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Developing countries in the WTO services negotiations

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World Trade Organization

Economic Research and Statistics Division

DEVELOPING COUNTRIES IN THE WTO SERVICES NEGOTIATIONS

Juan A. Marchetti: WTO

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DEVELOPING COUNTRIES IN THE WTO SERVICES NEGOTIATIONS

By Juan A. Marchetti *
WTO

Abstract:

The aim of this paper is to analyse developing countries' participation so far in the current round of services negotiations under the Doha Development Agenda. The paper analyses developing countries' negotiating positions, as evidenced by their multilateral negotiating proposals; their initial offers; and, to the extent allowed by the incomplete and sketchy information available, their participation in bilateral market access negotiations. A number of basic themes are raised: the essential role of services for economic development; the high costs imposed by trade protection; the benefits of liberalization; the need to make use of the WTO forum to enhance credibility and sustain domestic regulatory reform programmes; the challenges of regulatory reform and the importance of appropriate sequencing; and the benefits arising from seeking further market access overseas in those areas where developing countries have a comparative advantage.

JEL classification: D78, F10, F13

Keywords: GATS, trade in services, developing countries, liberalization, domestic policy reform.

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INTRODUCTION

After almost a year of stalled negotiations following the breakdown of talks at the Ministerial meeting in Cancún (México), WTO Members agreed last July on a framework package to give new momentum to the Doha round of trade negotiations. As part of those decisions, Members postponed the 1 January 2005 deadline for concluding the talks to an as-yet unspecified date, at least until the sixth WTO Ministerial Conference to be held in Hong Kong, China, in December 2005.

Although negotiations on agriculture got the primary attention of both negotiators and the media, WTO Members were not indifferent to the services negotiations, and urged countries to submit their initial offers as soon as possible and to revise the existing offers on the table by May 2005. In addition, they reaffirmed the objective of achieving progressively higher levels of liberalization and give special attention to sectors and modes of supply of export interest of developing countries.

The months ahead will probably be extremely busy for all WTO Members. The task is particularly challenging for developing countries, who have been active participants in the services negotiations since the very beginning in the early days of 2000. This is as good a time as any to assess what developing countries have done so far, and what they should be doing to achieve a deeper integration of their economies into the world trading system, and the advancement of higher and sustainable economic growth, in line with the goals of the Doha Development Agenda.¹

Before moving forward one caveat is necessary: there are such large differences between developing countries – from LDCs, with scarcely any modern domestic service industry, to some high income service economies, and many countries in between- that there may be little justification for generalizations. The recommendations made in this paper will have to be seen in that light.

The paper is organized as follows. The next section will briefly discuss the importance of services for development and the costs of protection. Section 2 will analyse the participation of developing countries in previous services negotiations, by focusing in particular on the pattern of their commitments in the Uruguay Round and extended negotiations. Section 3 will describe developing countries' negotiating positions thus far in the current round, as evidenced by their multilateral negotiating proposals; their initial offers; and, to the extent allowed by the incomplete and sketchy information available, their participation in bilateral market access negotiations. The section will be factual. Section 4 will then turn to an analysis of those negotiating positions, making the necessary policy recommendations. The final section concludes. As we will see, a number of basic themes will emerge from that discussion: the essential role of services for economic development; the high costs imposed by trade protection; the benefits of liberalization; the need to make use of the WTO forum to

¹ Trade liberalization and integration into the world economy is not an end in itself, but a powerful means to achieve the objective of sustainable economic growth and development. Powerful as it may be, it is worth remembering that trade liberalization is a necessary but not a sufficient condition to attain economic development. Many other factors, such as geography, resource endowments, the protection of property rights in its largest sense, and the quality of the institutional and regulatory frameworks, will be determinants of success. And it should be unfair to place all the expectations of success in only one aspect of any development policy – trade- and in only one section of the trade chapter, i.e. services. Therefore, all the arguments that will follow will have to be considered in that light, at the risk of course of oversimplifying certain elements.

enhance credibility and sustain domestic regulatory reform programmes; the challenges of regulatory reform and the importance of appropriate sequencing; and the benefits arising from seeking further market access overseas in those areas where developing countries have a comparative advantage.

1. Services, Development and the Cost of Protection

Simply defined, services are a diverse group of economic activities distinct from manufacturing, mining and agriculture. The term encompasses a broad range of industries that provide the basic economic infrastructure (communications, transport, distribution, energy-related services, construction, water supply, sanitation and sewerage services, waste collection and disposal), financial infrastructure (banking, insurance, financial markets), support to business (advertising, marketing, computer services, professional services), or needed social infrastructure (education, health and social services).

The share of services in GDP and employment tends to rise with income, but even for the poorest countries it is now significant. In 2001, service sectors accounted for 45% of GDP in low-income economies; 57% in middle-income; and almost 71% in high-income. Services activities in low- and middle-income countries have been expanding faster than GDP for the last two decades, and represent on average 5 to 10 percent points more of GDP than in the early 1980s. An implication of this continuous shift toward services is that the overall growth of productivity in the economy will be increasingly determined by what happens in the service sector (IMF, 1997).²

Services are essential for development, broadly understood as improvements to human welfare. Availability of essential services, such as water supply, sanitation, power supply, transportation, education or health, is associated with higher productivity and earnings. But services are often inaccessible, prohibitively expensive, or, even when accessible, of low quality and unsuited to the needs of consumers (World Bank, 2003). Moreover, services sectors can be particularly important in terms of employment, because many services are labour-intensive. In principle, the development of the labour-intensive sector can help reduce poverty by generating labour-intensive growth (McCulloch, Winters and Cirera, 2001).

However, productivity gains –and therefore growth and poverty reduction– are often hampered by an inefficient allocation of resources as a consequence of trade protection. Although countries usually approach multilateral trade negotiations with the objective of seeking “concessions” or market access opportunities in other markets, while minimizing the export opportunities that they grant in their own markets –a crude but real mercantilist approach to negotiations– it is worth emphasizing that trade protection results first and foremost in a cost to the country that imposes it.

Liberalization of services sectors means not only the reduction or elimination of barriers that affect the services per se, but also those barriers that affect services firms, such as restrictions on entry, legally established monopolies or oligopolistic market structures, discriminatory taxation, limits on foreign investment.³ The arguments for liberalizing trade in services are

² See the discussion on "Causes and implications of deindustrialization" in chapter III.

³ This is so because of the broad definition of trade adopted by the GATS, which encompasses both traditional forms of supplying services (e.g. cross-border) and the supply through commercial presence of juridical persons (mode 3) and natural persons (mode 4). See Article I GATS.

similar to those for trade in goods, and are based on the improvement of resource allocation in line with social marginal costs and benefits (the traditional static gains from trade); a better access to better technologies, inputs and intermediate services; greater domestic competition; transfer of know-how and technology through investment; and a shake-up of industry that may create a Schumpeterian environment especially conducive to growth (Dornbusch, 1992). Liberalization in the GATS context, which basically implies greater competition in the market and non-discrimination against foreign services and service suppliers, leads to a more economically rational market structure. Markets in protected economies are narrow, and lack of competition from the rest of the world, whether actual or potential, fosters oligopoly and inefficiency. Protectionism creates market power for domestic firms; while trade openness exposes those same firms to greater competition, reducing monopoly rents, driving down margins, and reducing prices for consumers. In a competitive environment, firms are forced to innovate, to introduce new products, and to improve quality constantly; otherwise, they will be forced to exit the market.

Protection in services (e.g. prohibitions of new entry into the market, or more restrictive operating conditions imposed solely on the new entrant, be it foreign or not) is, first of all, a tax on domestic consumers. The primary effect of protection is to reduce the supply of certain services and thereby force domestic demand towards more expensive, domestically produced services. Protection reduces supply and raises prices directly because of the higher costs of domestic producers. As such, protection becomes a tax on domestic consumers and leads to a redistribution of income from consumers to domestic producers. The effects of protection on prices to consumers can even be worse if the market is characterized by imperfect competition or a monopoly.

Although experiences have varied considerably across countries and sectors, the introduction of competition has generally led to improvements in services performance, increases in infrastructure investment and service coverage, improvements in service quality, and prices more closely aligned to underlying costs. The size of such changes depends enormously on the extent to which the market is liberalized and the effectiveness of regulation. In telecommunications, competition has boosted telecommunications coverage, lowered repair requests, raised call completion rates and reduce the time needed to receive a telephone line. In railroads, market reforms have increased locomotive availability. In ports, market reforms have shortened waiting times for vessels; while, in electricity, they have lowered energy losses, outages per customer, and rates of plant unavailability (World Bank, 2004a). In banking, foreign bank in the context of market reforms and strengthened prudential regulation, has had a dynamic positive impact on the efficiency and competitiveness of local banking systems (World Bank, 2001b).

Another reason why protection against foreign sources of service supply is bad for the economy is that it results in a tax on production in general. Many services –usually called “producer services”– are intermediate-demand (as opposed to final-demand) services that represent inputs into the production process of firms and other organizations across all sectors of the economy.⁴ These services include activities such as banking; finance; insurance; business services (e.g. various professional services, research, advertising, marketing,

⁴ For example, in Bangladesh, services-contents are the largest per unit of output in industrial production. For instance, the contribution of services to ready-made garments industry production (the largest foreign exchange-earner for Bangladesh) ranges between 20-25 per cent (Azad, 1999).

computer); transportation; storage; and communication services.⁵ Increases in the price of inputs due to protection will in many cases translate into a tax on the production of exportable and import-competing goods and services. Governments are often aware of the dangers of protection of tangible inputs into production processes, and that is why the so-called capital goods usually benefit from a preferential import regime, even in those countries most attached to import-substitution industrialization. But sometimes governments do not seem to realize –at least judging by their actions- to what extent protection of service inputs raises similar problems and to what extent it is costly (Hindley, 1988). Lack of storage capacity, poor stock management, unreliable transportation, expensive communications, poor product design, insufficient and costly financing, inadequate legal advice, or even outdated software products and processes are key determinants of firms' competitiveness and can even destroy otherwise favourable prospects for meeting domestic or export demand. The price and quality of these services are therefore crucial in determining the cost of all other products in the economy, and are a determinant factor of a country's chances of exploiting its comparative advantages, not only in service exporting but also in non-service exporting (e.g. mining, agriculture, textile, other manufactures).

The productivity gains in the final goods sector from liberalizing access of firms to foreign – and more efficient- intermediate services may be substantial (Markusen, Rutherford, and Tarr, 1999). A great part of the benefits of liberalizing access to producer services comes from the enlargement of the market motivated by the dynamics of trade between upstream producer service firms and downstream user industries: better and cheaper inputs reduce cost in the downstream industry; the downstream industry expands; demand facing the upstream industry increases; the upstream firms increase output and reduce costs; and a larger market attracts new entrants in the upstream industry (Hodge and Nordas, 2000). In countries where tariffs for manufactures are low and prices of services high, manufacturers may well end up facing low or even negative effective rates of protection (Hoekman and Djankov, 1997).

It is extremely difficult to estimate the costs of barriers to trade in services. Nevertheless, there is substantial evidence from case-studies that policies that reduce competition in services industries, particularly in those that are heavily used as intermediate products, are very costly (Box 1).

Estimations of the level of restrictiveness in different service sectors, albeit limited due to difficulties in identifying and quantifying barriers to trade in services, suggest that policies towards important service sectors that are used as inputs in production and trade (e.g. business services, transportation, finance, telecommunications) are frequently very restrictive in developing countries (Hoekman, 2000, and Warren and Findlay, 2000).⁶

⁵ In general, the vast majority of researchers agree that producer services are intermediate-demand (as opposed to final-demand) services that represent inputs into the production process of firms and other organizations (as opposed to households and individuals) across all sectors of the economy. At an operational level, however, the expression "producer services" has been used with different meanings. For some authors, the concept is synonymous with "business services", e.g. computer services; advertising; management consulting services; and various professional services, such as accounting services and legal services. For others, the concept includes business services plus finance, banking, insurance, real estate services. For others still, the concept includes all those services plus transportation, storage, distribution, and communication services. I tend to use a broad concept of producer services.

⁶ See Hoekman (2000) for a summary of the diverse attempts to quantify restrictions on trade in services, and Warren and Findlay (2000) for an explanation of the difficulties encountered in trying to quantify

Recent research using CGE techniques to assess the impact of service sector reform shows that there may be big gains in liberalizing services trade (Hoekman ,2000 , for a summary of the most important studies). Additionally, further econometric evidence, relatively strong for the financial sector and less strong but still statistically significant for the telecommunications sector, shows that openness in services influences long run growth performance. Indeed, countries that liberalized both sectors grew at faster rates than other countries (Mattoo, Rathindran, and Subramanian ,2001).

