

THE EURO AND ITS IMPLICATIONS ON SRI LANKA'S EXPORT SECTOR

IMPLICATIONS OF THE EURO ON SRI LANKAN TRADE

Introduction

Exports play a strategic role in the economic development process of Sri Lanka. The export sector consists of over 3000 exporters. There are also numerous indirect exporters who supply goods and services to direct exporters. The export sector contributed around 30% to the Gross Domestic Product in 1998. Total exports have increased from Rs. 273.7 Bn in 1997 to Rs. 306.32 Bn in 1998, registering a 12% growth rate. These facts would indicate the importance of the export sector to the economy of Sri Lanka.

The creation of the Euro, one of the major developments in the international trade will not only have an impact on European Union (EU) nations themselves, but will also affect the world economy as a whole. Considering the size of the Euro region and its trade with the rest of the world, the Euro will become considerably more important in international trade at the turn of the next millennium. Sri Lanka will also be influenced by the Euro, as the EU is Sri Lanka's largest trading partner.

A destination analysis of Sri Lanka's exports reveal that the North American Free Trade Area (NAFTA) and the EU together import more than two thirds of merchandise exports of Sri Lanka, which is an indication of the vulnerable position of the country's exports to changes in these economies. Total trade with the EU region constitutes more than 20% of the total foreign trade of Sri Lanka. Exports to this region account for more than 27% of the country's total exports, which amounted to Rs. 82 Bn in 1998. Garments, diamonds, tea and rubber goods are the major product categories exported to this region from Sri Lanka. Garments alone contributed more than 50% of the total exports to this region. It is evident then that one cannot afford to ignore the possible implications that the advent of the Euro may hold for the Sri Lankan economy.

Table 1 : Sri Lanka's Trade with the Euro Region

(As a Percentage of Total)

	1997			1998		
	Exports	Imports	Total Trade	Exports	Imports	Total Trade
EU	29.6	16.5	23.8	27.2	17.1	20.4
- Euro Region	17.2	9.9	14.0	15.1	10.8	12.0
- Non-Euro	12.4	6.6	9.8	12.1	6.3	8.4
NAFTA	37.6	4.9	20.7	41.2	5.2	20.3
ASEAN	1.6	7.8	5.4	1.5	9.0	5.4
NICs	3.9	26.0	17.3	2.9	26.4	15.1
Middle East	7.2	9.0	8.8	8.9	6.3	7.1
Japan	5.0	8.2	7.3	4.1	9.4	6.7
China	0.2	2.9	1.8	0.3	3.8	2.2
India	0.9	9.5	6.1	0.8	9.2	5.1

Source : Central Bank of Sri Lanka.

By adopting a common currency the 11 Euro countries are opening up a massive market with vast trade opportunities within the region and the rest of the world. The elimination of exchange risks within the Euro area will boost market transparency on the money, bond and stock markets. These developments in the Euro area is

expected to have significant implications particularly in prices, in supplier relationships and international organisation, investments and output within the region and the world. At the beginning of the next millennium, the Euro-area is expected to emerge as the world's second largest market. The higher demand generated within the Euro area will no doubt provide better trading opportunities for developing countries like Sri Lanka, which we must strive to capture.

The EU is one of the major trading partners of Sri Lanka. Elimination of exchange risk by introducing a single currency will make it more attractive for our business community to trade with the Euro area. Besides, the return from trading in the Euro as against trading with the dollar is also more advantageous as the exchange rate for Euro has currently been determined at Rs. 73.34.

Price transparency in a single currency is likely to narrow the differences between the prices paid for the same product in different countries. Therefore, the likely improvements in price transparency coupled with the reduction in transaction costs due to elimination of risk would lower the trading costs to our business sector.

It is expected that there would be higher growth in the Euro area under the single currency regime. These developments would have a spill over effect of higher investment by Euro nations outside the Euro area from which Sri Lanka can benefit.

The low long-term interest rates in this region would imply a low global interest rate structure, especially in industrialised countries. This will enable developing countries to borrow in international capital markets at low interest rate. This could also assist investment in Sri Lanka as we are geared to tap the international capital markets for domestic investment.

On the negative side, the arrival of a new currency will mean adjustments by every business operating in the world. Therefore, there would be a cost involved in training staff, converting machines and computer programmes to Euro compatibility. Besides it would take time before the full benefit can be reached.

Conclusion

The introduction of the Euro is one of the major developments in international trade. By eliminating distortions and differences that were hidden by currency fluctuations, EMU will create an environment conducive for business. These developments may lead to lower exchange risk and transaction costs as well as to better price transparency in the Euro area, which is one of our major trading partners. These factors will help our business sector in their trade and economic relations with Euro nations.

Table 2 :

Direction of Trade - Sri Lanka {(1997 - 1998) - (Rs. Mn.)}

Group of Countries	1997			1998		
	Exports	Imports	Total	Exports	Imports	Total
EU	81,112	57,049	138,161	83,582	64,868	148,450
Euro	47,124	34,408	81,532	46,384	41,103	87,397
Austria	354	403	757	491	1,177	1,668
Belgium-Luxembourg	11,601	8,105	19,706	10,033	8,678	18,711
Finland	841	1,009	1,850	447	692	1,139
France	6,028	3,014	9,042	6,529	4,718	11,247
Germany.	13,566	10,819	24,385	14,980	13,088	28,068
Ireland	651	405	1,056	770	455	1,225
Italy	4,387	4,842	9,229	4,378	5,370	9,748
Netherlands	8,074	4,719	12,793	6,774	6,192	12,966

Portugal	238	58	296	314	53	367
Spain	1,384	1,934	2,418	1,668	590	2,258
Non-Euro	33,988	22,641	56,629	37,198	23,855	61,053
Denmark	718	1,638	2,356	800	1,348	2,148
Greece	641	91	732	697	71	768
Sweden	1,638	4,254	5,892	1,444	2,749	4,193
United Kingdom	30,991	16,658	47,649	34,257	19,687	53,944
NAFTA	103,174	17,022	120,196	127,948	19,774	147,722
Canada	3,291	3,240	6,531	3,920	2,685	6,605
Mexico	1,583	2,773	4,356	1,939	2,264	4,203
U.S.A.	98,300	11,009	109,309	122,089	14,825	136,914
ASEAN	4,396	27,138	31,534	4,533	34,384	38,917
Indonesia	415	7,867	8,282	270	11,787	12,057
Malaysia	1,299	9,816	11,115	748	12,420	13,168
Philippines	699	410	1,109	899	754	1,653
Thailand	1,983	9,045	11,028	2,616	9,423	12,039
Middle East	19,876	31,130	51,006	27,275	24,051	51,326
CIS Countries	10,073	893	10,966	9,516	1,148	10,664
NICs	10,563	90,030	100,593	8,823	100,497	109,320
Taiwan	1,330	21,953	23,283	932	24,457	25,389
Hong Kong	3,200	24,265	27,465	3,376	26,546	29,922
S. Korea	2,624	26,939	29,563	1,704	29,413	31,117
Singapore	3,409	16,873	20,282	2,811	20,081	22,892
Japan	13,815	28,275	42,090	12,669	35,903	48,572
China	464	10,014	10,478	1,015	14,623	15,638
India	2,582	33,023	35,605	2,434	34,837	37,271

Source : Central Bank of Sri Lanka.

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