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Domestic Regulations in Trade in Services

Importance of Regulatory Reform

Rajesh Aggarwal
Chief,
Trade Facilitation and Policy for Business
International Trade Centre



Importance of Trade in Services

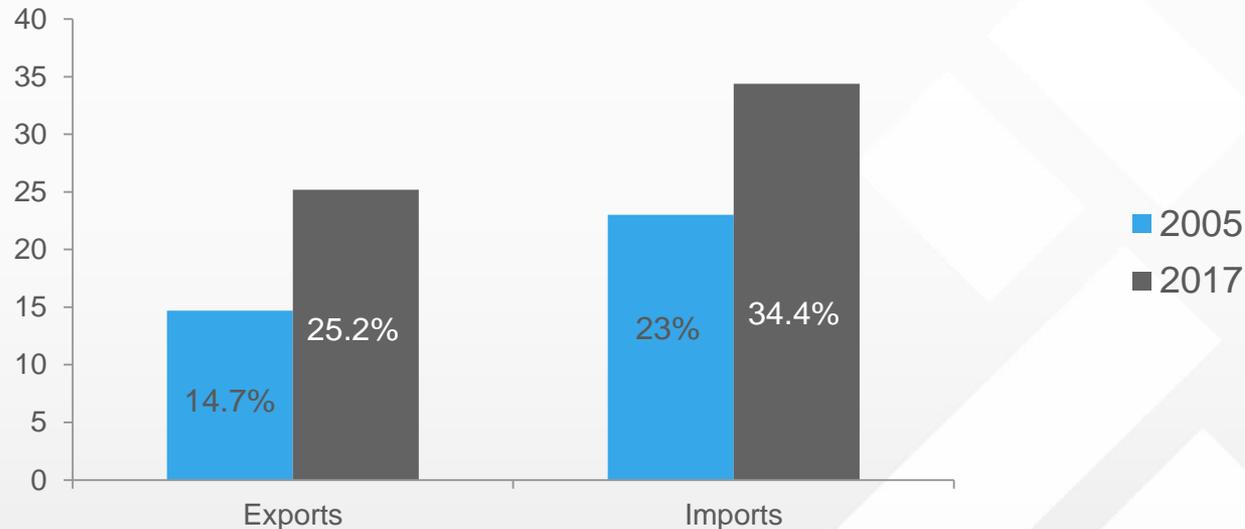
Services are key to achieving structural transformation of economies towards:

- Economic upgrading
- Diversification
- Greater Competitiveness

Services Sector Growth

- Between 2005 and 2017, trade in services grew at 5.4% per year, faster than trade in goods
- Contribution of developing countries to trade in services grew by over 10% in the same period; but remains concentrated in the 5 countries of China, Hong Kong (China), the Republic of Korea, Singapore and India

