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Sri Lanka - Singapore FTA Four Years On: Policy Context, Key Issues and Future Prospects

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Abstract

In May 2022, the Sri Lanka – Singapore Free Trade Agreement (SLSFTA) marked four years since coming into force - an FTA that was a landmark one for Sri Lanka in many respects. It was the country's first bilateral free trade agreement (FTA) in over a decade, the first FTA with an ASEAN country, and the first 'comprehensive FTA' in the country's history, which meant that it went beyond goods, to include services, investment, and economic and technology cooperation. It was widely seen as a signal to the world that the country was keen to move to a new era in international trade and investment, and a signal to South-East Asia of its keenness to forge closer ties with a region that Sri Lanka has hitherto had little trade integration with. A reference by the then Minister of Development Strategies and International Trade at a business forum for Singaporean investors shortly after the agreement was signed, of the SLSFTA potentially helping Sri Lanka be part of the 'Regional Comprehensive Economic Partnership (RCEP) in the future, makes this paper especially relevant in the current context. A key benefit touted of the SLSFTA is to leverage the 'trade-investment nexus', by attracting Singaporean investors to invest in services and manufacturing and forging new joint-venture opportunities for Sri Lankan companies. Some investment interest was seen immediately following the signing of the agreement. Yet, early indications suggest that domestic policy and competitiveness conditions held further progress back. This Working Paper reviews bilateral trade performance, explains some of the key domestic economic policy contexts during and after the FTA was signed, discusses some of the key issues that emerged, and an initial look at prospects. Research for the paper was drawn not only from published grey material but also from extensive primary interviews with key informants.

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ABOUT CSF

The Centre for a Smart Future (CSF) is an independent, interdisciplinary public policy think tank based in Colombo, with a network of researchers, policy professionals and industry leaders based around the world. This paper is produced under the 'Trade and Economic Competitiveness' thematic pillar of the Centre.

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Sri Lanka – Singapore Free Trade Agreement Four Years On: Policy Context, Key Issues, and Future Prospects

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1 Introduction

Sri Lanka – Singapore economic relations reached a significant milestone in January 2018 with the signing of the Sri Lanka-Singapore Free Trade Agreement (SLSFTA). This was a landmark agreement for Sri Lanka as it was the country's first bilateral free trade agreement (FTA) in over a decade and the first 'comprehensive FTA' in the country's history, that went beyond goods, to include services, investment, and economic and technology cooperation. It was widely seen as a signal to the world that Sri Lanka was keen to move to a new era in international trade and investment, and a signal to Southeast Asian countries that the country was keen to forge closer ties with a region it had hitherto had little trade integration. In fact, the then Minister of Development Strategies and International Trade asserted - at a business forum for Singaporean investors shortly after the agreement was signed - that the SLSFTA can potentially help Sri Lanka to be a part of the 'Regional Comprehensive Economic Partnership (RCEP) in the future.

This paper will first set out the Sri Lankan trade and economic policy context within which the SLSFTA was forged and explore the bilateral trade data to provide a first look at early trends. It will discuss selected features of the agreement, especially those that made it a landmark agreement at the time and critically assess some of the more contentious parts of the agreement, which attracted public debate. Given the investment focus of the agreement, the paper will discuss the nature and type of investment projects that were seen in the initial years of the agreement coming into force, as well as some key domestic issues that could have held back investor interest during this time. It is based on published material, and key informant interviews with officials closely involved with the SLSFTA process to provide a reader with unique insights and present a policy-oriented perspective.

2 Sri Lankan trade and economic policy context of the SLSFTA

In the years preceding 2015, Sri Lanka's trade regime had begun increasingly restrictive and inward-looking, with creeping para-tariff protection for preferred domestic sectors and firms, a shying away from concluding free trade agreements (talks on deepening the Indo-Lanka FTA to a CEPA² had been abandoned, and talks to forge an FTA with China had stalled), and lacklustre progress in attracting FDI, with much of the post-war inflows into domestic non-tradable sectors like infrastructure and property development rather than export-oriented manufacturing and services.

Following the Presidential election in January 2015, and the government formed with then President Maithripala Sirisena and Prime Minister Ranil Wickremasinghe, there was a concerted effort to reverse the years of inward-looking trade policy orientation and undertake economic reforms and improve ease of doing business. The economic policy regime, led by the UNP-faction of the Government, had a stated commitment to trade reforms, consisting of a) unilateral tariff and para-tariff reduction, b) forging bilateral free trade agreements, and c)

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² Comprehensive Economic Partnership Agreement

regaining the lost tariff preference scheme 'GSP Plus' from Europe, and d) accelerating trade facilitation improvement measures under WTO Trade Facilitation Agreement (TFA) commitments.

SLSFTA was considered as the linchpin of this strategy, one that was expected to provide a strong signal to global investors and trade partners that Sri Lanka was once again 'open for business'. The decision to first complete an FTA with Singapore was considered important for at least five reasons.

Firstly, Sri Lanka had regressed in terms of trade liberalization since the mid-2000s and was increasingly unattractive to foreign investors (especially those engaged in global production networks). As such, concluding an FTA with Singapore, a country widely recognized as having one of the freest trade regimes, would signal to the world that Sri Lanka is now keen to re-engage with the global economy and commit to a path of liberalization.

