

Session 8 – Simple analytical method for identifying an offensive I when negotiating an FTA: An example of Sri Lanka-China FTA negotiations

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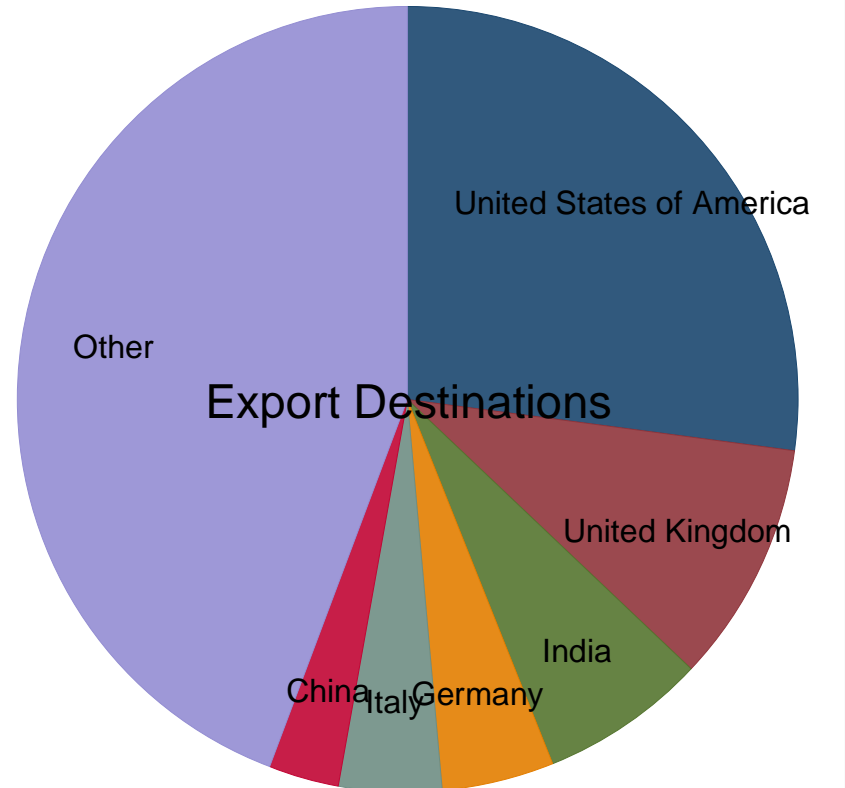
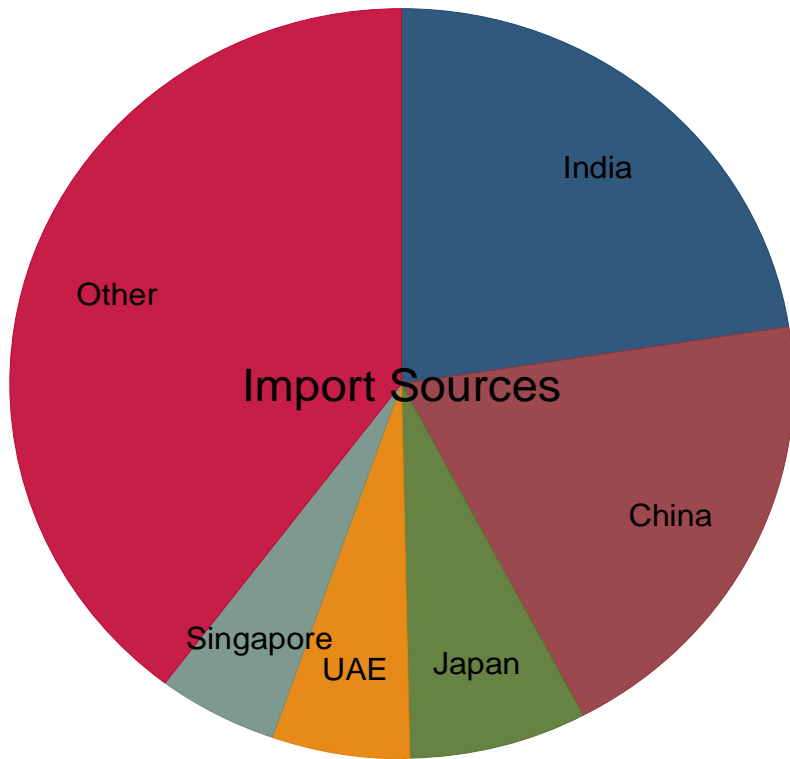
The “offensive list”

- Products are then included on the offensive list if they satisfy the following criteria if they are:
 - (i) imported by China,
 - (ii) produced by Sri Lanka with the capacity for expansion,
 - (iii) Sri Lanka must have comparative advantage in the product, and
 - (iv) China must already have a tariff on the product.

