The asymmetry was the design

Sri Lanka's first bilateral free trade agreement, signed with India in 1998 and in force from 2000, and what twenty-five years of measured use say about tariff architecture

Country decision study | MacroLens Research | Independent desk research - not peer reviewed - not investment advice

Abstract

In December 1998 Sri Lanka signed its first bilateral free trade agreement, with India; it entered into force in March 2000. The architecture was deliberately asymmetric: the larger economy conceded faster, opening 1,351 tariff lines at zero duty immediately and completing its phase-out within three years, while Sri Lanka kept 1,180 lines on its negative list and phased its cuts over eight. Twenty-five years of official trade records show what the design bought. Sri Lankan exports to India rose from 49 million dollars in 1999 to over one billion in 2025, with roughly sixty percent using the agreement's preferences; Indian exports to Sri Lanka grew far larger while barely a tenth used preferences in 2025. A vanaspati surge, litigation in Delhi and a negotiated quota tested the treaty, which held. This case examines asymmetric trade architecture: what it delivered, where it stalled, what Sri Lanka can conditionally draw from it.

Why this case for Sri Lanka

This is Sri Lanka's own case, not a borrowed one. The Department of Commerce in Colombo describes the India-Sri Lanka Free Trade Agreement, signed on 28 December 1998 and in force from 1 March 2000, as the country's first bilateral free trade agreement. The baseline it started from was a trade lane running almost entirely one way: in 1999 Sri Lanka imported 512 million US dollars of goods from India and exported 49 million, a ratio of 10.5 to one, on the Indian High Commission's figures. The question the case asks is what a small economy's first preferential deal actually delivered across twenty-five years of measurement: how much of the export growth was real and used, how the agreement survived its first stress test, and why the deeper integration twice negotiated has never been signed. The answer matters now because the successor negotiation remained unresolved as of September 2025.

The starting point: a one-way trade lane

By the mid-1990s Sri Lanka had been unilaterally liberalizing since 1977, but unilateral openness bought no preferential access to anyone else's market. The regional route was stuck: the South Asian preferential framework that became SAFTA did not enter into force until 1 January 2006, eight years after the bilateral deal was signed. India was the obvious market - close, large and growing - but protected by some of the higher tariffs in Asia at the time, and the political relationship carried the weight of the 1987-1990 Indian military deployment. Trade between the two countries in 1999 was small and lopsided: about 560 million dollars in total, with India supplying more than ten dollars of every eleven traded. A bilateral agreement was therefore a deliberate political decision on both sides, not a technical afterthought (desk interpretation).

The decisions: sign, sequence, discipline

The first decision was to go bilateral while the regional track was stalled. The agreement was signed in New Delhi on 28 December 1998 and entered into force on 1 March 2000, six years before SAFTA added a regional layer on top of it.

The second decision was the architecture, and the architecture was asymmetric by design. India's tariff liberalization programme conceded faster and deeper: an immediate zero-duty list of 1,351 tariff lines on entry into force, a residual list of 2,799 lines at a 50 percent margin of preference deepened to 100 percent within three years, and a negative list of only 429 lines. Sri Lanka's schedule was slower and thicker-skinned: just 342 lines at zero immediately, 880 lines stepped from 50 to 70 to 90 to 100 percent over three years, a phasing-out list of 2,802 lines brought down over eight years, and a negative list of 1,180 lines - nearly three times India's. By 2003, on the Department of Commerce's own tabulation, India offered duty-free access on over nine-tenths of the lines it had scheduled. Sensitive items were handled inside the deal rather than excluded from it: letters of exchange of 2 February 2000 set quota arrangements for tea (15,000 tonnes at 7.5 percent duty) and garments (eight million pieces at zero duty), with quotas later covering pepper, desiccated coconut and vanaspati.

The third decision was to police origin rather than trust paper. The rules of origin require at least 35 percent domestic value addition on the FOB price (25 percent where Indian inputs are used, provided combined value addition reaches 35 percent), a change of tariff heading at the four-digit level, the final manufacturing process in the exporting country, and direct consignment.

