

## **The Generalized System of preferences (GSP) and the International Trade of Sri Lanka**

I.G. Ayodya Niwarthana Perera<sup>1</sup>

### **Abstract**

The Generalized System of Preferences (GSP) is a popular preferential tariff system which is excluded from regular rules of the World Trade Organization (WTO). Many developing countries including Sri Lanka have granted the GSP benefit from the European Union (EU) and some other developed countries like United States of America. This article has discussed the importance of the GSP as a preferential tariff system in view of advantages, disadvantages and effects of withdrawing it from the European Union. The paper has revealed that the withdrawal of GSP plus from the European Union was not negatively affected on Sri Lankan foreign trade volume and values. The analysis was totally based on the secondary information such as custom reports, books and the internet.

**Key words:** Generalized System of preferences (GSP), International trade, Sri Lanka

### **Introduction**

The Generalized System of Preferences or GPS usually offers more generous tariff reduction to developing countries to climb out of poverty. Basically this benefit given by countries which are in European Union to some specific developing countries. This discussion about system of tariff preferences was started in 1960 at the conference of United Nations Conference on trade and development (UNCTAD). Nowadays this tariff preference system can categorized under 3 arrangements. Those are,

1. GPS
2. GPS Plus (+)

---

<sup>1</sup> B. A (special) in Economics, Third year ayodya\_perera@yahoo.com

### 3. EBA (Everything But Arms)

According to this agreement countries of preference receiving called beneficiary countries and countries who are giving the preference called donor countries (developed countries). Product coverage of GPS consists of agricultural, industrial, textiles, footwear, petroleum, canned tuna & etc. Donor countries are giving special tariff preferences for these kind of exports of beneficiaries. To grant this benefit a country has to be include in one of these three foremost categories such as,

1. A developing country
2. Least developed developing country (LLDC)
3. Special incentive arrangement for sustainable development and good governance

Among these EBA is automatically receiving from least developed countries and countries who has special incentive arrangement for sustainable development and good governance like Sri Lanka receives GSP plus (+). Those beneficiaries can enhance their export diversification from granting this benefit. To granting GSP plus specially those applicants have to engage with 27 international conventions of the EU (Abheyagunawardena, 2015). Generally donor countries cut off some percentage of their tariff which they usually charge on their imports (beneficiaries' exports) under this benefit. GPS plus basically depends on 2 criteria's. Those are 'Human and labor rights' and 'Sustainable development concept'. The all 27 international conventions are strictly related with these two topics. Among those conventions 15 are related to human and labor rights then the other 12 conventions are related to sustainable development and good governance. These are some countries that extend this benefit recently,

1. European Union (EU)
2. Australia

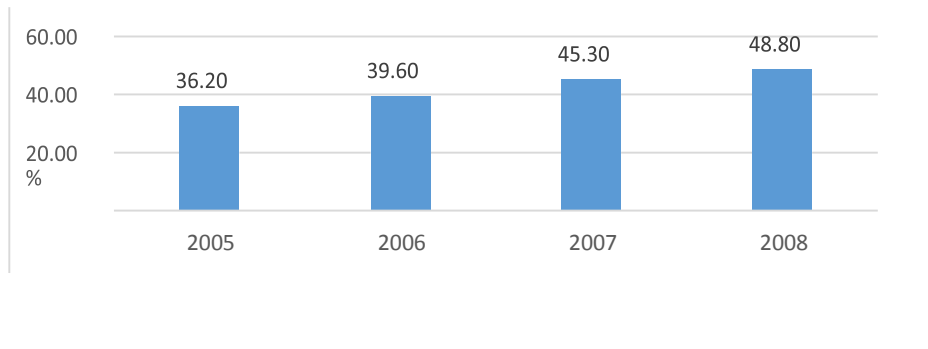
3. Canada
4. Japan
5. Norway
6. Switzerland

Nowadays nearly 29 countries provide GPS benefit according to their own respective schemes. Sri Lanka has also been granting this benefit since 2005. Sri Lanka received it from EU as GPS plus because they certify that Sri Lanka has engaged with their qualifications related to granting GSP plus benefit. Since in this paper we are going to discuss about what are the benefits that we gain from GPS plus and with elimination of the benefit how we continue our process of international trade. Basically this benefit is awarded for ten years and it is reviewed after every three years (CBSL, 2009). When they re-examine the beneficiary country if they have not continue their status according to the EU conventions and other qualifications, the benefit will be eliminated from that country.

