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Strategic Analysis for Asia

# **Sri Lanka's Export Problem**

**Not Concentration, but Composition**

**ECONOMICS**

**August  
2017**

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## **Not Concentration, but Composition**

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## 1. Introduction

Reviving exports has been a key policy priority of the government since it came into power in 2015. The government aims to increase Sri Lanka's exports from USD 10.5 billion in 2016 to USD 18 billion by 2020.<sup>1</sup> The country's exports were stagnant in dollar terms from 2011-2016. Exports stood at 12.7% of GDP in 2016 – a significant drop from 33.3% of GDP in 2000.

Sri Lanka's exports are heavily concentrated on a few markets and a few products. The government's recognition of export diversification as an important policy strategy to revive exports, indicates that both market and product concentration are seen as critical bottlenecks in this regard.<sup>2</sup>

This report compares and contrasts Sri Lanka's export product and market concentration and its export composition against that of the world and selected Asian economies. The objective of this brief analysis is to understand where Sri Lanka stands in the world and in comparison to its neighbours that have performed well in terms of export concentration and composition.

The countries selected for comparison in this report are all Asian economies that were among the top 25 exporters in the world in 2016. Three of the selected markets - South Korea, Singapore and Japan - are high-income countries, while the other three are middle-income countries. Among these middle-income economies, Thailand and Malaysia are upper middle-income, and Vietnam is lower middle-income, like Sri Lanka. The size of these countries in terms of GDP, land and population varies significantly. Yet, as set out in this report, trade statistics reveal common features among these countries in terms of market concentration and composition.

**Export concentration** refers to the dependence of export earnings on specific markets and products. Market concentration is expressed as a percentage of exports that depend on a given number of markets or a given number of products. For example, 44% of Sri Lanka's exports are concentrated in three markets. **Export composition** refers to the makeup of markets and products that a country's exports are concentrated in. For example, the three key markets that account for 44% of Sri Lanka's exports are the USA, UK and India.

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<sup>1</sup> Lanka Business Online, "Sri Lanka cuts export earnings target to 18 billion by 2020", 12 July 2017, Available at: <http://www.lankabusinessonline.com/sri-lanka-cuts-export-earnings-target-to-usd18bn-by-2020/>.

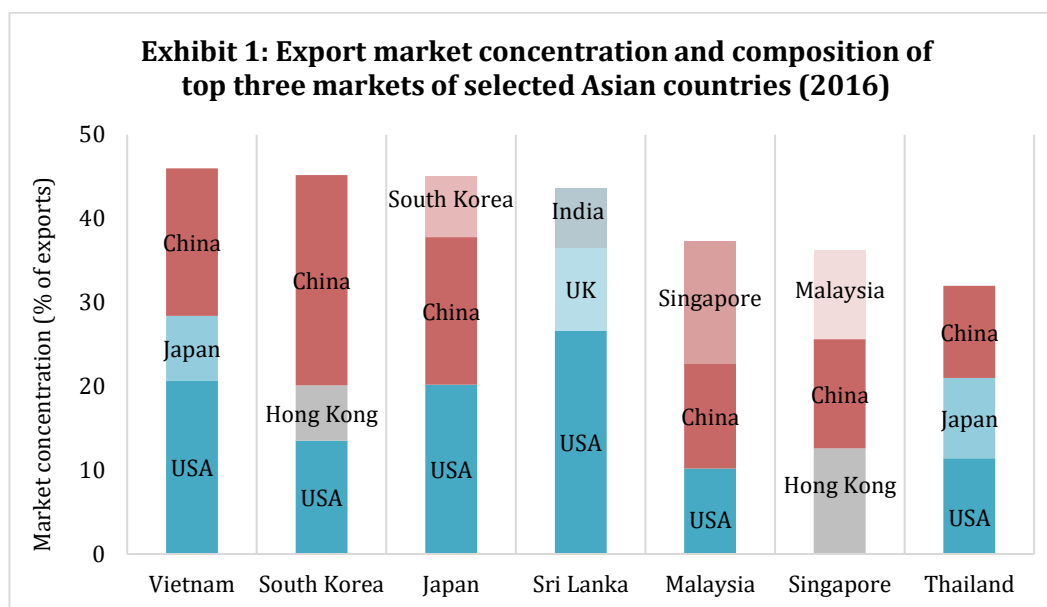
<sup>2</sup> Ministry of Development Strategies and International Trade, Policy objectives (2016). Available at: <http://modsit.gov.lk/policy-objectives.html>.