Figure: Share of developing economies in world trade in services

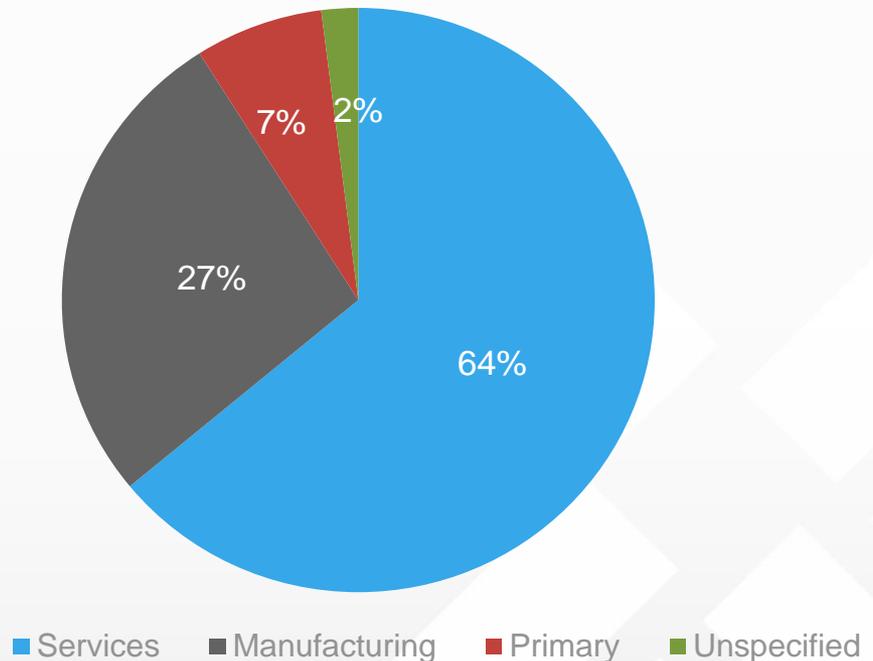


Source: WTO estimates (2019)

Foreign Direct Investment

The services sector accounted for 64% of world direct investments stock in 2014, significantly greater than its share of 23.3% in world trade, according to UNCTAD statistics.

Distribution of World Inward FDI Stock by Sector



Source: UNCTAD (2016)

Value Added of Services Embedded in Exports

- The services value-added that is contained in international goods and services exports accounts for close to half of world exports, compared to about 30 per cent in 1980 (Heuser and Mattoo, 2017)
- Services are important inputs along the production process as well as in after-sales activities in the manufacturing sector. Building the supply-side capacity of services sector will therefore benefit the competitiveness of all manufacturing sectors
- Services exports rely on services inputs from within the same sector as compared to inputs from other services sectors. The share of intra-sectoral value-added in exports is highest for real estate (78%); public health, education and social (71%); and finance and insurance (71%)

Source: OECD TiVA database (2018)

Efficient Services: Key to Developing Countries' Connectivity to the Global Economy

Openness in services enhances productivity

- ✓ Increase in FDI
 - Mode 3 openness
 - Manufacturing sector FDI (Eg: enhanced quality of logistics sector)

- ✓ Increase in competition

Efficient Services: Key to Developing Countries' Connectivity to the Global Economy (cont.)

Openness in services enhances productivity

- ✓ Potentially beneficial in the evolution of efficiency in technology intensive manufacturing industries [Francois & Woerz, 2008]
- ✓ Significant positive relationship between firm productivity and the performance of the service sector [Arnold, Mattoo & Narciso, 2008]

Determinants of Comparative Advantage in Services



Skills



Institutions



Regulatory and Governance Frameworks

Source: Van der Marcel, 2012

Services Openness

GATS disciplines invoke:

- Market access and
- National treatment

(Commitments based on Positive List Approach)

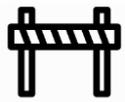
But, **National regulatory discretion** remains essentially unchecked, which may result in:

- ✓ Regulations being deliberately designed to give protection to domestic incumbents
- ✓ Inadvertently restricting trade while pursuing legitimate socio-economic objectives

National Regulatory Discretion

“While members stress the importance of market access as a stepping stone for further liberalization, our results indicate that an important determinant of trade patterns lies in domestic regulations. The estimates shown in this paper suggest that more attention should be paid to article VI of the GATS related to domestic regulations, as far as the promotion of world trade in services is concerned” – Crozet, Milet and Mirza, 2015

Importance of Services Trade Restrictions for Cross-border Exports



The impact of regulatory hurdles on export entry and export volumes is significantly less detrimental for larger firms



Previous export experience is a key asset to succeed in less open countries

Source: S. Benz- 2019, Dorothee Rouzet, Francesca Spinelli, CEP Working Paper 2019/1

Impact of Services Trade Restrictions on Cross-border Exports

- More restrictive countries obviously import less services, but also export less services. Detrimental effect on exports is twice as large as on imports. [Since service trade restrictions are behind the border, it affects competitiveness of domestic firms also]
- Trade restrictions in computer services, distribution services, telecoms, transport, courier, commercial banking and insurance have negative effect on trade in manufactured goods.