### **Sri Lankan international trade with GPS plus**

As a developing country the relationship with EU is vital for developing process of Sri Lanka, because of EU is the main export market and the second largest import market of Sri Lanka. For an example 50% of apparel products export to EU countries and 29% of industrial products import from EU countries (The Island, 2010). In 2005 EU decided to choose Sri Lanka as a GPS plus beneficiary country because Sri Lanka has engaged with their all international conventions rather than other regional countries in South Asia. Although they have decided to commence this agreement in 2006 (January) because of disaster Tsunami they commenced it from July 2005. And it has extended in 2009 again.

Figure: 01: GSP-Plus



Source: GSP-Plus removal ‘will raise many issues for EU in global trade debate| [www.island.lk](http://www.island.lk)

According to the above figure, in year 2005 (before become a beneficiary) the share of ready-made garments (RMG) to EU countries was 36.2%. However after became a beneficiary the share of export to EU has increased up to 48.8% while the US market of RMG has reduced its share from 59.4% to 45.2% (The Island, 2010). According to these facts and figures it is very clear that the GSP benefit acted as a tool to control the EU export market positively. Though as a feeble shareholder of EU market there are both advantages and disadvantages of this trade agreement. Therefore only depend on the EU market with the help of these kinds of benefits are not appropriate and Sri Lanka needs to has a diffused export market to survive in the international market.

### **Advantages and Disadvantages of GPS plus**

As mentioned earlier there are both advantages and disadvantages of granting GSP plus which are related to economic, political and social sectors of the country.

#### **Advantages**

- 1) As a result of tariff preference the price level of exports of Sri Lanka has declined. Since the demand for Sri Lankan products has increased.

- 2) The export income has shown a gradual increment since the major percentage of total exports (66%) have exported under the tariff preference to EU market.
- 3) Exports of Sri Lanka became more competitive in the European market because of the low price of these products.
- 4) Sri Lankan exporters became more stable in the European market and due to that their income has increased dramatically.
- 5) Due to development of the production process a large amount of occupations have generated.
- 6) Diversification of product range has increased because of intense competition.
- 7) Foreign and local investment in Sri Lanka has started to increase to enjoy the benefit of tariff preference.
- 8) The growth rate of the National Income has increased due to higher income from exports.

### **Disadvantages**

- 1) Efficiency of production process has reduced due to high rate of price levels compared to the usual system of tariff.
- 2) As a result of political influence the GSP plus became a political advantage rather than an economic concept.
- 3) The GSP plus has created a devious economic and political dependency on developed countries in the EU.
- 4) Developed countries usually use this agreement as a weapon to influence on developing country's (beneficiaries) economic systems by using their political power.
- 5) Production of some kind of export goods which were not preferred under the scheme have reduced. Hence the diversification of the export sector of Sri Lanka has also reduced.

### **Elimination of Sri Lanka from the beneficiary list**

Initially Sri Lanka applied for the GSP plus in 2005 and again the government of Sri Lanka sent an application to extend this benefit in 2008. The EU decided to extend this benefit from January 2009. Though there were some barriers against Sri Lanka to grant this privilege again. During the investigation they have recovered that Sri Lanka was incorporating with three (3) human rights conventions (Abayagunawardana, 2015).

1. International convention on civil and political rights (ICCPR)
2. The convention against torture (CAT)
3. Convention on the rights of the child (CRC)

Because of incorporation with these 3 conventions the EU decided that to eliminate Sri Lanka from the beneficiary list. The main reason for this disqualification was the civil war against terrorism which was continuing in Sri Lanka during that period. Hence they decided Sri Lanka was incorporated with these 3 human rights conventions. Secondly, as a result of become an “upper – middle” income country, they consider Sri Lanka is still not a vulnerable country furthermore. Finally, they informed to all beneficiaries that if they could not be able to continue this process of tariff preference due to the economic recession of some EU countries which occurred in nearly 2008-2009, beneficiaries must ready to survive without the tariff preference and those are the basic reasons for the elimination of Sri Lanka from GSP plus tariff preference system in 2009.

