

# SERVICES TRADE

## APPROACHES FOR THE 21<sup>ST</sup> CENTURY

Report of the Task Force established by the Asian Development Bank Institute  
and the Pacific Economic Cooperation Council



A long, brightly lit tunnel with two people walking in the distance. The tunnel's structure is composed of many parallel lines that converge towards the horizon, creating a strong sense of perspective. The lighting is bright and even, highlighting the smooth surfaces of the tunnel walls and floor. Two small figures of people are visible in the far distance, walking away from the viewer towards the light at the end of the tunnel.

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# ABBREVIATIONS

<b>ABAC</b>	APEC Business Advisory Council
<b>ADB</b>	Asian Development Bank
<b>ADB I</b>	Asian Development Bank Institute
<b>ACTA</b>	Anti-Counterfeiting Trade Agreement
<b>APEC</b>	Asia-Pacific Economic Cooperation
<b>ASEAN</b>	Association of Southeast Asian Nations
<b>BMP6</b>	6 <sup>th</sup> Edition of the Balance of Payments Manual
<b>DDA</b>	Doha Development Agenda
<b>FTA</b>	Free Trade Agreement
<b>GATS</b>	General Agreement on Trade in Services
<b>GPA</b>	WTO Agreement on Government Procurement
<b>G20</b>	Group of Twenty
<b>ICTSD</b>	International Centre for Trade and Sustainable Development
<b>ITA</b>	Information Technology Agreement
<b>IT-BPO</b>	Information Technology – Business Process Outsourcing
<b>MFN</b>	Most Favored Nation
<b>MSITS</b>	Manual on Statistics for International Trade in Services
<b>OAS</b>	Organization of American States
<b>OECD</b>	Organization for Economic Cooperation and Development
<b>PECC</b>	Pacific Economic Cooperation Council
<b>R&amp;D</b>	Research and Development
<b>RTA</b>	Regional Trade Agreement
<b>SME</b>	Small and Medium Sized Enterprise
<b>TPP</b>	Trans-Pacific Partnership
<b>UNCTAD</b>	United Nations Committee on Trade and Development
<b>UN-ESCAP</b>	United Nations – Economic and Social Commission for Asia Pacific
<b>WTO</b>	World Trade Organization

## Conference Organizers

**The Pacific Economic Cooperation Council** (PECC) is an independent, multi-sectoral organization committed to the promotion of cooperation and dialogue in the Asia-Pacific. The Council is the only non-governmental official observer of the APEC process. All members participate in their private capacity and discuss freely on current, practical policy issues in the Asia-Pacific region. Established in 1980, PECC's regional community building efforts led to the establishment of the official APEC process in 1989.

**The Asian Development Bank Institute** (ADBI), located in Tokyo, is the think tank of the Asian Development Bank (ADB). It was established in 1997 to identify effective development strategies and to improve development management in ADB's developing member economies. ADBI is a leading center for the creation and dissemination of information and knowledge on development in the Asia and Pacific region. For more details, visit <http://www.adbi.org>.

## Collaborators

Founded in 1963, **The Chinese University of Hong Kong** (CUHK) is a forward-looking comprehensive research university with a global vision and a mission to combine tradition with modernity, and to bring together China and the West. Based at CUHK, the **Hong Kong Institute of Asia-Pacific Studies** (HKIAPS) serves as a think tank for the Hong Kong government, the Chinese government and policy makers in the public and private sectors. The HKIAPS **Economic Research Centre** is oriented to promoting research and stimulating policy discussion on economic issues relevant to Hong Kong, Greater China, and the Asia-Pacific region. The Centre is responsible for editing and publishing the Asian Economic Journal for the Asian Economic Association.

Founded in 1861, the **Hong Kong General Chamber of Commerce** (HKGCC) is the oldest and largest business organization in Hong Kong, with around 4,000 members, including multinational companies, companies from Mainland China, PRC, and Hong Kong companies. The Chamber is a self-funded, non-profit making organization representing the diverse interests of the entire business community in the Hong Kong Special Administrative Region (SAR). The Chamber takes a strong role in promoting Hong Kong as an international business center in the heart of Asia.

## PECC Task Force on Services

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# SUMMARY OF KEY MESSAGES

The services sector now accounts for 68 percent of value-add in the Asia-Pacific region, making it the largest sector in the regional economy. It is also the single biggest creator of jobs in the region, accounting for 61 percent of employment in the Asia-Pacific region, up from just 27 percent when the Asia-Pacific Economic Cooperation (APEC) forum was founded in 1989.

While the services sector has come to dominate the modern economy, international trade in services lags behind. Exports of goods from APEC member economies are five times larger than exports of services although both have grown by close to 115 percent over the past ten years.

This work comes at a time when regional and global institutions such as APEC and WTO are considering how to get momentum behind global trade as the WTO Doha Development Agenda (DDA) is stuck.

The services sector has been the neglected component of international trade, and the missing element in the search for increased productivity and economic dynamism. The task force found three major sets of explanations for this lack of progress.

## **Lack of awareness of the contribution of services to the economy**

- The first part of the explanation lies in relative public ignorance of the factors that influence competitiveness and of the dominant contribution that services make to industry value-add, employment, productivity, export revenue, Gross Domestic Product (GDP) growth and poverty reduction.
- While there remain concerns in some economies that a more open services sector regime might lead to significant adjustment in the structure of activities of locally owned services providers, the consequences of greater openness for the competitiveness of the sector and indeed the economy as a whole, are important. Services providers are themselves significant users of other services – for example, tourism and air transport, or telecom services used in business processing. A more open sector offers more variety to users of services.
- A more competitive services sector contributes to productivity growth elsewhere in the economy. Research is now in progress which establishes the links between services sector reform and manufacturing sector productivity.
- The factors affecting competitiveness in the services sector are closely linked to the degree of openness in services trade and investment, as well as to regulatory efficiency. There is evidence that very big productivity gains are available from services trade and investment reform. This linkage has not been well understood but there is increasing appreciation of its significance.
- Businesses are often more aware of these linkages than policy makers. Businesses are frustrated by prolonged policy failure on services trade reform in the WTO and insufficient progress at a unilateral, bilateral or regional level.