To sum up, a reduction in protection for domestic services and service suppliers against foreign competition will, if appropriately implemented, further the economic interests of the country. The predominant view nowadays among economists is that an open trade regime is an important part of growth and development policy. Protection imposes not only direct – sectoral- costs, but also wider costs in terms of lost opportunities and growth.⁷ The adequacy of services in general will be a determinant factor of a country's success and another's failure, in diversifying production, expanding trade, coping with population growth, reducing poverty, and improving environmental conditions.

restrictions on trade in services. See additionally, the work done by the Australian Productivity Commission on this issue (<http://www.pc.gov.au>).

⁷ Pinning down the link between openness and growth is not an easy task, due to innumerable measurement and statistical problems. Having said that, it is also true that, as explained by one of the most critical analysts of studies on the relationship between openness and growth, “no country has developed successfully by turning its back on international trade and long-term capital flows” (Rodrik, 2001).

Box 1. How costly can protection of services be? Some examples.

In Chile, deregulation and liberalization of international **maritime transport services** led to a saving of some 22-25 per cent of the freight bill on Chile's exports to the US (Bennathan, 1993). For a small economy confronting given world prices of traded goods, higher **transport costs** reduce export prices and increases prices of delivered imports. The poor export performance of Sub-Saharan African countries has also been attributed to high transport costs, which where in turn adversely influenced by the anticompetitive cargo reservation policies adopted by most of these countries (Yeats et al., 1996).

Poor **infrastructure and logistics** may lead to high inventories, having adverse effects on companies' costs and competitiveness. A recent study found that raw materials inventories in the manufacturing sector in the 1970s and 1980s and 1990s were two to five times higher in developing countries than in the United States, despite the fact than in most developing countries real interest rates are at least twice as high. He identified poor infrastructure, ineffective regulation, and deficiencies in market development, as the main arguments for that result. Cross-country estimations show that a one standard deviation worsening of infrastructure increases raw materials inventories by 27% to 47% (Guasch and Kogan, 2001).

An important sector in the context of trade reform is **distribution**. If there are barriers to entry into distribution, those who control this sector may be the primary beneficiaries of trade liberalization, impeding the distributional effects in favour of consumers. In agriculture, para-statal marketing boards often strongly restrict competition for the products of poor farmers and restrain their incomes. For example, in Francophone African countries, the absence of any competition in the purchase of seed cotton from farmers has implied that farmers have been paid prices for their seed cotton that tend to be far below competitive levels. In terms of lint equivalent, seed cotton prices in these countries have generally been within a range of 40 to 50 percent of the export price of cotton lint, compared to ratios averaging almost 90 percent in India and around 80 percent in Zimbabwe (Hoekman, Michalopoulos, Schiff, Tarr, 2001).

Another example concerning **distribution** services: In Zambia, the government abolished the official purchasing monopsony in maize; the activity became dominated by two private firms which probably colluded to keep prices low and which abandoned purchasing altogether in remote areas. In Zimbabwe, on the other hand, three private buyers emerged after privatisation, including one owned by the farmers. Here the abolition of the government monopoly resulted in increased competition and prices and farm incomes rose appreciably (Winters, 2000).

2. Developing countries in previous multilateral services negotiations

The Uruguay Round marked the first time in which developing countries were significantly involved in multilateral trade negotiations, and also the first time in which they were called upon to negotiate on services trade. The introduction of services into the work programme of the GATT in the 1980s did not come without controversy, and was originally marked by North-South confrontation, with developed nations -led by the United States- supporting the issue and developing nations -led by Brazil and India- toughly opposing it (Bahgwati, 1987). The North-South confrontation of those years is long past, for one basic reason that can be

summed up in one word: flexibility, meaning the great freedom of governments to decide the level and scope of the commitments they make, and therefore the speed at which liberalization of their own services markets progresses. Indeed, while WTO Members may, via their GATS commitments, allow the access of foreign services and service suppliers to their markets, they are not obliged to. Moreover, if they choose to make commitments, they can maintain discriminatory measures or quantitative restrictions. Although WTO Members certainly negotiate with each other on the level and form of protection, the final outcome is, in the final instance, a unilateral choice by the Member concerned. As we will see, WTO Members, and most particularly the less developed among them, made ample use of the leeway provided by the agreement. Whether this reflects good policy-making is an entirely different question, to which we will turn in the following sections.

As might have been expected from the reluctant participation and extremely defensive position of developing countries in the services negotiations during the Uruguay Round, the initial sets of commitments arising from that process did not impose any liberalization obligation on these countries. Commitments made to allow market access were minimal and, when they were made, they did not go further than the binding of the status quo. The situation is not that different in the case of developed countries, although their sectoral coverage is much wider.⁸ It must be acknowledged that, unlike previous rounds of negotiations, which essentially focused on trade liberalization within an established framework of rules, services negotiations demanded the creation of a completely new framework of disciplines. For most developing nations, this was indeed a completely new negotiation universe. A great deal of negotiating effort went therefore to the rule-making aspects of the agreement (which remained incomplete anyway)⁹, and attention was certainly diverted from the objective of actually liberalizing trade in services. It is no wonder then that schedules of specific commitments came to reflect that situation.

Schedules of commitments do not necessarily involve liberalization, and in fact most of them appear to have been confined, in the best of the cases, to binding the status quo. A note of caution is in order, though. The schedules of commitments provide in general an incomplete picture of the real degree of liberalization in a market for two basic reasons: firstly, commitments on most sectors were made at the end of the Uruguay Round,¹⁰ and sectors may have well become more open since then; and, secondly, the absence of a commitment on a particular sector or mode of supply cannot be taken as indicating that access is forbidden or that foreign suppliers are discriminated. Countries may have refrained from making commitments for different reasons, including disinterest in the negotiations or tactical motivations linked to the preservation of negotiating coins for future multilateral or regional negotiations. Having said that, overviews of commitments are still useful, since they provide an indication of countries' past intentions, and the prospects and challenges for the current round of negotiations.

⁸ The extent of the gap between existing policies and GATS commitments is unknown due to the lack of systematic information on the former. However, anecdotal evidence, supported by experts in the various fields of services, supports the assertion that in general multilateral commitments did not go beyond the status quo (See Hoekman, 1996; and Dobson and Jacquet, 1998 for some examples).

⁹ Disciplines are still to be developed in the following areas: domestic regulation, emergency safeguards, subsidies and government procurement. Besides, there's hardly any discipline on private anti-competitive practices.

¹⁰ Formally concluded in April 1994, but schedules of services commitments were pretty fixed by December 1993.

The commitments currently in force can be assessed by reference to four aspects: the Members involved; the sectors covered; the modes of supply bound; and the commitments' restrictiveness. In terms of the number of sectors inscribed in schedules, the picture that emerges is clear: in general developing countries have committed substantially less than developed countries and transition economies. Moreover, on average, the number of subsectors included by transition economies is fairly similar to the number included by developed nations. The only criterion used here is the inclusion of a subsector in a Member' schedule.¹¹ This approach however does not allow an assessment of the quality of the relevant commitment in terms of the number of modes of supply covered or the existence and restrictiveness of limitations included (Table 1).

Table 1: Commitments by country group, January 2004

Countries	Average number of sub-sectors committed per country	Range (Lowest/highest number of scheduled sub-sectors)
Least-developed economies	20	1 – 110
Developing & transition economies	54 (106)*	1 – 154 (58-154)*
Developed countries	108	87 – 117
Accessions since 1995	106	37 – 154

* transitions economies only.

Notes: Total number of subsectors: 160; Total number of Members: 146.

Source: WTO Secretariat

An interest feature is that acceding countries, mostly low- and middle-income countries, undertook more ambitious commitments than many participants in the Uruguay Round.¹² The basic reason for that outcome may lie in the context of those negotiations, which is quite different from that in ordinary trade rounds. The terms of a country's accession to the WTO are negotiated in quite detail between the country and all WTO Members¹³, while the majority of current schedules has been negotiated in a more anonymous setting (WTO, 2001). In other words, in spite of their interactions with other Members, participants in a trade round have certain "independence" in making their commitments.

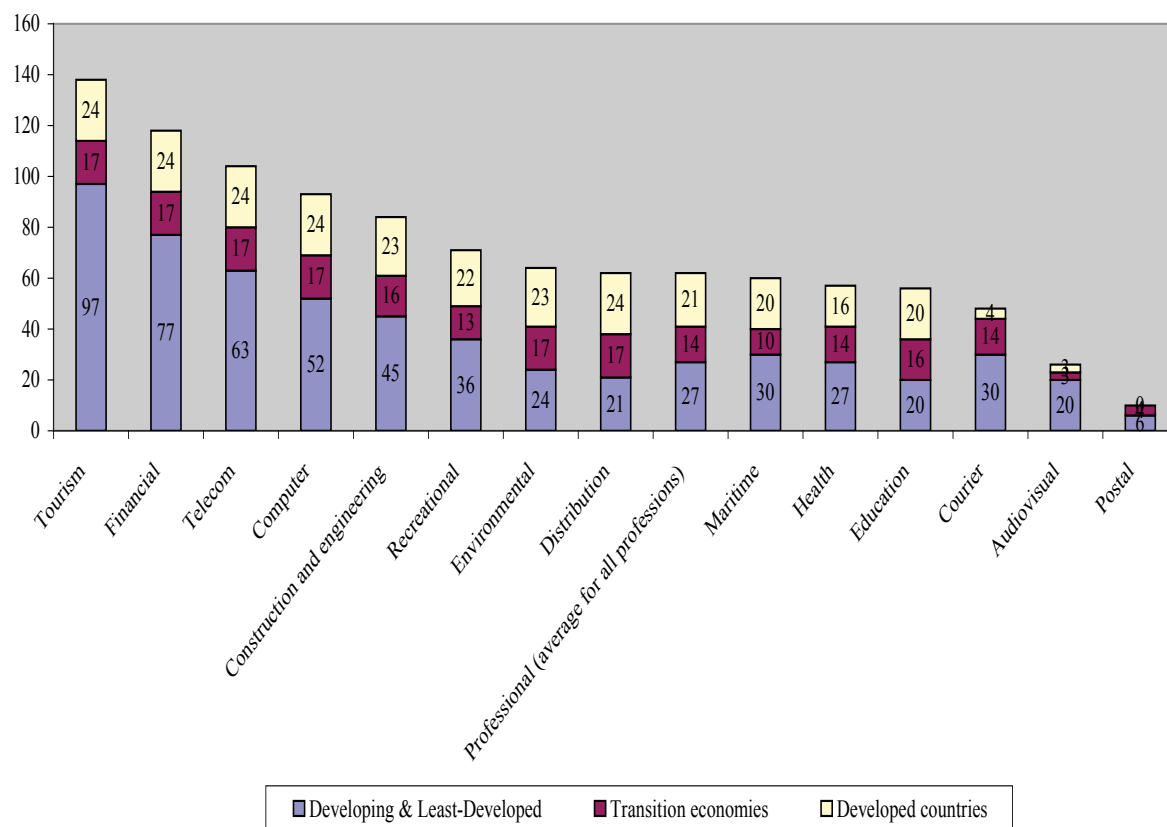
¹¹ The classification list generally used by WTO Members for scheduling commitments on market access and national treatment divides all services into 11 broadly defined service sectors, and these are further divided into some 160 sub-sectors. Those 11 sectors are the following: Business Services (including all professional services, and computer-related services); Communication Services (divided into Postal, Courier, Telecommunication and Audiovisual Services); Construction Services; Distribution Services (including both retail and wholesale); Education Services; Environmental Services; Financial Services (including banking, securities, and insurance); Health and Social Services; Recreational Services; Tourism and Travel-related Services; and Transport Services.

¹² Acceding countries is the expression used in general to make reference to the WTO Members that joined the Organization after 1995.

¹³ In practice, although all WTO Members give their blessing to the terms of a candidate's accession, the general details are negotiated by the those who decide to be part of the working party dealing with the particular accession; while the terms of the acceding country's schedule of commitments are negotiated with a smaller group of countries –those that expressed an interest in negotiating bilaterally with the acceding country.

