

WORKING PAPER 23 - EU-Sri Lanka relations: A bond between trade and human rights

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Abstract

The European Union (EU) is Sri Lanka's largest trading partner. The country has been a periodical beneficiary of the EU's Generalised Scheme of Preferences (GSP+) for the last 15 years. Through the utilisation of the GSP+ mechanism, the EU aims to help Sri Lanka boost its trade, comply with International Human Rights conventions, and achieve Upper-middle income (Umi) country status. However, when Sri Lanka does achieve Upper-middle income status, it will automatically lose eligibility for GSP+ benefits. How will Sri Lanka continue to maintain significant trade relations when removed from the list of GSP+ beneficiaries? It is argued here that Sri Lanka is not ready to be excised from the GSP scheme. The country must overcome social, ethnic, and religious cleavages in a post-conflict scenario; it is essential for the EU to ensure the continued provision of trade benefits. The GSP+ status is of utmost importance to consolidate current economic achievements – as well as improve the quality of democracy in the country. Prospects in EU-Sri Lanka ties beyond trade preferential schemes must also be explored.

Key words: Sri Lanka, European Union, EU, Generalised Scheme of Preferences (GSP), GSP+, Upper-middle income (UMI) country, Lower-middle income country (LMI), Trade benefits, Trade preferences, International conventions

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1. Introduction EU trade relations with Sri Lanka

The European Union's trade engagement with South Asian countries, which is intended to improve political relations and foster economic development, functions mainly through bilateral agreements. The EU's trade with these countries consists mainly of [textiles and garments](#) imports to the EU; the EU's exports consist largely of machinery. Overall, EU-South Asia trading policies revolve around the Generalised Scheme of Preferences (GSP). This is a trade instrument created to encourage developing countries to alleviate poverty and achieve sustainable development. [This mechanism](#) allows vulnerable, developing countries to enjoy trade preferences such as paying fewer or no tariffs on their exports to the EU. It contains three variations: the 'Standard GSP scheme', the 'GSP+ scheme' and 'Everything but Arms (EBA) scheme' (Mayr, 2020).

The Standard GSP reduces import tariffs for Low and Lower-middle income countries on around [66 percent of products](#) exported to the EU. The GSP+ scheme is a special incentive agreement offering vulnerable, Low and Lower-middle income countries the complete removal of tariffs on the same lines of the Standard GSP scheme – albeit in this context with an obligation to commit and effectively implement 27 core conventions on human and labour rights as well as the environment and good governance. Lastly, the ‘Everything but Arms’ (EBA) scheme offers Least Developed Countries (LDC’s) duty-free, unlimited exporting access of all products to EU markets except arms and ammunition (UNCTAD, 2015; Mayr, 2020).

In line with a previous policy brief formulated by the South Asia Democratic Forum (SADF) titled ‘[EU-South Asia trade perspectives: State of play](#)’, which conducted a case-by-case assessment of EU relations with a few selected countries from South Asia, here we will be examining EU-Sri Lanka relations.

Recent developments – the reclassification of Sri Lanka from an Upper-middle income (UMI) to a Lower-middle income country (LMI) by the World Bank for 2020-2021 – have quelled concerns regarding Sri Lanka’s potential loss of its GSP+ status. The question remains concerning how Sri Lanka’s could again be considered an Upper-middle income country while remaining a GSP+ beneficiary.

1.1 Acquiring GSP+ statute

The first economic and political regulatory act between the EU and Sri Lanka dates back to 1975, when a [Commercial Cooperation Agreement](#) between the Government of Sri Lanka and the European Commission was signed. In April 1995, the EU and Sri Lanka strengthened relations through a [general framework](#) for bilateral economic relations intended to overcome trade barriers and promote development and diversification of trade. A ‘[Cooperation Agreement on Partnership and Development](#)’ (CAPD) was established. Furthermore, a [Dialogue](#) was established between the EU and Sri Lanka under the Joint Commission, which oversees the CAPD. This Commission also addresses elements of the Working Group on Governance, Rule of Law and Human Rights and the Working Group on Trade and Development – both crucial in enhancing the EU-Sri Lanka bond and its developmental benefits.