This analysis reveals the following important insights about Sri Lanka's export problem:

- The reliance of exports on a few products and a few markets is not unique to Sri Lanka. The exports of Asian countries selected for the analysis also depend heavily on a small number of markets and products. The export success of these selected Asian economies indicates that a high degree of export concentration does not necessarily cause sluggish export performance (see Exhibits 1 and 6).
- The world market for exports is also heavily concentrated in a few markets and few product categories. The heavy concentration in both export destinations and products of the selected Asian countries corresponds to the concentration in the world market (see Exhibits 3 & 7).
- Sri Lanka's export structure differs from that of the world and the other Asian countries in its composition of markets and products, not in their concentration (see Exhibits 1 & 6).
- World trade has shifted towards Asia between 2001-2016. The market composition of Asian countries has shifted in line with the world market trend. However, Sri Lanka's exports fare poorly in leading Asian markets and continue to be overly dependent on few leading Western markets (see Exhibits 4 & 5).
- Sri Lanka's variance with world trends is particularly striking in terms of product composition. The country's top two exports are not even among the top ten products traded in the world. In contrast, the top two exports of the Asian countries selected for this analysis fall within the top five product categories traded in the world.
- This analysis indicates that Sri Lanka's export problem may not necessarily be in the extent of its product and market concentration but rather their composition – the particular markets and product categories in which the concentration persists.

## 2. Export Market Concentration and Composition

### 2.1. Market concentration: Sri Lanka is not an outlier



Source: International Trade Centre (2016)<sup>3</sup>

The market concentration measured in terms of the percentage of exports that goes to the leading three markets of the selected Asian countries and Sri Lanka is shown in Exhibit 1. The Exhibit indicates that the exports of all these countries, including Sri Lanka, are highly concentrated in a few markets. Three of the selected markets have high levels of concentration of over 40% like Sri Lanka; and over 30% of the exports of the other three countries are also concentrated in just three markets. As such, Sri Lanka is not an outlier in terms of depending on a few markets to generate a large share of the country's export revenue.

### 2.2. Export concentration of countries reflects global trends

The world market for exports is heavily concentrated on a few countries. According to the Trade Map of the International Trade Centre, in 2016 there were 228 trading nations that imported goods to the combined value of USD 16 trillion. Five countries alone accounted for 38% of the total world imports in 2016 (see Exhibit 2), and 20 out of the 228 accounted for 72% of the world market for imports. The remaining 96% of trading nations accounted for less than one-third of the world market. Thus, the concentration of a country's exports in a

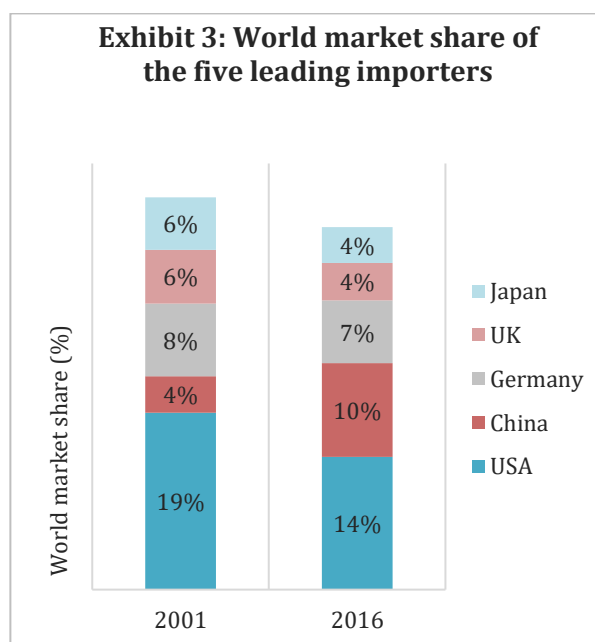
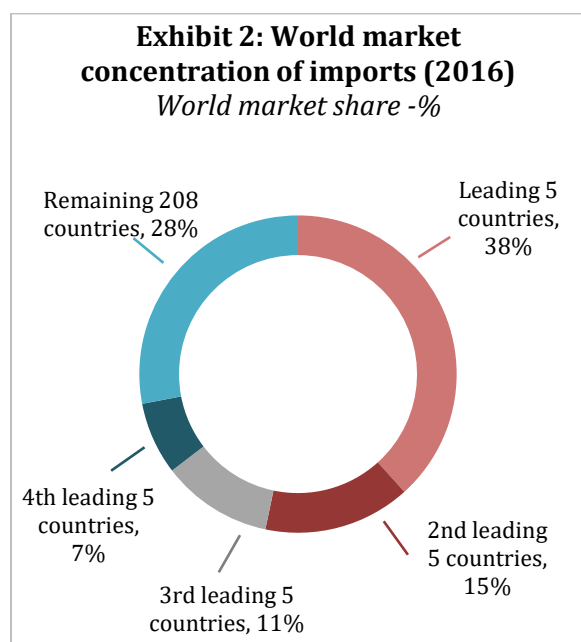
<sup>3</sup> International Trade Centre, Trade Map (2016) Available at: <http://www.trademap.org>