Chart 1

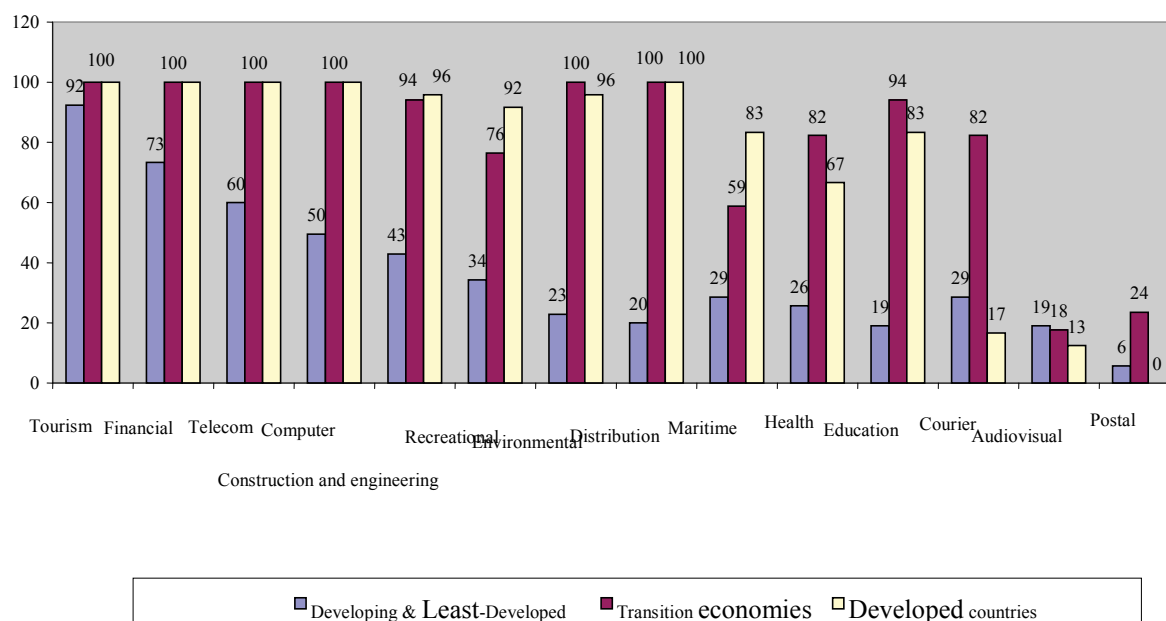
Chart 1. Number of WTO Members' with commitments in each sector, March 2004
(Maximum number: 146)



Source: own elaboration based on WTO database

Chart 2

Chart 2. WTO Members' with commitments in each sector, March 2004
(As percentage of each country group)



Source: own elaboration based on WTO database

Charts 1 and 2 reflect the sectoral pattern of commitments and, to a great extent, the scheduling preferences revealed by Members in past negotiations. We divided our analysis in three broad categories of Members: developing (including least-developed) countries, economies in transition, and developed countries.¹⁴ Chart 1 presents the number of commitments in the main sectors; while chart 2 shows the percentage of Members having made commitments within each country group (e.g. 80 per cent of all developed countries, 60 per cent of all transition economies, etc.). The latter gives us an additional indication of the scheduling preferences of Members within each group.

Among the main broad service sectors subject to negotiation in the past, tourism has drawn by far the highest number of commitments, followed by financial, and telecommunication services.¹⁵ In general, developed countries¹⁶ have made commitments in all major sectors, with the notable exceptions of courier, audiovisual, and postal services (where no developed country made a liberalization commitment). It is interesting to observe that a good number of

¹⁴ It is worth remembering that there is no legal definition of “developing countries”. Nevertheless, according to the taxonomy used for this analysis, out of 146 WTO Members at the time of writing this paper, we have 17 transition economies, 24 developed economies (basically all OECD countries less Mexico and the Republic of Korea), and 105 developing countries. The 15 EU Member States are counted individually. This taxonomy is, of course, without prejudice to the status of individual countries in the WTO.

¹⁵ In this analysis, we depart from the traditional presentation of commitments in the broad 11 categories referred to in the previous footnote, in order to avoid the misinterpretations arising from the highly aggregated nature of those categories. Our approach allows us to see the situation with respect to important “subsectors”, such as professional services, courier, postal, audiovisual, or computer-related services.

¹⁶ Developed countries in this section include the 15 EU Member States (before the enlargement in 2004), the US, Japan, Australia, New Zealand, Norway, Switzerland, Iceland, Liechtenstein, and Canada.

developed countries (33 per cent of all them) have also found it difficult to commit to liberalization or to allow market access in the area of health and social services. There is more variation among developing countries in the sectors chosen. Almost all developing countries (92 per cent of the total, including Least-Developed nations) have made commitments on tourism services, where they clearly seem to have a comparative advantage. It is also interesting to highlight that while a majority of developed countries have refrained from making significant commitments, the so-called transition economies have tended to follow the pattern of commitments of more developed nations, particularly in sectors such as finance, telecommunications, construction, computer, distribution and professional services, where all of them have committed to allow access to their markets. A closer look at individual schedules from transition economies reveals that access conditions are in general quite open. They have even been more forthcoming than developed countries in areas such as health, education, courier and postal services. What can explain this pattern of commitments from transition economies? In this author's view, the main reasons are to be found in the radical market reforms carried out by those countries in the early 1990s, after decades of state-trading regimes, and the perception of the benefits of commitments in terms of integration to the multilateral trading system and the attraction of investment.

The high number of commitments in tourism services from developing countries is fairly easy to explain, taking into account that most of these countries seem to enjoy a comparative advantage in this area, and access conditions to the main activities (e.g. hotel and restaurants) are fairly liberal worldwide.¹⁷ Other more "sensitive" areas, such as travel agencies and guides, are more often reserved to nationals.

The relatively "high" proportion of commitments on financial and telecommunication services by developing countries is, to a certain extent surprising, but may also be telling in terms of the political economy of liberalization and the advantages/disadvantages of pursuing narrowly defined sectoral negotiations. Negotiators and observers often discussed in the past whether sector-specific negotiations would be able to deliver meaningful results in the absence of cross-sectoral trade-offs that could benefit those countries not having a comparative advantage in the export of the sector subject to negotiation. As can be seen from the results of the negotiations on financial services and telecommunications, those assumptions proved to be wrong. It is fair to acknowledge that, in terms of quality, the negotiations on telecommunications appear to have been more meaningful, providing for genuine open markets in many cases. Many factors can explain the success of these negotiations, compared to contemporaneous negotiations on maritime transport and the movement of natural persons. In both telecommunications and financial services, the sectors were of key interest of developed countries, particularly the US and the EU. In addition, in the case of telecommunications, the success owed a great deal to the liberalization and deregulation trends in world telecommunication markets at the time. In that sense, even if the negotiations did not prompt further liberalization, they helped consolidate domestic reform programmes already underway. In both negotiations the involvement of central decision-makers was crucial, something that seems to be a key ingredient if international cooperation and multilateral commitments are to serve the purpose of accompanying and sustaining domestic reform processes.¹⁸ Clearly, in both sectors, final decisions were not taken just by

¹⁷ Even promotion activities, such as investment incentives for the construction of hotels, would not be against "liberal" commitments on market access and national treatment in the GATS, provided those incentives are granted on a non-discriminatory basis.

¹⁸ See Hoekman and Messerlin (2000).

trade negotiators but by the sectoral policy makers, which were at the same time involved in the regulatory reform programmes in their countries.¹⁹

In spite of the big achievement of both negotiations, the outcomes differ in significant respects. Telecommunication negotiations marked the first time in which WTO Members undertook additional commitments on regulatory disciplines on the basis of a common text. By the end of the negotiations, 57 (out of 69) WTO Member governments having submitted commitments on this sector also committed to the Reference Paper in whole or with few modifications;²⁰ while six other WTO Member governments undertook some kind of commitment on regulatory behaviour. Additionally, apart from locking in reforms already under way,²¹ many developing countries decided to give a sense of direction to those domestic reforms, by consolidating that market openness at future dates, allowing for a gradual, staged liberalization to be implemented, with a clear and fixed horizon for full liberalization.²²

In contrast to that experience, commitments on financial services raised doubts as to whether good economic policy was being promoted. Firstly, there was less emphasis on the introduction of competition through new entry than on allowing foreign equity participation or protecting the position of incumbents. Secondly, even where immediate introduction of competition was not deemed feasible, not much advantage has been taken of the GATS to lend credibility to liberalization programmes by precommitting to future market access (Mattoo, 1999)

Setting aside those two fundamental sectors, where still many developing countries have not undertaken commitments (27 per cent for financial services and 40 per cent for telecommunications), it is clear that developing countries have refrained from making commitments on key infrastructure sectors (e.g. maritime transport, courier, and distribution services) and business services (e.g. computer and related services, and various professional services). Interestingly, the extremely low number of commitments on professional services by developing countries may be an indication of the difficulties that these countries face in opening the supply of services through mode 4, which is a paradigmatic mode of supply for professionals.²³

Sectors such as basic telecommunications, banking and insurance services reveal a significant number of—economically highly restrictive— mode 3 limitations (WTO, 2001a). Although it is difficult to find adequate indicators reflecting the state of liberalization across modes of supply, Chart 3 gives a rough idea for four country groupings: developed, developing, transition, and least-developed economies. It is evident from Chart 3 that, regardless the level

¹⁹ The direct involvement of Lawrence H. Summers (US Treasury Secretary), and John Mogg (EU Commission Director General, Internal Market) is a clear testimony of that.

²⁰ As of today, 69 WTO Member governments have adopted the Reference Paper in whole or in part.

²¹ The use of commitments to lock-in reforms was further confirmed by the unprecedented unilateral submission of commitments on telecommunication services outside the negotiations by many Members (e.g. Cyprus, Egypt, and others).

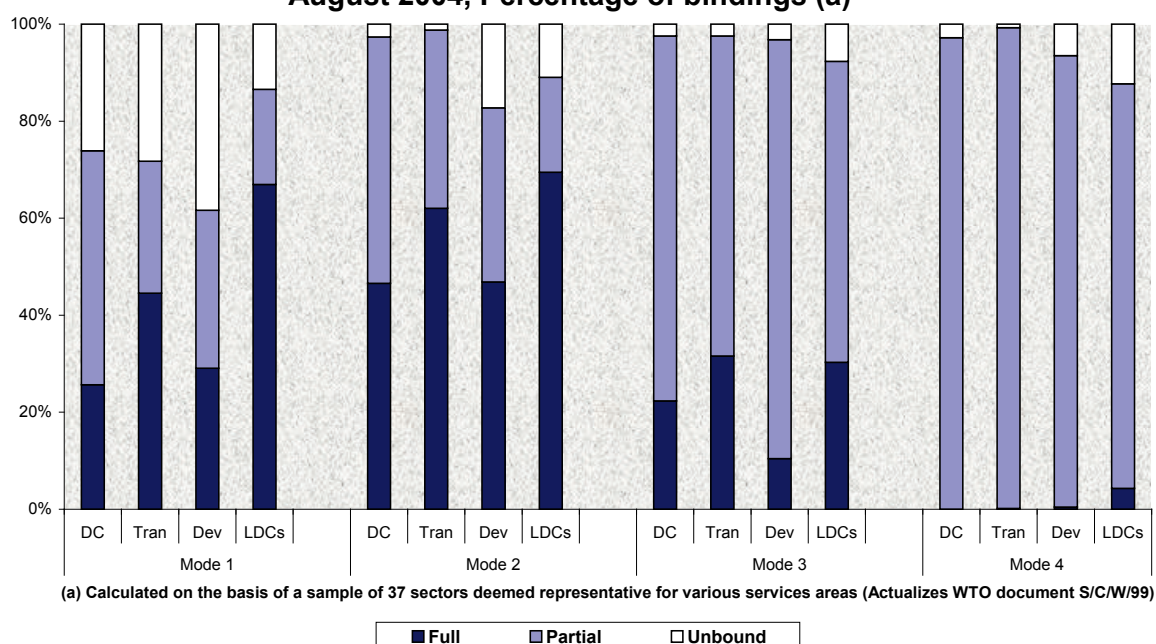
²² Such countries include *inter alia* Argentina; Hong Kong, China ; Indonesia ; Korea, Singapore ; and Thailand.