## **Concerns over impact of services openness**

- Governments however remain concerned about the implications of greater degrees of openness for the operation of their regulatory systems. Partly as a consequence of this concern, there are big differences between bound and applied commitments to services sector reform. Meanwhile this gap continues to hold back urgent investments in key infrastructural sectors that are critical to the development of a modern economy, and especially for bringing benefits of economic integration to the broader population.



- Governments would value more extensive guidance than the WTO General Agreement on Trade in Services (GATS) provides on best regulatory practice for the services sector.

### **Inadequacies in negotiating modalities**

- The third factor in the stalemate on services in the DDA derives from weaknesses in the modalities of those negotiations.
- The "request-offer" process has failed and that situation demands an urgent response. The time is right for a global initiative on the services sector. There is increasing appreciation of the significance of the services sector, and better understanding on the extent of the remaining impediments. In particular, services sector reform can make the trading system work better, in a supply-chain world where logistics, communication and finance are critical to trading costs and to the organization of production across all sectors of the economy. But the piece-meal approach to liberalization arising from the "request-offer" modality can only deliver fragmented results.

Based on this analysis, the task force has put forward specific proposals for further policy attention and follow-up. The proposals are clustered around two big ideas for improving regional and global governance in the services sector, both of which have implications for APEC.

### **Regulatory Principles for Services**

The first big idea is that governments should develop a set of regulatory principles for the services sector. One specific suggestion is for development of a generic cross-sectoral "Services Reference Paper", setting out pro-competitive principles that might have application to all services.

There are many potential sources from which such work may draw inspiration, including:

- the WTO Telecommunications Reference Paper;
- the OECD/APEC Integrated Checklist on Regulatory Reform;
- the Insurance Principles developed by the services business community during the GATS negotiations on Financial Services;
- the work over many years of the APEC Group on Services.

Regulatory regimes for network services might differ in some aspects from regulatory principles applicable to natural monopolies or to services affected by information asymmetries. However, with some economic analysis and conceptual imagination, it should not be difficult to arrive at a useful set of principles with relevance across the services economy.

APEC should initiate inter-governmental discussions, drawing in the discussion on inputs not only from policymakers and regulators but also from the knowledge community, on principles for all-of-services regulation, with a view to generating global interest in developing such principles. It is suggested that APEC should experiment with new ways of bringing services regulators together with trade officials, both sector-by-sector and at whole-of-services level. This will facilitate sharing of regulatory experience, raising awareness of regulatory incoherence and promoting discussions on options for improving regional practice, as well as encourage domestic regulatory audit and benchmarking of progress.

There is also evident support for the suggestion that governments should consider designing practical regulatory mechanisms, in consultation with the business community, to increase recipient economy confidence specifically on mode 4<sup>1</sup>.

### **A Stand-alone Negotiation on Services**

The second big idea is that governments might have a higher degree of inter-governmental negotiating success than has been achieved to date, if they were to pursue services negotiations within a new set of arrangements. There are three components to this structure – stand-alone, plurilateral and new formats for commitments.

<sup>1</sup> The General Agreement on Trade in Services defines four modes of delivery for trade in services: Mode 1: From the territory of one Member into the territory of any other Member (cross-border trade); Mode 2: in the territory of one Member to the service consumer of any other Member (consumption abroad); Mode 3: by a service supplier of one Member, through commercial presence in the territory of any other Member (commercial presence); and Mode 4: by a service supplier of one Member, through presence of natural persons of a Member in the territory of any other Member (movement of natural persons)

First, services negotiations could be organized on a stand-alone basis, i.e. independently of the additional complexities of negotiations on agricultural and manufactured goods. This option is already open to WTO members. Stand-alone services negotiations are mandated in the Uruguay Round built-in agenda and these could and should be recommenced, irrespective of developments in the DDA. A number of economies in the region have significant experience with this: under the ASEAN Economic Community (AEC) Blueprint, consecutive rounds of negotiations take place every two years which are designed to achieve commitments in a minimum of ten new sub-sectors by 2008, 15 by 2010, 20 in 2012, 20 in 2014 and another seven in 2015.

Second, given that less than one third of the WTO members have made services offers in the DDA, new negotiations could commence plurilaterally.

Third, as the "request-offer" process has effectively failed, consideration needs to be given to the alternative possibility of a new multi-modal framework accord, such as a standstill and rollback-type deal (with or without individual schedules of commitments, on either a positive, negative or hybrid list basis). The work undertaken for the collective requests might offer one possible place to start.

Progress will eventually depend on the effective use of the burgeoning body of research on services policy and on close consultation with the services business community. There will be widespread interest in exploring ways in which services negotiations might benefit from the insights from soon-to-be-published works on services sector trade restrictiveness measurement. These include works by the OECD and the World Bank and also recent work commissioned by the Policy Support Unit (PSU) of APEC. The work on services by the APEC Business Advisory Council (ABAC), as well as that of the Global Services Coalition, will also be instructive.

#### **APEC leadership role**

APEC has been seen as being uniquely well-placed to build a "critical mass" of political will for stand-alone services plurilaterals, just as it did in the case of the Information Technology Agreement (ITA).