The fourth decision was to discipline a surge instead of denying it. After an Indian notification of 18 March 2003 extended the 100 percent exemption to items including edible oils, Sri Lankan vanaspati - made from imported crude palm oil - flowed into India at volumes Indian producers put at 20,000 tonnes a month by mid-2005. Indian manufacturers sued, arguing in the Delhi High Court that hydrogenation could not meet the 35 percent value-addition rule. The dispute was settled inside the agreement's logic: in August 2005 India's agriculture and commerce ministers decided to cap duty-free vanaspati at 250,000 tonnes a year, a level Sri Lanka agreed to police, and India resolved to keep vegetable oils out of its future trade agreements. The court recorded the challenge in its judgment of 22 September 2005; the treaty absorbed the quarrel and continued.

The fifth decision was to attempt deepening, twice, and to stop twice. A Comprehensive Economic Partnership Agreement covering services, investment and cooperation was negotiated through roughly a dozen rounds from 2005, initialled by the two commerce secretaries in July 2008, and then shelved when President Rajapaksa's government declined to sign it at the Colombo SAARC summit days later, after domestic business groups and a nationalist coalition partner campaigned against it. A successor negotiation, the Economic and Technology Cooperation Agreement, resumed in October 2023 after a five-year pause and reached a fourteenth round in Colombo on 24-26 July 2024. India's commerce ministry reported in its 2024 year-end review that almost all chapters except some garment lines had been concluded; by September 2025 the talks stood at a standstill, with Sri Lanka yet to appoint a chief negotiator, the Daily Mirror reported. The same report records a 2025 Sri Lankan request, after new United States tariffs, to expand the agreement's garment quota from eight million to fifty million pieces, and India's position that such expansion belongs to the ETCA track.

The decision chain: dates

When	What happened
28 December 1998	ISFTA signed in New Delhi; the Department of Commerce records it as Sri Lanka's first bilateral free trade agreement
2 February 2000	Letters of exchange set quota arrangements for tea and garments
1 March 2000	ISFTA enters into force; India's immediate zero-duty list covers 1,351 tariff lines, Sri Lanka's 342
By 2003	India completes its phase-out: the 50 percent margin on 2,799 residual lines reaches 100 percent within three years
18 March 2003	Indian notification extends the 100 percent exemption to further items including edible oils (court record)
August 2005	India caps duty-free vanaspati imports from Sri Lanka at 250,000 tonnes a year; Sri Lanka agrees to discipline its exports
22 September 2005	Delhi High Court judgment records the Indian industry challenge to the FTA's edible-oil exemptions
1 January 2006	SAFTA enters into force, adding a regional layer over the bilateral pact
2008	Sri Lanka completes its eight-year phase-out; even two cement lines on its negative list end with reduced tariffs
July 2008	CEPA initialled by commerce secretaries; the planned signing at the 15th SAARC summit in Colombo is shelved days before
24-26 July 2024	Fourteenth ETCA round in Colombo; by September 2025 the talks stood at a standstill (press report)
FY 2025-26	Bilateral merchandise trade reaches about 7.1 billion US dollars (Indian figures)

Measured outcomes I: what the architecture delivered

The headline numbers are official on both sides. Total bilateral merchandise trade grew from 658 million dollars in 2000 to about 7.1 billion in FY 2025-26 (Indian Department of Commerce figures). Sri Lanka's exports to India rose from 49 million dollars in 1999 to 70 million in 2001, 559 million in 2005, 769 million in 2018 and 1,035 million in calendar 2025, on the Sri Lankan Department of Commerce's series; the Indian High Commission, citing the Export Development Board, records growth from 640 million dollars in FY 2020-21 to over 1.6 billion in FY 2025-26, with India now Sri Lanka's second-largest export market. Preference use on the Sri Lankan export side is substantial: 23 percent of exports to India entered under the agreement in 2001, a peak of 99 percent in 2003, and a band of roughly 55 to 68 percent ever since - 61.3 percent in 2025. The Indian High Commission also records cumulative Indian FDI in Sri Lanka above 2.8 billion dollars, citing the Central Bank of Sri Lanka's 2025 annual report. India's own trade ministry assessed that the agreement contributed significantly to the expansion of trade (attributed view). The counterfactual - what trade would have been without the agreement - cannot be measured from these series (desk interpretation).