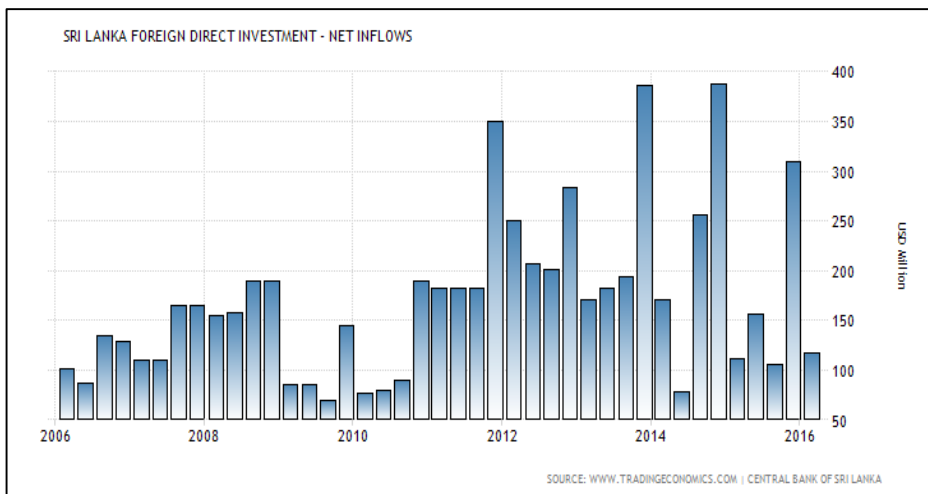
### **Sri Lankan international trade after the elimination of GSP plus**

With the elimination of the benefit Sri Lankan exporters could not be able to export their product on lower price rates because there is no more any tariff preference regarding Sri Lankan exports which export to the EU market. It was a challenge for all of our exporters to compete with other international rivals. Therefore, the business environment should need to change and be more efficient to make an intense competition to other rival exporters.

During that process initially, our exporters and investors could be able to

build a stable situation in the export market after the civil war period of Sri Lanka from 2009. And also business environment of the Sri Lanka has developed during the post war period due to political and social stability in the country. Hence exporters could be stable in the foreign market as before, though we did not have the GSP plus benefit. Then during the post war period lots of foreign investors arrived and invest in the country since their reliability had improved about our business environment. Furthermore, foreign reserves of Sri Lanka has increased gradually with in this period. It was a huge advantage for our exporters and investors. Then as a result of low rate of interest rates the demand for business loans has increased. As this reason investment in the business sector has increased rapidly.

Figure 02 : Gradual increment of foreign direct investment (FDI) after 2009

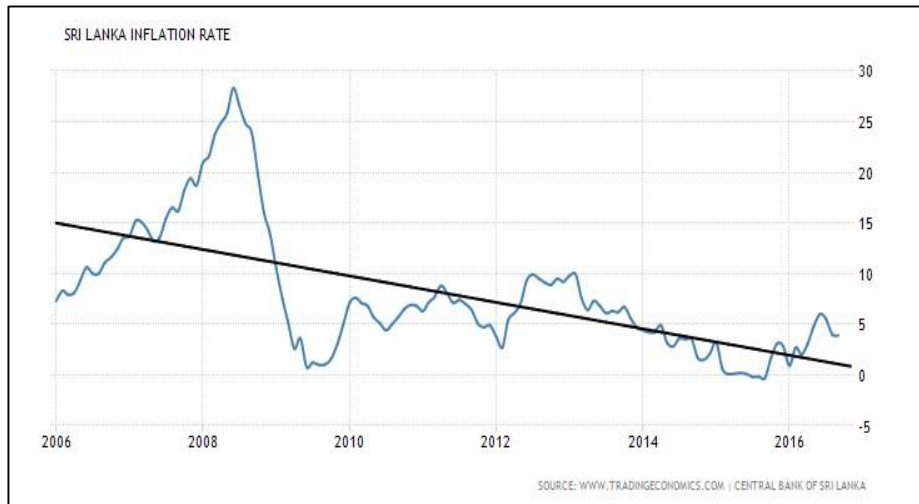


Source: [www.tradingeconomics.com](http://www.tradingeconomics.com) Central Bank of Sri Lanka

This graph shows the gradual increment of foreign direct investment (FDI) after 2009 and it was a privilege to continue the stability in the international market without having any tariff preference. Due to the political stability during the post war period, Sri Lanka has built a good reputation among other countries. Therefore our exporters could be able to increase their efficiency by improving the diversification of export products and it helped to increase the supply of exports to the foreign market regularly. As a result of reduction of the inflation rate after 2009 producers could be able to charge a lower price on exports (ආර්ථික විද්‍යා, 2009). For an example in 2008 rate of inflation was 22.6% and in 2009 it was 3.4%. From 2009 the rate of

