# Services Trade: Recent Policy Trends and Incentives

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Based on papers by Borchert and Mattoo (services overall) and Dhar and Srivasta (mode 4)

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# Services (should) matter

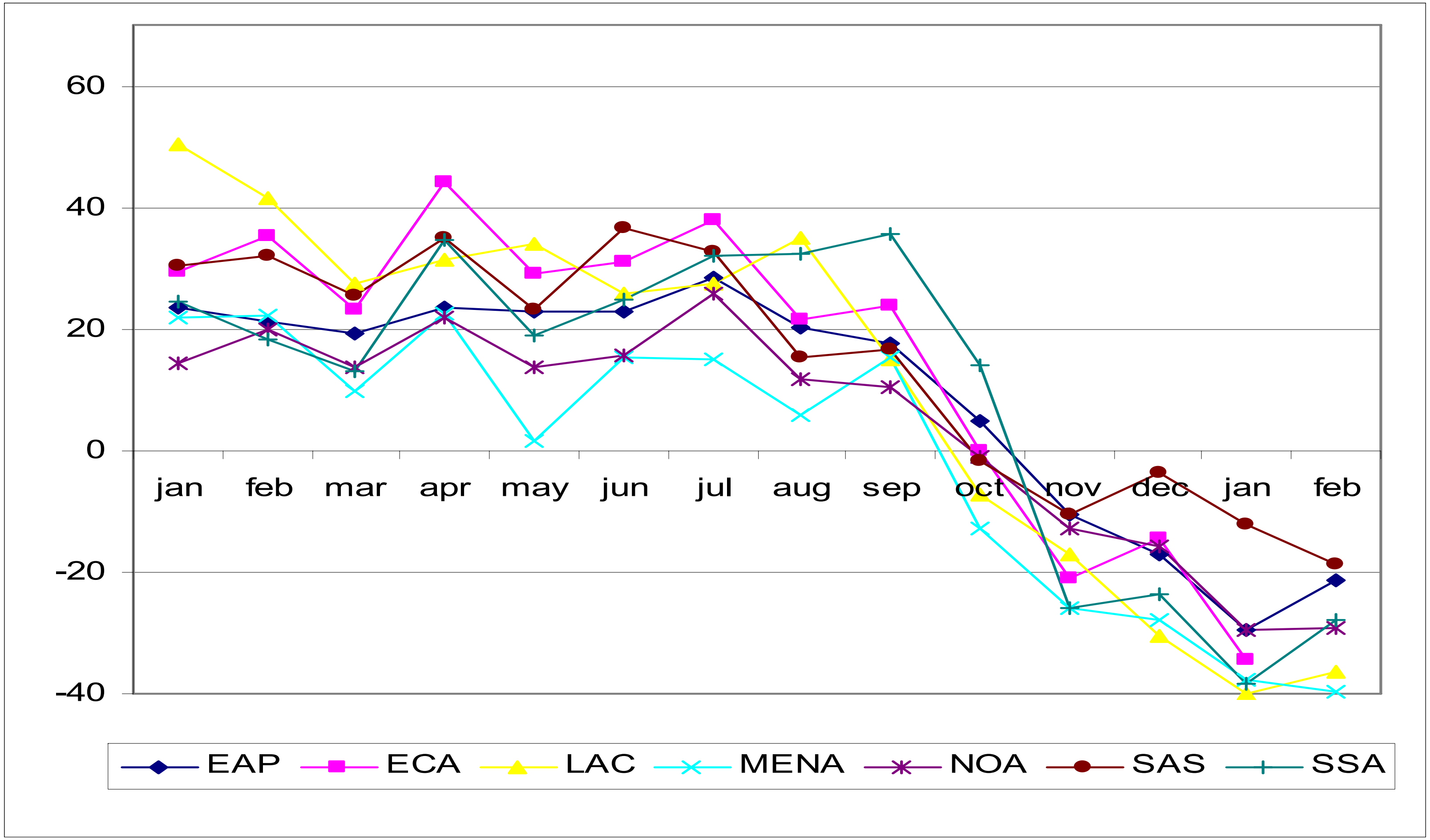
- For the world as a whole, share in GDP up from 55 to 70 percent between 1977 and 2007; even in low-income countries share is around 50 percent
- Services account for > 25% of world trade (cross-border transactions)
- Account for 60% of stock of global FDI and sales of affiliates
- But do not figure in WTO and other monitoring efforts (aside from financial sector bailouts)

# Modes of supply

- Mode 1: Cross-border trade
- Mode 2: Temporary movement of consumers
- Mode 3: Commercial presence, i.e., long-term movement of providers = ‘FDI’.
- Mode 4: Temporary movement of services providers