Measured outcomes II: what the architecture did not do

The same official tables mark the limits. First, the asymmetry narrowed but did not close: Sri Lanka imported 4,335 million dollars from India in calendar 2025 against exports of 1,035 million, a deficit near 3.3 billion. The import-export ratio improved from 10.5 to one in 1999 to about 4.2 to one in 2025, but the lane still runs mainly one way. Second, preference use is lopsided: Indian exports to Sri Lanka almost never claim the preferences - never above 29 percent (2004), under 10 percent every year since 2015, and 9.4 percent in 2025. The Indian High Commission reads this as evidence that Indian goods compete in Sri Lanka without using the preferences; it also means the agreement's liberalization mattered mostly in one direction (desk interpretation). Third, the export basket that uses the agreement is narrow: in 2025 the single largest line was prawn feed at 126.4 million dollars, 19.9 percent of all exports under the agreement, followed by nuts, vegetable fats and beverage cans. Fourth, deepening stalled: the 2008 CEPA was initialled and never signed, and fourteen ETCA rounds, the last in July 2024, had produced no agreement by September 2025, leaving services and investment outside the architecture a quarter-century after the goods framework was built.

Transfer limits: what ISFTA does not prove

First, this is a two-country geometry that does not generalize: a small island beside a continental economy, with shipping costs low and business ties dense, is not a template for trade agreements generally (desk interpretation). Second, the preference margin erodes: SAFTA since 2006 and India's other agreements give rival suppliers their own access, so the 1998 advantage is not frozen in time. Third, the numbers come in two series - calendar-year Sri Lankan and fiscal-year Indian - and this case never mixes them within a single comparison. Fourth, low import-side utilization does not prove low value: Indian exporters may simply clear most-favoured-nation rates profitably, and the Sri Lankan revenue question sits outside the trade data. Fifth, attribution is bounded: the export growth coincides with the agreement, and both governments credit it, but no official series isolates the agreement's effect from everything else that changed after 2000.

Conditional lessons for Sri Lanka

These are design observations, not prescriptions.

1. Asymmetry is negotiable. The smaller partner obtained the faster schedule: India opened 1,351 lines at zero immediately and finished its phase-out in three years, while Sri Lanka sheltered 1,180 lines and took eight. A small economy that brings a credible long phase-out can buy early access with patience, not money (desk interpretation).

2. Measure use, not tariff lines. The agreement's test is its utilization columns: 61 percent of Sri Lankan exports claimed preferences in 2025, while 90.6 percent of Indian exports entered without using the agreement's preferences. A trade ministry that publishes these numbers annually, as Sri Lanka's does, can see its agreement working or idling in near real time (desk interpretation).

3. Quotas can be pressure valves, not admissions of failure. Tea, garments, pepper, coconut and vanaspati were kept inside the framework through negotiated ceilings; the vanaspati quarrel ended in a cap both sides policed rather than a rupture. Sensitive sectors need a managed middle state between free and forbidden (desk interpretation).

4. Signing is the easy stage; deepening is the political stage. Goods tariffs fell on schedule for eight years; services and investment have waited twenty-five. The 2008 pullback shows that an initialled text is not a policy until domestic constituencies are carried (desk interpretation).

5. Diversify within the door already open. A fifth of preference-using exports in 2025 was a single animal-feed line. The agreement's remaining value for Sri Lanka lies in widening the basket that actually uses it (desk interpretation).

Conclusion

The case's claim is narrow. Sri Lanka's first bilateral free trade agreement was built asymmetric, held to its schedules, absorbed a serious stress test in the vanaspati dispute, and coincided with a twenty-fold rise in exports to India between 1999 and 2025, of which a stable majority uses the preferences. What it has not done is equally measurable: the trade lane still runs mainly toward Sri Lanka, the using basket is narrow, and the deeper agreement initialled in 2008 remains unsigned while its successor negotiation stood at a standstill as of September 2025. The open question the case leaves is whether the politics that shelved CEPA will treat ETCA any differently.