²³ The number of developing countries with commitments on professional services ranges from 10 (midwives and nurses) to 43 (engineers). In order to give a more balanced picture of the number of countries with commitments in all professional services, chart 2 only includes the average number of developing countries in all professional services.

of development, the bindings undertaken for mode 2 are significantly more liberal than those for other modes; while bindings on mode 4 are the least liberal of all. At least 45% of the entries under market access for mode 2 are without limitations for each group of countries; while the share of unlimited commitments on mode 4 is close to nil. In the case of modes 1 and 2, the level of unrestricted commitments does not differ significantly between developed and developing economies; while transition economies and least-developed countries have tended to undertake more open commitments. The situation is somewhat different for mode 3, where developing countries have tended to make more restrictive commitments than the other three groups of countries. In addition, it is interesting to note that although the movement of natural persons has often been presented as a North-South issue, there is no evidence that developing countries have found it easier to make commitments under this mode than their developed partners.

Chart 3

Chart 3. Structure of market access commitments by mode, August 2004, Percentage of bindings (a)



Note: DC (Developed Countries); Tran (Transition Economies); Dev (Developing Countries); LDCs(Least-Developed Countries)

Source. Own Elaboration based on WTO database

Cross-border supply (mode 1) and commercial presence (mode 3) are generally considered to be the economically most important modes, accounting for more than 80 per cent of world trade in services (Karsenty, 2000). Chart 3 not only reveals more full commitments, but also a far higher share of non-bindings for mode 1 than for mode 3 for each group of countries. Clearly, WTO Members have generally shown a preference for commitments on trade

through commercial presence.²⁴ As we will see, the liberalization of cross-border trade may become one of the most important challenges for developing countries in this round of services negotiations.

3. Developing countries in the current round of services negotiations.

A major difficulty in discussing developing countries' positions is that such countries as a group are quite heterogeneous. Developing countries differ widely in terms of their individual levels of development, their economic structures (and therefore the relative importance of different service sectors), and their economic policies (which reflect ideological, traditional, cultural, and political traditions). All these factors have an impact on their negotiating positions. Having said that, the participation of developing countries in this round of services negotiations can be analyzed by reference to the following elements: their general approach to the negotiations; their negotiating proposals; their initial offers; and their participation in other areas of the services work programme (negotiations on safeguards, subsidies, government procurement and domestic regulation).

Although there is no denying their active participation, generally speaking developing countries have approached these negotiations with caution and defensively. They have submitted negotiating proposals and bilateral requests, have coordinated positions with each other, and have participated in multilateral discussions, but that “activism” is not necessarily synonymous with a vigorous stance in favour of liberalization that would manifest not only in the quest for further market access abroad but also in the (commitment to guarantee) the liberalization of their own domestic markets. That attitude became apparent during the negotiations for the establishment of the negotiating modalities and procedures, when they supported –and managed to obtain- the reaffirmation of the following principles²⁵:

- Flexibility for developing countries to open fewer sectors and transactions;
- Non-exclusion of any sector or mode of supply from the negotiating table (code name for the non-exclusion of negotiations on mode 4);
- Emphasis on bilateral –request/offer- negotiations;
- No explicit inclusion of formulae approaches;
- No creation of sectoral negotiating groups; and
- A link between the market access negotiations and the rule-making work.²⁶

The negotiations for the establishment of modalities for the treatment of autonomous liberalization followed the same pattern, amplified by the technical difficulties surrounding the issue. Again, developing countries –supported this time by developed nations- opposed the establishment of a formula approach or quantitative targets that might have helped in the definition of a multilateral credit. Apart from that, the most important area of divergence between the two groups of countries concerned the likelihood of binding the measures undertaken autonomously in the past. It goes without saying, developing countries firmly

²⁴ Although it is fair to acknowledge that for some service activities, cross-border trade is technically unfeasible and therefore commitments would have had little value (e.g. hotel, restaurant or hospital services).

²⁵ The similarity between the negotiating proposal submitted by 23 of the most prominent developing countries and the final text of the negotiating guidelines and procedures is in that regard noteworthy.

²⁶ Rule-making work is understood to include the negotiating mandates on safeguards, subsidies, government procurement and domestic regulation.

opposed any obligation to bind the autonomous liberalization measures for which they were seeking recognition/credit.

Unfruitful attempts were also made, this time by least-developed countries, to establish a mechanism for Special and Differential Treatment under the GATS with the idea of making it possible to allocate quotas (e.g. on the movement of people) or to grant specific commitments only to specific groups of countries (i.e. the LDCs).²⁷ It is worth noting that this proposal met the opposition not only of developed countries but also of more advanced developing countries, who feared the loss of access opportunities in advanced economies, particularly with respect to the temporary movement of natural persons.

Influenced by this state of mind, the negotiations have been conducted on the basis of the so-called request/offer approach, which is mainly of a bilateral nature. There are virtually no WTO documents that could be used to trace the requests exchanged between WTO Members to date. Nor is it possible to know with exactitude which developing countries are involved. A look at the various reports of the Special Session of the Council for Trade in Services²⁸ and other sources, such as government reports or consultation papers, lets us see that around 20 developing countries have submitted requests.²⁹ In any case, since large developed countries seemed to have circulated requests to almost all other Members, there may be only a few developing countries not involved in bilateral negotiations with at least one major trading partner.³⁰ Anecdotal evidence suggests that mostly the largest developing countries have submitted initial bilateral requests to some trading partners.³¹

²⁷ This description is a statement of fact. It is without prejudice to the author's personal views on the issue, which will be discussed in the following sections.

²⁸ The Special Session of the Council for Trade in Services is the negotiating body in charge of overseeing the negotiations on trade in services within the Doha Development Agenda. It reports directly to the Trade Negotiations Committee.

²⁹ For example, Australia received requests from the following WTO Members: Argentina ; Brazil ; Canada ; China ; Chinese Taipei; Egypt; EC; Hong Kong, China; India; Japan; Korea; Malaysia; Mauritius; Mexico; Norway; Pakistan; Panama; Peru; Singapore; Switzerland; Uruguay and the US. The EC received requests from Argentina; Australia ; Brazil ; Canada ; China ; Chinese Taipei ; Egypt ; Hong Kong, China ; India ; Japan ; Kenya ; Korea ; Malaysia ; Mali ; Mauritius ; Mexico ; New Zealand ; Pakistan ; Panama ; Paraguay ; Peru ; Singapore ; Switzerland ; Uruguay and the US. See Australian Government (2003); and European Commission (2003).

³⁰ The European Union for example submitted requests to 109 WTO Members. See European Commission (2003).

³¹ See various reports of the meetings of the Council for Trade in Services, document series S/CSS/M and TN/S/M). The number of requests submitted by developing countries, according to their own reports to the Council, go from 15 (Thailand) to 22 (Argentina) to 56 (Panama).

Table 2: Sectoral/modal intents expressed by developing countries in their multilateral negotiating proposals, as of 1 august 2004

Subject	Submitted only by developing countries	Submitted jointly with developed countries	Number of developing countries
Business services			
Business (no prof.)			
Advertising			
Professional	1		1
Legal			
Accounting			
Architectural			
Engineering			
Computer services	4		7
Communication			
Postal/Courier	1		5
Telecom	5		5
Audiovisual	1		1
Construction	5		5
Distribution	4		7
Education	-	-	--
Energy	3		3
Environmental	2		2
Financial	4		4
Tourism	7		17
Transport			
Maritime	3	1	17
Air	3		3
Land (rail & road)			
Other transport			
Logistics services	1	1	3
Mode 4	5		20
Mode 1	1		3

Source: own elaboration

(Memorandum item: Total number of developing countries having expressed interest in at least one sector: 36)

In the absence of information on bilateral requests, it is hard to second-guess the sectors and modes of supply where developing countries have shown a special interest. One indication can be found, nevertheless, in the negotiating proposals submitted during the last three years.³² Setting aside the negotiating proposals or position papers on so-called “horizontal

³² In the absence of a clear calendar for the negotiations on services that started autonomously in January 2000 (following the negotiating mandate contained in GATS Article XIX), WTO Members started to submit negotiating proposals on different sectors, issues or modes of supply. These are position papers by which Members made their views and interests known to each other. Most of them advocate further liberalization for the sectors or modes addressed, but some of them also express other concerns (e.g. the impact of liberalization on Small and Medium Size Enterprises).

issues”, out of 134 proposals submitted thus far, 50 came from developing countries (43 from low and middle income countries). In other words, 37% of the proposals came from developing countries. Table 2 shows the sector focus of those proposals. A few factors are worth noting:

- No proposals have been submitted by least-developed countries.
- Only one African country –Kenya- submitted a proposal showing its sectoral interests.
- Most of the proposals came from middle-income countries.
- Latin American countries have been particularly active in this exercise. All of them have expressed interest in at least one sector or mode of supply.
- East and South-East Asian countries have hardly participated in this process. Key WTO Members, such as Malaysia, Thailand, Indonesia, Singapore, Philippines have not submitted any negotiating proposal at all; although some of them have recently joined other WTO Members on callings to liberalize maritime transport and mode 4, and have submitted bilateral requests to trading partners.³³
- The number of developing countries having expressed interest in at least one sector or mode of supply is 36 (counting 17 that joined collective submissions on maritime transport and mode 4).
- Some proposals have been submitted jointly by developing and developed countries in an unprecedented expression of common negotiating interests in the services negotiations (17 developing countries joined a collective submission on maritime transport services; while 3 developing countries co-sponsored a proposal on the liberalization of logistics services).

Developing countries’ interests seem to be concentrated on mode 4, tourism, and maritime transport services. Twenty developing countries have expressed an interest in the liberalization of mode 4; while 17 have focused on the liberalization of tourism and maritime transport services. The interest on mode 4 was not only expressed through specific proposals for this mode of supply, but also through sectoral proposals with an emphasis on the movement of natural persons as the essential mode of supply (e.g. proposals on computer services and on professional services).³⁴ The movement of natural persons seems to have been the object of bilateral requests by developing countries, as evidenced by summaries of requests published by some developed countries (e.g. Australia and the EC). For example, most of the requests submitted to Australia and the EC address mode 4 issues.³⁵

Some negotiating proposals submitted by developing countries have even addressed domestic regulatory issues.³⁶ Cases in point concern tourism services, where some developing countries have proposed to elaborate a specific sectoral Annex in order to address anti-competitive actions by private operators; and the movement of natural persons, where proposals put emphasis on solving problems arising from various regulatory hurdles.

³³ See Australian Government (2003) and European Commission (2003).

³⁴ This emphasis on mode 4 has been recently reaffirmed when Members adopted the so-called “July package”, to which reference was made in the introduction to this paper.

³⁵ See Australian Government (2003) and the European Commission (2003).

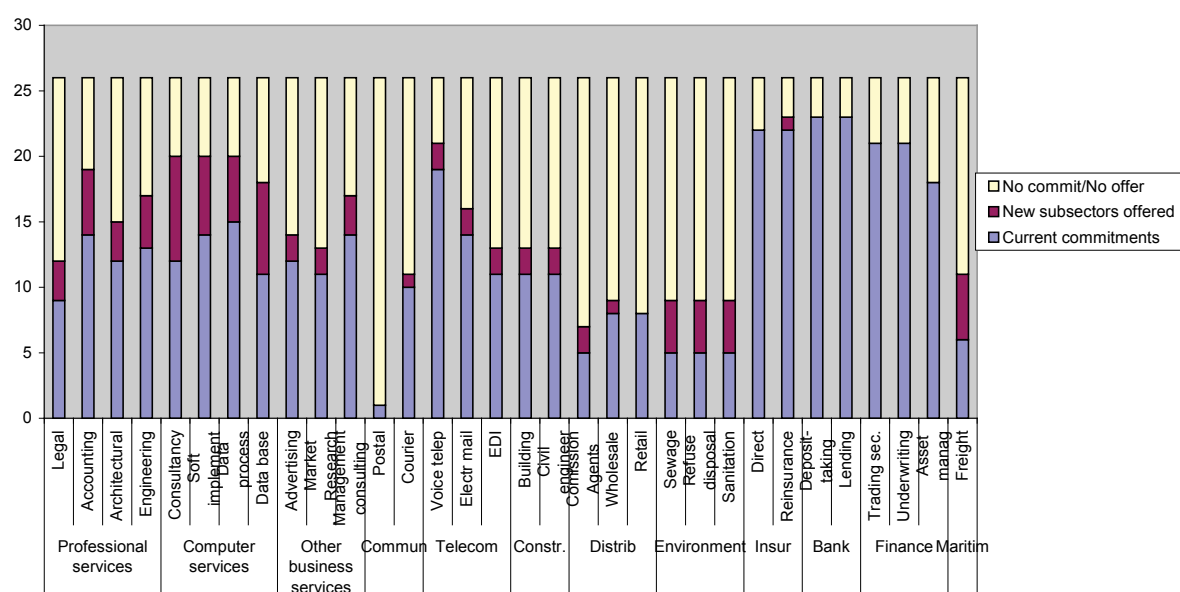
³⁶ Domestic regulation in the GATS refers to measures not subject to scheduling as Market Access or National Treatment limitations, but that could nevertheless constitute hidden barriers to trade. They are the object of Articles VI and XVIII GATS.