Secondly, concluding not just a goods agreement, but a comprehensive agreement that also covered services, investment, and economic cooperation, with a country like Singapore, would be worthy of being Sri Lanka's first such comprehensive agreement and indeed, the country's first FTA in nearly 15 years.

Thirdly, forging an agreement that contains an investment chapter with Singapore, being the regional hub for many investors and Asia-focussed capital, could boost Sri Lanka's chances of attracting much-needed foreign direct investment. Fourthly, the new Government was keen to balance its geo-political relationships with India and China and forging its first FTA with either country (both of which were in the pipeline at that point) could have caused problems and forging its first FTA with Singapore instead provided a more neutral option. Finally, with the Government's strategic intentions to foster closer trade and investment ties with fast-growing South-East Asian economies (especially with the RCEP and TPP³ being forged), concluding an agreement with the then chair of the ASEAN bloc, could provide Sri Lanka with a good entryway to a larger market⁴. In this regard, Prime Minister Ranil Wickremesinghe addressing an investor forum in Singapore in 2018 stated the following: "The Singapore-Sri Lanka FTA is part of a broader strategy of looking East to renew our trade relationships. While we focus on growing and sustaining our traditional markets of the US and Europe, we have begun to diversify our markets towards Asia and focus on plugging into Asian supply chains. This FTA is our first agreement with a South-East Asian country - and we envisage this as a first step towards closer integration with the Regional Comprehensive Economic Partnership Agreement."⁵

With the change of leadership and government in Sri Lanka in 2019/2020 with President, Gotabaya Rajapaksa and Sri Lanka Podujana Peramuna (SLPP) coming into power, there has been a reversal of policies including Sri Lanka's external orientation with a preference for import-substitution strategy and calls to 'revisit' all bilateral trade agreements signed in the past five years⁶. At the same time, the new regime recognises the need to develop strong trade relations with Asian countries as highlighted in the 'National Policy Framework (NPF) - Vistas of Prosperity and Splendour', thereby creating an uncertain future for the SLSFTA⁷.

³ Trans Pacific Partnership

⁴ Interestingly, the next trade negotiations that were launched subsequent to the Singapore FTA was with Thailand, the then-incoming chair of ASEAN.

⁵ Colombo Stock Exchange, 2018. "Invest Sri Lanka takes center stage in Singapore" CSE, 4 March. Accessed April 8, 2021. <https://cdn.cse.lk/pdf/press/invest-srilanka-forum-singapore.pdf>

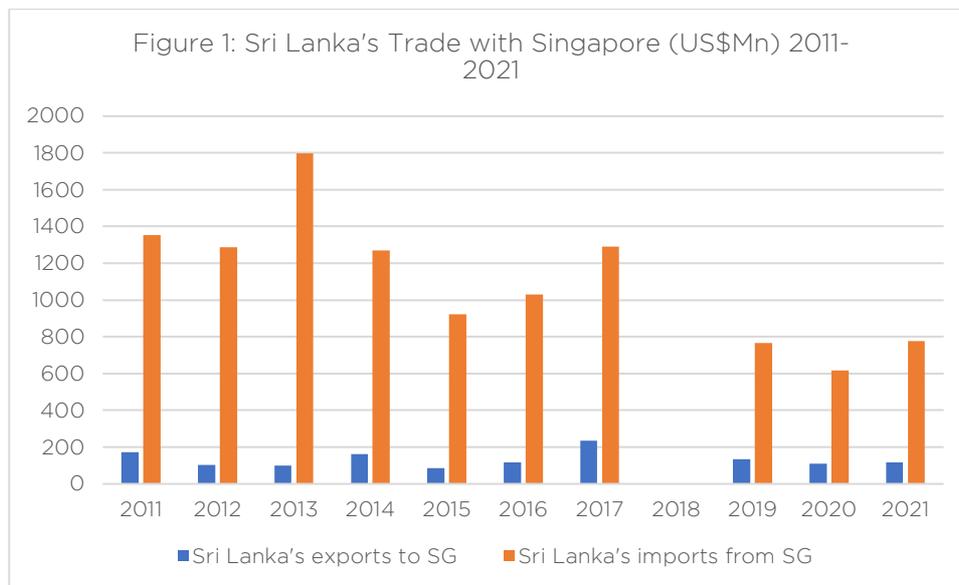
⁶ NewsFirst, 2020. "Government decides to review Sri Lanka - Singapore FTA," 6 February. Accessed April 10, 2021.

<https://www.newsfirst.lk/2020/02/06/government-decides-to-review-sri-lanka-singapore-fta/>.

⁷ Kapur, Roshni, and Chulanee Attanayake, 2019. "Singapore Sri Lanka Relations Under Gotabaya Rajapaksa." ISAS Brief, December. https://www.researchgate.net/publication/338935948_Singapore_Sri_Lanka_Relations_Under_Gotabaya_Rajapaksa.