inflation has reduced gradually as follows,

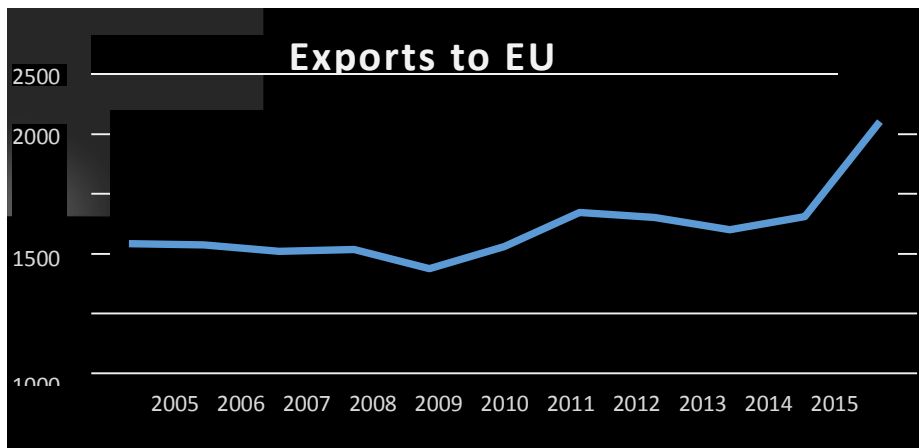
Figure 03 : Sri Lanka Inflation rate



Source: [www.tradingeconomics.com](http://www.tradingeconomics.com) | Central Bank of Sri Lanka

Then the export income and the quantity of export to the EU market has also increased gradually from mid of 2009 as a result of those above mentioned factors as follows (ආර්ථික විද්‍යා, 2009).

Figure 04: Sri Lankan Export to EU



Source: European Union, Trade in goods with Bolivia European Union, Trade with Bolivia Imports 2013 Exports 2013

The above facts and figures clearly show that the export sector of Sri Lanka



did not fail by elimination of the GSP plus benefit. However there were some circumstances to compete with other beneficiaries who have the tariff preference with higher quality and due to the political stability during the post war period, low rate of interest, low rate of inflation and increment of FDI helped us to survive in the international market without any tariff preference. Similarly with the appointment of the new government discussion about the GSP plus benefit began to re-new. It will be an ideal opportunity for our exporters to enhance their production and profit again with low price rates. Though it is very clear that we must not depend only on this benefit because of the uncertainty of the benefit and the dependency on market forces of few developed countries. Therefore we need to use this benefit only as a tool to manage the international market and we must have a widely diversified export range with Sri Lankan brand which are unique for us. For that we can,

1. Use a more developed technology for the production process.
2. Improve the quality of products through improvement of efficiency and productivity of labors.
3. Improve the diversification of product range furthermore.
4. Develop economic infrastructure facilities furthermore.
5. Both government and private sectors need to be more organized.

## **Conclusion**

According to this analysis it reveals that the GSP plus is a very important tool in determining trade share of the international market. It shows both advantages and disadvantages. Since these kinds of systems of tariff preferences usually act as indirect market invaders in the global economy, the GSP could use only as an alternative tool to compete with other rivals. Therefore it is necessary to develop our own stability in the international market to get the maximum benefits from foreign trade.

## Reference

Abayagunawardana, V. (2015), “*GSP plus international conventions and Sri Lanka*”, <http://www.dailymirror.lk/68777/gsp-international-conventions-and-sri-lanka>, viewed on 28 October 2016.

Central bank of Sri Lanka (2009), “*An Analysis of the GSP+ Scheme and Sri Lanka -from a Risk Management Perspective*”, [www.cbsl.lk/pics\\_n\\_docs/02\\_prs/\\_docs/speeches/presentation\\_20091029e.pdf](http://www.cbsl.lk/pics_n_docs/02_prs/_docs/speeches/presentation_20091029e.pdf), viewed on 29 October 2016.

Central Bank of Sri Lanka, [www.tradingeconomics.com](http://www.tradingeconomics.com)| Central Bank of Sri Lanka, viewed on 29 October 2016.

Figures, K. (2014). “*European Union , Trade in goods with Bolivia European Union , Trade with Bolivia Imports 2013 Exports 2013*”, 1-12.

The Island Online, “*GSP-Plus removal ‘will raise many issues for EU in global trade debate’*”,

<http://www.island.lk/2010/03/12/business6.html>, viewed on 29 October 2016.

විදුදැය ආර්ථික විද්‍යා , “*GSP+ ගැන මහ බැංකු අධිපති පැහැදිලි කරයි*” (2009), විදුදැය ආර්ථික විද්‍යාල 2009 නොවැම්බර්, 04 කලාපය, 02 කාණ්ඩය, ශ්‍රී ලංකා වරලත් ගණකාධිකාරවරුන්ගේ ආයතනය.