Apart from the negotiating proposals, more information can be obtained from the initial offers. The overall momentum of the request-offer process has not been particularly impressive. By August 2004, almost one year and a half after the target date (end March 2003), only 43 offers have been submitted, representing 57 WTO Member governments³⁷ (about one-third of the WTO Membership). A bit more than half of the offers belong to developing countries. The regional distribution of offers has remained uneven. While relatively many countries from Latin America and -to a lesser extent- Asia have made contributions, Africa and the Arab region are still on the sidelines. The “quality” of offers, both in terms of sectoral coverage and liberalizing content, has been in general rather disappointing. This disappointment, and the consequent need to improve offers, was reflected in the recommendations adopted by WTO Members as part of the so-called “July package”.

Chart 4 can give an indication of the general thrust of the offers made by developing countries so far. The chart shows the coverage of selected sectors in current commitments and in initial offers of all the developing countries with an initial offer on the table. The sectors are deemed to be representative of basic infrastructure and business services.

Chart 4

Chart 6. Sectors offered by developing countries, Number of Members, as of August 2004



Note: Developing countries included are those who have submitted an initial offer.

Source: Own Elaboration, based on WTO database and initial offers

³⁷ The discrepancy between the number of offers and the number of Member governments is due to the EC 15. The WTO Members that submitted an offer as of August 2004 are the following: Argentina; Australia; Bahrain; Bolivia; Brazil; Bulgaria; Canada; Chile; China; Chinese Taipei; Colombia; Costa Rica; Czech Republic; EC; Fiji; Guatemala; Hong Kong, China; Iceland; India; Israel; Japan; Korea; Liechtenstein; Macao, China; Mauritius; Mexico; New Zealand; Norway; Panama; Paraguay; Peru; Poland; Singapore; Slovak Republic; Slovenia; Sri Lanka; St. Christopher & Nevis; Suriname; Switzerland; Turkey; Uruguay; and the US.

4. Developing countries in the services negotiations: doing enough?

4.1 To commit or not to commit? That is the question.

Protection is first of all a domestic problem. As experience shows, the basic reason for many developing countries embracing freer trade policies and abandoning import-substitution policies in the early 1990s, was a clear dissatisfaction with the results delivered by decades of protectionist policies at home (Dornbusch, 1992). The realization of this, and the poor performance of service activities in the past, has led industrial, developing and transition economies to undertake –in some cases- ambitious domestic reform programmes. These reforms have entailed a combination of competitive restructuring, privatization, and establishment of modern regulatory mechanisms and institutions.

The previous considerations serve as a preamble to argue that the first order of priority for developing countries should be to pursue vigorous domestic reform programmes, which in many cases are already under way, in order to boost services sectors' efficiency. This is basically a suggestion for unilateral action. Domestic policy priorities go in fact beyond multilateral negotiations and delaying the introduction of necessary reforms would entail costs for the rest of the economy. Additionally, those domestic priorities should not be held hostage to external bargaining imperatives. Having said that, the questions that arise are the following: Why should countries engage in multilateral trade negotiations? And, how can multilateral trade negotiations help achieve that national reform agenda?

The main limit of trade policy reform in developing countries is the lack of credibility, i.e., the difficulty faced by policy makers to convince business, labour and consumers that trade reforms will be lasting, and that governments will stick to them and will oppose any adverse reactions, particularly in the short term, when adjustment costs may be felt. Reform processes are frequently met with scepticism on the part of the private sector, particularly in countries with a history of policy reversals. Since the magnitude of adjustment, particularly in the labour market, is unknown when reforms start, the commitment of the leadership to the reform will often remain suspect in the eyes of the public. Formally, there is an instance of asymmetric information: the leadership may know its commitment to reform, but may be unable to communicate it and convince the private sector (Rodrik, 1992). The immediate objective of trade liberalization is to shift relative prices in order to induce investment in, and an expansion of, the exportable sector where the comparative advantage lies. The quicker the expansion of the exportable sectors the better, because resources are reallocated with minimal adjustment cost. If reform is not credible, and private sector participants suspect that the government will re-impose restrictions to protect the import-substituting industries (which, by the way, may be lobbying to reverse reforms), investments in the exportable sectors will not materialize, and the country will not reap the full benefits of reform in time.

There is an additional consideration in the case of services liberalization in developing countries. The effects of reforms may not necessarily materialize in an immediate increase in services exports, where in some cases developing countries may not have a clear comparative advantage. Rather, the likely effect of introducing reforms, like the elimination of monopolies or the abolition of limitations on foreign investment, is the expansion of business opportunities in those liberalized sectors provided returns to investment are sufficiently high. Again, the country will only reap the full benefits of reform (e.g. capacity expansion, lower prices, higher product quality) provided those potential investors believe that the reform will not be reversed and investments are worthwhile to justify eventual sunk costs. Once sunk

investments have been made, bargaining power shifts from suppliers to regulators. Regulators can then decide or threaten to impose special taxes, require special investments, control procurement and employment practices, restrict the composition and movement of capital, or put a cap (or even lower) the regulated prices that utilities can charge for services, particularly social discontent arises due to higher prices. Recognizing these risks, private companies will likely invest less than is optimal—especially in activities with large sunk costs—or demand high risk premiums unless governments can credibly commit to regulatory stability (World Bank, 2004a). Therefore, the “credibility” needed relates to two dimensions: first, credibility that the investments will not be confiscated³⁸; and, second, credibility that the regulatory framework will be consistent, fair and predictable.

What is the possible contribution of GATS commitments to solving this credibility problem? Commitments may help increase credibility by making exit from them cost enough to outweigh the gains from simply abrogating commitments and reversing policy.³⁹ But in order to take advantage of GATS negotiations in this way, a greater dose of unilateralism is required when making commitments.⁴⁰ A purely bilateral request-offer approach might not bring satisfactory results along these lines, because (i) it creates a holdback problem (I would minimize what I give and try to maximize what I get)⁴¹; and (ii) it has a bias towards second-best results depending on the negotiating circumstances.⁴² The challenge is to make the right choices in terms of policies and multilateral commitments, particularly taking into account that the GATS does not impose any hierarchy between the protective instruments –market access or national treatment limitations- which are treated equally as long as they are scheduled. In other words, the Member concerned is not pushed to choose the most efficient means of protection (e.g. tariffs instead of quotas, as in the GATT context⁴³), but has the freedom to decide by itself on any of them.⁴⁴

³⁸ I use the expression “confiscation” in a broad sense, to make reference not only to outright confiscations, but also to the imposition of a greater regulatory or fiscal burden once important investments have been committed. In other words, sudden changes in the rules of the game for businesses may amount to confiscation in this sense.

³⁹ The “tangible” cost of abrogating a commitment will be given by the amount of compensation to be paid, either as a result of renegotiating the commitment under Article XXI GATS or as a result of a defeat in a dispute. The “intangible” cost will be given by the lost in reputation that such behaviour, if repeated over time, may entail. Specific commitments to grant full market access and national treatment would make costly any attempt to (re)introduce monopolies, to limit the number of companies in the market, to introduce limitations to foreign investment in the sector, or to impose taxation or regulation that discriminates against foreign suppliers. There are other instances of “confiscation” that belong to the realm of domestic regulatory measures. See the examples in Box 2.5 of World Bank (2004a).

⁴⁰ Hoekman and Meserlin (2000).

⁴¹ For a discussion of the difficulties in applying strict reciprocity in the services negotiations, see Marchetti and Mavroidis (2004).

⁴² For example, the “demandeur” approaches the negotiating table with a first-best objective –obtain full liberalization. However, if this turns out to be impossible, he/she will turn to the plan “B”, a second-best result –protect the acquired rights of the companies already in the market. This may well explain the dynamics that led to second-best compromises, such as the scheduling of grandfathering, which protects the incumbents but fail to introduce competition in the market.

⁴³ See the discussion on efficient means of protection in the GATT and the GATS, in Mattoo (2003).

⁴⁴ As explained by Sykes (2000), “...the various market access limitations are unlikely to be equivalent in their welfare consequences. Presently, however, GATS treats all market access limitations equally as long as they are scheduled. Just as GATT seems to encourage efficient protection in goods markets, so too could GATS undertake to do more to channel market access restrictions into particular instruments based on an assessment of which tend to do the least damage...as in the case of the market access restrictions, measures that deny national treatment can have radically different welfare consequences. As with the market access restrictions discussed

It is worth recalling however that not all types of commitments promote good policy. A number of simple rules of thumb may be identified in that regard. First, emphasis should be given to producer and infrastructure services, whose efficiency will be important for all other economic activities. Obvious candidates are telecommunications, maritime transport, financial services, computer and related services, various professional services, distribution services, and logistics-related services. Secondly, emphasis should be given to the introduction of competition through unimpeded entry instead of committing only to changes in ownership or to the protection of incumbents' rights. In fact, in today's regulatory perspective, competition can be introduced even in network utilities, which are seen as encompassing distinct activities that can be unbundled, with potentially competitive segments under separate ownership from natural monopoly components. (World Bank, 2004a).⁴⁵ But even where natural monopoly components remain, competition may be introduced indirectly, by allowing competitive bidding for the right to provide such exclusive services. Thirdly, explicit discrimination between domestic and foreign suppliers should be eliminated.

A last word on the convenience of undertaking multilateral commitments. Even in an essentially mercantilist setting like multilateral trade negotiations, undertaking commitments can contribute to his/her own bargaining position in the negotiations. If a country is not willing to open its own market and to guarantee certain conditions of operation, it deprives itself of the most obvious means of inducing its trading partners to do the same. This would indirectly suit the protectionist interests of trading partners because it allows them to avoid liberalization in sensitive sectors.⁴⁶

4.2 Seeking enhanced access in foreign markets: where and how.

As explained, the principal beneficiary of trade reform is the reformer, particularly if it is a small country. Nevertheless, if other countries liberalize their markets in sectors of own export interest, the unilateral liberalizer benefits twice because a country cannot on its own improve access for its exports to foreign markets (World Bank, 2001a). The pertinent question raised therefore is not whether to seek more access in foreign markets, but where (in what sectors or modes of supply) and how. This is the objective of this section.

Services have been among the fastest growing components of world trade over the last two decades, particularly in the 1980s. Indeed, over the period 1980-1990, the average annual growth rate of services exports was over 8 per cent, compared to 5,7 per cent for merchandise exports.⁴⁷ The performance of services trade was particularly impressive in the second half of

above, GATS could do more to channel the denial of national treatment for protective purposes into less destructive avenues.”

⁴⁵ For example, in electricity, transmission and distribution (less competitive) should be separated from generation (more atomistic market); in telecommunications, the local loop should be separated from long-distance, mobile and value added services; in natural gas, high-pressure transmission and local distribution (non-competitive) should be split from production, supply and storage (more competitive activities); in railroads, tracks, signals, and other fixed facilities should be separated from train operations and maintenance. See World Bank (2004a). These considerations might even help negotiators figure out a more updated classification for certain service sectors under negotiation (e.g. energy services).

⁴⁶ See the argument being used in a discussion of India's stance in multilateral trade negotiations (Mattoo and Subramanian, 2000).

⁴⁷ Measured on a Balance-of-Payments basis, which covers primarily services trade under modes 1 (cross-border) and mode 2 (consumption abroad).

the 1980s, with an average growth rate of 15,5 per cent per annum. However, thereafter the record is mixed. At the aggregate level, services and merchandise trade have evolved in a roughly similar way since 1990 (both growing at 6,6 per cent per annum), leaving the share of trade in services in international trade stagnant, at around a fifth of all cross-border trade (Tables 3 and 4)

Table 3: Average annual growth of exports of different products, in percentage.