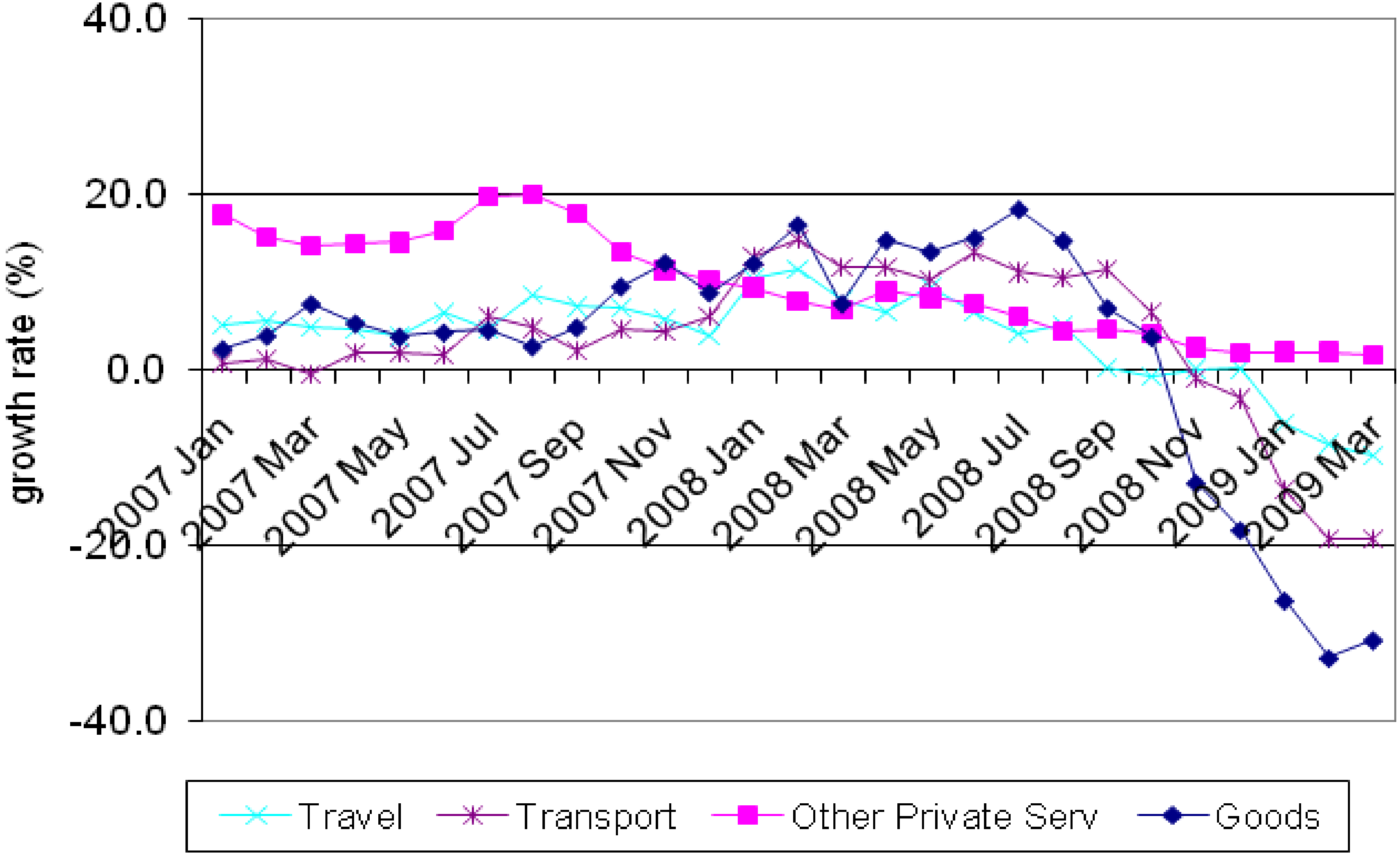
# Trade is severely impacted everywhere

*Export Growth by Region, Jan 08 – Feb 09, yoy change*

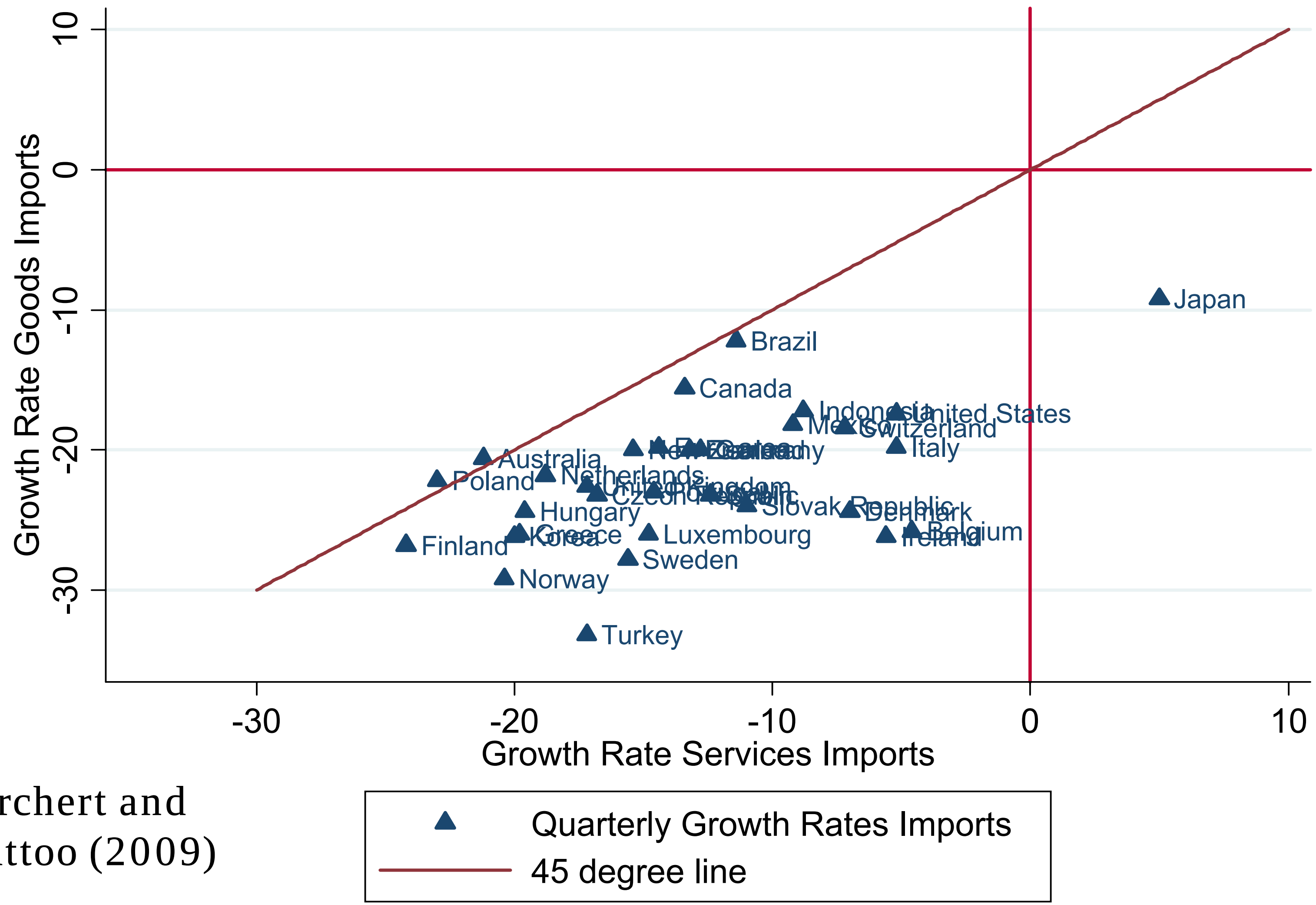



*Source: Datastream, U.S. Commerce Department and authors' calculations. Simple average of growth rates across economies within regions for a balanced sample of 45 economies reporting data*