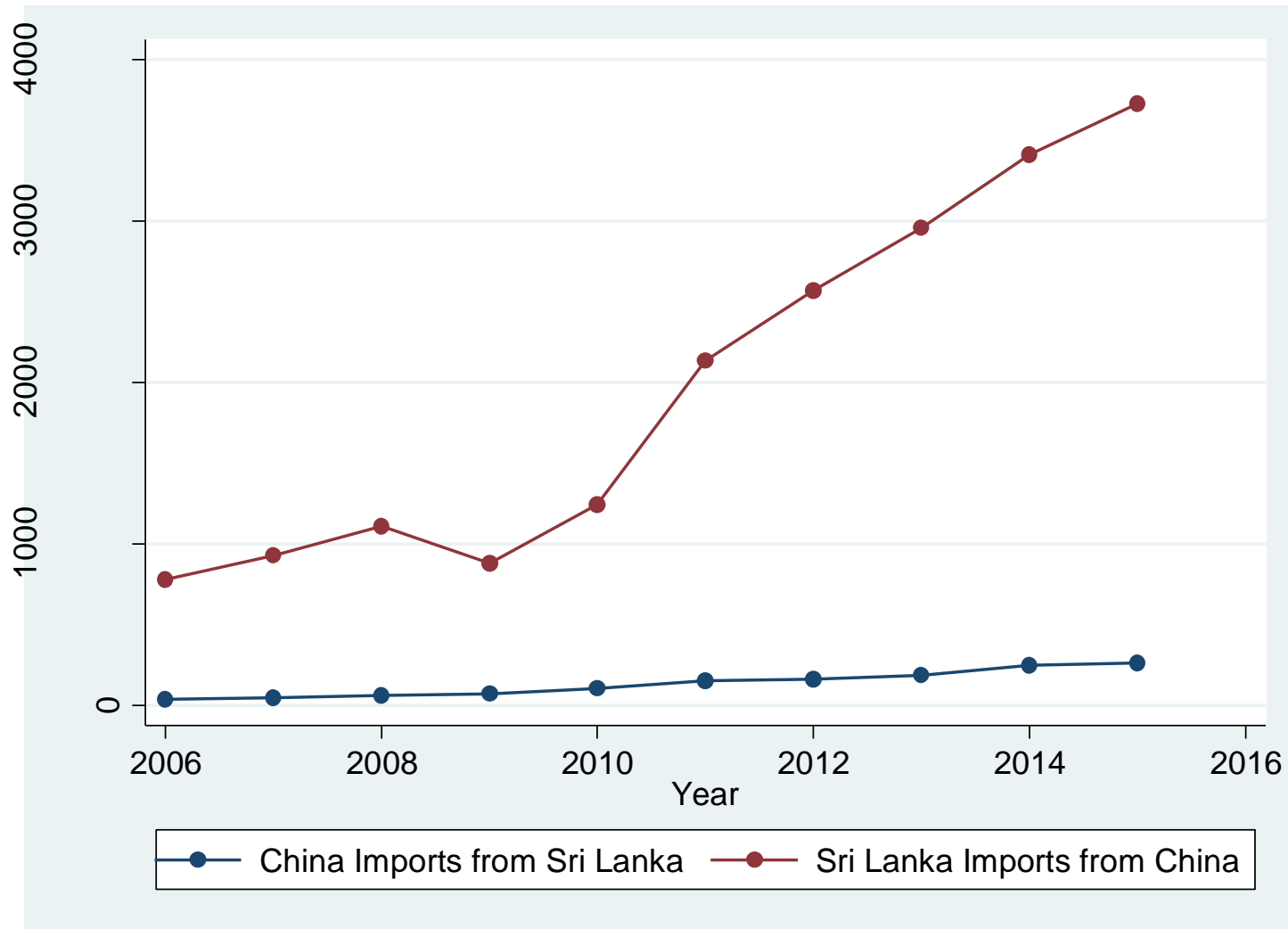
Key Findings

- Key findings from this analysis are that Sri Lanka's key offensive interests lie mainly in their biggest global exports (including tea, coconut products, rubber products and textiles), with the main exceptions being important exports which do not currently face a Chinese tariff. However, many of the products on the offensive list are not currently exported to China, but are included because there is potential for bilateral trade expansion here.