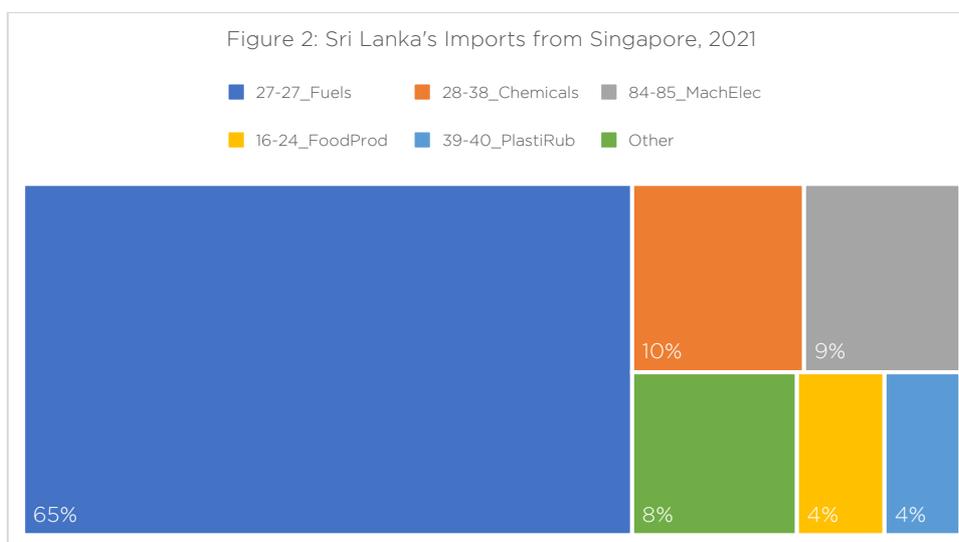
3 Overview of bilateral trade and investment data, pre-FTA

Trade between Singapore and Sri Lanka has grown, with bilateral trade crossing the US\$ 1 billion mark since 2006, with a trade deficit (difference between exports and imports) growing heavily in favour of Singapore (Figure 1). In 2021, Singapore was Sri Lanka’s fifth largest source of imports after China, India UAE and Malaysia, accounting for 3.6 % of Sri Lanka’s total imports. In terms of value, Sri Lanka imported from Singapore goods amounting to US\$ 776 million, comprising mostly fuels, machinery and electrical equipment, and chemicals (Figure 2).



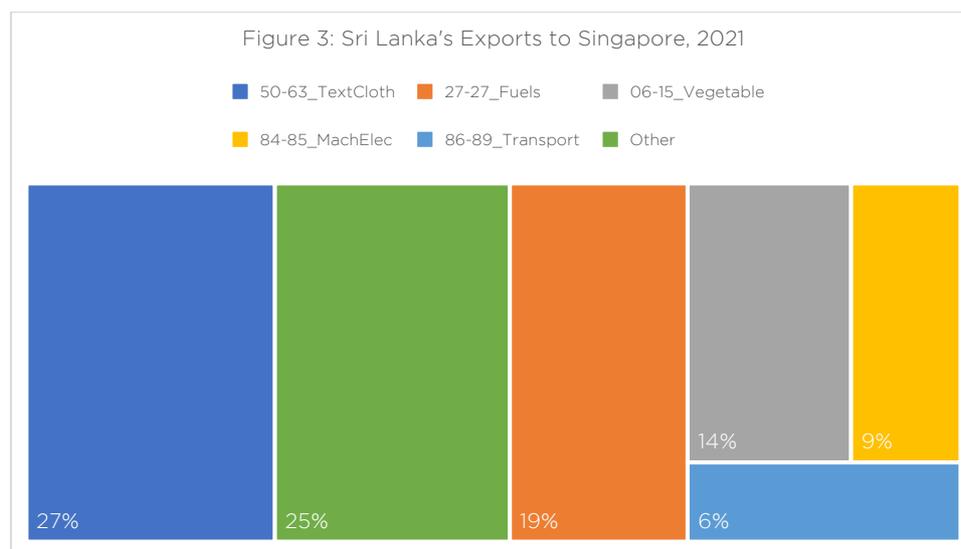
Source: Compiled from TradeMap Database

In 2021, Sri Lanka’s exports to Singapore totalled US\$ 118 million, and consisted of apparel, electrical machinery and equipment, fuels, and food (Figure 3). Singapore accounts only for 1 % of Sri Lanka’s total exports; it is not an important export market for Sri Lanka. Currently, it ranks at 24th position as an export market of Sri Lanka. Nonetheless, Sri Lanka has an estimated untapped potential⁸ to increase exports by an addition of US\$84 million, mostly in rubber, tea, and apparel to Singapore.



Source: Compiled from TradeMap Database

⁸ Estimated untapped potential trade is the difference between the actual trade and the expected potential trade in five years' time



Source: Compiled from TradeMap Database

Based on a preliminary examination of trade data, SLSFTA does not appear to have had an impact on bilateral trade in goods to date. This is to be expected given that Sri Lankan exporters already have duty-free access to Singapore while reciprocal access for Singaporean businesses to the Sri Lanka market would become available over the course of 12-15 years from the time of implementation of the agreement. In fact, bilateral trade has fallen since SLSFTA came into effect, reflecting the slowdown of Sri Lanka's trade with the world since 2018 amid import controls and COVID-19. Simulations based on World Integrated Trade Solutions (WITS) SMART Model indicate that zero imposition of duties by Sri Lanka could lead to an increase in imports from Singapore by 20 % (US\$ 192 million) while no increase in exports to Singapore is expected given its existing zero duty regime⁹. Given the limited benefits of the trade in goods, the Sri Lankan government at the time of signing the agreement promoted it with an expectation to increase foreign direct investment flows into the manufacturing and services sectors and to link to global production and value chains.