# Modes 1 & 2: US Monthly Imports of Goods and Services

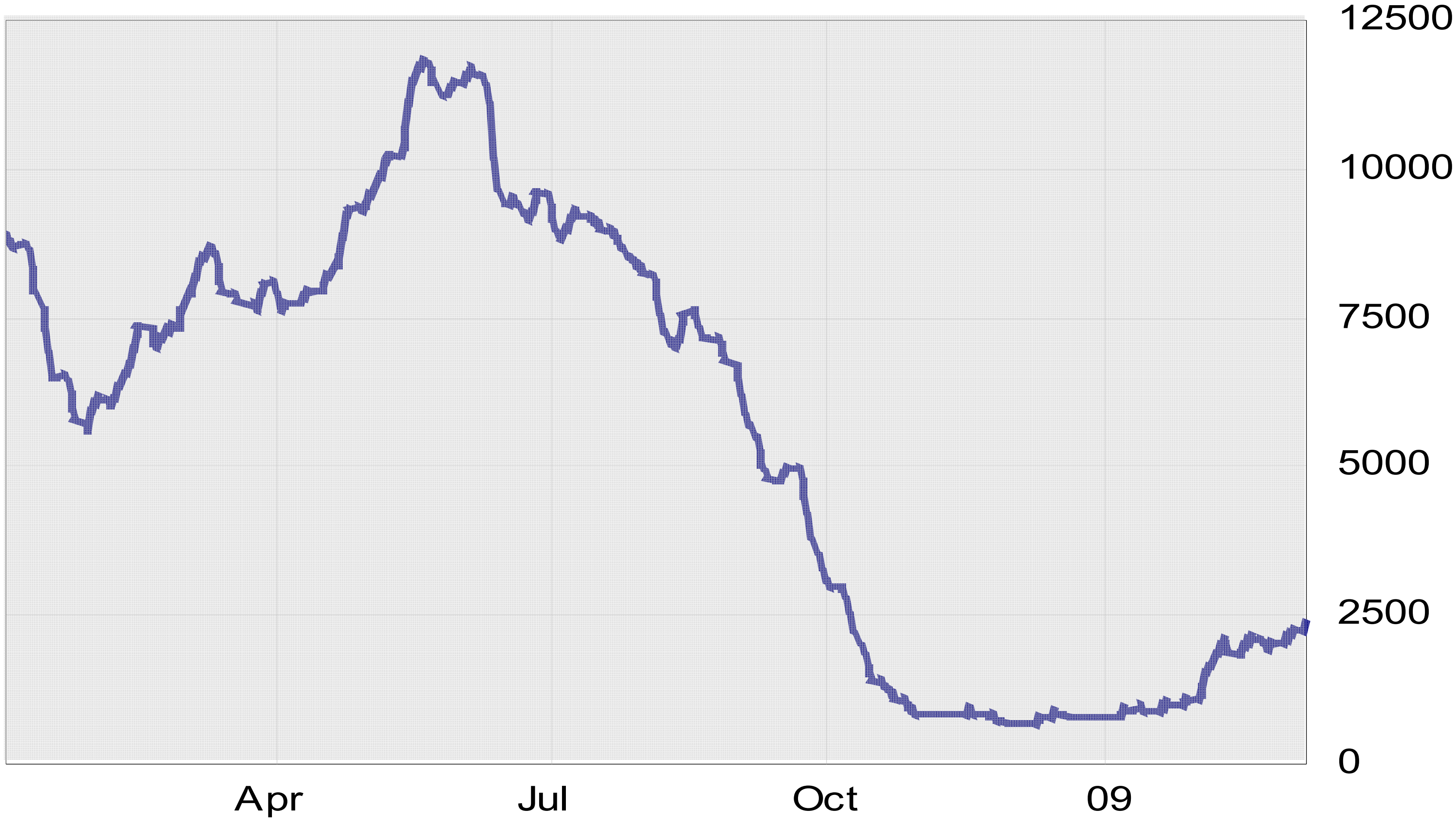


# Modes 1 & 2 overall: more robust than goods trade

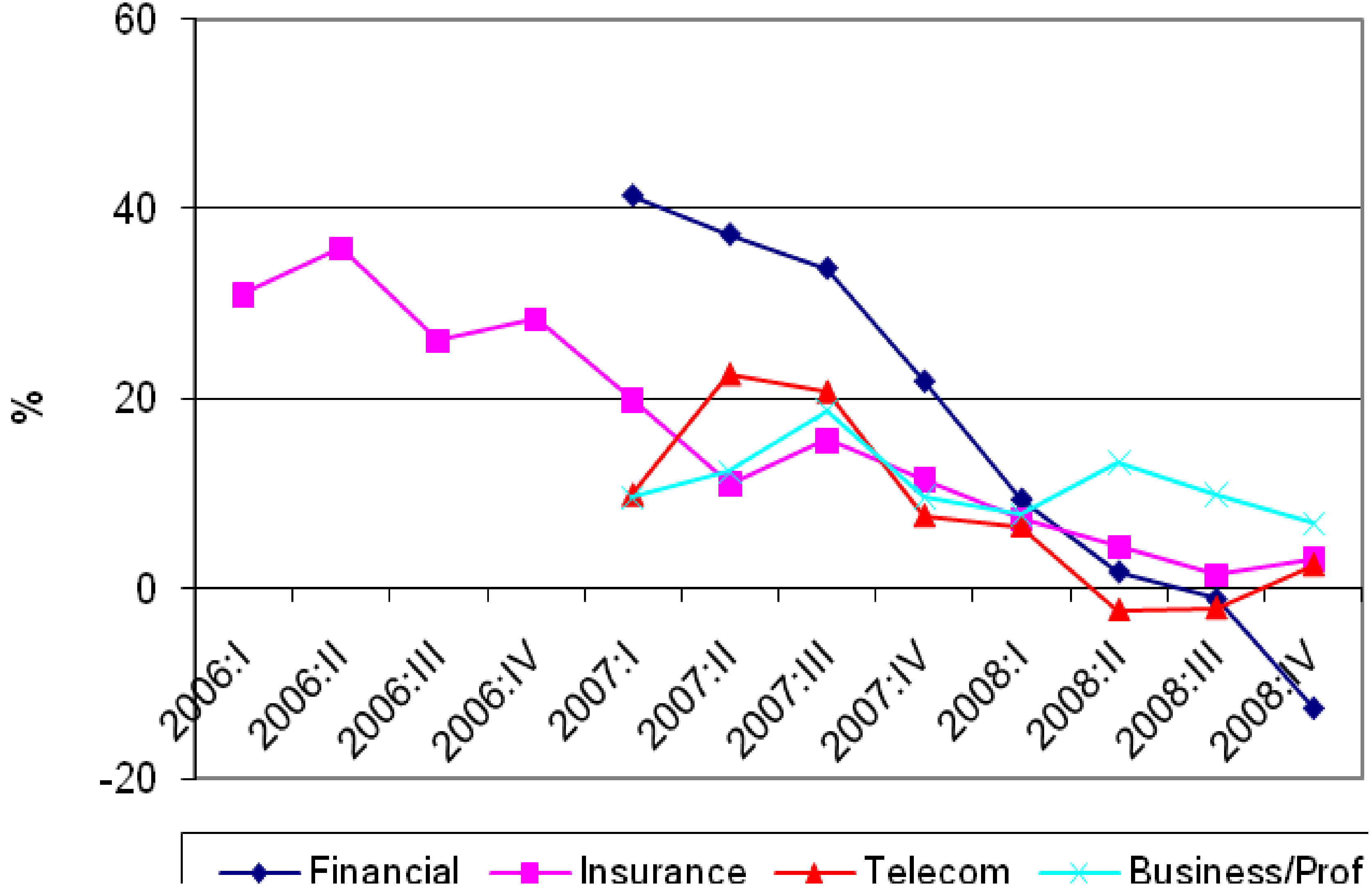



*Source:* Borchert and Mattoo (2009)

# Mode 1 (transport)
# Baltic Dry Index: linkage at work

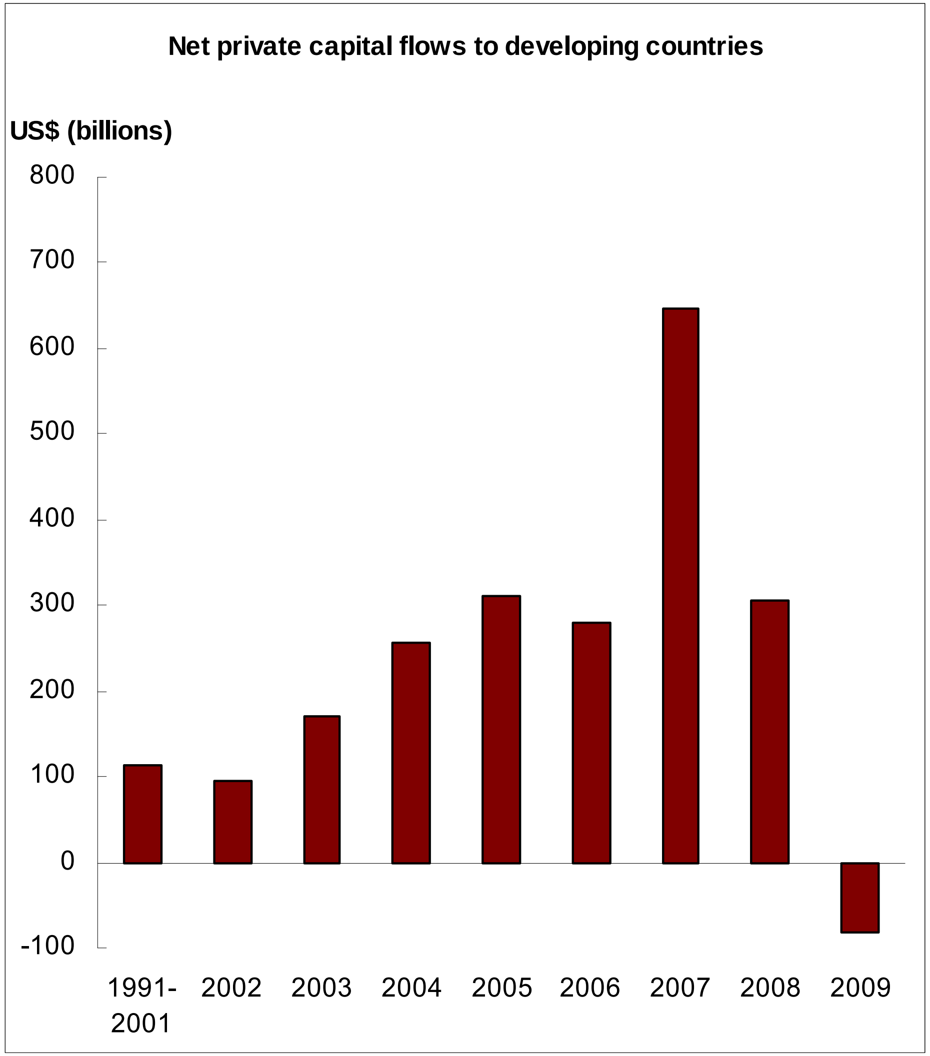


# Mode 1: US Monthly Imports of Types of Other Private Services



# Mode 3: Private capital flows to developing countries in steep decline

- Net private capital flows to developing countries will likely turn negative in 2009—a more than $700 billion drop from 2007 peak
- After a peak in 2007 at a record US$1.9 trillion, global FDI fell by roughly 15% in 2008. In 2009, FDI decline will be deeper and will spread to the developing world
- NB: No breakdown for services share