few markets is in fact a reflection of the global import concentration of products in a few markets.

While the skewed nature of world trade has remained the same over the years, there have been internal shifts in its makeup since the turn of the century. The notable change in composition has been China's increasing share: China moved up four places to become the world's second largest importer with a market share of 9.9% in 2016 compared to 3.9% in 2001 (see Exhibit 3). Chinese imports grew over six-fold from USD 243 billion to USD 1,588 billion over this period.

The other notable shift has been the emergence of India as an important market for the world's exports. India moved up 11 places from 2001 to 2016 to become the 14<sup>th</sup> largest importer in the world (see Annex 1). India's imports grew over seven-fold during this period from USD 50 billion to USD 357 billion, and the country's world market share increased from 0.8% to 2.2%.

Both China and India were the only two economies of the top 20 trading nations to experience annual average growth rates of over 20% during 2001-2016 in comparison to a 10% average growth of world imports. Growth in world demand for exports has considerably dampened in the last decade, with an average of only 1.4% between 2007 – 2016. However, imports to China and India have remained relatively robust, growing at over 5%.



Source: International Trade Centre (2016)

Largely aided by these two Asian giants, the share of Asian imports within the top 20 countries has increased from 25% to 35% between 2001 and 2016. These shifts indicate that while a larger share of world trade continues to be concentrated in the West, this share has declined significantly.

### **2.3. Market composition: Limited success in Asia makes Sri Lanka different from the rest**

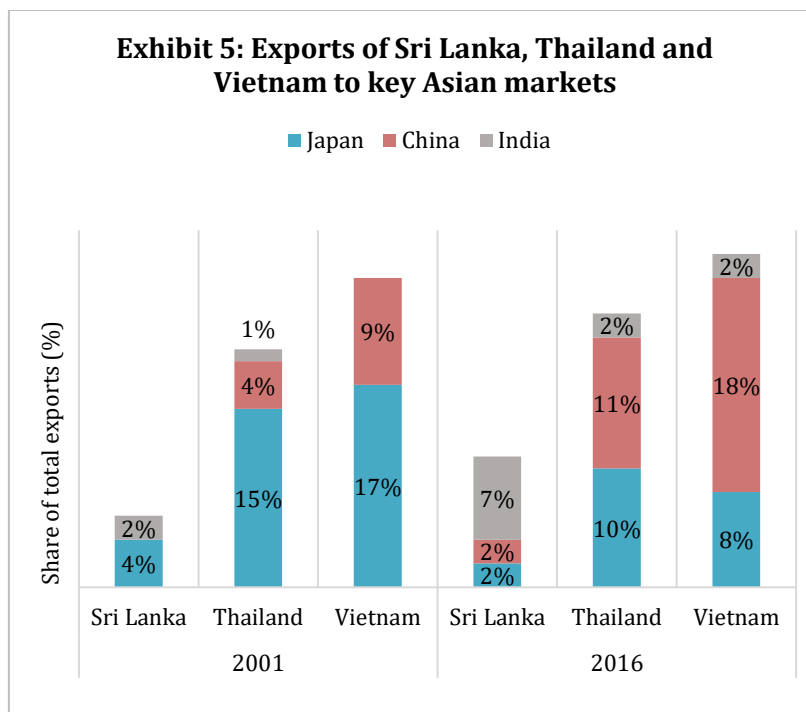
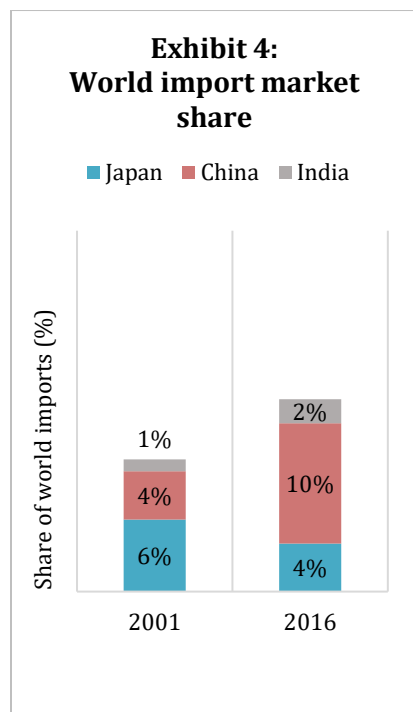
While Sri Lanka's level of market concentration is similar to that of the other countries, China emerges as the notable difference between the composition of Sri Lanka's top three export markets and that of the other selected Asian economies (see Exhibit 1). China is among the top three export markets of all the selected countries except Sri Lanka. While China accounted for over 10% of exports of these selected countries, it accounted for only 2% of Sri Lanka's exports in 2016 (see Exhibit 5).