The EU and Sri Lanka have remained committed to their bilateral relations through these [Working Groups](#). The EU’s approach to trade and development with Sri Lanka now revolves around the GSP+. Prior to Sri Lanka benefitting from the GSP+ scheme, it benefited from the Standard GSP, which was established in 1971 under a recommendation by the United Nations Conference on Trade and Development ([UNCTAD](#)).

Sri Lanka was granted GSP+ beneficiary status in 2005. The concession was related to several factors. First, Sri Lanka's was classified as a 'vulnerable country', fulfilling [economic eligibility criteria](#) – for instance, it showed low diversification in exports and meeting Rules of Origin (RoO) criteria¹; it was also classified as a 'Lower-middle income' by the World Bank. Second, non-economic (political) [eligibility criteria](#) included the effective implementation of 27 international conventions concerning human and labour rights, sustainable development and good governance, as well as the maintenance of these ratifications (European Commission, 2015, August).

1.2 The meaning of the GSP+ Statute for Sri Lanka

The EU has been identified as Sri Lanka's largest export destination (followed by India, China and the US) since 2008 – with the greatest impact on the [apparel market](#). Exports grew incredibly from 1.8 billion prior to the introduction of GSP+ in 2004 to 2.9 billion in 2009, depicting an increasingly rapid [average annual growth](#) from 2005-2009.

Moreover, the GSP+ statute underwent changes as introduced by the [Regulation \(EU\) No. 978/2012 of the European Parliament and the Council of the European Union](#), which became effective in January 2014. These changes were implemented to allow countries most in need to reap benefits from the GSP scheme. As a result, the list of beneficiary countries was reduced from 177 to 88 (UNCTAD, 2015). However, Sri Lanka remained a beneficiary following these adjustments and a temporary suspension from the GSP+ scheme in 2010. Sri Lanka is one of the countries which have most benefited from the GSP+ and privileged access to the EU market.

1.3 Suspension from GSP+: Failures to commit to Human Rights Conventions

According to the EU's terms for trade preferences, for a country to benefit from the GSP+ it must effectively apply 27 international conventions. However, in 2010 Sri Lanka displayed 'serious failures' in implementing some of these conventions, resulting in the temporary withdrawal from GSP+ preferences. According to Article 19.1(a) of the [2012 regulation](#), the European Commission and its monitoring bodies have the possibility to consider the suspension of preferences as a result 'of serious and systematic violation of principles laid down in the conventions listed in Part A of Annex VIII' (the UN and ILO conventions on core human rights and labour rights).

¹ Rules of origin determine where goods actually originate – meaning not where they were shipped from, but where they were produced or manufactured. As such, the 'origin' is the 'economic nationality' of goods traded in commerce.

This includes the failure to implement three UN Human Rights conventions: The International Covenant on Civil and Political Rights (ICCPR), the ‘Convention against Torture’ (CAT), and the Convention on the Rights of the Child (CRC).

In the wake of civil war, the Sri Lankan government displayed [inadequate](#) efforts to fulfil the primary responsibility of protecting its minorities. It was [accused](#) of numerous human rights violations, largely carried out during the last stages of the long and brutal, twenty-nine years-long civil war between the Sri Lankan military and the Liberation of Tamil Tigers of Eelam (LTTE). This led to the withdrawal of the GSP+ preferences. The [EU reiterated](#) that the Sri Lankan authorities were obligated to improve the implementation of the three UN Human Rights Conventions in order to restore Sri Lanka’s GSP+ beneficiary status and maintain the deep relations the country had cultivated with the EU thus far.

Trade relations between the EU and Sri Lanka slowed down, and this impacted Sri Lanka’s trade and economic growth. The EU market is crucial for the Sri Lankan economy; the withdrawal from the GSP+ had a huge impact and [disrupted](#) the country’s annual growth rate. Export rates declined from 16.4 percent to 7.4 percent during the period of 2010-2014.