Trade Statistics

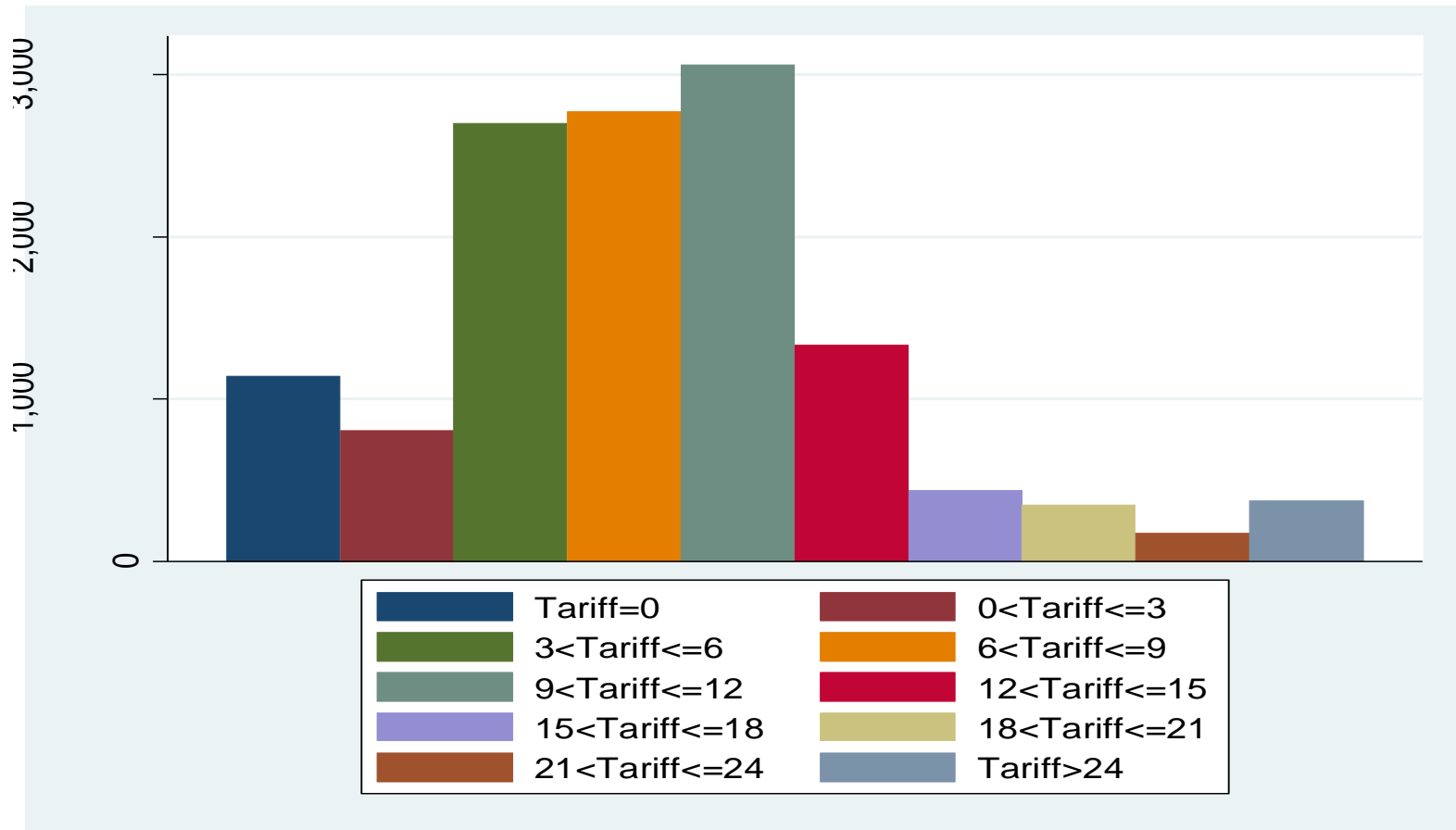


Bilateral Imports and Exports 2006-2015



- The key result from this analysis is that tariff free exports for all 439 goods on the offensive list would increase Sri Lankan exports of these goods to China by 69%. As these goods form the bulk of Sri Lanka's bilateral exports, this would also account for a 58% increase in total Sri Lankan exports to China.

