

Executive Summary

The Industry Analysis

Based on the value chain analysis of upstream, midstream and downstream industrial sectors that can increase trade opportunities between Thailand and Sri Lanka if the FTA becomes effective, this study identifies results into two categories as follows;

1. Industries that Thailand might be benefited from the FTA

1.1 Industries that Thailand might be benefited throughout the value chain are; (1) **juice industry** which Sri Lanka sometimes has surplus in upstream supplies. Thai businesses may explore opportunities to invest in manufacturing upstream product or increase trade and export of downstream products to the Sri Lankan market; (2) **textile and apparel industry** which Sri Lanka only has tariffs on downstream products of textile and apparel industry

1.2 Industries that Thailand might be benefited from some stages of the value chain are; (1) **Jewelry and Gem Industry**, Thailand has high potential to produce and export of both the design and the body of jewelry on downstream. If Sri Lanka reduces the prevention of export on upstream products, Thailand may use the upstream products from Sri Lanka to support downstream production in Thailand. (2) **Machinery and Electrical Appliance Industry**, Thailand has the potential to export the products to Sri Lanka such as agricultural machinery (two-wheel tractor, paddy harvester, rice milling machine), household electrical appliances (refrigerators, air conditioners and radios) and industrial appliances (ie. electrical generators, battery and molding machines). (3) **Automotive industry**, products which Thailand has potential exports to Sri Lanka and could be benefited from the agreement are personal cars, trucks, motorcycles, automotive parts and motorcycle parts (4) **Metal Industry**, there are many products which Thailand has the potential to export to Sri Lanka and benefit from the agreements which currently the existing tariff rate are between 7.5% -25% and (5) **Processed food industry**, products which Thailand has the potential to export to Sri Lanka and benefit from FTA are aquatic products (powdered or pellets), fruits (fresh, chilled, frozen, dried and ground), fish meal and canned fish.

2. Industries which Thailand maybe affected from the FTA

Industries which Thailand maybe affected from Thai-Sri Lanka FTA by some stages of the value chain are; (1) **Industrial and Electrical Machinery** included electrical transformer, accumulator, steam turbine for electric generator and parts of circuit board (2) **Automotive Industry**, only one product that could be affected by Sri Lanka's exports is concrete trucks,

which Thailand currently maintains high tariff rate at 40%. (3) **Metal Industry**, products which Thailand maybe affected are copper brass and nickel pipes, stone drilling machine (4) **Tea Industry**, Sri Lanka has strong upstream industry in terms of quantity and quality of tea. However, downstream production and packaging are still primary. Hence, Thailand has potential to invest in packaging or importing upstream products and transform into ready-to-drink tea for distribution and export (5) **Processed food industry**, subsectors that might be affected from imports are such as aquatic (fresh, chilled, frozen and crushed), wheat and flour products (sweet biscuits), fresh coconut, spices (cinnamon, cumin) and palm hearts.

Trade and Investment Policies, Rules and Regulations

Sri Lanka is quite open when it comes to promoting direct investment. Foreign shareholding is allowed up to 100 percent in most businesses. This study will highlight important rules and regulations with regard to foreign investments and trade in services in Sri Lanka.

Investment Rules and Policies

The Investment Promotion Laws. The Sri Lankan Board of Investment (BOI) is responsible for issuing and updating investment policy. The BOI's authority is based on the BOI Act. The establishment of businesses under the BOI Act can be categorized in 3 groups, which are general investments, BOI promoted investments, and investments that support the national development strategy.

The Investment Promotion Measures of Sri Lanka can be grouped in 2 categories which are Tax Incentive Measures and Non-tax Measures. Tax Incentives include Tax Holiday measures (Temporary Corporate Tax Exemption), Dividend Withholding Tax Measure, Import Duty Exemption and Fiscal Stability Agreement. Non-tax measures are such as long-term land lease to foreign investors can be extended up to 99 years. Moreover, Sri Lanka also relax other rules and regulations to attract foreign investment such as land ownership, international remittance, machineries imports, government procurement, and trade competitiveness policy.