1.4 Sri Lanka’s government in 2015 - progress in Human Rights commitments and path to readmission

The year 2015 could be described as a turning point for Sri Lanka – with a change in government and a new agenda focussed on good governance and national reconciliation. The Maithripala Sirisena administration (2015-2019) expressed its desires to improve and recalibrate its foreign policy to re-engage Sri Lanka with the international community. Sri Lanka’s commitment to national reconciliation was also displayed through the co-sponsorship and signing of the Human Rights Council Resolution 30/1 on Promoting reconciliation, accountability, and human rights. The initiatives taken by Sri Lankan authorities also resulted in the resumption of EU-Sri Lanka dialogues under the 1995 Cooperation Agreement — the Joint Commission and its Working Group on Governance, Rule of Law and Human Rights. Many reforms were established, as was an Office for Missing Persons and Office for Reparations; [several legislative](#) steps were adopted so as to improve the rights of women and children, the fight against discrimination, against domestic violence, etc.

In April 2015, the Sirisena government passed the [19th Amendment to the Constitution](#) so as to confront impunity, ensure reconciliation and justice, and prevent the recurrence of human rights violations – especially regarding the minority Tamil population. The EU granted [Sri Lankan authorities](#) two years to ensure the careful execution of these new reforms – which eventually lead to the restoration of their GSP+ beneficiary status in 2017.

The reformed agenda by the Sirisena government also opened opportunities for civil society to be more deeply involved in ensuring the effective implementation and adherence to the human and labour rights conventions outlined in the GSP+ scheme.

In terms of trade, the EU was committed to help Sri Lanka re-establish and re-immers itself in the GSP+ scheme. This was visible through the [Multi-Indicative Programme \(2014-2020\)](#), which focussed on rural development and democratic governance and reconciliation. The programme supported an increase in trade capacity and Sri Lanka's compliance with the core international conventions. Another example is the [Trade related Assistance \(2015-2023\)](#), which focussed on supporting Small and Medium Size Enterprises (SMEs) so as to increase their competitiveness in both South Asian and EU markets.

1.5 GSP+ restoration

Following the Presidential and Parliamentary Elections in 2015, the [European Commission](#) recognised the political transition and the vast efforts demonstrated by the Sri Lankan government to improve commitments and implement human and labour rights conventions. This included much political will and various concrete steps intended to restore democracy, good governance and an increased respect and adherence to human rights. A green light to [regain the GSP+ status](#) was obtained in May 2017. The restoration of Sri Lanka's status as a GSP+ beneficiary was not so much due to the rhetorical implementation of the 27 conventions but rather linked to the significant commitments displayed towards actually implementing them. The then EU Trade Commissioner, Cecilia Malmström, so [expressed](#): 'Granting GSP+ to Sri Lanka [...] is a vote of confidence from the European Union that the Sri Lankan Government will maintain the progress it has made in implementing the international conventions. At the same time, no one is pretending that the situation is perfect.'² Sri Lanka had shown a sustained effort to abide to these international conventions.³ (European Commission, 2018).

Sri Lanka's return to the GSP+ [reopened the doors](#) for trade and economic growth, raising the potential for increased investments, particularly in the textile and apparel industries. [In 2018](#), the two-way trade was worth around EUR 4.5 billion, and Sri Lanka benefitted from a trade balance surplus of EUR1.3 billion.

² The process of replacing the Prevention of Terrorism Act still needs to be completed. There are still too many incidents of torture, there are still children being forced into marriage, there are still laws that discriminate against sections of Sri Lankan society. We want to see an end to these practices. The EU will work closely with the Government and Non-Governmental Organisations to rigorously monitor progress".

³ Through actions such as the National Action Plan for the Promotion and Protection of Human Rights (2017-2022) and a National Plan of Action for Children. Further, the authorities are vehemently engaging on delivering several other reforms with direct relevance to the human rights conventions outlined in the GSP+ scheme (European Commission, 2018).

During the period of June 2017- May 2018, Sri Lanka exported over EUR 2.2 billion worth of goods under the GSP+ scheme. The advancements made [in 2018](#) indicated that the EU was Sri Lanka’s largest trading partner and main export destination – accounting for 16% of the total trade, and thus surpassing India (14.6%) and China (13.4%). As demonstrated by the figure below, Sri Lanka’s reintroduction to the GSP+ led to an increase in imports from the EU as well.