In terms of foreign investments, Singapore has been an important investor in Sri Lanka for the past two decades; it has consecutively been among the top 10 investors in recent times. In 2017, US\$ 203 Mn worth of foreign direct investments were made by Singapore in Sri Lanka; this amounted to about 15 % of total FDI flows to the country in that year¹⁰ (see Figure 4). However, since then the flow of Singaporean investments into the country have fallen.

It is reported over 100 Singaporean businesses operate in Sri Lanka.¹¹ Singapore firms have been active in areas such as property development (Overseas Realty Ceylon PLC), construction (WohHup Construction), tourism (Shangri-La Hotels), food and beverage processing (Prima Ceylon, Asia Pacific Breweries), and telecommunications (Lanka Bell)¹². Overseas Realty PLC, a publicly listed property developer worth LKR 20 billion has operated in Sri Lanka since 1980, and 90% of the company, which is the developer of Colombo's iconic World Trade Centre and the landmark Havelock City residential complex, is owned by the Shing Kwan Group. Prima Ceylon was the first Singapore company to set up operations in Sri Lanka as early as 1977. With a core business in wheat flour milling and distribution, it has diversified its business and become a household name over the last four decades, contributing

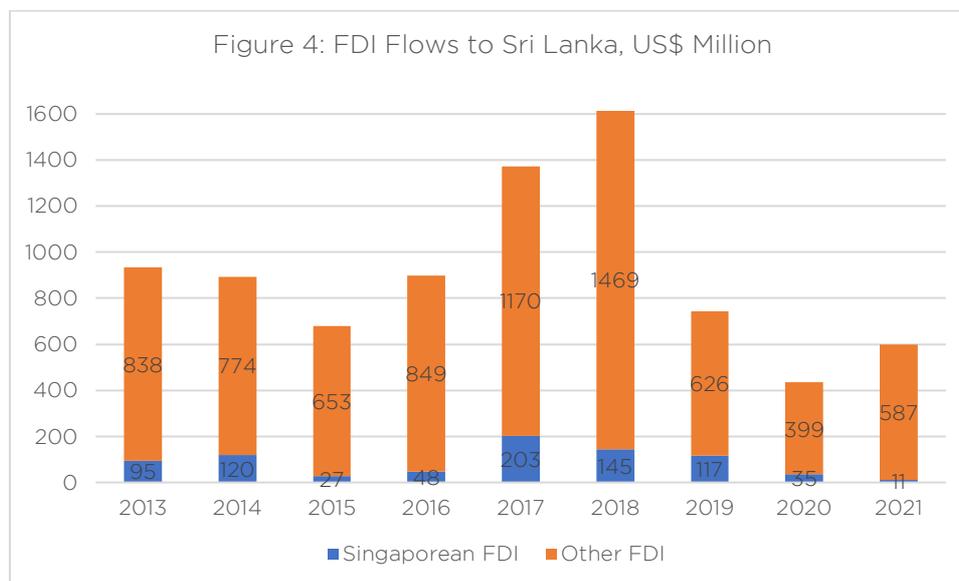
⁹ Commonwealth Secretariat, n.d. Supporting Sri Lanka's Free Trade Agreements. Unpublished, London: Commonwealth Secretariat.

¹⁰ Central Bank of Sri Lanka, 2020. "Annual Report 2019." CBSL. Accessed April 8, 2021. <https://www.cbsl.gov.lk/en/publications/economic-and-financial-reports/annual-reports/annual-report-2019>.

¹¹ Divya, Hundlani, 2018. "Sri Lanka-Singapore Free Trade Agreement." Lakshman Kadirgamar Institute. 18 September. Accessed April 2, 2021. <https://iki.lk/publication/sri-lanka-singapore-free-trade-agreement/>.

¹² Wijayasiri, Janaka, and Kithmina Hewage, 2018. Straight Talk on Sri Lanka - Singapore FTA: What it Means for Trade and Investment Flows. 28 January. Accessed April 14, 2021. <https://www.ipslk/talkingeconomics/2018/01/24/straight-talk-on-sri-lanka-singapore-fta-what-it-means-for-trade-and-investment-flows/>.

to Sri Lanka's food security, foreign reserves, and employment opportunities¹³. Other well-known Singaporean brands operating in Sri Lanka include: BreadTalk, Charles & Keith, and Pastamania.



Source: Central Bank of Sri Lanka, various issues

Some of the sectors in which investors from Singapore have expressed interest in Sri Lanka and its growing market include consumer goods and retail, infrastructure, tourism, and trade. Likewise, Sri Lanka has identified infrastructure development, IT and IT-enabled services, education, and tourism as targeted sectors for attracting FDI from Singapore.