Overall, Sri Lanka demonstrates limited success in exporting to key Asian markets: Japan, China, South Korea and Hong Kong. These four countries are among the top ten markets for exports in the world, accounting for 20% of the total value of the market (i.e. USD 3 trillion) in 2016. In contrast, these three countries accounted for only 6% of Sri Lanka's exports in 2016 (USD 619 billion). Sri Lanka's only success in Asia remains India (see Exhibit 5). While India has advanced rapidly as an important market for exports, it is currently ranked at 14, well below Japan, China, Hong Kong and South Korea (see Annex 1).

A detailed analysis of Sri Lanka's exports to key Asian markets with that of Vietnam and Thailand further confirms this trend (see Exhibits 4 and 5). The world market value of the three key Asian markets - Japan, China and India - increased fourfold from USD 644 billion to USD 2,552 billion between 2001-2016. Sri Lanka's share of exports to these three markets in 2016 was 11%, compared to Thailand's and Vietnam's share of 23% and 28%, respectively.

In addition to China, a notable difference in the composition of Asian markets that has an impact on Thailand, Vietnam and Sri Lanka is the role of Japan. Sri Lankan exports have barely made it into the Japanese market despite the country being a leading market for exports for decades. In comparison, Japan has remained a key market for the exports of Thailand and Vietnam (see Exhibit 5).

This analysis reveals that Sri Lanka has been out of sync largely in terms of market composition rather than in terms of market concentration, in comparison to the world market and selected Asian countries. This is largely due to the limited success of Sri Lankan exports in Asian markets.



Source: International Trade Centre (2016)