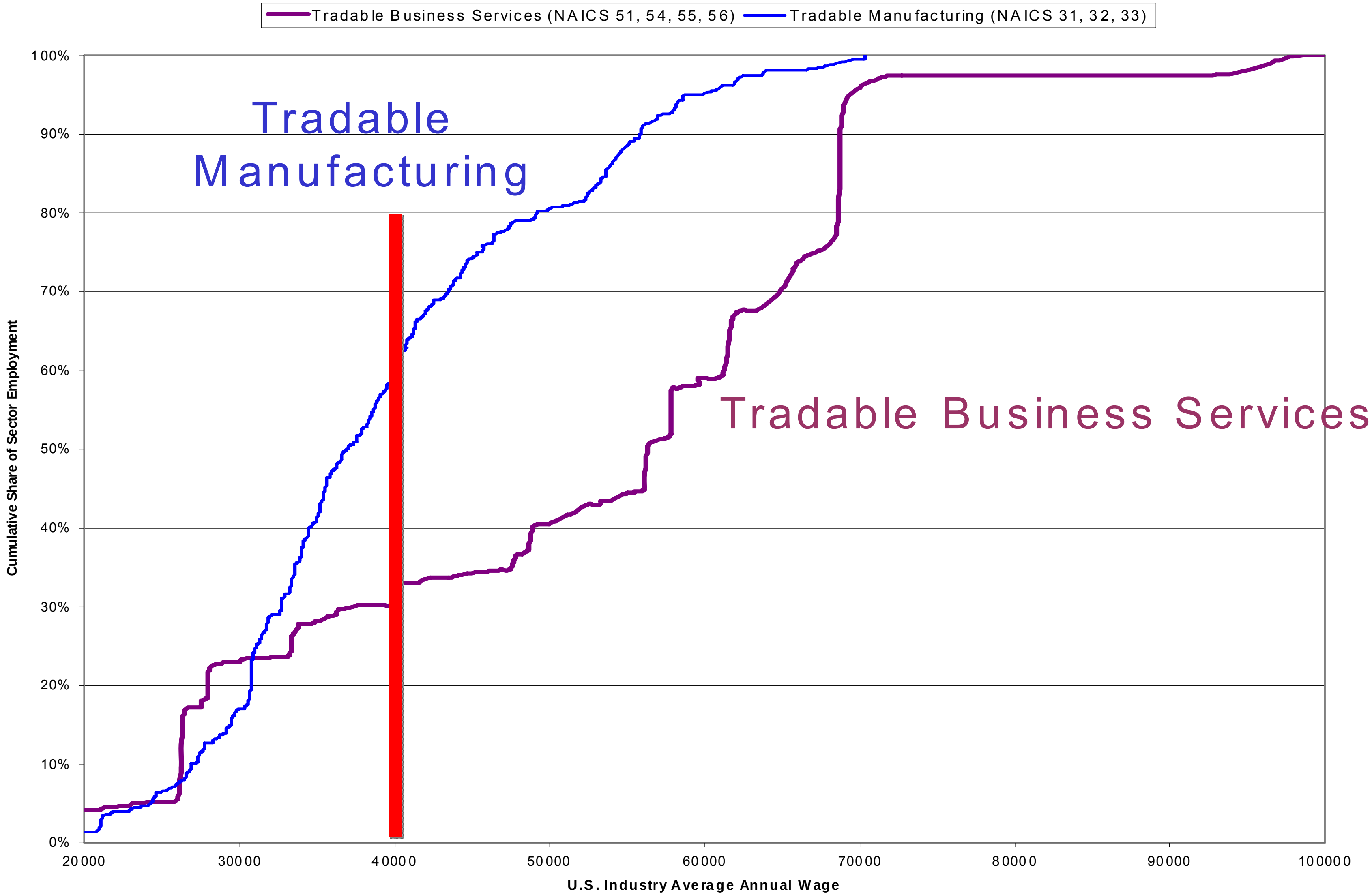
# Why is services trade more resilient?

- Demand for imports is less cyclical:
  - Producer services (business process outsourcing) an integral part of production function of OECD firms
  - Also a way to cut costs in a very competitive environment
- Services trade is less external finance dependent
  - E.g., Indian firms are fully internally financed
- Not much action to restrict trade (so far)

# How strong are protectionist incentives?

- Mode 1: Producer services (business process outsourcing)
  - limited incentives to protect because of integration into production function
  - worry about retaliation (OECD major exporter of services; US and EU account for 65% of global exports; China and India for 6%)
  - Less jobs "at risk" – services still less tradable; and if tradable, only one-third of all services jobs are at risk vs. some two-thirds in manufacturing (Jensen and Kletzer, 2008)
  - Exceptions: transport (air, road – e.g., NAFTA dispute); but here baseline is restrictive
- Mode 2: Protectionism does not "work" for sectors such as tourism – cannot offset fall in demand
- Mode 3: Makes little sense to go after firms that are already established; but may have incentives to be more restrictive re: new entry – here need more monitoring/data
- Mode 4: Major (political) incentive to be protectionist – but are starting from an already very restrictive baseline