	1980-1990	1985-90	1990-2000	1990-95	1995-2000	1990-2002
Agricultural products	3,59	9,42	3,17	7,38	-1,04	3,10
Mining products	-0,65	3,92	7,26	1,98	12,54	5,27
Manufactures	8,46	15,24	7,13	9,39	4,88	5,99
Memo item : All merchandise	5,68	12,09	6,64	8,64	4,65	5,59
Transport	5,51	12,39	4,60	6,42	2,79	4,11
Travel	10,33	18,29	6,04	8,78	3,29	5,18
Other Commercial services	9,06	15,74	8,51	10,52	6,49	8,06
Memo item : All Services	8,25	15,46	6,66	8,80	4,51	6,10

Source : own calculations, based on WTO International Statistics Database, on the basis of current billion dollars (Data retrieved in August 2004)

Table 4: Share of major goods and services categories in total world exports (percentage)

	1990	1996	2002
Agricultural products	10,2	9,5	7,6
Mining products	12,0	9,8	10,3
Manufactures	58,6	60,6	61,5
Transport	5,5	4,9	4,7
Travel	6,5	6,8	6,2
Other Commercial serv	7,2	8,4	9,7
Memo : All Services	19,21	20,07	20,62

Source : own calculations, based on WTO International Statistics Database (Data retrieved in August 2004)

Developments are more varied however at a disaggregated level (Table 3. Disaggregated data reveal that since 1985, one services category (transport) and two merchandise product groups (agricultural and mining products) have expanded less rapidly than world trade. As a consequence, the relative importance of transport services in world services exports declined from 5,5 per cent in 1990 to 4,7 per cent in 2002. On the other hand, exports of travel services expanded vigorously in the 80s, but then slowed down in the 90s, leaving its share in international trade at around the same level. The driver behind services trade over the last two decades has undoubtedly been "other commercial services", which has proven to be the most dynamic segment of world trade in the 1990s, particularly in the first half. As a result, the share of Other Commercial Services has increased from 7,2 per cent of all cross-border trade in 1990 to 9,7 per cent twelve years later. Trade in "other commercial services" now represents 47 per cent of world trade in services, up from 37 per cent in 1990.

Table 5: Share in world services exports, by income group

	1990	1996	2002
Low & Middle income countries	16,0	20,0	23,5
High income countries	84,0	80,0	76,5
Memo item: OECD high income	75,3	70,2	73,6

Source : own calculations, based on WTO International Statistics Database (Data retrieved in August 2004)

Where do developing countries⁴⁸ stand in world services trade? As a group, low and middle income countries have witnessed a more rapid increase in their service exports, and a consequent increase in their share in world services trade from 16 per cent in 1990 to 23,5 per cent in 2002 (Table 5). The great dynamism shown by these economies in world services trade has translated into an increase in their participation in all segments of services exports. Their exports now account for 23 per cent of world exports of transport services; 30 per cent of world exports of travel services; and 20 per cent of world exports of other commercial services (Tables 6 to 9 for average annual rates of growth, and relative shares in world exports). From a regional perspective, between 1990 and 2000, the exports from Low and Middle-income Asia, Central and Eastern Europe, and Latin America and the Caribbean grew at higher average annual rates than world services exports (Table 10).

Table 6: Transport Services, average annual growth of exports, by income group.

	1990-1995	1995-2000	1990-2000	1990-2002
Low income	6,10	0,88	3,49	3,66
Middle income	11,15	5,68	8,41	8,06
High income	6,27	2,03	4,15	3,53

Source : own calculations, based on WTO International Statistics Database (Data retrieved in August 2004)

Table 7: Travel Services, average annual growth of exports, by income group.

	1990-1995	1995-2000	1990-2000	1990-2002
Low income	11,26	3,70	7,48	5,23
Middle income	15,57	6,84	11,21	9,71
High income	7,60	2,17	4,88	4,13

Source : own calculations, based on WTO International Statistics Database (Data retrieved in August 2004)

⁴⁸ There is no institutional definition of developing countries in the WTO. Members identify themselves as such on the basis of a sort of self-selection. In the statistical analysis that follows, I'd rather make use of geographical groups and income groups following the World Bank classification. Economies are divided according to their 2003 GDP per capita, and the groups are: low income (\$756 or less); middle income (between \$766 and \$9,385); and high income (\$9,386 or more).

Table 8: Other Commercial Services, average annual growth of exports, by income group.

	1990-1995	1995-2000	1990-2000	1990-2002
Low income	4,12	21,49	12,81	13,02
Middle income	21,08	1,80	11,44	9,22
High income	9,67	6,38	8,03	7,93

Source : own calculations, based on WTO International Statistics Database (Data retrieved in August 2004)

Table 9: Share of different country groupings in Transport, Travel and Other Commercial Services, in percentage of total for each sector

	Transport			Travel			Other Commercial Services		
	1990	1996	2002	1990	1996	2002	1990	1996	2002
Low & Middle income countries	17	18	23	18	25	30	13	17	20
High income countries	83	82	77	82	75	70	87	83	80

Source : own calculations, based on WTO International Statistics Database (Data retrieved in August 2004)

Table 10: Average annual growth of services exports, by region, in percentage.

	1990-1995	1995-2000	1990-2000	1990-2002
Africa	6,89	3,39	5,14	4,59
Asia	14,79	3,41	9,10	8,16
Low & Middle income Asia	20,30	5,23	12,76	12,30
Central and Eastern Europe, the Baltic States and the Commonwealth of Independent States	17,58	2,61	10,09	10,03
Latin America and the Caribbean	8,30	6,48	7,39	5,61
World	8,80	4,51	6,66	6,10

Source : own calculations, based on WTO International Statistics Database (Data retrieved in August 2004)

Table 11: Average annual growth rates of exports to the United States, between 1995 and 2000, in percentage.

	Private Services Imports (i.e. cross-border imports)	Sales by MOUSAs to US persons
Latin America & Western Hemisphere	10,05	27,90
Developing Asia	10,71	6,54

Source: own calculations, based on "U.S. International Services: Cross-Border Trade in 2002 and Sales Through Affiliates in 2001", October 2003, Bureau of Economic Analysis.

While some developing countries are increasingly exporting through commercial presence abroad (Table 11 and Nielson and Taglioni, 2004)⁴⁹, the two key modes in which they have a

⁴⁹ Between 1995 and 2000, the sales of services by Latin American and Asia-Pacific countries through commercial presence in the US grew at average annual rates of 27,9 and 6,5 per cent, respectively (Table 10). In

comparative advantage are the presence of natural persons (mode 4) and cross-border supply (mode 1).

4.2.1 The mode 4 agenda

The temporary movement of natural persons (mode 4) remains a crucial means of delivery for developing countries, which have always been perceived as having a comparative advantage in labour-intensive services. Greater freedom for the temporary movement of service providers, still highly restricted in GATS commitments, would enable developing countries to supply the labour component of various service activities, such as construction, distribution, transport and others.

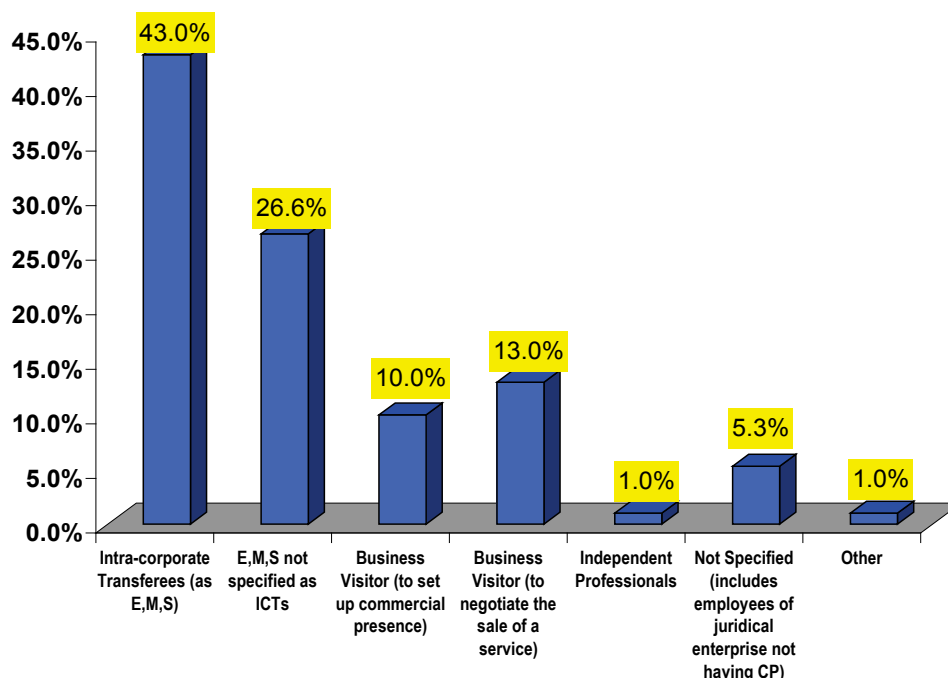
In spite of the benefits for the host and home countries, which have been thoroughly discussed elsewhere and will not be elaborated here,⁵⁰ the liberalization of the movement of service providers has so far been extremely limited. The reluctance to make significant commitments in this area is common to both developed and developing countries. Commitments made so far privilege high-skilled personnel and especially providers associated with the establishment of foreign companies. These intra-corporate transferees are the group targeted by about 43 percent of all current horizontal commitments. Another 26,6 percent of commitments relate to executives, managers, and specialists (not specifically related to intra-corporate transferees); 13 percent to business visitors in charge of setting up a commercial presence; and 10 per cent to other business visitors. Independent professionals account for only 1 per cent of all commitments on mode 4 (Chart 5).

the case of Latin American and Western Hemisphere countries, this rate is much higher than the annual growth rate of their sales to the US on a cross-border basis.

⁵⁰ See OECD (2001), Mattoo and Carzaniga (2004), and World Bank (2004b). The most quoted estimate comes from Alan Winters, who suggests that a relaxation of the quotas on inflows of workers into developed countries, by 3% of their labour forces, would generate global gains of over \$150 billion a year. See his paper in Mattoo and Carzaniga (2004).

Chart 5

Chart 5. Structure of Horizontal Commitments on Mode 4 (2003)



Source: WTO Secretariat

In spite of their alleged interest, developing countries as a group have found it difficult to articulate a collective position on this issue. Only recently have important developing countries managed to make joint proposals on this issue.⁵¹ The first collective proposal on mode 4 was submitted in July 2003 by a group of developing countries (including India),⁵²

⁵¹ A very elaborated proposal had been previously submitted by India in November 2000. That proposal called for the following: a) De-linking commitments with Mode 3 by including a category of “Individual Professionals” among the categories covered by horizontal commitments; b) Uniform definitions and coverage of personnel categories included in the horizontal commitments; c) further expansion in the scope of categories covered by horizontal entries by expanding the coverage of “other persons” and “specialists” to include middle and lower level of professionals; d) Additional sectoral commitments for professional and business services where movement of professionals is important; e) use of disaggregated categories of services providers at a sectoral level, by super-imposing ILO’s International Standard Classification of Occupations (ISCO-88) on the WTO Services Sectoral Classification. The ISCO has established an internationally adopted classification of 9 major occupational groups; f) Establishment of multilateral agreed criteria on the use of Economic Needs Tests (“Reference Paper on the Use of ENTs”), and reduction of the number of occupational categories subject to such tests; g) Strengthening GATS disciplines on recognition of qualifications (GATS Article VII); h) Introduction of a special GATS visa for categories of personnel covered by horizontal and sector-specific commitments, in order to separate temporary services providers (mode 4) from permanent labour flows (immigration); i) Exemption of developing country professionals from social security contributions and conclusion of bilateral totalisation agreements between countries.