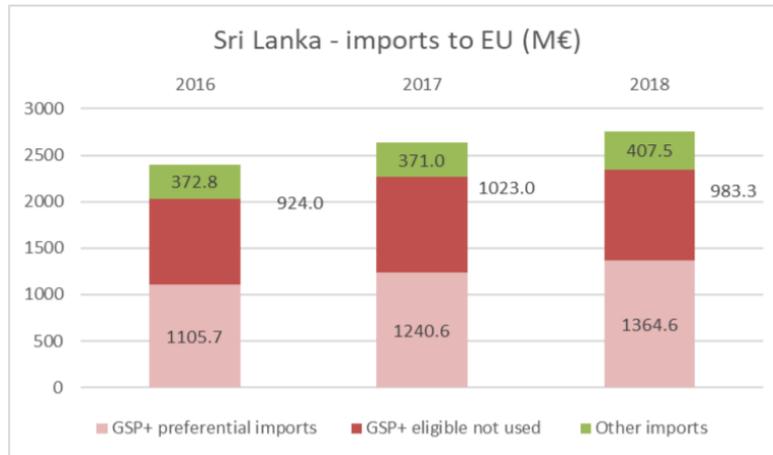


Figure 1: Imports to the EU 2016-2018 by regime (Source: [European Commission](#))

The European Commission also understood the value of the 2015 reforms as regards [empowering other stakeholders](#) such as civil society and the business community. These stakeholders were provided with the opportunity to monitor state authorities’ compliance with GSP+ obligations and play a greater role in the diversification and wider utilisation of GSP+ trade preferences.⁴

Despite other key [shortcomings](#)⁵ to international conventions, Commissioner Malmström [voiced](#) that a vote of confidence in Sri Lankan authorities and cooperation with the UN bodies created the opportunity for restoring GSP+ to Sri Lanka.

⁴ Such initiatives were adopted by another GSP+ beneficiary, Armenia. Armenian authorities delegated the monitoring and implementation of the National Strategy on Human Rights Protection in 2014-2016.

⁵ This includes the repeal of the Prevention of Terrorism Act (PTA) and its replacement with counter-terrorism legislation. This concerns addressing the continued use of torture, the amendment of the Code of Criminal Procedure to include the right of detainees to immediate access to legal counsel, the return of land occupied by the military, and establishing the truth regarding the fate of those missing and disappeared during the civil war and its aftermath.

2. An Evaluation of the status of EU-Sri Lankan trade relations and its prospects

2.1 The 2019 elections and the new Sri Lankan government's engagement with GSP+ and the EU

In November 2019, the new Sri Lankan government raised many concerns for democracy and as concerns reconciliation processes in the country. The theme of national security governed the 2019 elections, which also reintroduced ethnic and religious disputes. The efforts made by Sri Lankan authorities following the GSP+ restoration in 2017 have been slow and some challenges remain unequalled.

The maintenance and continuous ratification of human rights conventions as outlined by the EU depends heavily on political will by the new Gotabaya Rajapaksa government⁶. The Sinhala-Buddhist⁷ nationalistic rhetoric demonstrated by Gotabaya caused great concern among the minorities in the country as well as within the international community. The EU's values of democracy were displayed when an [EU Electoral Observation Mission \(EOM\)](#) was deployed to Sri Lanka during the Presidential election period in late 2019.⁸

Further concerns rose at the [Joint Commission meeting](#) in February 2019, which discussed the [new constitution](#) (introduced in 2015). Focussed attention was paid to specific shortcomings such as the repeal and replacement of the Prevention of Terrorism Act (PTA). The new government indicated that the current version of the Counter Terrorism Act (CTA), proposed by the Sirisena administration to replace the controversial PTA, would not be accepted. It is nevertheless essential to repeal the PTA, as it [allows arrests](#) on unspecified, unlawful acts without warrant – and who may be pardoned only by the President.⁹

⁶ The Gotabaya administration came into power, following his victory at the 2019 Presidential Elections.