Chinese Tariff Rates Under APTA at 10 Digit Tariff Line



Source: International Trade Centre (2016) Market Access Map tool. All data is for tariffs in 2015. Calculations carried out by authors. Tariff rates are ad valorem equivalents; for the vast majority of categories, this is identical to the simple tariff

A Summary of Free Trade Agreements to Date

- To date, Sri Lanka has signed 4 Preferential Trade Agreements (PTAs). These are the Asia-Pacific Trade Agreement (APTA, a partial scope agreement), the South Asian Free Trade Area (SAFTA), the India-Sri Lanka Free Trade Agreement (ISFTA) and the Pakistan-Sri Lanka Free Trade Agreement (PSFTA).
- China is an important player in the recent proliferation of Free Trade agreements, and has signed a full 13 FTAs to date. Partner countries are Australia, the Republic of Korea, Switzerland, Iceland, Costa Rica, Peru, Singapore, New Zealand, Chile, Pakistan, ASEAN, Hong Kong, China and Macao, China

Chinese Trade Agreements

- Common defensive list items include various grains (wheat and maize), rice, sugar, wool, oils, wood and paper products, motorcars, film, and textile products.
- One consequence of these Chinese FTAs is the possibility of trade diversion should Sri Lanka not sign its own FTA with China; several countries, many of which share similar industries with Sri Lanka, have duty free access to the Chinese market. Further, developing countries in the region, for example Myanmar – a developing country - enjoy preferential rates through the Chinese duty-free, quota-free (DFQF) programme. In contrast, Sri Lanka's access to the Chinese market is only a limited number of items and the APTA preferential rates are only partial reduction on the WTO Most Favoured Nation (MFN) tariff levels and not duty free.

How the Offensive List is Calculated

- The product must be one which China imports
- The product must be one which Sri Lanka produces
- The product must be one which Sri Lanka has the capacity to increase exports
- China must currently have a tariff on the product
- The product must be one in which Sri Lanka has demonstrated comparative advantage bilaterally or generally

The criteria

- The length of the list will differ depending on how the criteria are applied. For example, one set of criteria could be that China has imported some amount in the last 3 years, that Sri Lanka has exported at least \$1m to the world in the last 3 years, that Sri Lanka has revealed comparative advantage, and that China has a tariff of greater than 5%. This would produce a different list compared to a different set of criteria (for example, changing the final criterion to a tariff of greater than 10% would shorten the list).

The product must be one which China imports

- Only products which China has imported from anywhere in the world in 2013, 2014 or 2015 are included in the data for this analysis.
- *Criterion: China must have imported at least 1 million USD of the product in at least one of 2013, 2014 or 2015*

The product must be one which Sri Lanka produces

- *Criterion: Sri Lanka must have exported some amount of the product to the world in 2013-15*

The product must be one which Sri Lanka has the capacity to increase exports

- *Criterion: Sri Lanka must have exported at least 1m USD of the product to the world in at least one of 2013, 2014 or 2015*

China must currently have a tariff on the product

- Some of Sri Lanka's largest bilateral (to China) export categories have tariff-free access to China currently, for example 'Zirconium ores and concentrates' (HS code 26151000), and 'Titanium ores & concentrates' (HS code 26140000) Sri Lanka's 7th and 10th biggest exports to China in 2015 respectively. Thus whilst these products are of vital importance to Sri Lanka's bilateral trade with China, they are excluded from the offensive list for this purpose.
- *Criterion: China must currently apply a tariff on the product for Sri Lankan exporters*

The product must be one in which Sri Lanka has demonstrated comparative advantage bilaterally or generally

- Bilateral Revealed Comparative Advantage (*BRCA*) and Standard Revealed Comparative Advantage (*SRCA*)
- *Criterion: Sri Lanka must show BRCA or SRCA for the product, or the tariff for the product must be greater than the mean amount*