4 Overview of the FTA and key features

Negotiations on the SLSFTA were launched by Minister of Trade and Industry, S. Iswaran and his counterpart minister for Development Strategies and International Trade Malik Samarawickrama, in the presence of Prime Minister Lee Hsien Loong and Sri Lanka Prime Minister Ranil Wickremesinghe on 18 July 2016¹⁴. They were led by a Cabinet-approved National Trade Negotiation Committee and 12 of its sub-committees, chaired by all the relevant public sector institutions¹⁵. Eight rounds of negotiations were held between the respective negotiation teams for about 18 months, culminating in the final negotiations in November 2017. During this time, more than 20 consultations were held with a wide range of stakeholders including chambers, industry associations, and professional associations. There were common consultations regarding all ongoing FTAs, but different Sub Committees had sectoral consultations on specific areas under each FTA with relevant Associations and Chambers. Subsequently, the agreement was signed on 23 January 2018, and it came into force on 1 May later in the same year.

SLSFTA is Sri Lanka's sixth trading agreement and the first signed since 2005¹⁶. By contrast, Singapore has over 20 agreements with bilateral and regional partners across the world, from ASEAN to the Asia-Pacific region, North and South America, Europe and the Middle East¹⁷. The

¹³ DailyFT. 2018. "Prima Ceylon celebrates landmark 40 years in Sri Lanka." DailyFT, 14 March. Accessed April 5, 2021. <http://www.ft.lk/Other-Sectors/Prima-Ceylon-celebrates-landmark-40-years-in-Sri-Lanka/57-674621>.

¹⁴ MTI. 2018. "SRI LANKA-SINGAPORE FREE TRADE AGREEMENT ENTERS INTO FORCE ON 1 MAY 2018." Ministry of Trade and Investment Singapore, 20 April. Accessed April 4, 2021. <https://www.mti.gov.sg/-/media/MTI/Newsroom/Press-Releases/2018/04/Sri-Lanka-Singapore-Free-Trade-Agreement-enters-into-force-on-1-May-2018/sri-lanka-singapore-free-trade-agreement-enters-into-force-on-1-may-2018.pdf>.

¹⁵ It is noteworthy that there were exploratory talks as early as 2003 on a Comprehensive Economic Partnership Agreement (CEPA) between the countries, followed by a second round of discussion in 2004, but there was no progress on this regard at that time failing to reach an agreement.

¹⁶ Sri Lanka is a party to the following reciprocal trade agreements: Asia-Pacific Trade Agreement (APTA), SAARC Preferential Trading Arrangement (SAPTA), Agreement on South Asian Free Trade Area (SAFTA), India-Sri Lanka Free Trade Agreement (ISFTA) and Pakistan-Sri Lanka Free Trade Agreement (PSFTA)

¹⁷ Hundani, Divya. 2018. "Sri Lanka-Singapore Free Trade Agreement." Lakshman Kadirgamar Institute, 18 September. Accessed April 2, 2021. <https://lki.lk/publication/sri-lanka-singapore-free-trade-agreement/>.

agreement with Sri Lanka is Singapore's second comprehensive FTA with a South Asian economy after India. According to the Minister for Trade and Industry, S. Iswaran, "For Singapore, this agreement marks another step-forward in our commitment to free and open markets, and to deepening our bilateral ties with Sri Lanka, and through Sri Lanka into the South Asian region".

The SLSFTA is a modern, comprehensive, and high-quality agreement, unlike other agreements that Sri Lanka has signed to date. It contains 17 Chapters covering a wide range of areas beyond trade in goods, trade remedies, trade facilitation and dispute settlement and includes trade in services, investment, intellectual property rights, government procurement, competition and e-commerce, and economic and technical cooperation.

4.1 Trade in goods

Under the Trade Liberalization Programme (TLP), custom duties on 50% of tariff lines are eliminated immediately by Sri Lanka (approximately 3719 tariff lines out of a total of 7,438 at 8-digit HS level) upon the agreement coming into force. This percentage will be gradually increased to 80 % over a period of 15 years, a relatively long adjustment period. Singapore already grants Sri Lanka tariff-free access on 99% of goods. Sri Lanka's Negative List contains 1,488 items, which account for 20 % of the country's tariff lines. This list contains sensitive items based on revenue (i.e., petroleum products, alcohol, and tobacco) and domestic considerations (many agricultural products) which would not be subjected to tariff elimination by Sri Lanka. In addition to custom duties, para-tariffs like Cess and Ports and Airports Development Levy (PAL) on imports from Singapore will be eliminated over time, providing Sri Lankan businesses sufficient time to adapt to the new market conditions. All goods under the agreement must fulfil general rules of origin (ROO) of 35% domestic value addition (DVA) or a change of tariff headings (CTH) at 4-digit HS level to benefit from the duty-free access. Rules of origin are criteria which determine a product's originating status. They are specified in a trade agreement to ensure that only goods originating from the FTA partner countries will benefit from tariff concessions. For some export products (1866 products), there are specific process rules, which are more flexible than the above general criteria. No ASEAN cumulation is allowed under the FTA which prevents goods from the ASEAN region to be channelled to Sri Lanka via Singapore.

4.2 Non-tariff measures, trade remedies, customs issues

International standards and practices have been adopted to reduce non-tariff measures impeding trade, and the agreement refers to trade remedies including anti-dumping subsidies, countervailing measures, and safeguards which can be used in case imports cause serious harm or injury to domestic businesses. The agreement also reduces business costs and red tape around customs processing/procedures to facilitate trade.