⁷ Sinhalese Buddhist nationalism is a political ideology which combines a focus upon Sinhalese culture and ethnicity with an emphasis upon Theravada Buddhism, which is the majority belief system of most of the Sinhalese in Sri Lanka.
https://en.wikipedia.org/wiki/Sinhalese_Buddhist_nationalism.

⁸ Previous SADF publications have discussed the crucial functionality of the EOM in ensuring the positive and fair conduct during the 2019 Presidential elections in Sri Lanka (Mayr & Wolf, 2019; Mayr, 2019). During the election period, High Representative/Vice-President of the European Commission, Federica Mogherini, [expressed](#): 'I am confident that the deployment of an EU EOM under the leadership of Chief Observer Marisa Matias will contribute to an inclusive, credible and transparent election. This election is important for Sri Lanka to continue making progress on its path of reform and national reconciliation.'

⁹ Sri Lanka's Tamil National Alliance (TNA) spokesperson and former Jaffna parliamentarian M.A Sumanthiran called for a repeal of the PTA and to release political detainees who were allegedly involved with the Liberation Tamil Tigers of Eelam (LTTE).

For example, Human Rights Watch (HRW) Director for South Asia, Meenakshi Ganguly, [voiced](#): ‘The EU, which offers Sri Lanka preferential trading terms in return for human rights guarantees, should demand the repeal of the Prevention of Terrorism Act’. Replacing the PTA is crucial if Sri Lanka is to upgrade its legislation to international standards on counterterrorism legislation and address its human rights shortcomings.

Moreover, the Gotabaya administration made the decision to withdraw its co-sponsoring of the UN Human Rights Council resolution 30/1 on promoting reconciliation, accountability, and human rights (which was introduced in October 2015 by the Sirisena government). Additionally, in May 2020, President [Gotabaya Rajapaksa highlighted that he would withdraw Sri Lanka from any international organisations targeting the military with allegations of human rights violations during the civil war.](#)¹⁰

These political decisions have caused unease among the EU and the international community at large concerning Sri Lanka’s concurrence with international standards on human rights and democracy. This could hinder the country’s trade benefits and GSP+ status, as human rights policies are fundamental values to the EU. The EU [reiterated](#) its opposition and viewed the new government’s stances as a setback in Sri Lankan legislation and in path to improve human rights.

2.2 The long-term view - Sri Lanka as a GSP+ beneficiary until 2023 - Achieving Upper-middle income country status

As previously highlighted, Sri Lanka continues to suffer from the consequences of its long civil war. Reconciliation processes, peace building and democracy are not achieved instantly. It is a complex and long drawn path, but EU officials are confident that Sri Lanka will pursue the relevant objectives. New Ambassador of the EU to Sri Lanka and the Maldives, Denis Chaibi, [stated](#) in an interview earlier this year: ‘More fundamentally, the long-term prosperity of Sri Lanka can only be guaranteed by repairing decades of conflict, which is undoubtedly an enormous complex task.’

Additionally, the former EU Ambassador to Sri Lanka and the Maldives, Tung-Lai Margue, [expressed](#) the tremendous improvements in EU-Sri Lanka relations over the past few years. As part and parcel of the improvement and repairing the years of conflict, both parties engaged in several projects. For example, providing budgetary support through the Strengthening Transformation, Reconciliation and Inclusive Democratic Engagement’ ([STRIDE](#)) initiative in October 2019.

¹⁰ "If any international body or organization continuously targets our country and our war heroes, using baseless allegations, I will also not hesitate to withdraw Sri Lanka from such bodies or organizations." [AP News](#).

This focusses on assisting poor communities and developing businesses; it also aims to increase product competitiveness in the local and international market. Other projects include EU-funded action towards supporting overall trade growth and more specifically SME's to expand their export capacities – thus allowing further diversification of products and a maximum utilisation of the GSP + preferences.