It is the hope of the task force that APEC members will take heed of these two recommendations and take the opportunity that APEC as an organization provides, to incubate these new ideas.

There are different ideas on the form a stand-alone services trade discussion should take. A study group in APEC could be created to better understand the ramifications of a services agreement and the incentives for economies.

APEC must have concrete outcomes visible to businesses if it is to sustain regional business interest. A services trade initiative from APEC would achieve this objective, especially if it is linked, as ABAC has suggested, to dealing with the choke points in regional supply chain operations. The initiative should bring new depth and energy to APEC's work on regulatory cooperation, in particular, developing principles for regulatory coherence in the services sector.

APEC should look beyond the DDA and open the way forward for considering fresh negotiating processes and exercising flexibility with respect to negotiating modalities, specifically in services. This is a way for APEC to show its leadership on the global issues that have most impact on creating jobs for future generations.



# INTRODUCTION AND CONFERENCE THEMES

The services sector now accounts for 68 percent of value-add in the Asia-Pacific region, making it the largest sector in the regional economy. It is also the single biggest creator of jobs in the region accounting for 61 percent of employment in the Asia-Pacific, up from just 27 percent when the APEC forum was founded in 1989.

While the services sector has come to dominate the modern economy, international trade in services lags behind. Exports of goods from APEC member economies are five times larger than exports of services although both have grown by close to 115 percent over the past ten years.

The PECC and the ADBI established a task force in 2011 to consider what actions can be taken to unleash the potential of services sector trade for improving productivity and creating jobs.

From 1 to 3 June 2011, the PECC and the ADBI held an Inaugural Conference, with support from the HKGCC, on "Services Trade: Approaches for the 21st Century", at the Economic Research Centre of the CUHK Institute for Asia-Pacific Studies. Hong Kong was chosen as the Conference venue in recognition of its status as the most services-oriented economy in the world. Services (including utilities and construction) account for over 97 percent of GDP and employ 95 percent of the Hong Kong work force. It is consequently one of the few economies in East Asia that is a net services exporter.

The Conference was the first of its kind to bring together the world's top experts on the services economy from the academia, government and the private sector. International experts hailed from WTO, OECD, the World Bank, ADBI, UNESCAP, ICTSD, ASEAN and APEC Secretariats, as well as from the local and regional business community, including ABAC and the various business associations allied with the Global Services Coalition.

Professor Sir James Mirrlees, 1996 Nobel Laureate for Economic Sciences opened the Conference on behalf of CUHK, along with Dr Charles E. Morrison, President of the East-West Center in Hawaii and Co-Chair of the PECC, Dr. Masahiro Kawai, Dean of the ADBI and Ms Maria Kwan, Director-General of the Hong Kong Department of Trade and Industry.

The Conference enjoyed very active participation from senior regional business and government representatives. The program included an innovative seminar activity organized with the HKGCC and the Pacific Basin Economic Council (PBEC), designed to reach out to the wider Hong Kong community. Mr Fred Lam, Chief Executive of the Hong Kong Trade Development Council, addressed a Conference luncheon on how to promote services exports, while Mr Anthony J.L. Nightingale, Managing Director of Jardine Matheson Limited and Chair of the ABAC Action Plan and Advocacy Working Group, moderated the final policy discussion. The Conference dinner speaker was Dr William Fung, Deputy Chairman of Li and Fung, supported by Mr Nicholas Brooke, Chairman of the Hong Kong Science and Technology Parks Corporation, and Mr Robert Vastine, Chief Executive of the Coalition of Services Industries, United States.

Policy research papers and other presentations were specially commissioned for the Conference, often on a collaborative basis, stressing the need for original work, a strong evidence base and in-depth consultation with the private sector. The Conference aimed not only to add significantly to the academic literature and to nurture an emerging network of regional researchers, but also to help

deliver policy recommendations for APEC and G20 Leaders at a time of stagnation in the DDA and considerable uncertainty in the multilateral trading system.

Against the background of an increasing services-to-goods ratio in world trade, the Conference was designed to generate an intense and deliberately whole-of-services focus on the most demanding research, as well as business and policy questions arising from trade in services today. The themes explored included:

- understanding and documenting the regional services economy;
- the role of the services sector in growth and development, employment, productivity and innovation;
- trends in services trade and investment;
- services industry value chains;
- barriers to doing international business;
- determinants of services competitiveness; and
- tackling the need for improvements in global and regional governance arrangements for services.

## ROLE OF SERVICES IN GROWTH AND DEVELOPMENT

Although the services sector accounts for over 68 percent of global GDP and close to 61 percent of employment in the world and the APEC region, the role it plays in economic development has been poorly understood. Recent analysis shows that the services sector plays an important role in overall economic competitiveness and in the development of the manufacturing and agriculture sectors.