4.3 Trade in services

The SLSFTA provides better access to markets in Singapore and Sri Lanka for service providers, with liberalization across different modes of trade in service sectors. Trade in services was negotiated on a positive list basis whereby countries specified the sectors which would be liberalised. Sri Lanka has made specific commitments in communications, financial services, transport, construction, other business services, hotel and restaurant services, tourism and travel-related services, sports and other recreational services, professional services,

environmental services, and distribution services. Professional services include legal advisory services, architectural services, and Engineering Services but they are limited¹⁸. In comparison, Singapore's sectoral commitments are more extensive in coverage and depth. Also, they are of export interest to Sri Lanka¹⁹. Not only are Singapore's service trade commitments to Sri Lanka of significantly more depth and coverage than Sri Lanka's to Singapore, but Singapore's commitments are also 'GATS+' and particularly relevant for important services for Sri Lanka including professional services such as legal advisory services, wholesale & retail trade, R&D services, logistical services including road freight transportation, and emerging services such as environmental services and real estate services.

4.4 Other key features - e-commerce, investment, movement of people, and government procurement

There are two separate chapters in the agreement on e-commerce and telecommunications given their importance to both countries. The movement of natural persons under the agreement is controlled and linked to the commercial presence (e.g., intra-corporate transferees) and limited to high-level skilled positions ('specialists, managers, or executives'). Under the agreement, visas are also given for business visitors for a period of up to 30 days to facilitate trade and investment linkages between the two countries. The investment chapter protects investors and investments from both countries thereby attracting investments to Sri Lanka. The investment chapter of the SLSFTA replaced the Bilateral Investment Treaty (BIT) between Sri Lanka and Singapore which was in effect since 1980, providing more investment protection for both sides.²⁰ Government procurement (GP) is included in the agreement, ensuring Sri Lankan businesses can compete with Singapore businesses for government contracts. This is the first time Sri Lanka has included GP in one of its trade agreements. Protection and enforcement of Intellectual Property (IP) rights are also covered in the agreement. A clear process to settle disputes is also specified in the agreement.

5 Selected issues and controversies

Given Sri Lanka's slow progress with forging bilateral trade agreements in the preceding decade or more, there was a high level of concern among domestic stakeholders regarding the contents of the agreement. At times, the concern morphed into undue fears and propelled misleading views and myths. When a market is opened to competition, there will be winners - usually the consumers and the public - and those who will be adversely affected, usually domestic industries and professionals. The latter group is often more concentrated and effective at voicing their concerns²¹. This section describes a selection of these myths.

5.1 Tariff liberalization on imports

A concern raised by some is that due to the Tariff Liberalization Programme (TLP) of the SLSFTA, Sri Lanka would lose border tax revenue. According to the commitment in the SLSFTA, Sri Lanka would liberalize 50% of tariff lines immediately as the agreement comes into force. In fact, most Sri Lanka's tariff lines (around 50% or 3,719 items) are already duty-free, and this applies not only to goods imported from Singapore but from any other country as well. Consequently, there is no additional revenue loss or threat to the domestic industry

¹⁸ Ceylon Chambers of Commerce. 2018. Free Trade Agreement between Sri Lanka and Singapore. Accessed April 6, 2021. <https://www.economy.lk/singlepage-article.php?id=33>.

¹⁹ DailyFT. 2018. Highlights of Sri Lanka-Singapore FTA which makes watershed in Sri Lankan economy. 6 February. Accessed April 8, 2021. <http://www.ft.lk/business/Highlights-of-Sri-Lanka-Singapore-FTA-which-makes-watershed-in-Sri-Lankan-economy/34-648827>.

²⁰ Ceylon Chamber of Commerce. 2018. Insights and Findings on the Sri Lanka-Singapore Free Trade Agreement. 20 September. Accessed April 6, 2021. https://www.chamber.lk/images/pdf/InsightsandFindingsonSLSingaporeFTA_EIU_TIP.PDF.

²¹ These concerns resulted in the appointment of a Committee of Experts to evaluate the SLSFTA by President Maithripala Sirisena in 2018.

from the SLSFTA due to the TLP right away. As with any such agreement, the TLP of the SLSFTA was formulated in consultation with, and agreement of, the Ministry of Finance.

On further liberalization commitments under the SLSFTA, Sri Lanka undertook to liberalize up to 80% of tariff lines over a gradual period of 12 - 15 years; a further 15% of tariff lines (1,116 items) from the 1st to 6th year in equal instalments, the next 14.3% (1,064 items) from the 7th to the 12th year in equal instalments, and 0.7% (51 items) from the 11th to the 15th year. Since tariffs on petroleum products, tobacco, spirits, and alcohol are important revenue items for the government, they have been included in Sri Lanka's Negative List of products that will not be subject to liberalisation, thereby protecting revenue. This steady tariff phase-out is expected to manage the revenue as well as domestic industry implications quite generously.

5.2 Liberalisation of services

This aspect became a point of heavy contention, where vested interest stakeholders, as well as politically motivated actors, claimed that the SLSFTA will pave the way for an unchecked inflow of workers from Singapore to Sri Lanka. The agreement did not provide for such entry. Both Sri Lanka and Singapore decided early on that the SLSFTA should be limited only to business visitors and intra-corporate transferees, linked to investment. This is also limited to specific categories like Managers, Executives, and Specialists, which are further defined in the agreement, such entry is governed by applicable immigration rules, and has restrictions like the duration they can remain in the country for. In Mode 3 ('Commercial presence', i.e. investment), Sri Lanka's commitments under the SLSFTA do not go beyond the prevailing level of openness offered through the Foreign Exchange Management Act of 2017. In fact, in some cases such as construction services, while the existing regulations allow 100% foreign equity ownership, the SLSFTA commits to only up to 40% foreign equity ownership.