Source: OECD Trade Policy Paper No. 178

Impact of Services Trade Restrictions on Cross-border Exports (cont.)

- Restrictions in telecom and maritime transport affect all manufacturing sector's exports and imports
- Air transport and courier services affect products that are sensitive to lead time
- Banking and insurance services have a relatively large impact on exports of intra-industry trade in motor vehicles, non-durable consumer goods and electronics

Source: OECD Trade Policy Paper No. 178

Rationale for Regulation of Services

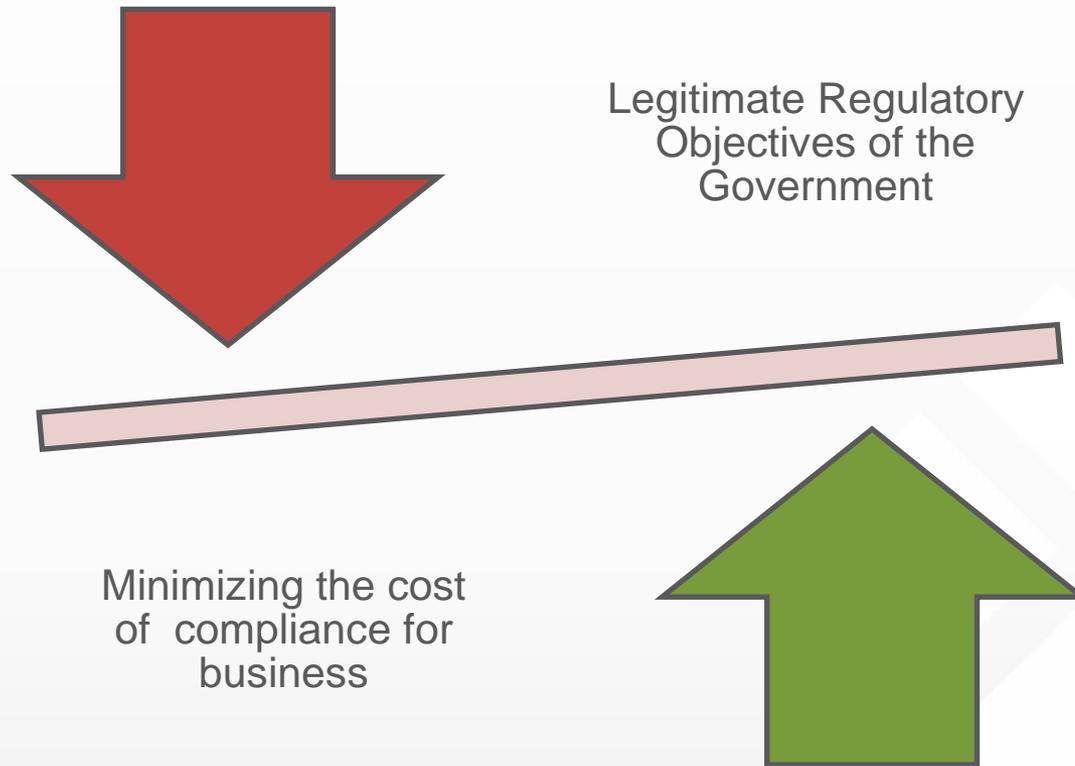
Addressing market failures and serving the public interest by:

- ✘ Preventing monopolies in network based services
-  Addressing externalities and asymmetric information in knowledge and intermediation based services (Eg: financial and professional services)
-  Striving for universal access in essential services (Eg: health and education)

Challenges to Effective Regulations

- ❗ Unnecessary and burdensome procedures on business, raising costs and weakening countries' competitiveness
- ❗ Non-transparent and anti-competitive measures may deter new suppliers from entering the market

Regulatory Reform is a balancing act between:



Regulatory Strategies

- **Provision of services by the state**
- **Command and control regulation (imposition of binding standards by state)**
 - Prior approval or licensing
 - Target/performance/specification standards
- **Incentive-based regimes (taxes and subsidies)**
- **Market harnessing controls (competition law, franchising, tradable permits)**
- **Disclosure regulations**