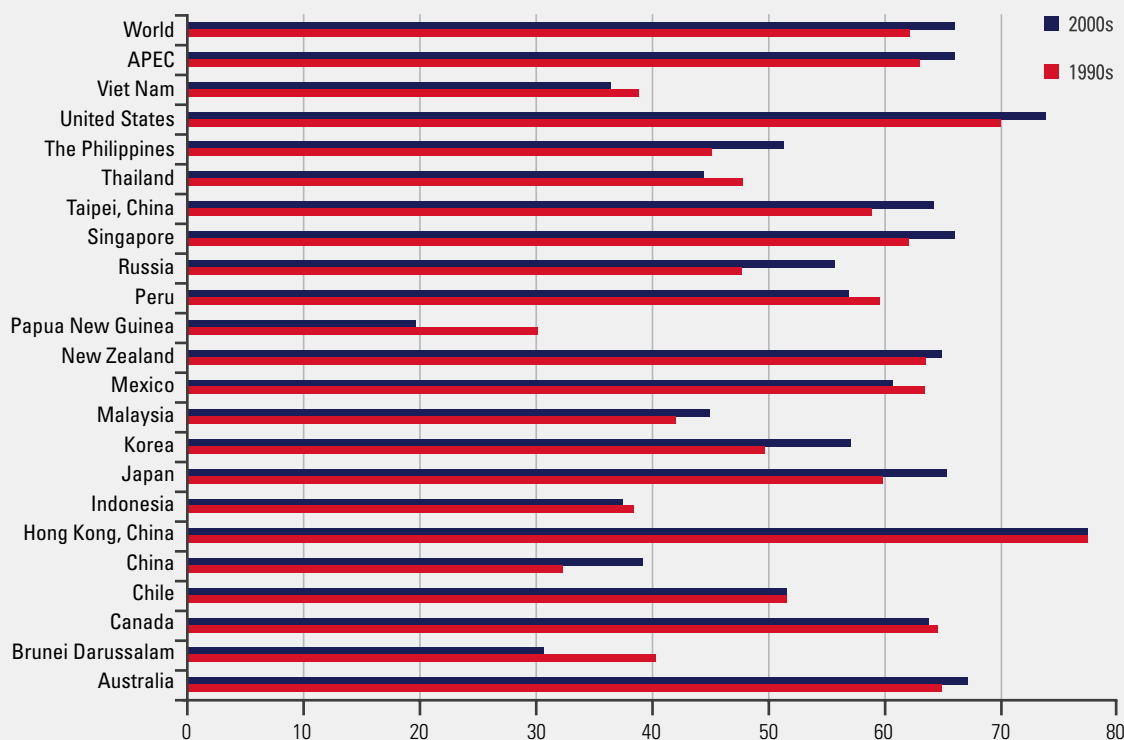
Critically in this period of low growth, economic analysis comparing the impact of services and manufacturing on GDP growth shows that the impact of services sector growth on GDP growth is almost double that of manufacturing (Ghani 2010). As will be discussed later in this report, the services sector's importance lies not just in and of itself but also in the role it plays as an enabler of international trade in a world characterized by supply chains.

### *Services and the Economy*

Over the past 20 years the services sector has been growing in importance across both the Asia-Pacific region and the world as shown in Figure 1. While there are some notable exceptions, these tend to be in economies where manufacturing or primary industries have been growing at a more rapid pace than services.