As such, the agreement excludes any commitment to liberalize entry of independent professionals/movement of natural persons (i.e., liberalisation of Mode 4). Accordingly, Sri Lanka's commitments in Mode 4 trade in services are in line with its existing level of openness the country has committed under the WTO GATS agreement and does not provide Singapore with any new market access in this regard.

5.3 Toxic waste importation

Another concern that arose quite surprisingly was that the SLFTA - and the tariff liberalization offered - would permit harmful products such as garbage, clinical waste, nuclear waste, chemical waste etc. to be imported to Sri Lanka. The argument by those individuals and groups that raised this issue was that since waste products are included in the TLP, such items can be dumped into the country under the agreement. To be clear, the reduction or elimination of tariff does not grant automatic entry of a product into a country - all applicable domestic regulations and mechanisms would still apply, including any applicable import licensing requirements, standards, and other regulatory approvals. The SLSFTA does not take away Sri Lanka's rights under International Environmental Protection Treaties to which Sri Lanka is a signatory and therefore, relevant environmental laws and regulations would apply to such imported products with no exception for those imports from Singapore under the SLSFTA. Moreover, under Article 20 on "General Exceptions" of GATT 1994, Sri Lanka has the right to take measures to protect human, animal and plant life or health. This provision has been incorporated into article 17.7 of the agreement which ensures this right.

6 Foreign direct investment

Singapore was once one of the largest investors in Sri Lanka, in the early years of the country's economic reforms and 'opening up', with prominent investments by companies such as Shin Kwan Group and Prima Ceylon.

It was clear early in the FTA process that investment attraction was one of the primary motivations for Sri Lanka in forging the SLSFTA - the urgent need to attract high-quality FDI to Sri Lanka coupled with the fact that Singapore is a regional headquarter for many global companies looking to invest in the region. In his speech to fellow MPs following the tabling of the SLSFTA in Parliament, the then Minister of Development Strategies and International Trade Malik Samarawickrama noted, "...a prime objective of the SLSFTA is to attract FDI from Singapore into Sri Lanka in the manufacturing and services sectors and to link to global production and value chains".

Prior to the SLSFTA, Singapore only accounted for about 5.3% of total FDI inflows into Sri Lanka during 2014-2017. Some early initiatives were held to drum up investor interest in Singapore, following the signing of the agreement in January 2018. In March 2018, an 'Invest Sri Lanka' forum was held in Singapore to mainly reach capital market investors²², with the participation of the Sri Lankan PM and Singaporean trade and industry minister. In July 2018, an investment forum was held in Singapore targeting FDI investors with the participation of the Minister of Development Strategies and International Trade, Malik Samarawickrama, which drew substantial interest from investors keen on opportunities in services, manufacturing, and tourism. Subsequent to these forums, the Board of Investment announced that FDI projects amounting to over US\$ 16 billion were under negotiation²³, including an export-oriented oil refinery and sugar refinery in Hambantota (US\$14.8 billion and US\$ 200 million respectively), a steel manufacturing facility in Trincomalee (US\$1 billion) and a flour manufacturing facility catering to local and export demand (US\$50 million). This was in addition to several other investment prospects being negotiated, according to an interview with a senior Government official leading investment promotion at the time.

Another government official from Sri Lanka involved in commercial bilateral relations and based in Singapore observed, "We saw much interest in exchanging delegations soon after signing the agreement [...] Few MOUs entered during the signing visit were implemented and several investments were materialised". Following the SLSFTA, three Singaporean companies signed agreements for four new projects in food, aquaculture, hospitality and infrastructure in Sri Lanka: Food Studio (a food court operator), Ark Holdings (an aquaculture company specialising in wild harvest trading and seafood distribution) and HPL Hotels & Resorts (a hospitality management company).²⁴ According to officials familiar with the investor landscape at the time, the immediate interest came from investors with a higher risk appetite, and those first-movers were looking for direct negotiations with the Government and speedy decision-making. Notably, this initial interest was in real estate and tourism, particularly the heritage properties in the Colombo Fort area.

Actual FDI performance in the years immediately following the forging of the SLSFTA was marred by political instability, and this would no doubt have impacted the prospects for FDI

²² Cassim, Nisthar . 2018. 2018's first 'Invest Sri Lanka' Forum opens in Singapore today. 2 March. Accessed April 12, 2021. <http://www.ft.lk/front-page/2018-s-first-invest-sri-lanka-forum-opens-in-singapore-today/44-650388>.

²³ Daily News. 2018. Over \$16 bn investment projects under discussion with Singapore. 16 July. Accessed April 12, 2021. <https://www.dailynews.lk/2018/07/16/business/156938/over-16-bn-investment-projects-under-discussion-singapore>.

