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Inclusive Trade Policies: What went wrong  
with the Indo-Lanka CEPA?

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# **Inclusive Trade Policies: What Went Wrong with the Indo-Lanka CEPA?**

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# Outline

- Background to the IL-CEPA
- Rationale of the Agreement
- Structure of the Agreement
- Role of Stakeholders in preparation of SL's Commitments
- Constraints to Liberalisation of trade in services
- Balancing the Benefits and Challenges of Liberalisation
- Challenges of Liberalising trade in services
- Dilemmas of the extent of stakeholder transparency
- Conclusions

# Background

- India-SL growing economic integration in the 1990s culminated by signing of the FTA in 1998
- Strong performance in terms of aggregate trade growth and associated investment flows
- Joint Study Group Appointed to examine potential for deepening economic integration
- Proposal to implement a Comprehensive Economic Partnership Agreement (CEPA) in 2003
- Negotiations began in February 2005 and continued for over 3 years until July 2008
- After finalising draft commitments and the framework agreement – CEPA was taken off the table in the wake of vocal domestic opposition to the Agreement in Sri Lanka.

# Rationale of the Agreement

- Rapid growth of services sector in India along with general economic growth
- Increasing costs of FoP in India meant that SL services were increasingly competitive
- Several sectors in Sri Lanka with potential – tourism, accounting, maritime services, IT related services, construction
- SL also hoped to attract 3<sup>rd</sup> party investment looking to enter the Indian market
- Importance of securing market access when political-economy conditions were conducive
- Import of services could be enhanced through more transparent investment regime

# Structure of the Agreement

- Positive list, request-offer approach, sequential liberalisation
- Asymmetries of the two economies considered
- Sri Lanka allowed to maintain a great deal of flexibility in the liberalisation of services
- Such safeguards required due to Sri Lankan stakeholder perceived concerns, largely related to India's size
- The same issues dominated the debate on the IL-FTA
- Flood of goods/services, lower labour standards in India, subsidies, NTBs and red tape issues for exports
- Fresh issues such as regulating services

# Role of Stakeholders in Sri Lanka's Commitments

- India's requests covered almost all sectors in the UN CPC list
- SL negotiators worked in partnership with business chambers and Indian requests were shared amongst the chamber members
- Industry views on feasibility and extent of liberalisation, required safeguards and export interests were sought
- Consumer interests were not cohesively represented in SL
- Overall defensive stance of the service sector in SL with regard to the CEPA
- Several sectors could not be liberalised at all due to stakeholder concerns
- Accountancy, engineering, construction and other business services
- Several reasons for this – legislative problems, regulatory issues and lack of domestic market maturity

# Constraints to Liberalisation – Regulatory and Legislative

- Legislative Issues – Construction Services Act had not been passed through parliament in SL, therefore reluctance to make international commitments without a finalised domestic legislative position
- Institute of Architects lacks the provision to register foreign architects and a commitment in CEPA would require a change to the domestic legislation
- Reluctance to make commitments in Mode 1 due to the lack of clarity in this area in domestic legislation
- Even in areas which are unilaterally open, commitments could not be made due to shortcomings in contemporary regulatory practices – eg. Mode 4 health services due to instances of under-qualified foreign doctors practicing in SL
- Another issue in mode 4 health services is the heterogeneity of qualification standards in India, and the regulatory burden this would place on SL regulators.



# Constraints to Liberalisation - Competition

- Flooding of Indian workers was a concern
- Many safeguards were incorporated to allay stakeholder concerns
- However the negotiations took place in an environment of uncertainty as a result of the teething problems in the FTA which diminished stakeholder confidence in the Agreements.
- Unilateral imposition of quotas on SL exports by India, Rules of Origin criteria which undermined market access for garments and tea, lack of reciprocation of SL extending visa on arrival to Indians (and the abuse thereof).
- All these factors contributed to reluctance by SL to liberalise mode 4.
- SL negotiators expected that at the early stages such apprehension is to be expected, but that this would diminish once confidence in the Agreement grew – allowing some liberalisation of mode 4 in an economically productive manner.

# Balancing the Benefits & Challenges of Liberalisation

- SL negotiators utilised the inherent flexibilities in the positive list approach to services to tailor liberalisation to SL's economic requirements.
- Health Services – India Requested full commitment in Mode 3 – also of benefit to SL in terms of access to health. Mode 3 commitment allowing investment outside the Western Province given economic priorities.
- In M1 India requested full commitment – which could have been beneficial to SL in terms of development of the health sector and access to services
- However stakeholder concern in regulating quality of remote health services therefore commitment in M1 allowed only doctor-doctor transactions
- Convention Services – India requested full commitment in Mode 3. Also of interest to SL due to the importance of the M.I.C.E market.
- But stakeholder concerns regarding domestic market maturity and size and therefore M3 commitment was made in JV form.
- Maritime services – Shortages of certain skills therefore limited commitment in mode 4.

# Challenges of Liberalisation of Services

- Short term labour shortages could be plugged with imported labour – but stakeholders were concerned that in the long run this may deter locals attempting to fill such positions if they are dominated by foreign labour.
- Debate over the incremental benefit of commitments in Mode 3 – particularly in the context of a weak investment climate and a liberal autonomous regime.
- Lack of data on services made it very difficult to analyse potential benefits and costs of liberalisation.

# Dilemmas of the Extent of Stakeholder Transparency

- SL negotiators took stakeholder concerns into careful account in drafting commitments in the CEPA. Evidence is the gulf between autonomous regime and draft commitments under CEPA.
- However the Agreement was not signed as scheduled at the 15<sup>th</sup> SAARC Summit due to domestic stakeholder concerns – captured by 3 primary concerns
  - 1) CEPA should not proceed until teething problems in the FTA are dealt with – but CEPA entails provision to have regular reviews.
  - 2) CEPA undermines SL's economic independence from India – this argument fails to account for the flexibilities provided in the Agreement
  - 3) Other than the services sector, the broader public was not aware of the Agreement details

# Dilemmas of the Extent of Stakeholder Transparency

- Third argument is the key
- Issue of timing – 1 month between conclusion of negotiations and the scheduled signing gave the impression of the whole process being rushed
- Negotiators were concerned about making the negotiations public until there was some finalisation – since this would have compromised the negotiating position.
- Alternative was to have gone ahead without public awareness – akin to the 1977 liberalisation and the 1998 ILFTA.
- This could be most effective when consumer interests are not clearly articulated and as a result the negatives will outweigh the positives in public debate.

# Conclusions

- The major concern amongst opponents to the CEPA was the lack of broader transparency.
- The Agreement may have stood a better chance if the Framework Agreement had been made public prior to the scheduled signature of the Agreement. SL government did not do so.
- However – the political climate at the time (mid 2008) was not conducive since the civil war in SL was at an intense phase and nationalist sentiment was at a high level
- In this context any Agreement that was perceived to undermine national interest would be opposed vociferously – particularly one with India.
- Given the on-going problems with the ILFTA (vanaspathi and copper issues) it was difficult for negotiators to sell the benefits of the ILFTA to the public
- In this environment it could be argued that greater stakeholder dialogue may not have had much effect
- CEPA still on the shelf – one and a half years after the standoff.

# Thank You

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