# US Employment Shares in Tradable Manufacturing and Services Industries

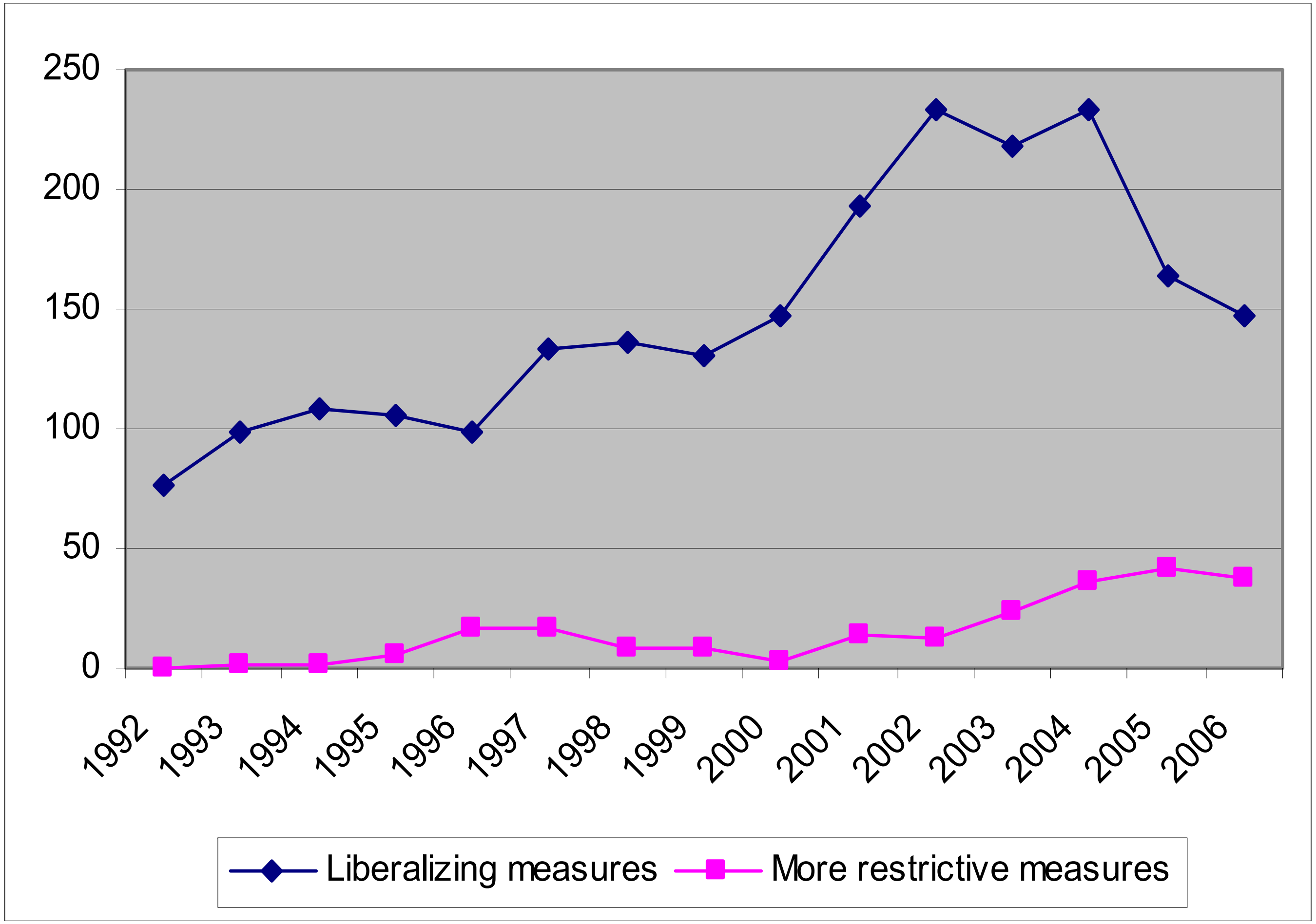



Source: Jensen and Kletzer (2008)

# Recent Measures

- Not covered by the WTO monitoring report (so far)
- Preferential procurement – no focus on services so far
  - But we have seen efforts in past – e.g., New Jersey
- American Recovery and Reinvestment Act: restrictions on hiring H-1B visa holders by financial firms receiving bailout funds
- Changes in UK legislation re: skilled immigrants (but UK has been more liberal)
- Reversal of outsourcing decisions – e.g. Sallie Mae's "repatriation" of 2,000 jobs
- China: postal law – exclusion of foreign express carriers from the local market
- Financial bailouts and "nationalism" – potential crowding out of developing country borrowers