²⁴ IE Singapore & Singapore Business Federation. 2018. Joint Press Release: IE Singapore partners SBF to help Singapore companies in consumer, tourism and infrastructure access opportunities in Sri Lanka. 24 January. Accessed April 12, 2021. https://www.nas.gov.sg/archivesonline/data/pdffdoc/20180124003/MR00418_1E%20Singapore_SBF%20Joint%20Release_Sri%20Lanka%20Singapore%20Business%20Forum%202018_2018%2001%2024.pdf.

from Singapore. Notably, the October 2018 coup that resulted in a 52-day political stalemate and saw a rapid deterioration of relations between the President and Prime Minister, the April 2019 Easter Sunday terror attacks and subsequent communal riots that made investors fearful of the security situation, and the change of Government through November 2019 Presidential and August 2020 Parliamentary elections that saw an upheaval of the administrative leadership of all institutions and a distinct policy shift away from trade liberalization. As a result, FDI flows from Singapore in 2019 dropped by almost 20% from the previous year to US\$117 million²⁵. Inflows continued to further drop to US\$ 35 and US\$ 11 million in 2020 and 2021, respectively.

While the SLSFTA opened opportunities for Singaporean companies, Sri Lanka's overall investment climate needed to improve. As a senior government official commented during interviews, "It is not just the agreement that mattered for investment - it is also the conducive environment within Sri Lanka, including the ease of doing business and the decisiveness of policy". At the same time, it was acknowledged that more could have been done to market the SLSFTA at the time of its signing with Singaporean companies to promote opportunities in Sri Lanka. "We expected the Singaporeans to come here, but we didn't go and market enough in Singapore. I think we should have done that by the time SLSFTA was getting cleared".

7 Conclusion and future prospects

The SLSFTA elevated bilateral relations between Sri Lanka and Singapore which have been long-standing trading partners. At the time of its negotiation and signing, the government of Sri Lanka was keen to diversify its export products and markets, create linkages to global production and value chains, integrate Sri Lanka into the global economy and attract FDI into the country. In this context, Sri Lanka signed the SLSFTA which was unlike other trade agreements signed by it to date - it is a modern, comprehensive, and high-quality free trade agreement. Since the agreement was signed, however, some local interest groups and politicians have criticised aspects of the SLSFTA, often due to a lack of awareness, and poor understanding of the agreement and its contents, calling for its revision. This points to the need for wider communications on the benefit of the SLSFTA as well as the role it plays in the larger effort to improve Sri Lanka's trade and investment competitiveness. Additionally, the SLSFTA provides for a joint review of the agreement after the first year of implementation to discuss and ameliorate issues that either side may have and agree on any areas for amendment. For this, both sides must appoint a joint review committee, but as of July 2022 this process had not been initiated.

Foreign direct investment flows to Sri Lanka were affected by the adverse domestic conditions in the country. Easter Sunday attacks and the political uncertainty have undermined investment and overall investor confidence in Sri Lanka, thereby limiting the expected immediate benefits of the agreement.

During 2021-2022, Sri Lanka's investment climate deteriorated substantially with the emergence of an acute foreign reserves crisis. This led to the government placing numerous unilateral restrictions on imports - ranging from outright bans and restrictive licensing regimes to 100% cash margins for Letters of Credit and stipulations that importers must obtain 180-days credit from their overseas suppliers. Firms with international transactions were unable to obtain sufficient foreign currency from the domestic banking system to make overseas

²⁵ Central Bank of Sri Lanka. 2020. "Annual Report 2019." CBSL. Accessed April 8, 2021. <https://www.cbsl.gov.lk/en/publications/economic-and-financial-reports/annual-reports/annual-report-2019>.

payments, and some even reported an inability to repatriate profits in full and on time. During the first half of 2022, the climate worsened, with long hours of electricity cuts and a shortage of fuel for transport and power generation. Sri Lanka's sovereign credit rating was reduced to 'Restricted Default' status by international rating agencies after an announcement in April 2022 that the country will suspend debt servicing. At the time of writing, an IMF bailout programme is due, debt restructuring negotiations are commencing, and an uneasy political cohabitation is in place. Investors would expect prolonged economic strains over the next 2-3 years, with chances of political and policy instability. Consequently, all investors – not least Singaporean ones – are likely to take a 'wait-and-see' approach to Sri Lanka – how the crisis and recovery unfold and the kind of policy regime that is installed in its wake. Looking ahead, it is important to communicate the benefits the SLSFTA offers to foreign investors by providing a stable investment regime protected under a sovereign bilateral agreement.

Beyond the current macroeconomic crisis, the prospects of the SLSFTA will largely be determined by Sri Lanka's commitment to following the TLP on goods embedded in the agreement, as well as Sri Lankan government stakeholders' proactive engagement in the economic cooperation chapter of the agreement (for instance, in information technology, innovation and the digital entrepreneurship ecosystem) and Sri Lankan firms' proactive push to gain from services sector market access opened to Sri Lanka by Singapore.

Overall, international firms looking to trade with, and invest in, Sri Lanka will look not only at the SLSFTA in isolation but at the country's overall trade and investment regime. A senior government official interviewed acknowledged that "domestic reforms are required in the areas of legal and regulatory structures related to service liberalization and investment". To fully leverage the SLSFTA for increasing bilateral trade and investment, Sri Lanka must accelerate reforms to make the country a more attractive trade and investment hub in the region, including rationalizing and reducing border taxes, improving trade facilitation, facilitating FDI, and ensuring policy stability, regulatory predictability, and procedural transparency.

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