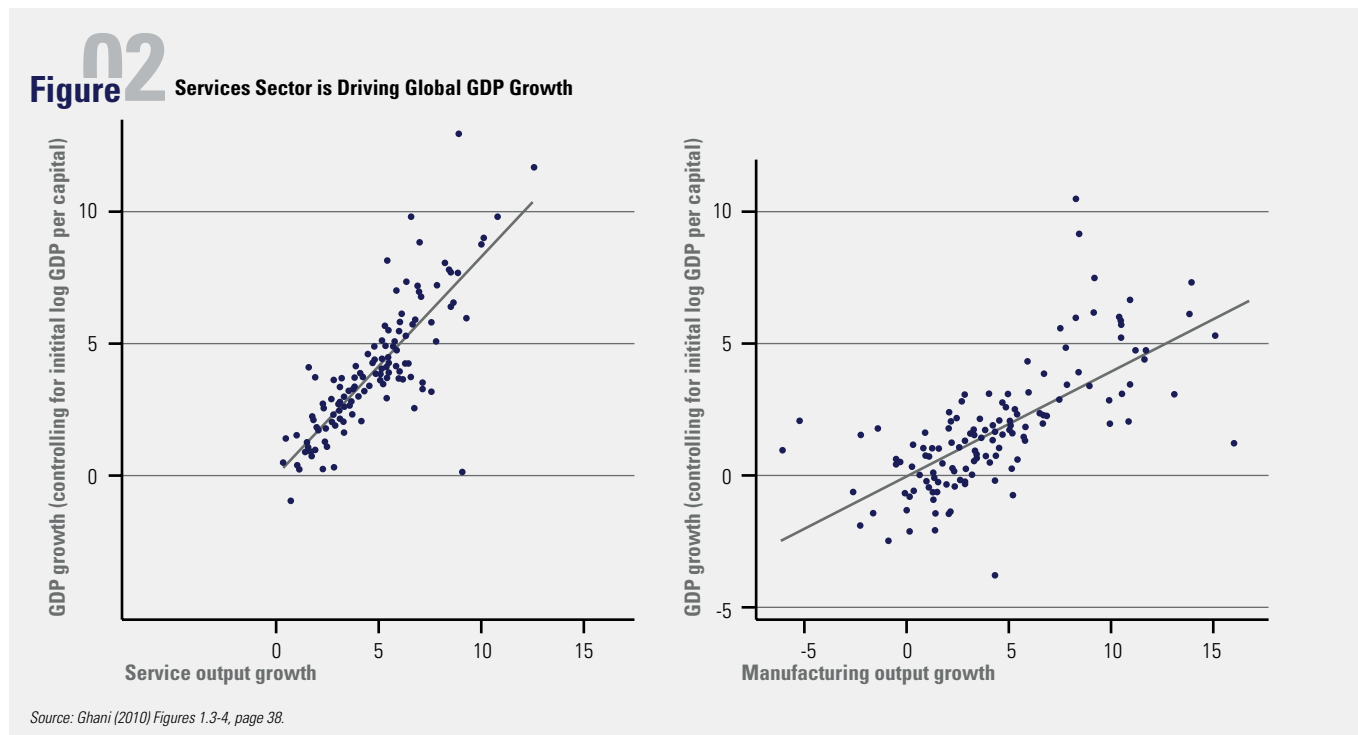
### 01 Figure

**Services as a Share of GDP**

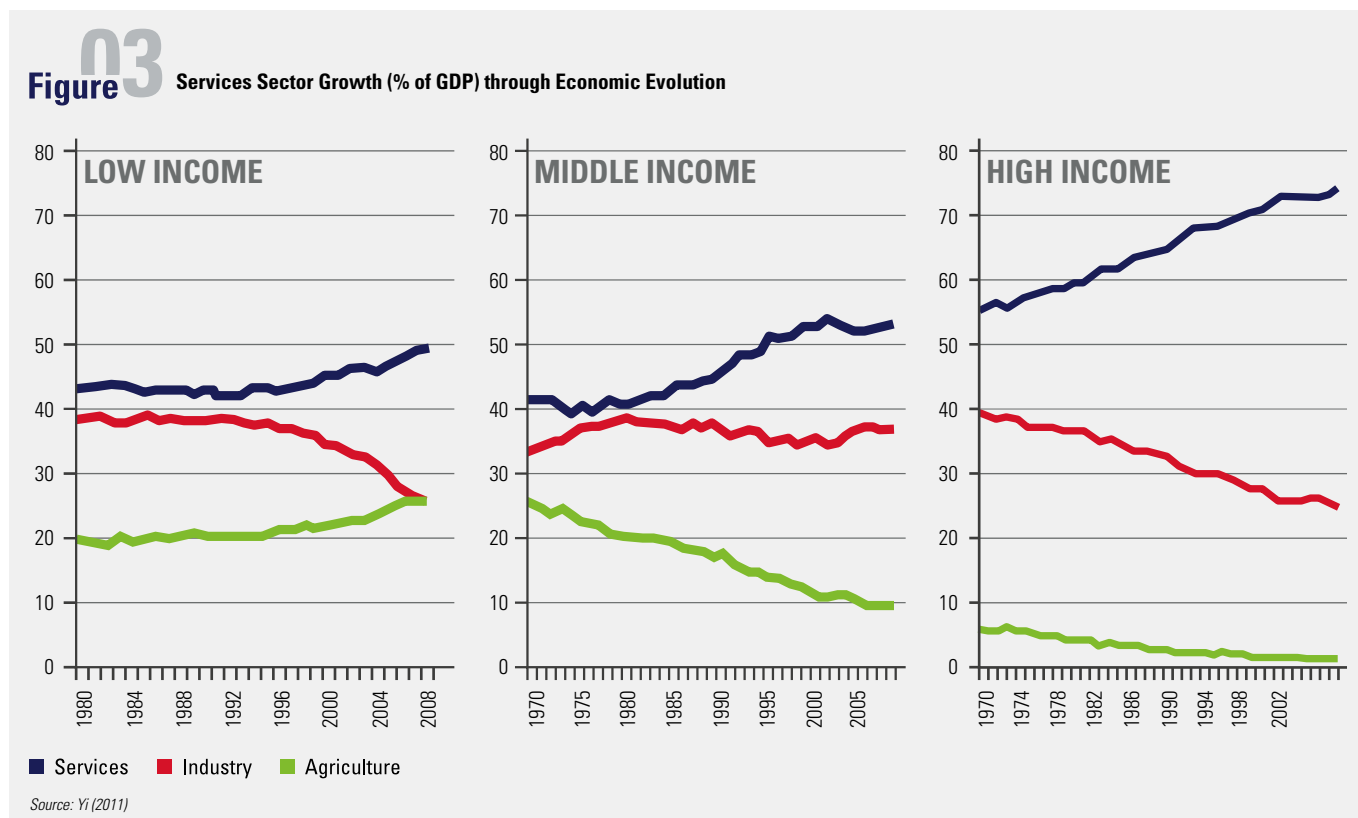


Source: World Trade Organization, Time Series on International Trade, adapted from Pasadilla and Chanda 2011

Across the world, GDP growth goes hand-in-hand with services sector growth and with even stronger correlation than with manufacturing growth, as shown in Figure 2, which includes data for 134 economies from 2000 to 2005.