# Mode 3? Global FDI policy trends



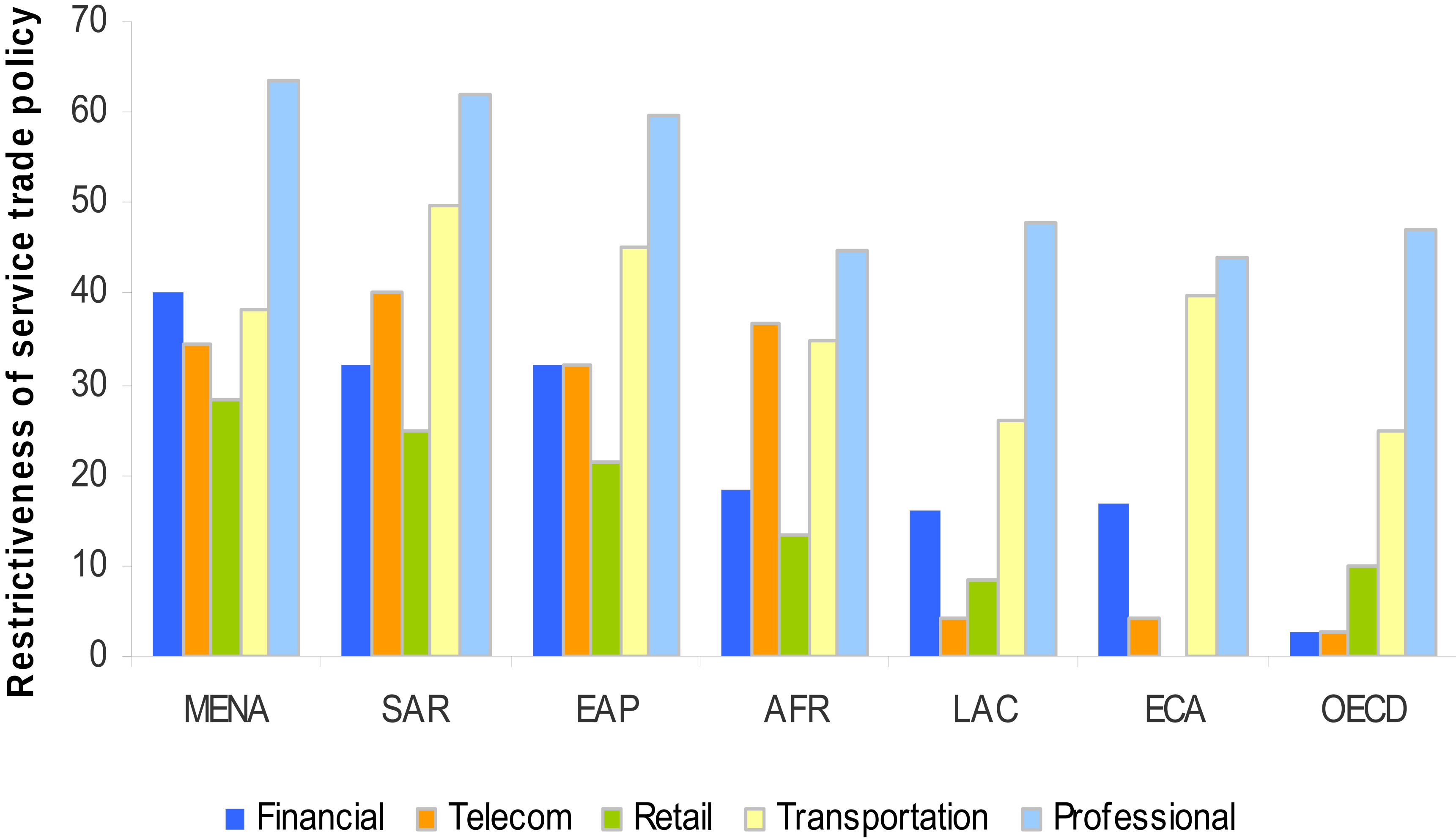

Source: UNCTAD

# Patchy progress to expand GATS

## E.g., EU-15 GATS commitments and Doha offer

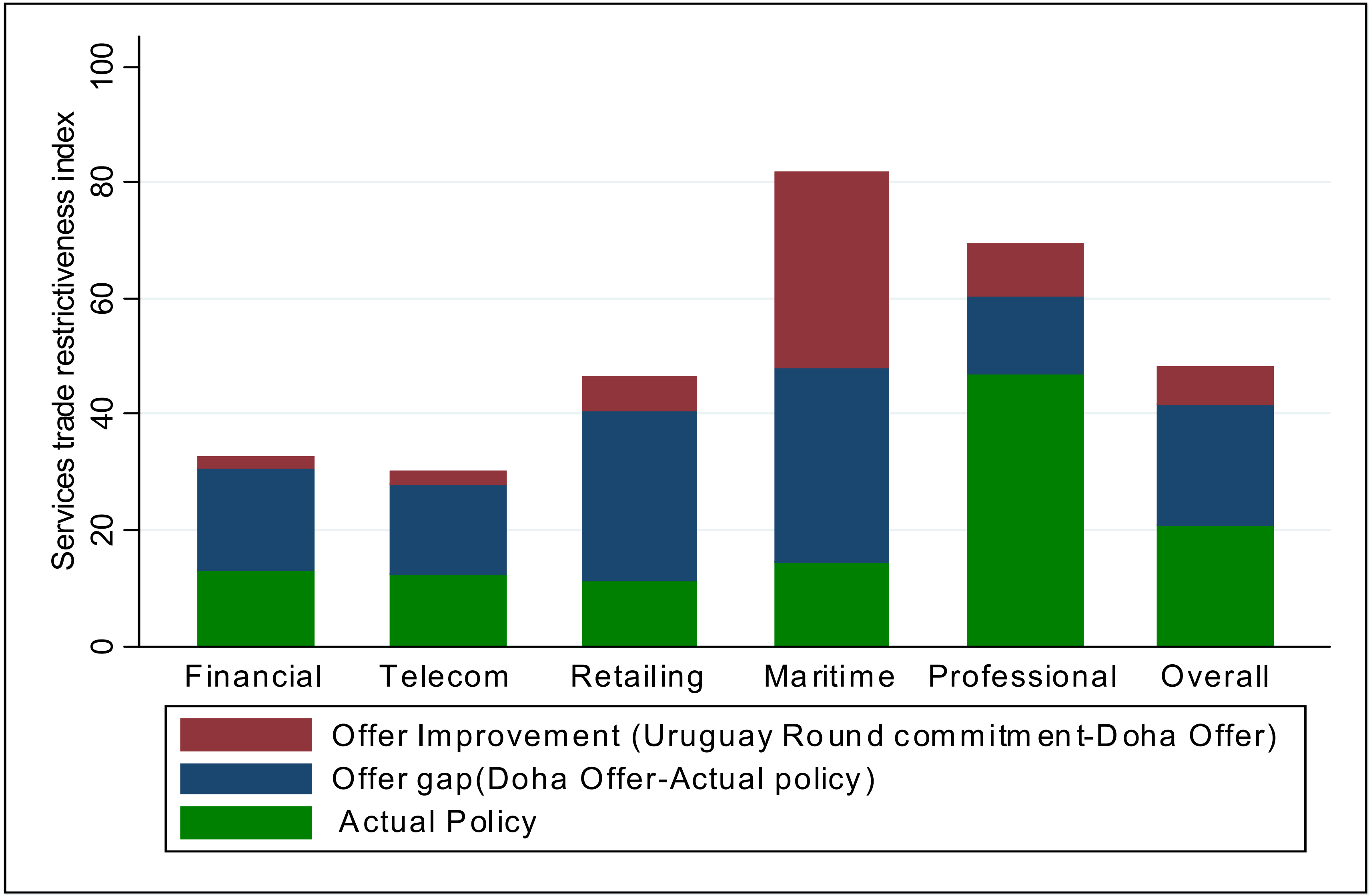
| Mode of supply | Pre-Doha | Doha offer | Difference (% points) |
|---|---|---|---|
| | | | |
| Mode 1 | 50.5 | 57.2 | 6.7 |
| Mode 2 | 66.9 | 88.2 | 21.3 |
| Mode 3 | 63.0 | 82.9 | 19.9 |
| Mode 4 | 3.5 | 4.5 | 1.0 |
| | | | |
| Total | 46.0 | 58.2 | 12.2 |