The EU's development assistance has remained a vital initiative to EU-SL relations for the past twenty years, under which the EU has provided Sri Lanka EUR 800 million in development and humanitarian assistance. The significant support provided by the EU has not only contributed and enabled Sri Lanka to reach an Upper-middle income (UMI) country status, according to the [2019 World Bank ranking](#), but it has also incentivised Sri Lanka to persist and strive to respect human and labour rights — and SDGs. However, as Chaibi [mentions](#), Sri Lanka at its current economic and beneficiary position must continue to boost its economy by attracting investors, diversifying its products and avoid becoming stagnated in a middle-income position.

Additionally, the [EU monitoring process](#) serves as an efficient tool to encourage Sri Lanka to achieve long-term prosperity. Monitoring assesses any impediments to the effective implementation of conventions and provides the opportunity to engage with various stakeholders (primarily businesses and civil society groups) so as to build awareness about the GSP+ and exhibit the EU's expectations (DRI, 2017). Additionally, the GSP+ Dialogue between the EU and Sri Lanka has also thus far promoted, for example, the establishment of the [National Export Strategy \(NES\)](#), which is funded by the EU and aimed at facilitating trade and economic growth.

As mentioned above, Sri Lanka's categorisation as an [Upper-middle income country](#) (according to the World Bank) in 2019 indicates that the country could cease to benefit from the unilateral trade preferences offered by the EU's GSP+ scheme by 1 January 2023 (European Commission, 2020). Sri Lanka's Upper-middle income status represents a significant achievement, signalling a transition into a new type of trade agreement with the EU, after the GSP+.

A transition to, for instance, a Free Trade Agreement (FTA) could occur. Sri Lanka would then have the opportunity to become a partner country of the EU, which would strengthen bilateral relations and encourage a steady, long-term partnership (European Commission, 2018).

2.3 Comparison to former GSP+ and Standard GSP beneficiaries

In this section, Paraguay and Malaysia are examined, in an attempt to provide an understanding of the economic and political progress made by a country following its graduation into an Upper-middle income country as per the World Bank ranking. Paraguay is examined due to its previous GSP+ beneficiary status. Malaysia was chosen with the aim of comparing Sri Lanka to another country in Asia. However, unlike Paraguay, Malaysia was part of the Standard GSP scheme. Therefore, it is important for Sri Lanka to ensure that its relations with the EU remains uninterrupted, similar to what was the case with both Paraguay and Malaysia – and this despite Sri Lanka’s potential departure from the GSP+ scheme in 2023.

[Paraguay](#) benefitted from the GSP+ arrangement from 2009-2018 and exited the scheme in 2019. It made incredible progress as a GSP+ beneficiary. In terms of human rights, Paraguay established an effective monitoring system (SIMORE), allowing the country to implement international human rights mechanisms. As for trade, [Paraguay’s role](#) in the Mercosur trade bloc has created a unique opportunity to expand relations with the EU more easily and effectively. As a result, it is expected that the EU will continue to grow closer to Paraguay – and that their [bilateral relations](#) will be reinforced through the EU-Mercosur Association Agreement. The future of EU-Paraguay relations relies heavily on the political agreement reached between the EU and Mercosur in June 2019, as Paraguay departed from the GSP+ scheme in January 2019.

Paraguay has been consistent in applying UN conventions on human rights. For example, comparing efforts between Sri Lanka and Paraguay on the ‘Convention against Torture’, it must be mentioned that Paraguay has adopted a [National Mechanism of Prevention of Torture \(NMPT\)](#). This mechanism aims to alert authorities of any cases of abuse or mistreatment. Sri Lankan authorities are yet to act more swiftly and invest significant efforts into ensuring systematic changes are made to address this shortcoming of the CAT. Since January 2006, Malaysia benefitted from the EU’s Standard GSP scheme. The EU, in turn, is Malaysia’s fourth largest trading partner (Armanovica, 2012). Malaysia experienced a trade surplus until 2011 – one which, due to its very rigorous export strategy, successfully transformed the nation from a developing country into an industrialised economy. Malaysia was heralded into the Upper-Middle Income country category.

After Malaysia exited the Standard GSP scheme, it focussed on becoming a High-income country by 2020. The country introduced a ‘Government Transformation Programme’ to deal with corruption and upgrade rural infrastructure – strengthening Malaysian civil society and supporting democratic reforms through the European Instrument for Democracy and Human Rights (EIDHR).