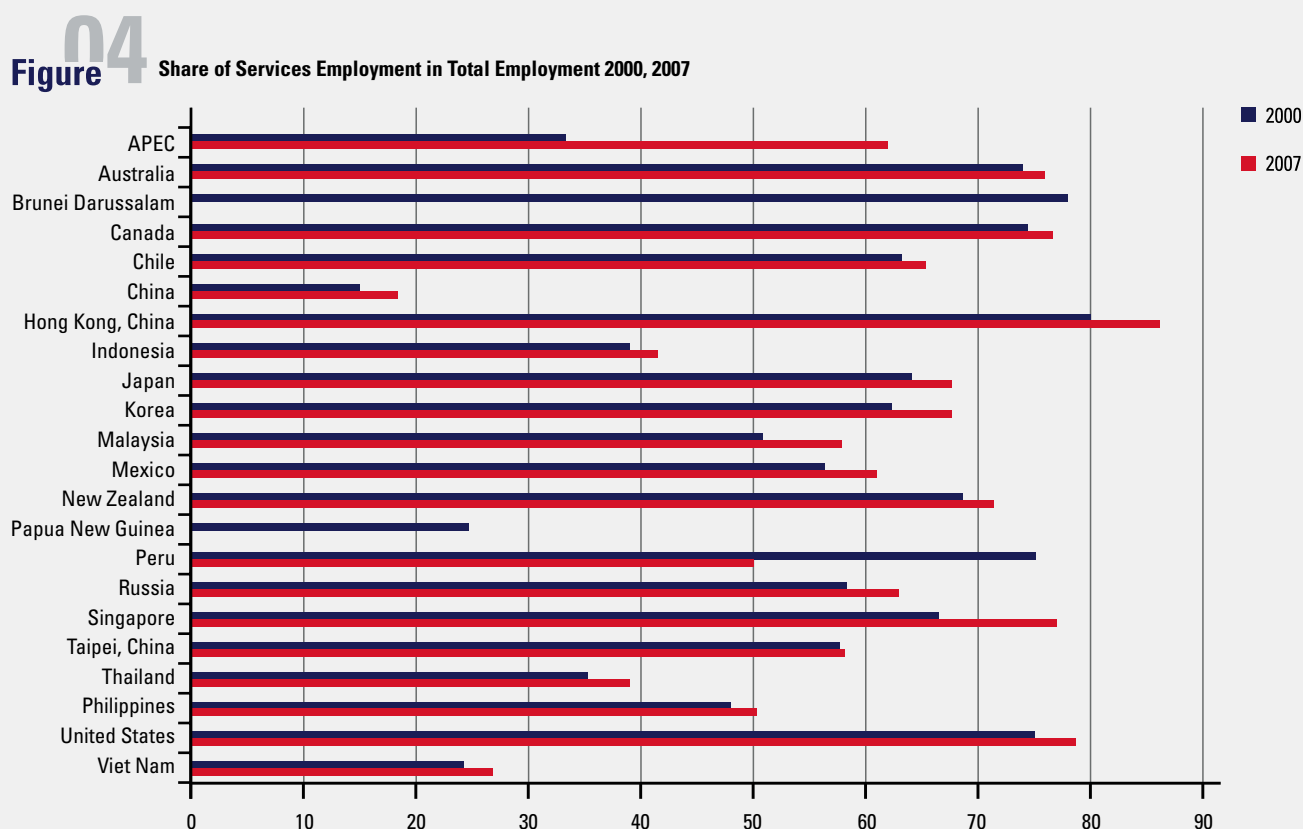


Conventional wisdom is that services sector-driven growth comes after periods of agricultural and manufacturing dominance. However, as shown in Figure 3, even low-income economies have services reaching close to a 50 percent share of economic output. On average, the services sector value-add is now well over 50 percent for most APEC economies. While the services sector is more dominant in high income economies, it is also strong in low income economies and increasingly so.

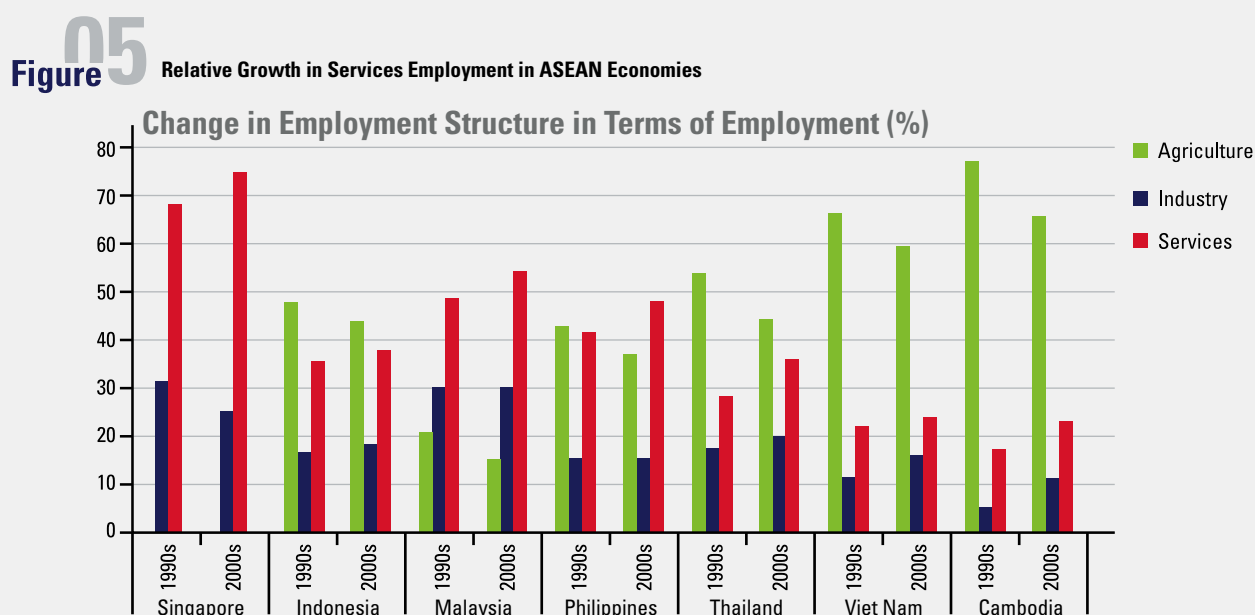


## Services and employment

In most economies, the services sector is also the major source of employment, accounting for 61 percent of employment in the Asia-Pacific region, slightly more than double the level of 30 percent in 2000. In majority of APEC economies, employment in the services sector exceeds 40 percent of total employment (Figure 4). In the same period, employment in agriculture declined from 44 percent to 40 percent, while the share of employment in industry has been flat. Globally, skilled jobs are growing faster than unskilled jobs.