# Professional and transport services trade relatively more restricted



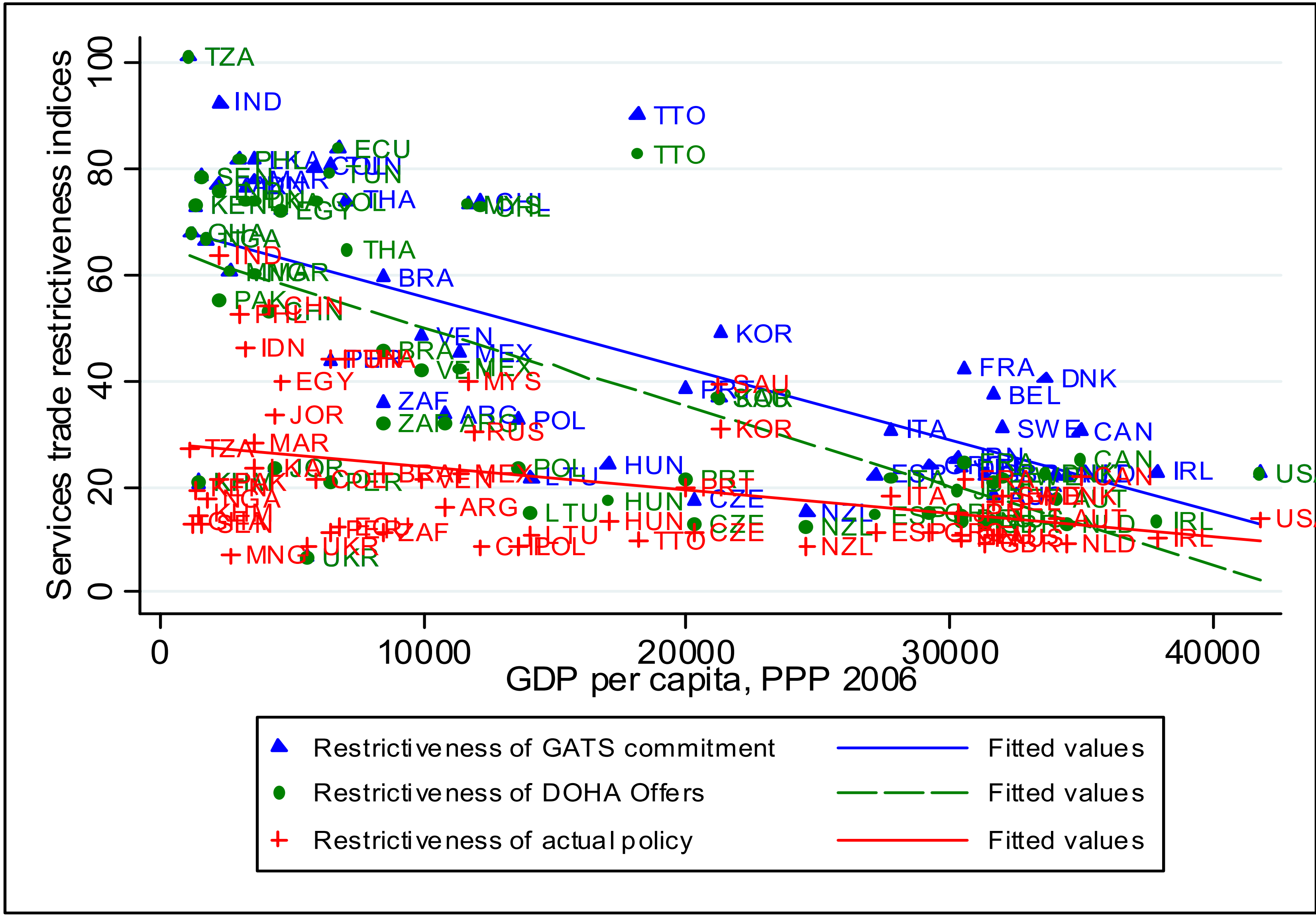

Source: Gootiz and Mattoo (2009)

# Doha offers and actual policy




Source: Gootiiz and Mattoo (2009)

# GATS schedules, Doha offers and actual policy




Source: Gootiiz and Mattoo (2009)

# Holes in the GATS

- A services deal in Doha will help, but much greater ambition needed to come close to locking-in status quo policies
  – GATS does not cover procurement – only have GPA, with limited membership and coverage
  – GATS does not address subsidies
  – Nor does it have disciplines on *exports* of services – analogy to weak rules on export taxes in GATT: governments are free to restrict exports (e.g., direct finance to home firms & consumers)
- Need to do much better on abiding by notification requirements (Art. III)
  – More monitoring/analysis of effects/incidence