Similarly, Sri Lanka could collaborate with the EU to deploy the EIDHR and support its own democratic reforms (Armanovica, 2012).

Moreover, the Free Trade Agreement (FTA) option explored by Malaysia and the EU after its removal from the GSP beneficiary list could present a promising prospect for Sri Lanka as well. The purpose of an FTA is to obtain unprecedented access to a market, thus helping to create an open and competitive international marketplace. However, in order to negotiate an FTA, Sri Lanka would need to make significant efforts as regards cooperation on sustainable development – especially as concerns environmental and social dimensions, as these are crucial aspects in obtaining an FTA.

[Paraguay's](#) relations with the EU is more strongly connected to Mercosur¹¹. Paraguay has one of the highest GDP's in this trading bloc and plays an important role in attracting Foreign Direct Investment (FDI). The country could gain much from the EU following its removal from the GSP+ beneficiary list in 2019, as it occupies a strong position in the Mercosur bloc. On the other hand, [Malaysia's growth](#) in comparison to Sri Lanka was due to increased FDI. The Malaysian governments' market liberalisation and governmental transparency allowed it to attract more FDI (Armanovica, 2012).

By contrast, Sri Lanka's strongly protectionist behaviour is known to influence the flow of FDI into the country – which of course impacts economic growth. Sri Lanka must explore external investor options carefully, in addition to lowering its strong protectionist measures. For example, FDI constitutes only two percent of Sri Lanka's GDP, whereas it accounts for three to four percent of Malaysia's national income (Oxford Business Group, 2019).

2.4 Prospects for Sri Lanka: What could happen after a potential removal from the GSP +

Sri Lanka's potential lies in the democratic functioning of its institutions and government. It needs to develop a new policy agenda to overcome its political crisis. As such, Sri Lanka requires a more stringent and potent monitoring system capable of reconciling and reuniting the country regardless of the EU's involvement in monitoring practises. Current authorities must create a monitoring system capable of ensuring the continued implementation of the international conventions on human and labour rights as well as the environment and good governance.

¹¹ The Southern Common Market (MERCOSUR for its Spanish initials) is a trading bloc in Latin America.

Currently, President Rajapaksa's security-orientated approach to governing Sri Lanka presents a negative prospect as regards the advances made towards further consolidation of democracy, free market development and the provision of equal economic opportunities within the island. A prime example of this is visible through the 'Military in Business'¹² attitude, in combination with the prevailing of state-owned businesses. These could have an obstructive effect on minorities and on all citizens more generally speaking (Mayr & Wolf, 2019). The [EU communicated](#) to Sri Lankan authorities that 'GSP is not automatic' and that failing to meet the EU's human rights obligations will have consequences – which will impact the country's economy as well. In short, and as mentioned above, it is essential for the Gotabaya administration to implement legislative reforms such as the PTA – capable of improving the situation regarding general trade prospects and the GSP+.

In economic terms, a maximum utilisation of trade preferences produces wealth and has a wide impact on several aspects of socioeconomic and environmental development. [Sri Lanka's current access](#) to the EU market through the GSP+, in conjunction with the maintenance of political developmental goals such as respecting human rights, the rule of law and good governance, could portray Sri Lanka as an ideal locus for investment opportunities. Attracting international investors and boosting FDI could provide a sense of economic stability to the country in the long run. Upholding the environmental and social obligations of the GSP scheme, coupled with incoming FDI, could lead Sri Lanka to the path followed by Paraguay and Malaysia after trade preferences were removed. Opportunities could arise for an EU-Sri Lanka FTA – with unprecedented access to the EU market and a strong increase in trading propensity.

[In case Sri Lanka](#) loses the GSP+ status before it is ready to do so, as Ambassador of the EU Mr Chaibi [warned](#), it could face stagnation as a middle-income country. In order to overcome this stagnation, Sri Lanka must take policy decisions capable of transforming the country into one of high-income status – by focussing more on innovation, expanding its export base, and actively implementing structural economic and political reforms (Warusavitarana, 2019). This 'middle-income challenge' is visible throughout much of Asia; however, through suitable policies and guidance from more experienced regions (i.e. the EU) Sri Lanka could perhaps excel.