⁵² The group was composed of the following Members : Argentina, Bolivia, Chile, China, Colombia, Dominican Republic, Egypt, Guatemala, India, Mexico, Pakistan, Peru, Philippines and Thailand. A further submission was made in March 2004 by Bolivia, Brazil, Chile, China, Colombia, Cuba, Dominican Republic, Ecuador, Egypt, Guatemala, India, Indonesia, Mexico, Nicaragua, Pakistan, Peru, Philippines, and Thailand.

who, regretting the lack of substantial improvements in the offer submitted at that time (26 in total), proposed the following approach:

- Use of common categories of persons, both linked and de-linked from commercial presence in the horizontal section of Members' schedules. Such categories are: (a) Intra-corporate Transferees; (b) Business Visitors; (c) Contractual Services Suppliers; and (d) Independent Professionals.
- Further sector specific commitments to allow for deeper liberalization, particularly at (lower) skill levels not covered in broad horizontal commitments.
- Establishment of a separate visa or separate sub-set of procedures for temporary movement.
- Additional commitments under Article XVIII GATS regarding transparency and procedural aspects affecting temporary entry and stay. These additional commitments could cover procedures for verifying a foreign service provider's competence to provide the service. The idea would be to introduce a hierarchy of measures with the burden of proof being placed on the domestic regulator to move from a less burdensome measure to a more burdensome one. For example, it may be considered that administering a test of service provider's competence and/or educational attainment to verify the foreign service provider's competence is the least burdensome measure. Only where it was *necessary* would a foreign service provider be required to make up objectively verifiable deficiencies in their education, training and experience.
- Elimination of Economic Needs Tests applicable to the common categories identified above.
- Development of disciplines under Article VI:4 of GATS covering the areas of qualification requirements and procedures, licensing requirements and procedures and technical standards.
- Strengthening the framework for Recognition Agreements under Article VII of GATS through (i) compliance with notification and consultation requirements; and (ii) development of possible multilateral guidelines and principles guiding the establishment of such Recognition Agreements, with a view to including them as Additional Commitments under Article XVIII GATS.

Bilateral requests also seem to focus on mode 4. For example, both the European Union and Australia⁵³ have indicated that most of the requests received address mode 4 at a horizontal

⁵³ See Australian Government (2003) and European Commission (2002). Australia received requests from the following WTO Members: Argentina; Brazil; Canada; China; Chinese Taipei; Egypt; European Communities; Hong Kong China; India; Japan; Korea; Malaysia; Mauritius; Mexico; Norway; Pakistan; Panama; Peru; Singapore; Switzerland; United States; and Uruguay. The European Communities received initial requests from the following: Argentina; Australia; Brazil; Canada; China; Chinese Taipei; Egypt; Hong Kong China; India; Japan; Kenya; Korea; Malaysia; Mali; Mauritius; Mexico; New Zealand; Pakistan; Panama; Paraguay; Peru; Singapore; Switzerland; United States; and Uruguay

level and tend not to be sector-specific. The level of ambition of the requests seem to vary widely, from requests to allow complete free movement of persons providing services, to rather more limited requests to improve transparency. The most frequently made requests to the EU (each made by five or more countries) are as follows:

- Sectoral coverage of Contractual Service Suppliers (CSS) to apply equally to all Member States (in other words, if one Member State has made a commitments on – say – management consulting – this should be made by all Member States).
- Sectoral coverage of CSS to be extended to cover sectors not currently committed (some countries have specified sectors of interest, whilst others seek a commitment for all service sectors covered by the Service Sectoral Classification List).
- Extend the permitted length of stay for CSS to between one and three years.
- Specify the length of stay for Intra-corporate transferees (between 3 years and indefinite stay).
- Specify the length of stay for Business Visitors (90 days).
- Create a new category of ICT for training purposes.
- Removal of Labour Market Testing requirements,
- Acceptance of the principle that the third country qualifications recognised by one EC Member State should be recognised throughout the EC,
- Improved transparency of rules and procedures linked to mode 4 (e.g. in relation to work and residence permits), and faster processing times.

In addition, the following requests to the EU have been made by two or more countries:

- Removal of all restrictions, allowing free movement of persons who provide services (two countries have requested this for all categories of service supplier, one country for ICTs only and one country for certain job types only).
- Commitments on lower skill levels,
- Commitments on foreign employees of domestic companies (persons recruited directly from overseas).
- Commitments on independent professionals (self-employed persons established overseas and entering the EC to provide services on the basis of a contract).
- Allow persons to provide after-sales/after-lease services without requiring a work permit.
- Permit multiple entry for persons covered by commitments.

In spite of the emphasis placed on the liberalization of mode 4 in the last few years, which has translated into several papers, symposia and other initiatives undertaken by international organizations, business groups and academics; no significant progress has been witnessed so far in the negotiations. Out of 43 initial offers submitted as of August 2004 (representing 57 Member governments), only 16 have expanded their commitments on this mode of supply. Although those offers contain improvements in certain areas (e.g. inclusion of new categories of natural persons; better definitions for each category; extension of the duration of stay; clarification of the application of economic needs test requirements; expansion of activities permitted to service suppliers; or even the inclusion of horizontal commitments by Members which did not have them in their existing schedule of commitments), the gap between these offers and the proposals and requests made by developing countries is still significant. For example, although some of those 16 Members made new commitments on additional categories of workers, most of these categories relate to intra-corporate transferees (movements tied to Mode 3). Only a limited number of offers contain commitments on contractual service suppliers, both as employees of juridical entities and as independent service suppliers. None of the offers includes semi- and low-skilled workers. On the other hand, no significant progress has been made with regard to the restrictions and procedural hurdles affecting the entry and stay of natural persons supplying services. In fact, the most noticeable improvement introduced by some of the offers concerns the length of stay allowed for intra-corporate transferees (but not to other categories, such as independent providers), which could again be seen as favouring movement of natural persons linked to mode 3. Only one offer from a developed country reduces the scope of application of the economic needs tests. There is no indication that other procedural hurdles have been addressed. In fact, only one offer from a developing country contains additional commitments allowing for multiple entry permits for all categories of persons.

Expectations on this issue are high among a number of developing countries. However, the fulfilment of those expectations will depend on the interplay of positive and negative factors underlying the negotiations on this area of trade, and the final outcome is difficult to predict at this stage. On the positive side, there is a growing sense within the international community of the need to ensure a more equitable and fair outcome for these negotiations, and this area of trade is seen as essential in that regard. Besides, both developing and developed countries –as well as their respective service industries- are more aware of the benefits arising from increased temporary mobility of natural persons. In spite of those positive factors, the issue continues to be the subject of high political sensitivities. First, governments find it difficult to distinguish in practice between temporary labour movements and permanent migration, and the fear that entrants through temporary arrangements may seek to prolong their stay through any possible means informs immigration and labour policies. This problem may be behind the lack of significant support gained thus far by the idea to develop a "GATS visa" or "Service Provider Visa".⁵⁴ Second, negotiations will have to contend with considerations related to heightened security concerns worldwide. Third, taking into account cyclical movements of labour markets, governments may be reluctant –if only for political reasons- to undertake ambitious commitments in this area.

From a negotiating perspective, although the most interested developing countries have rightly identified the main barriers and obstacles on mode 4, and have suggested various ways to overcome them, the action does not seem to have been fruitful enough. The recent

⁵⁴ This perception may have to be qualified, though, because there is no information on whether any progress is being made on this issue plurilaterally, at the so-called informal friends' groups.

proposals put forward by developing country WTO Members have a high degree of generality and, in some cases, have not gone beyond the enunciation of objectives (e.g. development of a GATS visa, the assumption of additional commitments on regulatory matters, or the use of common categories of service suppliers for the sake of making commitments). More detailed multilateral proposals on each of these issues is therefore needed, although it must be acknowledged that the liberalization of temporary movement of persons supplying services (and the expansion of commitments) raises challenges not only to developed countries but also to developing countries.⁵⁵

4.2.2. Reaping the benefits of the outsourcing trend

Apart from the undeniable interest in supply through mode 4, a number of developing countries seem to have developed a genuine interest in the expansion of commitments on cross-border trade (mode 1). Technological advances increasingly allow the spatial fragmentation of goods and services production, and off-shoring to operational units abroad and even outsourcing to a foreign third party service supplier has become common practice among multinational corporations. Developing countries are indeed becoming exporters of so-called Business Process Outsourcing (BPO) services. Low-labour costs, the availability of a well-educated pool of workers, and the improvement in the quality and price of international telecommunications, have allowed several developing countries to take the lead in this field. The most notable case is India's, but other countries are joining the club (e.g. China, Malaysia, and Philippines).⁵⁶

Typical BPO services include the following functional areas:

- *Administration*: tax processing, claims processing, asset management, document management, transcription and translation
- *Finance*: billing services, accounting transactions, tax consulting and compliance, risk management, financial reporting, financial analysis
- *Human resources*: benefits administration, education and training, recruiting and staffing, hiring administration.
- *Payroll services*: records management; payment services; credit/debit card services; cheque processing; transaction processing;
- *Logistics and Distribution*: materials management; distribution/warehouse management; logistics management; procurement.
- *Customer care*: database marketing; customer analysis; telesales/telemarketing; inbound call centre.
- *Content development*: engineering; design; animation; network consultancy and management; research and development.

For the moment, the vast majority of the services are the paper-based back-office ones that can be digitalized and communicated over telecommunications networks anywhere around the world. However, the more advanced developing countries are even moving from this type of services (data entry, etc.) to more integrated and higher-end service bundles in fields like customer care, human resource management, and product development.

⁵⁵ Again, this statement may be qualified by the lack of information on whether any progress is being made on each of these issues in the informal friends' groups discussions.

⁵⁶ The offshoring and outsourcing businesses remain predominantly English-speaking, but some Latin American and French-speaking African countries are also entering the business (Nielson and Taglioni, 2004).

Indeed, as evidenced by the so-called indices of Revealed Comparative Advantage, some developing countries have developed or are in the process of developing a comparative advantage in “other business services”, which include many of the activities outsourced to developing economies (Table 12).⁵⁷ It is to be expected that technological evolution, together with business practices, will make it possible for developing countries to profit from increased cross-border exports of even more sophisticated services (R&D, engineering services, etc.).

⁵⁷ An RCA index is calculated by taking the share of a particular sector's exports in total exports of goods and services, and dividing this share by the share of all countries' exports in this sector in aggregate global exports of goods and services. An RCA index value greater than unity indicates a comparative advantage in the sector; a value less than unity indicates a comparative disadvantage. A change in the index, even if it still remains under unity, is also important as an indication of eventual changes in comparative advantage. The estimates must be interpreted with caution because the RCA index is in many ways a crude measure of comparative advantage. For example, it does not account for intra-industry trade, it does not take into consideration the presence of trade barriers; and, since it is based on BOP data, it does not give any indication of a country's comparative advantage in supplying services through commercial presence or the movement of individual service suppliers.

Table 12: Revealed comparative advantage, selected countries

	Transport			Travel			Insurance and Financial Services			Computer, Information, communications and other commercial services		
	1990	2002	% change	1990	2002	% change	1990	2002	% change	1990	2002	% change
Argentina	1,77	0,58	-67,13	1,05	0,94	-10,75	0,00	0,01	-	0,22	0,30	40,85
Brazil	0,86	0,54	-37,10	0,72	0,50	-30,37	0,28	0,54	95,86	0,38	0,91	139,73
Chile	1,58	2,29	45,19	0,89	0,57	-36,09	0,73	0,27	-63,61	0,69	0,54	-21,36
China	0,89	0,37	-58,82	0,44	0,97	121,75	0,28	0,05	-82,89	0,24	0,48	96,45
Costa Rica	1,05	0,81	-22,76	2,39	2,82	18,01	0,37	0,20	-45,66	1,54	0,81	-47,69
Dominican Rep	0,42	0,21	-50,89	3,79	5,80	52,89	0,06	0,00	-100,00	1,41	0,26	-81,19
Egypt	6,52	4,87	-25,34	2,26	4,81	112,56	0,49	0,51	4,51	2,34	2,44	4,53
India	0,95	0,81	-15,26	1,17	0,71	-39,81	0,47	0,32	-32,26	1,35	3,40	152,39
Indonesia	0,06	0,39	604,35	1,30	1,44	10,31	0,00	0,00	0,00	0,15	0,04	-74,51
Jamaica	1,84	2,89	56,93	6,00	6,98	16,37	0,54	0,80	47,49	0,25	1,22	380,71
Malaysia	0,81	0,62	-23,26	0,86	1,14	31,77	0,01	0,12	1160,84	0,41	0,57	38,39
Mexico	0,42	0,16	-62,74	1,96	0,88	-54,95	0,59	0,44	-24,55	0,15	0,10	-35,26
Philippines	0,50	0,38	-24,68	0,72	0,76	6,06	0,11	0,11	-3,54	3,04	0,20	-93,35
Singapore	0,76	1,74	127,97	1,21	0,49	-59,61	0,12	0,30	163,01	1,36	1,13	-16,71
South Africa	0,59	0,71	18,96	1,16	1,38	18,62	1,12	0,44	-60,71	0,23	0,16	-30,03
Thailand	1,01	0,91	-9,96	2,51	1,62	-35,18	0,04	0,07	89,82	0,33	0,64	92,26