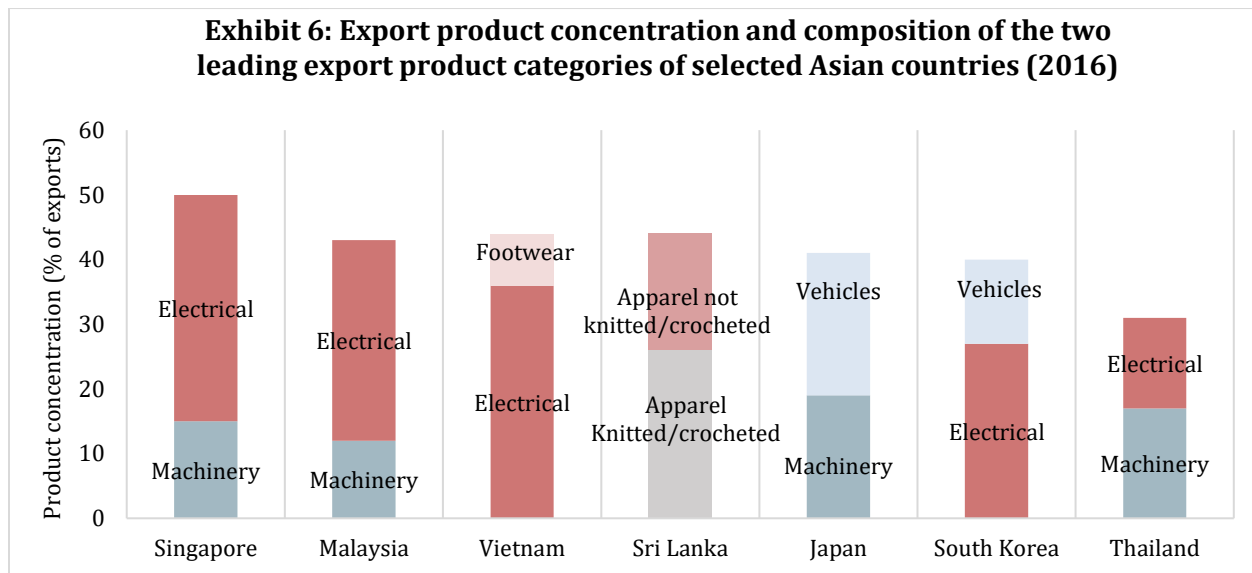
### 3. Export Product Concentration and Composition

#### 3.1. Product concentration: Sri Lanka is not an outlier<sup>4</sup>

This section relies on the harmonised system of classification (HS) of products developed by the World Customs Organization to assess the product concentration and composition of exports. The broadest categorisation of products under the HS classification (at 2-digit level) aggregates all products traded in the world into 97 categories. Exhibit 6 shows the level of export concentration of the largest two product categories exported out of the 97 product categories for selected Asian countries, including Sri Lanka. The data reveals that a heavy reliance on a few product categories is not unique to Sri Lanka and that other countries also show similar trends. Compared to Sri Lanka, some of the other Asian economies identified as export success stories, such as Singapore and Vietnam, show even higher levels of product concentration.

<sup>4</sup> This analysis excludes trade in mineral fuels such as petrol and gas which fall under HS27.

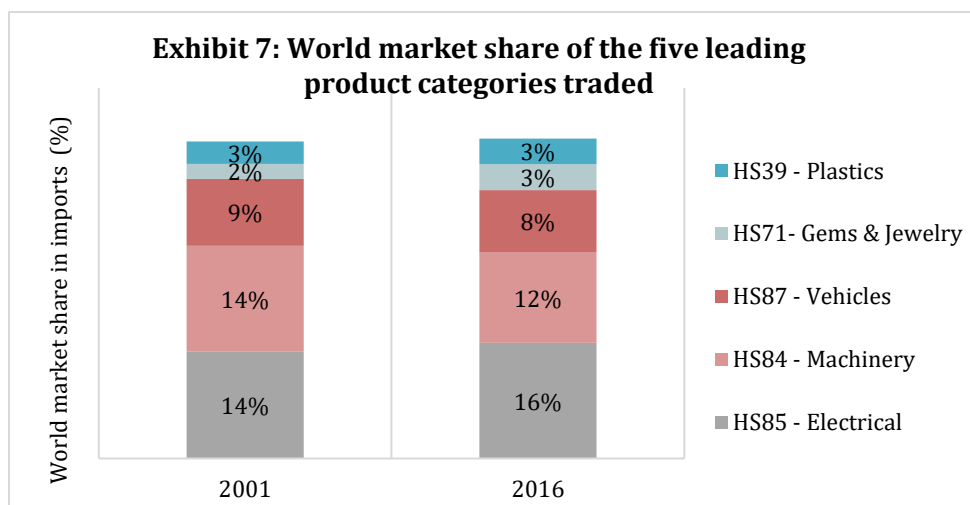




Source: International Trade Centre (2016)