¹² This identifies the increase in state-owned businesses and monopolistic power displayed by the Sri Lankan government in various sectors of the national economy.

Conclusion

Sri Lanka's [improvements](#) in economic and political terms have greatly solidified the country's relationship with the EU. After 2015, human rights policies and labour rights improved vastly – especially as concerns the reduction of child labour to one percent and a promise to eliminate it completely by 2022. Regarding good governance, Sri Lanka adopted measures on anti-money laundering – which led to its removal from the Financial Action Task Forces' (FATF) grey list (European Commission, 2020).

According to the latest [report](#) from the European Commission, Sri Lanka secured the ratification of all 27 GSP+ relevant conventions and is up to date with all reporting obligations. However, except under one human rights convention (the Convention on the Elimination of All Forms of Racial Discrimination - CERD), one labour rights convention (Convention No. 105 on the Abolition of Forced Labour) and two environmental conventions (CITES and UN Framework Climate Change Convention - UNFCCC) the country fell short in its concrete, applied obligations (European Commission, 2020). Nevertheless, the EU's diligent monitoring process is sure to ensure the ratification of the remaining shortcomings.

Sri Lanka's transition from a Lower-middle to an Upper-middle income country was visible in its rapid [growth period](#) between 2007-2016, which featured a substantial decrease in severe poverty levels and an active engagement to make progress on the SDG's (preceded by the Millennium Development Goals; ADB, 2017). In September 2017, Sri Lanka launched a new development plan – Vision 2025 – aimed at transforming the country into an Upper-middle income country and even into 'the hub of the Indian Ocean' (Oxford Business Group, 2019).

However, based on recent assessments by the World Bank for the new fiscal year 2020-2021, which began on the 1 July 2020, Sri Lanka has been [reclassified](#). This reclassification contained a move from an Upper-middle to a Lower-middle income category due to a decrease in per capita income.

The World Bank's threshold for a UMI country classification also increased, from \$3996 to \$4046. Due to the combination between these changes in income classifications and the drop in Sri Lanka's GNI to \$4020, Sri Lanka will now have to take a step back in its development plans, as well as on the SDG's (Serajuddin & Hamadeh, 2020).

What are the repercussions of the World Bank's reclassification on Sri Lanka? What does this mean for Sri Lanka's position and access to the EU market? Will the EU keep Sri Lanka on its GSP+ beneficiary list, as it is no longer considered an Upper-middle income country?

On the one hand, from an economic perspective, Sri Lanka's Export Development Board (EDB) Chairman Prabhash Subasinghe viewed Sri Lanka's move to a Lower-middle income country as an opportunity for the export community and the country more generally. He [opined](#) that 'It is good for the continuation of the European Union's (EU) Generalised Scheme of Preferences (GSP+) for another four and a half years' (de Silva, 2020). Since Sri Lanka already currently enjoys GSP+, in order to continue to benefit from it the country must simply fulfil its obligations in terms of implementing the 27 international conventions related to human rights, labour rights, protection of the environment and good governance (F. Deraedt, personal communication, July 20, 2020).

On the other hand, it must be understood that reconciliation is a precondition to economic development and President Rajapaksa's approach to economic development as an alternate path to reconciliation is a risky, one-way strategy which should not be endorsed (Ali, 2020). The lack of a collective effort towards reconciliation on the part of the various Sri Lankan communities will remain a constraint. A failure to overcome this hurdle will hinder not only political developments but economic progress as well.

In conclusion, for the EU to maintain its strong bond with Sri Lanka, the country needs to reassess its protectionist strategies and improve its capacities for political and legislative reforms – which would develop the country into an economically and politically formidable global player. Despite certain shortcomings and new developments in its World Bank ranking, Sri Lanka continues to work towards matching international standards of reconciliation and respect for human rights – as well as transitional justice and protection of minorities. These are salient issues the EU expects its trade beneficiaries to focus on consistently and in the long run.

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