Services Rules and Regulations

Regulations that limit Trade in Services in Sri Lanka are categorized in 3 groups which are (1) businesses which require permission from government or specific authority such as Air transport services, coastal transport services and lottery, (2) businesses which may allow foreign equity up to 40 percent or higher if permitted by the BOI are such as transport of goods, education, telecommunication services, travel guide services and shipping agency services, (3) businesses that do not allow foreign investment such as security, retailing services

(less than 1 million US dollar) lending services and pawn shops. This study compiles rules and regulations of Sri Lanka related to trade in services focusing on 3 services sectors which are (1) Transport Services that includes maritime transport services, rail and road transport services and air transport services; (2) Tourism and Travel Services that the government of Sri Lanka has been promoting by allowing Visa on Arrival for Asian tourist; (3) Telecommunication services which is fully liberalized and being regulated by the Telecommunications Regulatory Commission of Sri Lanka (TRCSL). The study also highlights that transport services and tourism and travel services are 2 services sector that Thailand is more competitive but Sri Lanka still does not allow 100% foreign equity.

Services Sector

This Chapter provides studies on the potential area for trade in services liberalization negotiation as well as recommended measures to be undertaken in 5 trade in services sub-sectors including (1) Travel (2) Construction (3) Transportation (4) Wholesale and retail and (5) Business services. The recommendations are based on the 4 modes of supply as provided in GATS' definition, which are (1) Mode 1: Cross Border Supply (2) Mode 2: Consumption Abroad (3) Mode 3: Commercial Presence and (4) Mode 4: Presence of Natural Persons. The study also underlines the fact that that Mode 1 and Mode 2 in services are difficult to regulate because of its cross-border nature, Mode 3 implementation must comply with domestic regulation of the country, and Mode 4, especially skilled workers and experts, involves laws related to alien and professional workforce.

As a result of the study in each services sub-sector, the researchers recommended the Thai negotiation team to request Sri Lanka to further liberalize services sector beyond GATS commitments (GATS Plus) in Mode 1, Mode 2 and Mode 3. Since Sri Lanka has already made GATS Plus commitments in other FTAs, it is possible to negotiate in some sub sectors which Thailand has stronger competitiveness such as financial service, transportation and other sectors. This will support and facilitate Thai businesses in trading and other investment in Sri Lanka. Regarding Mode 4, most Thai workers have stronger competitiveness than Sri Lankans, while basic wage in Sri Lanka is lower than that of Thailand. Therefore, Thai investors in Sri Lanka can gain advantage of the lower wage cost by mainly using local Sri Lankan workforce and import only skilled labor or professionals from Thailand for strategic planning or solving problems on occasional basis. In addition, although BOI of Sri Lanka allows foreign workers to work in Sri Lanka, it is still unclear about related legalities. Therefore, there is a merit for negotiation on Mode 4 with Sri Lanka to improve clarity and confidence for Thai investors in the future.

Regarding the horizontal commitment for Thailand in the Schedule of Commitments, Thailand should clearly specify that all businesses establishment must comply with the Foreign Business Act B.E. 2542.

Regarding Mode 1 and Mode 2, the report recommends Thailand to focus on the importance of securing national safety or security when making any commitment on Mode 1.

For Mode 3, the study highlights that Sri Lanka allows 100% of foreign ownership in most service sectors, which benefits Thai investors whom are more competitive when comparing to Sri Lankan businesses. As a result, Thai investors are highly likely to invest in Sri Lanka more than Sri Lankan investors do in Thailand. Therefore, the researchers suggest “Unbound” or “None other than that indicated in the horizontal section” in the commitments except for sectors which Sri Lanka has not liberalized to other parties such as Transportation, auction house and vending machine. Furthermore, there is a suggestion to negotiate Sri Lanka to further liberalize in sectors such as transportation to prepare for the future strategic planning on using Sri Lanka as the gateway for Thailand to access to markets in South Asia.

Investment Sector

From the Trade in Goods part, it has pointed out many industries in which both Thailand and Sri Lanka has a good potential to invest in. However, there are 5 industries that were chosen as target industries for an in-depth analysis. These 5 industries are Processed food, Beverages, Textile and Garment, Gem and Jewelry, and Electricals. However, in some of the industries such as electrical industry, Sri Lanka still lack basic infrastructure and backing industries to support the investment therefore, the investment outlook in this industry is still low. However, the industries that Thailand has high investment potential in Sri Lanka and should be prioritize in the “Positive list” are Processed food, Beverages, Textile and Garment and Gems and Jewelry.