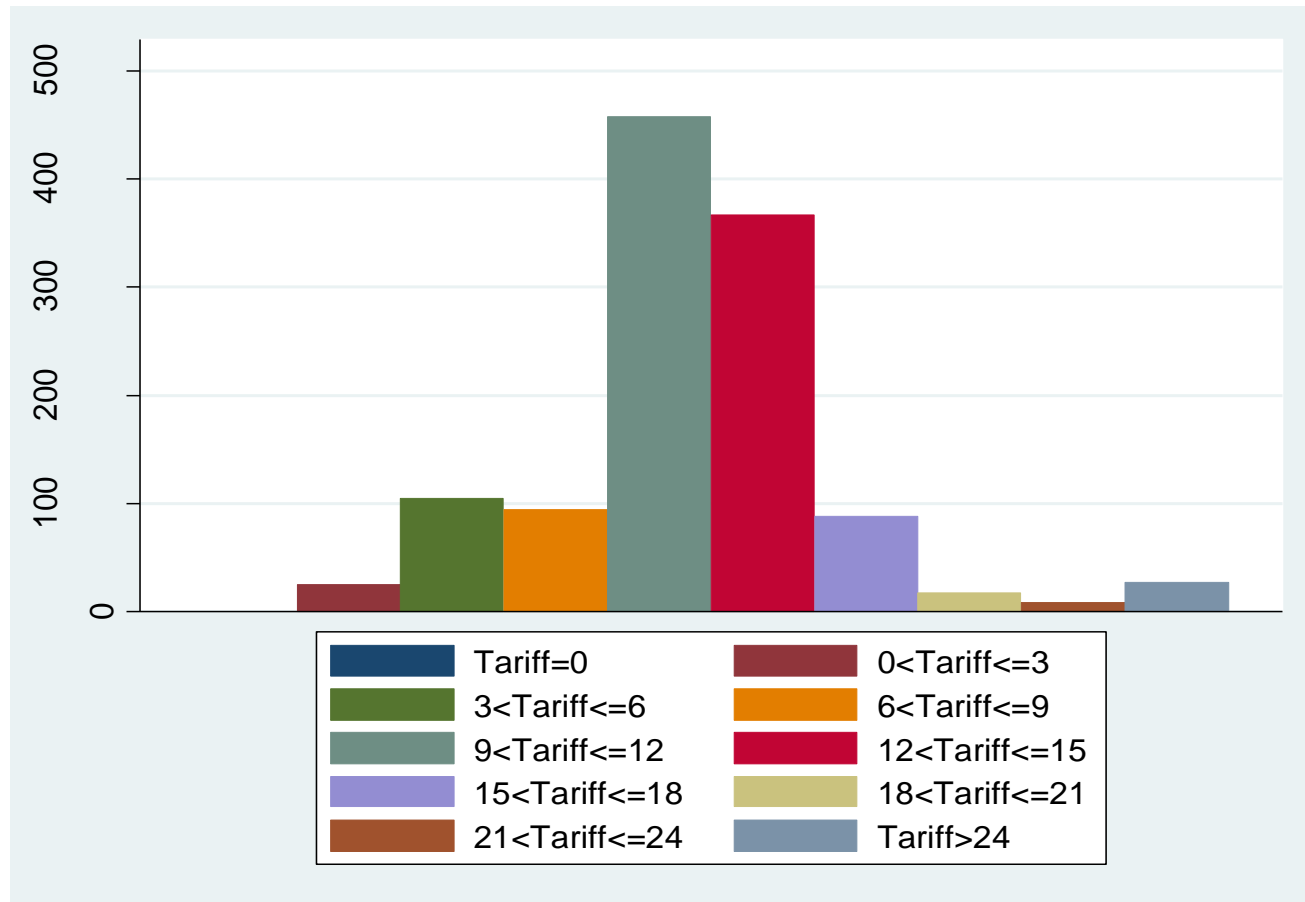
Further Analysis

- *Importance = Standardised Bilateral Exports to China * (Standardised Tariff + Standardised Standard Revealed Comparative Advantage)*
- Further, a simple economic analysis is carried out for each product on the list regarding whether China is likely to act in a defensive manner
- China seems willing to liberalise tariffs on goods for which there is a significant domestic industry, but in which the partner country has limited or no domestic capacity. For example, while China usually retains tariffs on tobacco products, it has liberalised these products in its bilateral FTAs with Chile and New Zealand, both of which countries export no tobacco products to China, and limited values worldwide..

Chinese Defensive list

- To be considered as a defensive Chinese interest, a product must satisfy the following two conditions:
 - Exports of the product from China to the world are in the top 75% of Chinese export values. This proxies for domestic production
 - The value of bilateral exports from Sri Lanka to China is over 10% of the total value of Chinese exports for that good. This proxies for the threat Sri Lankan imports pose to Chinese production

Chinese Tariff Rates Under APTA at 10 Digit Tariff Line for Offensive List Goods



Source: International Trade Centre (2016) Market Access Map tool. All data is for tariffs in 2015. Calculations carried out by authors. Tariff rates are ad valorem equivalents; for the vast majority of categories, this is identical to the simple tariff

SMART Analysis of the Effect of this PTA

- Much of the total increase in trade under Chinese liberalisation is expected to come from trade diversion, in which Sri Lankan exports displace exports to China from other countries. This is particularly the case for clothing and rubber products, though it is less true for tea and coconut products. However, one should note that many countries, particularly in the Asia-Pacific region, currently have preferential access to the Chinese market due to their having signed bilateral FTAs with China, or preferential rates through the Chinese duty-free, quota-free (DFQF) programme. Hence much of this trade diversion may result from Sri Lanka regaining access to a level playing field, rather than being due to Sri Lanka receiving an unfair advantage.

Input output analysis

- Of the 30 most important products on the offensive list, 5 are raw materials, 7 are intermediate goods, 18 are consumer goods, and only 1 is a capital good