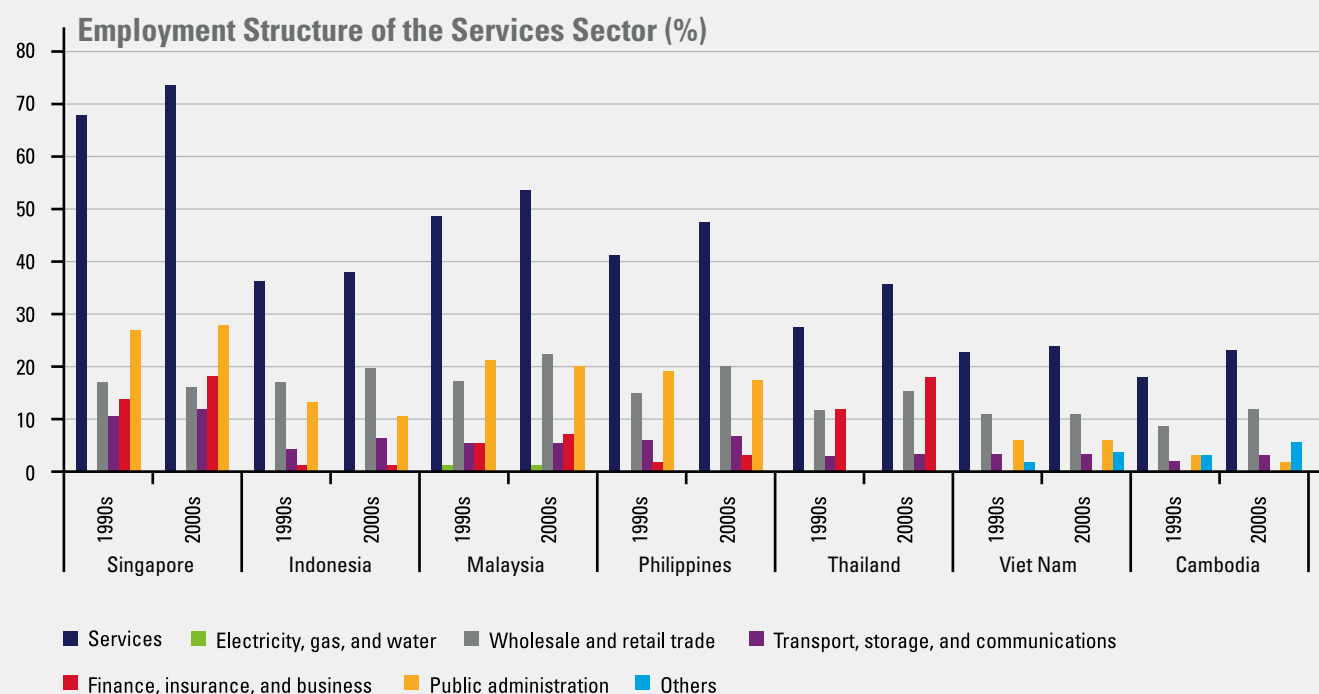
In the case of ASEAN, the services sector's contribution to employment is on the rise while employment in agriculture is declining. Employment in manufacturing industry is, however, either stable or still growing (Figure 5).





The relative importance of different types of services is also changing. While retail and wholesale trade is still the dominant employer (after public administration), financial and business services and transport and communications are growing (Figure 6).

**Figure 06** Changing Composition of Services Employment in ASEAN Economies



Source: Aldaba and Pasadilla (2011) ASEAN Services Sector and the Growth Rebalancing Model, ADBI Working Paper No 246 (Table 4).

Business process outsourcing (BPO) has become an important driver of services exports and value-add in several Asian economies. The main ingredient for such services is manpower, often specifically skilled English-speaking manpower. In South and Southeast Asia, growth in BPO services exports has been accompanied by rapid increases in direct employment of skilled persons over the last decade. It has also led to increases in indirect employment from supporting services such as transport, real estate, catering, housekeeping, security and training (Chanda and Pasadilla 2011). There is also evidence of various positive socio-economic and gender-related employment trends that are critical for addressing growing income inequality in the region.

Much of the BPO sector in Asian economies owes its growth to outsourcing and foreign investment from services firms in developed economies, leading in some cases to concerns in the home economy about potential domestic job loss. However, evidence from a United States (US) International Trade Commission (ITC)<sup>2</sup>, finds that intra-firm services exports from the US parent to the foreign affiliate are supporting jobs at the US headquarters, as well as throughout their US-based services supply chains. The ITC finds that establishment abroad by US services firms supports around 700,000 US-based jobs.

The services sector also creates more jobs. For example, in Korea, one billion won of investment in services creates almost twice the number of jobs as compared to the same amount of investment in manufacturing.

**Table 01** New Jobs Created in Each Industry Sector in Korea, with 1b won New Investment Injection

Category	2000	2003	2005	2006	2007
Manufacturing industry	8.8	8.6	7.2	6.9	6.6
Electricity, gas, water services	4.7	3.9	3.2	3.1	3.1
Construction	14.6	16.3	14.8	15.2	14.8
Service industry	13.7	13.7	12.6	12.6	12.6