Negotiation Suggestion

Thailand should use Sri Lanka as platform to connect to other South Asia countries which have to further negotiation for services and investment sectors.

Tax Reduction Suggestion

1. Normal Track.

- (1) Products which Thailand may increase export to Sri Lanka include wood, automotive, plastic, industrial and electrical machinery, metal and sugar.
- (2) Products which Thailand may not be affected include leather, shoes, apparel, stones, ceramic products, glass, fat, oil, chemical products, ores, watch, medical equipment, musical instruments, arts and antiques.
- (3) Products which have investment potential in both Thailand and Sri Lanka include rubber, plant products, fishery products and processed or preserved fishery products, beverages, tobacco, cereals, rice, flour and products from powders and jewellery.

2. Sensitive Track

Products which Thailand may increased import from Sri Lanka include animal products, paper, miscellaneous, textile and apparel.

3. Exclusion List

Products which Sri Lanka have more competitiveness to export than Thailand include tea, coffee, cocoa and beverages.

As Sri Lanka's economy is smaller than Thailand and trade value is not significant, the industry studies mostly focused on cooperation / mutual benefits. That said, "Thailand is therefore able to exempt customs duties on almost all types of goods from Sri Lanka." At the same time, Thailand should try to negotiate with Sri Lanka to minimize the exemption list.

A note for negotiation purposes, the volume of exports on downstream apparel products from Sri Lanka to Thailand may increase, but will not affected to Thai entrepreneurs because of the low trading value. Therefore, Thailand may list the downstream apparel products on her sensitive list. In addition, although Sri Lanka has higher competitiveness on tea product, but Sri Lankan tea is different in both type and market. As a result, it is believed that Sri Lankan tea will not negatively affect the Thai tea farmers.

Non- Tariff Barriers. Sri Lanka have not yet adopt international standard for certification, such as, ISO. Importors must obtain product certification from Sri Lankan authorities only. Therefore, Thailand should negotiate to reduce NTB to facilitate certification process in Sri Lanka such as initiating Mutual Recognition Agreements (MRA) on standard certification since Thai products are mostly meeting international standard.

Rules of Origin. In the past, Sri Lanka had no clear rules of origin for products. However, it was found that the current rules of Sri Lankan origin are more detailed. Therefore the negotiators should pursue both parties to adopt the rules of origin that Thailand uses in the previous FTAs such as in JTEPA and AJCEP as an guideline to consider the ROO for Thailand-Sri Lanka FTA. For example, Thailand may define "Wholly Obtain Rule" or "Regional Value Content Rule" or "Change in Tariff Subheading" for most products and "Harmonised tariff Nomenclature" for some products, especially electrical machinery products and automotive products and "Product Specific Rules" for textile and apparel products.

On the market access for goods, Thailand can commit to open around 95.9% to Sri Lanka, except 4 products on EL include tea, coffee, cocoa and other beverages and 245 apparel products (HS 61 and HS 62)

Suggestions to implement related policies

Proactive Strategies

In general, both parties should focus on improving knowledge and awareness for both Thai and Sri Lankan entrepreneurs starting from;

- Promote “Tourism between Thailand and Sri Lanka” to motivate and create awareness in both Thai and Sri Lankan.
- Organize “Roadshows” and “Business Matching” through trade exhibition in both countries.
- Arrange for “Business Match Makers” to organize series of business matchings, in return, they will get shared benefit from successful cases. This will motivate business match markers to arrange events and match businesses as many as possible.

Receiving Strategies

Many products from Thailand and Sri Lanka have mutual benefit, however, some products that producers from Thailand may experience negative effect from increasing import from Sri Lanka such as downstream apparel products.

In Addition, there are many products which seems to be advantage or disadvantage for both countries but in fact can complement each others in the end, such as some items on spices (cardamom and caraway) that Sri Lanka have high potential while Thailand do not have such products. On contrary, on tea products which Sri Lanka has the potential to produce black tea, while Thailand produces green tea (Chinese tea). Therefore, if both countries develop cooperation between each other, it will find mutual benefit from each other.

Strategies that Thailand should implement is (1) enhancing the agricultural production restructuring for country competitiveness fund, currently under administration by the Ministry of Agriculture and Cooperatives and the Ministry of Commerce, which is better than creating a new fund and (2) establishing networks and training programs between Thai and Sri Lankan entrepreneurs to enhance quality and standard of products.