Advantages and disadvantages of sri lanka entering into free trade agreements

Sri Lanka is a known country for the trade during the ancient and medieval times. Its native high quality products such as Gem Stones, Ivory and Spices have gained popularity not only the neighboring countries like India, China & Persia (Present day Iran) but also in ancient Kingdoms such as Greek & Rome. Facts of Sri Lanka has mentioned in Greek and Roman writings dating from the third century BC by Kalisthenes, Oneskritus, Megasthenes, Strabo, and Pliny. Also Sri Lanka was included in the map of Asia, drawn in 150 AD by Ptolemy.

Ptolemy’s Map of Sri Lanka (Taprobane)

Location of Sri Lanka in the world map

Sri Lanka’s First trade Agreement In 1952 Sri Lanka entered into a Rubber-Rice barter agreement with China. Under this agreement 01 ton of Sri Lankan Rubber has exchanged to 06 tons of Chinese Rice Traditional Sri Lankan Export commodities

Sri Lanka’s traditional Exports were Tea, Rubber and Coconut products and after 1977 the Apparel industry too added to this. But, it is not viable any more to depend on these products in the long run due to the competition, trade barriers, high taxes, substitutes, political differences and recessions in countries etc. Therefore as the mission statement stated by the Department of Commerce of Sri Lanka “ To develop and Promote Sri Lanka’s foreign trade relations at bilateral, regional & multinational levels by the effective implementations of government trade policy, with a view to raising the standards of living and realizing a higher quality of life through the increase of total production, income & employment levels, thereby actively contributing to the overall economic growth of Sri Lanka" the future lies with trade agreements enter with the neighboring countries. The advantages and disadvantages of such trade agreements are as follows Advantages

* Chance to cater bigger markets The population of Sri Lanka is around 20 mn whereas India alone the population is 1210 mn. If we add up the total population of the SAARC region it exceeds 1. 7 billion which is nearly a ¼ of the world population. Hence it will be an immense market for Sri Lanka

* Economies of scale When production increases to cater to a bigger market the unit production cost comes down and it will help to increase the domestic living standards and to fight with other multinationals in the region

* Reduce the price level of commodities & services Reduction or the complete wipe out of taxes will help to dismantle the border protection of high tariff, expansion of exports, diversifying the export basket and reduce the prices * Reduce transport cost

Navel routes of Sri Lanka Due to the strategic geographical location of Sri Lanka it is a hub for Air & Sea transportation. Thus, the neighboring countries can use this facility to transfer their goods via Sri Lanka and it helps to generate more jobs & revenue

* Being an Island nation There are no borders of Sri Lanka. Therefore no political barriers for the neighboring countries to import their essentials through Sri Lanka. Especially like crude oil where the India and China as known as the energy thirsty economies and the countries surrounding them have political differences with them

* Establish trade links with growing economies According to recent IMF report India recorded the highest growth rate of 10. 4% in 2010. Also their imports grew by 21%. Hence the opportunities are there for Sri Lanka in long term basis to fulfill their requirements

* Chance to deviate from traditional exports As mentioned above the traditional exports of Sri Lanka (Tea, Rubber & Coconut) is declining and it can be replaced with new products and services like, Porcelain Table ware, Ceramic ware, furniture, edible oil (vanaspathi oil), canned food, Fruits & vegetables etc.

Disadvantages * Unemployment may occur due to removal of trade barriers Some companies may have to close down their businesses as they cannot cope with the low prices offered by the foreign companies from their economies of scale and efficiency

* Domestic economy may instabilize due to economic downturn of neighboring countries If a country in the trade agreement falls into a recession it will effect to all trading partners due to the failing of export income

* International markets are not level paying fields Countries with surplus products or services will try to dump it in other trading countries by hiding behind the rules of the trading agreement (edible oil named vanaspathi oil and pepper exports from Sri Lanka to India has almost demolished those two sectors in India and they had to intervene and put a volume cap to reduce the imports)

* Loss of foreign Exchange Since the Sri Lankan currency is weaker against the most countries in Asia, there is a exchange loss for Sri Lanka for the every import they made

* Loss of Tax revenue When the tariff removed from many products, it will result in revenue loss for Sri Lanka and to arrest that they have to increase the tax portion of other remaining products heavily (The tax for motor cars imported to Sri Lanka is almost 400%)

Conclusion Therefore as mentioned above there are advantages and disadvantages for entering into trade agreements and most disadvantages are due to the under developed economy of the country. Hence, before entering into any trading agreement Sri Lanka must clearly take necessary actions to protect the local businesses