

Sri Lanka's Apparel and Tea Exports: Performance Outlook

By Jayani Ratnayake

The latest available export results for August 2016 show that for the first time this year exports recorded a year-on-year growth, reversing an 18-month decline. According to export statistics released by the Central Bank Sri Lanka's cumulative export earnings during the first 8 months of 2016 dropped by 4.1% on a year-on-year basis, but August recorded a growth of 8%. This week's TIPS column looks at the export performance of two key export products of Sri Lanka - tea and apparel - in 2016, and industry experts' views on the outlook for the near term.

Apparel Sector – Export Performance

Apparel exports contracted by 1.2% year-on-year during the first ten months of 2016. The two major export markets - EU (42.3%) and USA (45.8%) - accounted for a share of 88.2% of total apparel exports of Sri Lanka in the period under review. Cumulative exports to USA grew at 6.6% year-on-year retreating to a single digit growth rate from the vibrant 14.7% and 14.5% growth rates recorded in 2014 and 2015 respectively. Exports to EU contracted substantially by 9.8% as uncertainty loomed over the EU market with the Brexit vote in the UK and elections in other European countries like Italy and Austria further aggravating an already weak market. Sri Lanka's EU market share has witnessed a steady decline since the withdrawal of the EU GSP-plus from 50.1% in 2012 to 42.3% by 2016.

Apparel Sector – Near-term Outlook

Following the Sri Lankan Prime Minister's visit to Brussels in late October 2016, it was announced that Sri Lanka's application to regain GSP Plus is currently going through a technical assessment process. Industry leaders the author interviews remain hopeful about Sri Lanka's ability to regain the GSP-plus concession. Meanwhile in the US, Congress has raised a red flag on the Trans-Pacific Partnership (TPP) agreement, stating that the USA will not go ahead with the deal, even before the President-Elect Donald Trump takes office in January 2017. Sri Lanka competes in the US market for the same apparel products with TPP partners like Vietnam, Mexico and Peru and if the deal was struck, Sri Lanka's apparel exports would have been affected severely by losing out to Vietnam. The stalling of the TPP deal brings fresh hope for the Sri Lankan apparel industry. Yet, some industry experts commented that the stalling of the TPP deal will only give Sri Lanka temporary breathing space, as countries like Vietnam have already

started making significant domestic reforms to improve their competitiveness. Sri Lanka will need a proactive strategy to improve competitiveness and expand market access to stay ahead of the game.

Tea – Export Performance

Cumulative tea export earnings during the first 9 months of 2016 recorded a 2.1% marginal growth from the same period last year, but this was a significant 13.1% drop when compared to 2014 earnings. Weak export demand stemming from structurally low oil prices and macroeconomic instabilities in the Middle East and the Commonwealth of Independent States (CIS) including Russia (which accounts for about 63% of Sri Lanka's tea market) are the main factors for this sluggish export performance.

Tea – Near-term Outlook

In 2016 the tea industry faced significant headwinds from both the domestic and the global economy. Regional Plantation Companies (RPCs) are concerned about rigidities in domestic supply conditions. The serious shortfall in crops and the drop in production (-22% on YoY basis during first 10 months of 2016/2015) as a result of bad weather and the inability to fertilize due to the government ban on important weedicides (since April 2015) are critical challenges being faced by the industry. Moving forward, these are leading to actual costs being much higher and could be around LKR 550/- to 600/- per KG. Industry leaders anticipate a slight improvement in the Middle East, Russia and other CIS countries during the first half (H1) of 2017. The Russian market has started showing some signs of recovery with the Russian Ruble strengthening 20% against the US dollar, from the January 2016 low of USD/RUB 82.5 to 66 in late November. The price of Brent oil has increased approximately by 53% during same period. The Industry is also anxiously watching the developments in OPEC (with regard to a cut in production and a possible rise in prices), which will influence tea demand in Sri Lanka's key export markets. Even if global market conditions improve over H1 2017, supply rigidities will make it challenging for the domestic tea industry to reap the full benefits.

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