### 3.2. Product concentration is a global feature

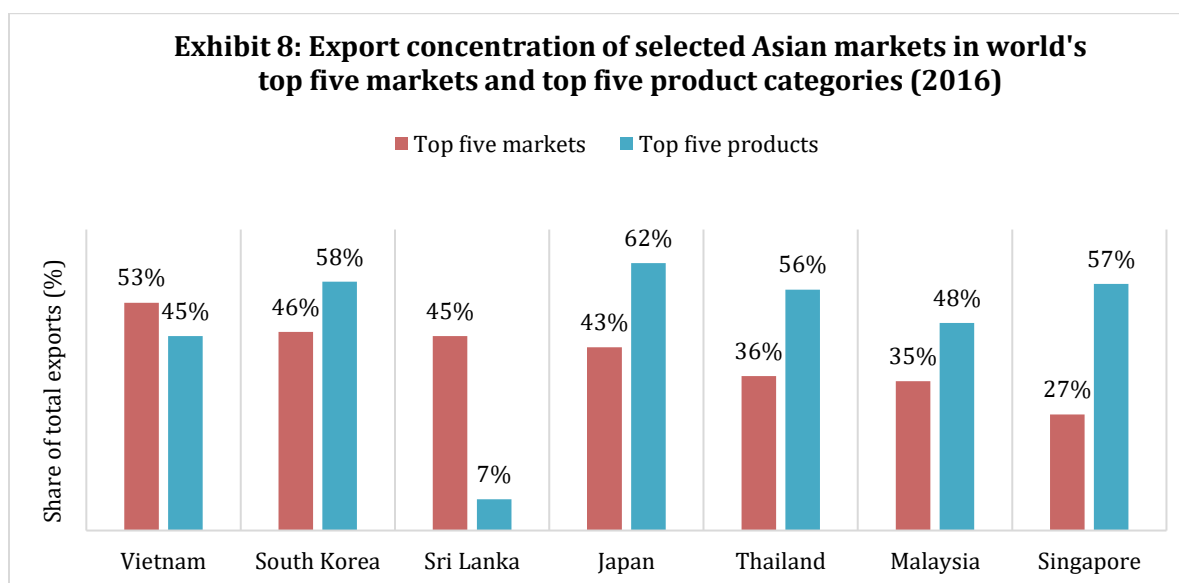
The world market is heavily concentrated on a few products categories (see Exhibit 7) as it is on a few countries. The top five categories of exports in the world account for 43% of the total world market. Therefore, it is to be expected that a country's exports would be concentrated in these products that are mostly in demand in the world. The levels of concentration and composition of key product categories traded in the world have remained the same over the years.



Source: International Trade Centre (2016)

### 3.3. Product composition: Sri Lanka is a clear outlier

Unlike in the case of export markets, where a significant portion of Sri Lanka's exports end up in leading world markets, only a small portion of the country's exports belongs to the top five product categories traded in the world (see Exhibit 8). While the five leading product categories account for 43% of the total world market, only 7% of Sri Lanka's exports belong to the top five traded in the world. In contrast, over 40% of the exports of all the other selected Asian countries fall within these top five product categories.



Source: International Trade Centre (2016)

In terms of product composition, Sri Lanka's two leading exports are not among even among the **top ten** product categories traded in the world (see Annex 2 for product details). In contrast, the two key export product categories of all the other selected Asian countries fall within at least one of the **top five** product categories traded in the world.

Sri Lanka's two key export product categories (HS 61 and 62 – Apparel) that accounted for 44% of the country's exports in 2016 constituted only 2% of the world market. In contrast, the two leading exports of the other selected Asian economies belonged to product categories that accounted for over 20% of the world market (see Exhibits 6 and 7).

### 3.4. Is product composition a factor that determines Sri Lanka's market composition?

The heavy reliance of Sri Lanka's export products on Western markets such as the USA and the UK is mainly the result of the Sri Lanka's product composition. These two markets accounted for 36.5% of Sri Lanka's total exports in 2016. Out of total exports to these two countries, 75% to the USA and 79% to the UK comprised of apparel exports (HS 61 and 62). These markets together accounted for 64% of Sri Lanka's total apparel exports in 2016.

The value of the world market for apparel in 2016 was USD 396 billion. As shown in Exhibit 9, the UK and the USA are among the five leading destinations for apparel exports, accounting for 27.4% of the world market. The data clearly shows that the heavy reliance on the USA and the UK is driven by Sri Lanka's export composition.