Making Regulations Less Burdensome

- ↓ Decreasing the burden of regulations while retaining the same overall strategy
- ↻ Changes in strategy itself

Alternatives to Common Regulatory Practices to Decrease their Restrictiveness

- Pro-competitive strategies in regulating 'natural' monopolies
- Decreasing the burden of Command and Control regulation (reform of the licensing system)
- Shifting regulatory strategies to Incentive-based/ Market harnessing/ Disclosure regulation mode

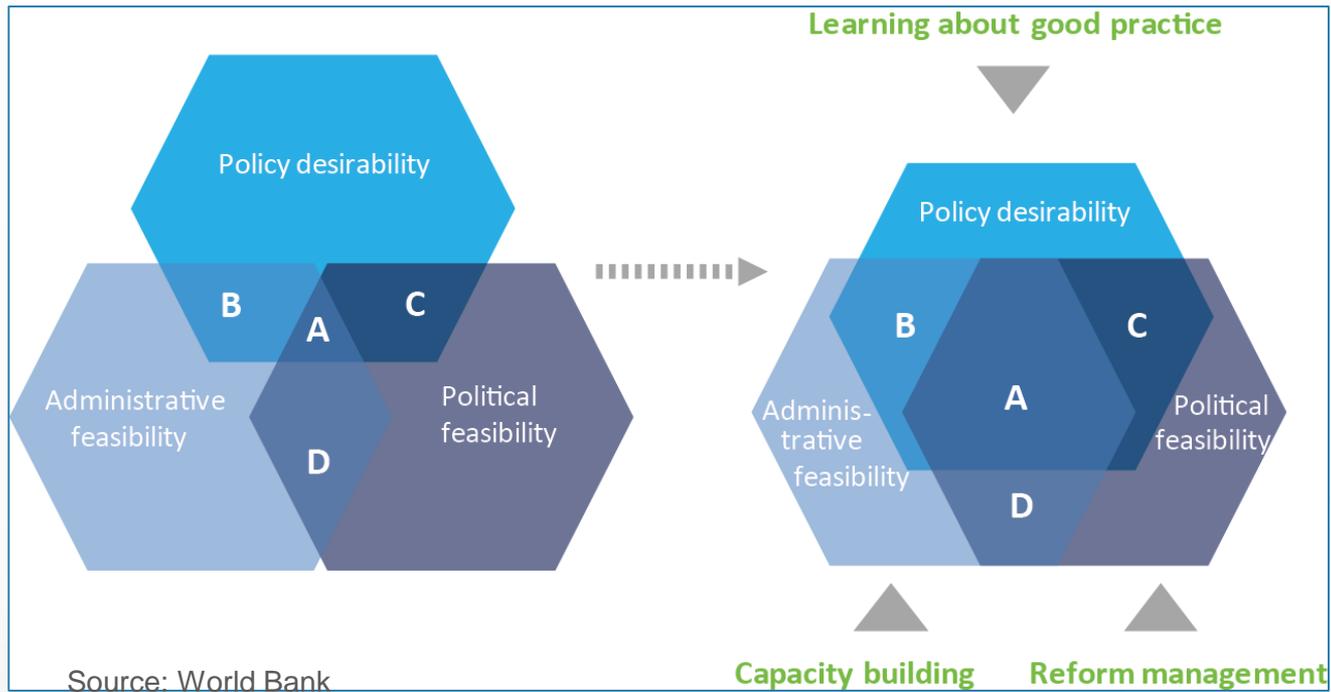
Choice of Alternative Strategies

Determining Factors

- Political Economy context
- Institutional Capacity (including Judicial capacity)
- Consumer characteristics

The domestic context within which alternative regulatory options are recommended should be carefully assessed.

Broadening the Scope and Desirability for Good Policy/Regulatory Options



Thank you!