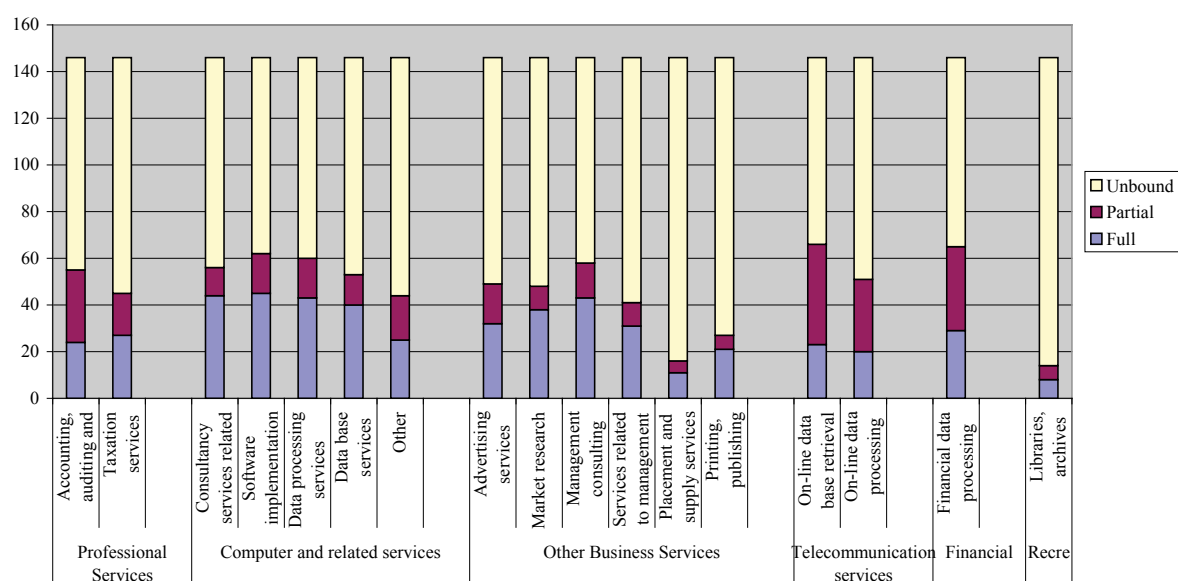
Source : Own calculations on the basis of IMF Balance of Payments Statistics.

The development potential of cross-border trade in services is not limited to more advanced developing countries. Other (relatively smaller) developing countries will also enter BPO activities in parallel with increasing wages and a move of the current service suppliers up the value chain. Unfortunately, there are already signs of incipient protectionism emerging in developed countries, which has so far translated only in initiatives to introduce, e.g. in the US, an outsourcing ban with respect to government contracts. However, only a few developing countries⁵⁸ have recently focused on this issue, highlighting the limitations of the request-offer approach in this area, and hinting at the possibility of developing another approach, most probably a formula.

The use of a formula in this area seems to be justified because of two basic reasons. Firstly, it would be impossible to anticipate the full range of services that could be supplied on a cross-border basis due to constant technological changes and to the emergence of new products and services. Secondly, although 95 per cent of current BPO spending is still for discrete processes, such as billing or payroll, a high share of organizations (61 per cent) is asking single providers to handle multiple processes to simplify relationships and improve integration (Accenture, 2003). Technical issues have recently been analysed and several options have been proposed elsewhere, from an ambitious and sweeping liberalization of the cross-border supply for all sectors to a more modest model schedule grouping the sectors that are currently the object of outsourcing and increased cross-border trade (Mattoo and Wunsch, 2004). Liberalization commitments of modes 1 and 2 for all service sectors may not be feasible at this stage. However, the development of a model schedule to target some of the key services involved is worth considering. The challenge is important and more work is needed in this area (The situation of commitments for some of the key sectors that might be targeted by such a formula is shown in Chart 6).

Chart 6

Chart 6. Structure of market access commitments on mode 1 for selected sectors, Number of Members, as of August 2004



Source: Own Elaboration based on WTO database.

⁵⁸ Chile, India and Mexico.

4.3 Domestic Regulation: Taking care of special circumstances

Services negotiations are also under way to complete the GATS framework of disciplines in a crucial area: domestic regulation.⁵⁹ The object of this section is to analyse developing countries' interests and positions in this issue.

Certain forms of protection are embedded in domestic regulatory conduct and are certainly difficult to identify and discipline. Difficult to apprehend, these hidden barriers may take the form of, *inter alia*, unduly high minimum capital requirements or licensing fees; cumbersome procedures for the recognition of qualifications; cumbersome and opaque licensing requirements; and lengthy and opaque licensing procedures. In order to attain effective access to services markets, Article VI.4 GATS calls for the development of disciplines to ensure that "measures relating to qualification requirements and procedures, technical standards and licensing requirements do not constitute unnecessary barriers to trade in services." According to the same mandate, "such disciplines shall aim to ensure that such requirements are, *inter alia*, (a) based on objective and transparent criteria, such as the competence and the ability to supply the services; (b) not more burdensome than necessary to ensure the quality of the service; and (c) in the case of licensing procedures, not in themselves a restriction on the supply of the service."

In order to reap the full benefits of the liberalization process, developing countries need to accompany openness with policies to foster competition and avoid anti-competitive conduct (e.g. telecommunications), to solve informational asymmetries arising in many markets (e.g. professional services), to avoid systemic risk (e.g. banking), or to take care of social concerns (e.g. universal service). Thus, as part of the move towards competition, new regulatory frameworks, procedures, and bodies will be needed. Particularly for developing countries, these should be lean and efficient, for otherwise they become drains for the public sector and may hamper the full realization of welfare gains. In this process, developing countries could benefit from multilateral cooperation. Part of this efficiency could indeed come from being prepared to adopt regional or international standards or emulate those of other –more experienced– trading partners, rather than seeking to fine-tune standards to perceived local idiosyncrasies or to avoid improvements to the regulatory framework because of lack of resources. On the other hand, hidden trade barriers, such as the ones targeted by future Article VI.4 disciplines, also affect the access of developing country providers to foreign markets. This is indeed the case for licensing and qualification requirements and procedures, which may be particularly burdensome for natural persons seeking to provide services on a temporary basis overseas. As previously shown, developing countries have already realized the importance of this work, and are actively engaged in these discussions.

Having said that, particularly where domestic regulation is concerned, it is fair to acknowledge that developing countries are different. They often regulate in a less efficient manner, need to set up standards and regulatory arrangements from scratch, lack enough monetary resources, and have a deficit in competent human resources. Recent research on business regulation shows that there is a relationship between the level of development and regulatory burden. Rich countries have less burdensome entry regulations than developing

⁵⁹ Other Uruguay Round left-over include Emergency Safeguards, Subsidies and Government Procurement, which will not be addressed in this paper. For a discussion on the rationale for a safeguard mechanism in services, see Marchetti and Mavroidis (2004).

countries (World Bank, 2004b).⁶⁰ Overcoming these constraints takes time and countries in this situation need special consideration. This should not be seen however as an excuse to delay the introduction of competition in its own market or the adoption of multilateral commitments. Here again, developing countries should use the multilateral system to inform and support their own reforms (especially against entrenched interests, whether domestic or foreign-owned). A gradual approach may be necessary. Rather than pressing to water down the substantive content of disciplines that would only favour domestic vested interests and work against developing countries' exports of services, developing countries should consider the adoption of strong disciplines on domestic regulation and, if necessary, seek transition periods and technical assistance to adapt domestic regulatory structures to the challenges ahead. This is particularly true for sectors where market access limitations (e.g. limitations on the number of suppliers or foreign equity caps) or discriminatory regulation cannot be justified on economic grounds (e.g. business services, telecommunications, maritime transport services, logistics services, distribution services). A promise of full market access and national treatment would definitely be a good starting point in informing and supporting domestic regulatory reform; while transition periods could help individual countries update their regulatory frameworks to comply with an additional layer of multilateral disciplines of the type being developed under Article VI.4 GATS.

CONCLUDING REMARKS

The aim of this paper was to analyse developing countries' participation so far in the current round of services negotiations under the Doha Development Agenda. In contrast with their participation in the Uruguay Round, which led to a very shallow level of liberalization commitments, developing countries have been particularly active in this round. They have submitted negotiating proposals and bilateral requests, have coordinated positions with each other, and have participated in multilateral discussions making their views and interests known. However, they have generally adopted a cautious and defensive approach towards liberalization of trade in services *per se*. This has manifested in a small number of offers from developing countries (less than 30) with no major improvements in their sector coverage.

The paper has tried to show how costly protectionism in services can be, and why developing countries should be putting priority on domestic reform. Due to the various sectoral linkages, an economy-wide perspective should be adopted for such reforms, recognizing in particular the importance of liberalizing entry into business and infrastructure services that are used as essential inputs into the production processes of other goods and services. The availability of first-best intermediate services, regardless of their origin, may be crucial in expanding export opportunities in sectors where countries may have a comparative advantage (e.g. manufacturing, agriculture, or even services). Apart from the "unilateralism" implied in that suggestion, I have tried to show how multilateral commitments may contribute to overcome the credibility deficit that developing countries often have due to a history of unpredictability and policy reversal. The challenge is not only to undertake liberalization commitments in key service sectors but also to shape those commitments in such a way as to promote good

⁶⁰ For example, high income-countries appear to have the smallest number of entry procedures with a median of 7, followed by upper middle-income countries with a median of 10 procedures and lower-middle income countries with a median of 12 procedures. The time to register a company is again the shortest in the richest countries (less than one month), takes around 50 days in middle-income countries and is the highest in the poorest countries, where the median number of days is 63. See World Bank, 2004.

economic policy and a sustainable sequencing of reforms, making full use of the flexibility provided by the Agreement in that regard. A more pro-active stance in liberalizing its own market would also contribute to the developing countries' bargaining position, since it would highlight how serious their engagement in these negotiations is, and how many opportunities may lie ahead in those markets if that opening is reciprocated by liberalizing commitments in areas of export interest of developing countries.

The temporary movement of natural persons is a crucial area of export interest for many developing countries. However, in spite of the emphasis placed on the liberalization of mode 4 in the last few years, no significant progress has been witnessed so far in the negotiations. Even though expectations on this issue are high among a number of developing countries, the fulfilment of those expectations will depend on the interplay of positive and negative factors underlying this area of trade. From a negotiating perspective, although the most interested developing countries have rightly identified the main barriers and obstacles on mode 4, and have suggested various ways to overcome them, the action does not seem to have been fruitful enough. The recent proposals put forward by developing countries have a high degree of generality and, in some cases, have not gone beyond the enunciation of objectives (e.g. development of a GATS visa, the assumption of additional commitments on regulatory matters, or the use of common categories of service suppliers for the sake of making commitments). More detailed multilateral proposals on each of these issues is therefore needed, although it must be acknowledged that the liberalization of temporary movement of persons supplying services (and the expansion of commitments) raises challenges not only to developed countries but also to developing countries.

The liberalization of mode 4 is not the only area where developing countries should be focusing their attention. In the last few years, a number of developing countries have developed or are in the process of developing a comparative advantage in the supply of various business services, benefiting from the worldwide trend towards business process outsourcing. Even though the business environment for this type of activities is fairly open, there are already signs of incipient protectionism emerging in developed countries. The challenge for developing countries would be to get all WTO Members to lock-in that open trade regime through commitments in these negotiations. Only a few developing countries have recently focused on this issue. The challenge is important and both technical and political/negotiating work in this area is needed.

The paper has finally addressed the development of disciplines on domestic regulation, not from a technical point of view but from a political economy perspective, acknowledging that deeper disciplines in this area are needed. Arguably, when it comes to domestic regulation, developing countries are different. They often regulate in a less efficient manner, need to set up standards and regulatory arrangements from scratch, lack enough monetary resources, and have a deficit in competent human resources. Overcoming these constraints takes time and countries in this situation need special consideration. A gradual approach may be necessary. However, rather than pressing to water down the substantive content of disciplines that would only favour domestic vested interests, developing countries should consider the adoption of strong disciplines on domestic regulation that would inform their own domestic reform processes; and, if necessary, seek transition periods and technical assistance to adapt domestic regulatory structures to the challenges ahead.

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