**Exhibit 9: Import demand for the two key export products (HS 61 & 62 – Apparel) of Sri Lanka in selected markets (2016)**

Country	Share of world apparel imports	Value of the apparel imports (USD Bn)	Apparel as a share of total imports to the country
USA	21.2 %	84.0	3.7 %
UK	6.2 %	24.5	3.9 %
Japan	6.6 %	26.2	4.3 %
China	1.5 %	5.9	0.4 %

Source: International Trade Centre (2016)

Exports to Japan however, demonstrate that Sri Lankan exports have faced challenges in Asia, even when there is a large market for the country's key export products. For example, Japan is one of the top five markets in the world for apparel. However, the country accounted for only 0.9% of Sri Lanka's total apparel exports in 2016. China accounted for 1.4% of Sri Lanka's total apparel exports in the same year and remains a relatively small market for apparel, both in terms of share and value.

Thus, while product composition explains the heavy concentration in the USA and the UK, it does not necessarily explain Sri Lanka's limited success in terms of accessing Asian markets, particularly Japan. This analysis indicates that in addition to product composition, other factors seem to have played a role in limiting the success of Sri Lankan products in Asian markets. Although this report does not delve into identifying these factors, a solid understanding of these issues will be key to succeeding in these markets.

## Annex 1

### Top 20 importers in the world (2016)

Importing country	Share of world imports (2001)	Share of world imports (2016)	Growth in imports (2001 -2016)
United States of America	18.7 %	14.0 %	7.4 %
China	3.9 %	9.9 %	23.2 %
Germany	7.7 %	6.6 %	9.1 %
United Kingdom	5.7 %	4.0 %	6.6 %
Japan	5.5 %	3.8 %	6.3 %
France	4.6 %	3.5 %	7.4 %
Hong Kong, China	3.2 %	3.4 %	11.7 %
Netherlands	3.1 %	3.1 %	11.1 %
South Korea	2.2 %	2.5 %	12.5 %
Italy	3.7 %	2.5 %	6.2 %
Canada	3.5 %	2.5 %	6.9 %
Mexico	2.7 %	2.4 %	9.7 %
Belgium	2.8 %	2.3 %	8.5 %
India	0.8 %	2.2 %	24.2 %
Spain	2.5 %	1.9 %	7.7 %
Singapore	1.8 %	1.8 %	10.4 %
Switzerland	1.3 %	1.7 %	13.8 %
Taipei, Chinese	1.7 %	1.4 %	8.9 %
United Arab Emirates	-	1.3 %	N/A
Turkey	0.7 %	1.2 %	19.0 %
<b>Total (top 20)</b>	<b>76.1%</b>	<b>72.0%</b>	
Remaining countries	23.9%	28.0%	

Source: International Trade Centre (2016)

## Annex 2

### Top product categories traded (2016)

Rank	HSC	Product Description	Share of world imports (2016)
1	85	Electrical machinery and equipment and parts thereof; sound recorders and reproducers, television ...	16%
2	84	Machinery, mechanical appliances, nuclear reactors, boilers; parts thereof	12%
3	87	Vehicles other than railway or tramway rolling stock, and parts and accessories thereof	8%
4	71	Natural or cultured pearls, precious or semi-precious stones, precious metals, metals clad ...	3%
5	39	Plastics and articles thereof	3%
6	90	Optical, photographic, cinematographic, measuring, checking, precision, medical or surgical ...	3%
7	30	Pharmaceutical products	3%
8	29	Organic chemicals	2%
9	99	Commodities not elsewhere specified	2%
10	72	Iron and steel	2%
11	73	Articles of iron or steel	2%
12	88	Aircraft, spacecraft, and parts thereof	2%
13	94	Furniture; bedding, mattresses, mattress supports, cushions and similar stuffed furnishings; ...	1%
14	62	Articles of apparel and clothing accessories, not knitted or crocheted	1%
15	61	Articles of apparel and clothing accessories, knitted or crocheted	1%
16	38	Miscellaneous chemical products	1%
17	40	Rubber and articles thereof	1%
18	76	Aluminium and articles thereof	1%
19	48	Paper and paperboard; articles of paper pulp, of paper or of paperboard	1%
20	44	Wood and articles of wood; wood charcoal	1%
		<b>Total (top 20)</b>	<b>66%</b>
		Remaining product categories	34%

Source: International Trade Centre (2016)