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Indo-Sri Lanka Economic Relations in Modi's India

An LKI Roundtable with Dr. S. Narayan – former Finance Secretary, Ministry of Finance, India

Discussants: Dr. Razeen Sally, Chairman, Institute for Policy Studies (IPS)

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Three key takeaways from the IPS-LKI joint lecture delivered by Dr. S. Narayan on “Indo-Sri Lanka Economic Relations in Modi’s India” -

- 1. The trade deficit between Sri Lanka and India seems to be alleviating with increased Sri Lankan exports to India. Vibrant informal trade also exists.**
 - 2. Sri Lanka should attempt to further improve its export competitiveness by emphasising domestic reform on existing regulatory frameworks and implementing unilateral trade liberalisation measures.**
 - 3. Perceptions relating to India’s supposed political shift in alliances with the US should be tempered with the reality that India realises it needs to balance its counterparts in both Russia and China. This has implications for Sri Lanka.**
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Introduction

- Dr. S. Narayan – former Finance Secretary, Ministry of Finance, India – gave the inaugural IPS-LKI lecture on “India-Sri Lanka Economic Relations in Modi’s India” on 20 November 2017 at the Lakshman Kadirgamar Institute (LKI).
- The lecture was attended by around 130 academics, government officials, private sector representatives and diplomats.
- The lecture was followed by a panel discussion with Dr. S. Narayan and Dr. Razeen Sally, Chairman of the Institute for Policy Studies (IPS). The discussion was moderated by Dr. Ganeshan Wignaraja, Chair of LKI’s Global Economy Programme.

Takeaways from Dr. S. Narayan’s Lecture:

Current dynamics of India and Sri Lanka’s trade relationship

- Total India-Sri Lanka trade has grown from a small base to about \$5 billion today.
- While a balance of trade deficit persists in favour of India, the ratio of Indian imports to Sri Lanka to Sri Lanka’s exports to India has declined from 9:1 to the current 6:1.
- Some Sri Lankan businesses – in food, furniture and textiles – have enjoyed export success in the Indian market in recent years and contributed to raising the quality of Indian domestic manufacturing in certain sectors.
- Informal trade between the two countries is also on the rise encompassing ‘boat trade’, and the importation of goods through passenger air traffic, which presents a challenge on how to transition such activities into the formal sector and regulate them effectively.

Challenges and Bottle-necks hindering Indo-Sri Lanka trade growth

- Ongoing trade negotiations between India and Sri Lanka need to address non-tariff barriers, especially on the Indian side.

- Sri Lankan exporters and businesses have kept their geographical focus too narrow, concentrating too much on expansions into the state of Tamil Nadu at the expense of other trade-friendly South Indian states (e.g. Karnataka, Kerala, Andhra Pradesh and Telangana).
- Current regulatory frameworks on health and safety standards have not been updated to meet the demands of efficient trading networks.

Implications of the structural changes taking place in the Indian Economy

- India's economic outlook is good, with some labelling it one of the fastest growing regional economies.
- A substantial portion of India's informal economy, if transformed into the formal sector, will potentially spur India's growth rate even further beyond the current 6-7% growth rate.
- The initiation of the Goods and Service Tax (GST) in India has successfully brought a substantial increase in revenue to the Indian federal government and is seen as a step in the right direction in formalising informal economic activity.
 - The continued increase in total revenue from the GST will potentially see the overall tax rate decline in the future.
 - The introduction of the GST in India also represents an opportunity for smaller Sri Lankan IT firms to offer services to Indian companies in their needs for auditing, accounting and digitising records, as the domestic supply in India is not geared to keep up with current demand.

The Indian Economy and Foreign Policy

- Despite the perception that India is making a firm shift to align itself with the US on foreign policy matters, India has not abandoned engaging with other competing powers such as Russia and China.
 - This is reflected in the multilateral ministerial meetings that the countries are scheduled to attend to discuss policy matters.
- India is cognisant of the fact that it cannot match the speed and efficiency of China when it comes to big infrastructure development projects in the region.
 - India, however, does outperform China in delivering soft development assistance, such as knowledge sharing, and has been doing this for a much longer period than China, not only in Asia but in Africa as well.

Points from the Panel Discussion:

Improving economic cooperation to increase mutual economic benefits

- Sri Lanka should expand its trade agreements beyond India, China and Singapore in order to not leave Sri Lanka vulnerable to a few trading partners, especially when there is an imbalance in political power and economic size.

- Sri Lanka should look at linking up more effectively with the Southern Indian states to integrate Sri Lankan manufacturing into various value chains present in the Indian manufacturing sector.

Protecting local industry from import competition.

- Trade adjustment policies are sometimes developed for political, rather than strictly economic, reasons.
- However, a carefully calibrated program of trade adjustment, comprising of targeted assistance to affected industries (e.g. retraining workers) and trade remedies (e.g. anti-dumping measures and special safeguards) can be used to tackle import surges.
 - Such measures should, however, be prioritised to help individuals facing the loss of livelihoods as a result of increased import competition.
 - Trade adjustment programmes can be used as a form of political patronage, by protecting local businesses from import competition.

Suggested Readings:

Puri, H. (2017). *India's Trade Policy Dilemma and the Role of Domestic Reform*. Carnegie India. [online] Available at: <http://carnegieindia.org/2017/02/16/india-s-trade-policy-dilemma-and-role-of-domestic-reform-pub-67946> [Accessed 1 December 2017].

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Kotelawala, H. (2016). *ECTA - To Sign or Not?* Roar Media. [online] Available at: <https://roar.media/english/reports/economy/etca-%E2%80%92-sign-not/> [Accessed 1 December 2017].

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Hindustan Times. (2017). *GST launched: All you need to know about India's biggest tax reform*. <http://www.hindustantimes.com/india-news/gst-launched-all-you-need-to-know-about-india-s-biggest-tax-reform/story-9mYillRITDDfztqsuNL6bP.html> [Accessed 1 December 2017].

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