Sources

The agreement and its schedules:

https://www.doc.gov.lk/index.php?Itemid=154&id=43&lang=en&option=com_content&view=article (Sri Lanka Department of Commerce: signing on 28 December 1998 as Sri Lanka's first bilateral FTA, entry into force 1 March 2000, full tariff liberalization programme, negative lists, TRQs, rules of origin, and the official ISFTA trade and utilization table 2001-2025)

https://www.eicindia.gov.in/WebApp1/resources/PDF/ISFTA.pdf (text of the agreement: Annexes A and B phase-out schedules, rules of origin including the 35 percent value-addition and change-of-tariff-heading criteria)

https://www.custada.in/document/document/Ntfn-26-01.03.2000-Indo%20Sri%20Lanka%20FTA.htm (Indian customs notification of 1 March 2000 implementing the concessions)

https://www.commerce.gov.in/international-trade/trade-agreements/india-sri-lanka-fta/minutes-of-the-meeting-on-tariff-rate-quota-arrangement-for-tea-and-garments/ (Indian Department of Commerce: letters of exchange of 2 February 2000 on tea and garment quota arrangements)

Bilateral trade and investment figures:

https://www.hcicolombo.gov.in/page/india-sri-lanka-economic-and-trade-engagement/ (Indian High Commission in Colombo: FY 2025-26 bilateral trade of 7.1 billion dollars, Sri Lankan export growth from 640 million dollars in FY 2020-21 to over 1.6 billion in FY 2025-26, India as Sri Lanka's second-largest export market per the Export Development Board, cumulative Indian FDI above 2.8 billion dollars per the Central Bank of Sri Lanka 2025 annual report, SAFTA in force 1 January 2006, ETCA fourteen rounds with the fourteenth on 24-26 July 2024)

The vanaspati dispute (contemporaneous press, flagged as advocacy-adjacent industry and official claims):

https://lawfyi.io/bhatinda-chemcials-ltd-and-ors-vs-union-of-india-uoi-and-ors-on-22-september-2005/ (Delhi High Court judgment of 22 September 2005: the 18 March 2003 notification's 100 percent exemption, the 35 percent value-addition challenge to vanaspati made from imported palm oil)

https://bilaterals.org/vanaspati-imports-from-lanka-may (August 2005: ministers decide the 250,000-tonne cap on duty-free vanaspati, Sri Lanka's agreement to discipline exports, India's decision to keep vegetable oils out of future FTAs)

https://bilaterals.org/interview-free-trade-hurting-india (July 2005: Indian industry claim of some 20,000 tonnes of vanaspati entering monthly - an interested party's figure, used as such)

The failed deepening (contemporaneous press and analysis):

https://www.livemint.com/Politics/7Y6q195B7sHP87gpy6Ud2K/Sri-Lanka-develops-cold-feet-on-trade-pact-with-India.html (28 July 2008: the signing deferred days before the Colombo SAARC summit; domestic opposition; twelve rounds over three years)

https://www.livemint.com/Politics/7ww9e4cJvy99VoSyedgPUN/India-takes-the-economy-way-to-score-political-points-with-L.html (11 August 2008: CEPA initialled by the commerce secretaries in July 2008; the about-face absorbed without rupture)

https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2031626 (Nag 2012, academic analysis: CEPA initiated 2005, concluded July 2008 after thirteen rounds; Sri Lanka's reservations and the FTA-first argument)

The successor negotiation's status (official and press, date-bounded):

https://www.mea.gov.in/Portal/ForeignRelation/India-Sri_Lanka-2025.pdf (Indian Ministry of External Affairs bilateral brief, March 2025: ETCA negotiations resumed October 2023 after five years, latest round the fourteenth in July 2024)

https://pib.gov.in/Pressreleaseshare.aspx?PRID=2088048 (Indian Department of Commerce 2024 year-end review: almost all ETCA chapters except some garment lines concluded)

https://www.dailymirror.lk/breaking-news/Sri-Lanka-yet-to-heed-Indias-request-for-appointing-chief-negotiator/108-320568 (Daily Mirror, 26 September 2025: talks at a standstill after fourteen rounds, Sri Lanka yet to appoint a chief negotiator; the 2025 garment-quota request and India's ETCA-track position - attributed to an informed source, used as press reporting)