This contribution comes in the form of expanding export industries, more FDI, more retail outlets for import trading, etc., which in turn create more jobs and better living standards

From FTAs to CEPAs

- To gain more from FTAs, they need to expand to cover trade in services and investment flows, then the FTAs become Comprehensive Economic Partnerships (CEPAs)
- CEPAs can be deepened by adding procurement policies, competition, intellectual property rights, etc., but this happens when both parties are fairly confident and trust each other in economic transactions
- The higher trade and investment impact on the domestic economy by a CEPA makes it an important component of a development strategy in a number of developing countries in the world

- Thank you