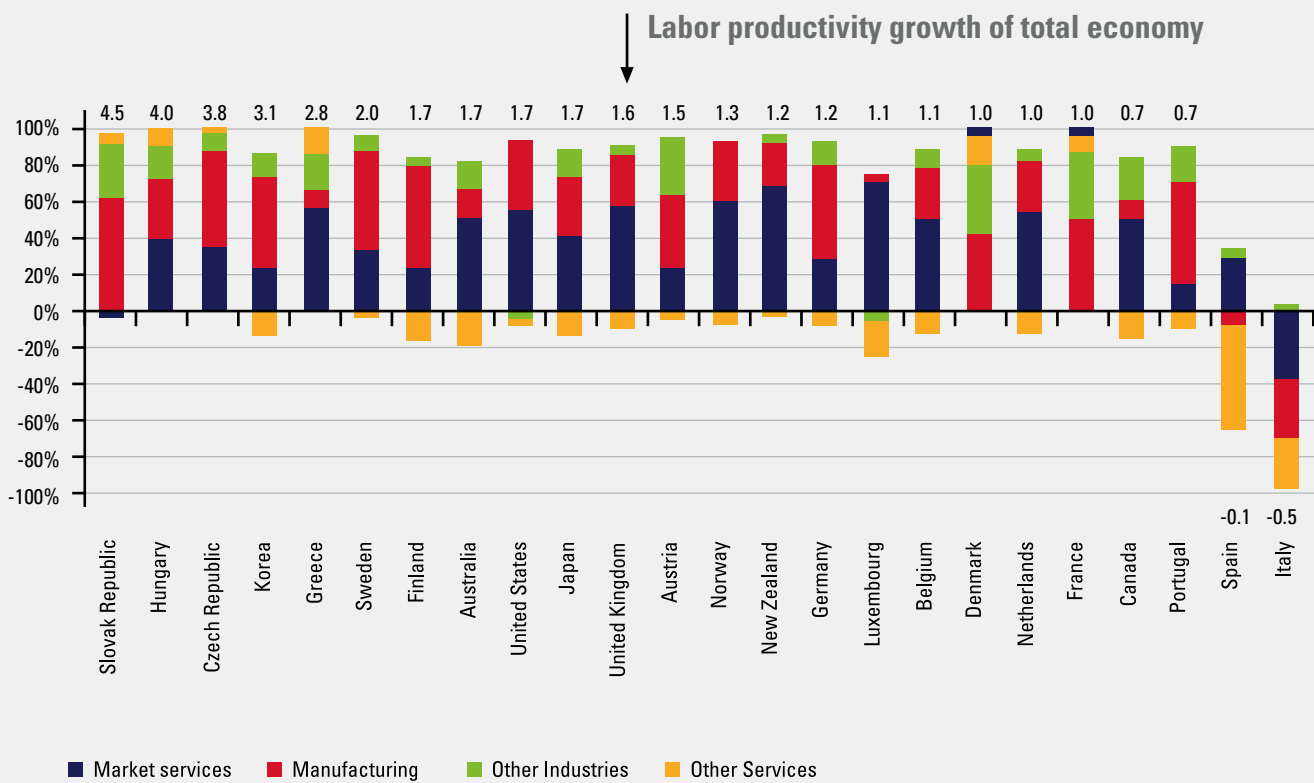
Source: Tcha (2011)

<sup>2</sup> ITC (2011)

In addition to being a creator of value and jobs in its own right, the services sector provides the essential infrastructural networks for the goods-producing sector. The sector consequently plays a key enabling role across the whole economy (Atje and Mugiyani 2011). One of the factors making services so important is the consequent role that services productivity growth plays in generating productivity gains across the whole economy. In OECD economies, labor productivity in services, especially market services, outweighs labor productivity in manufacturing in its contribution to GDP growth (Figure 7).

## 07 Figure

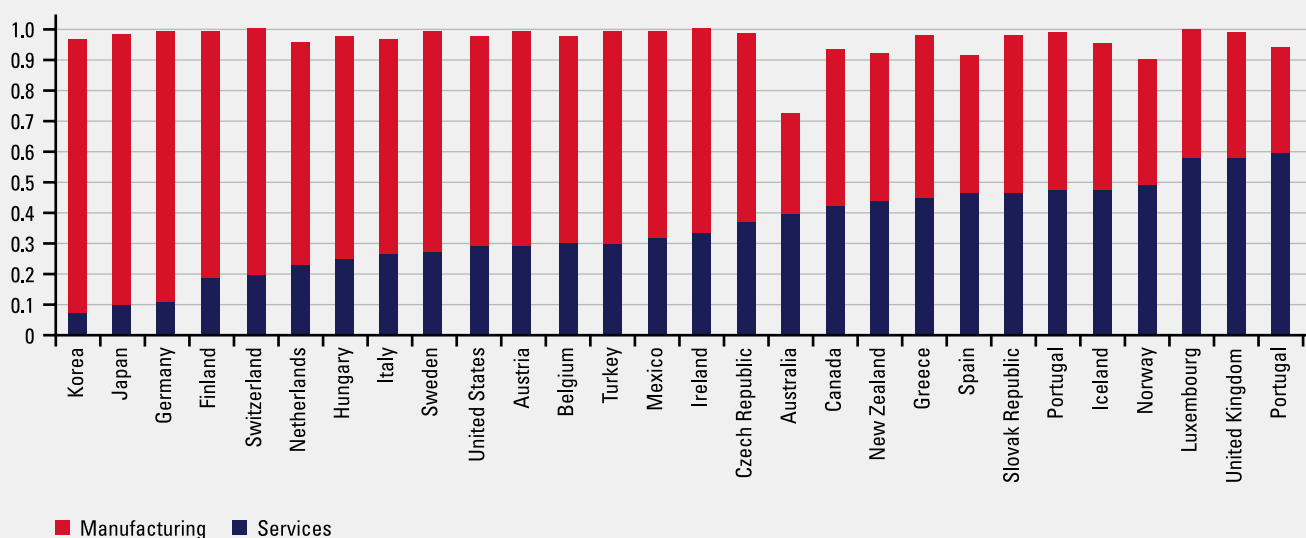
**Labor Productivity in Services, as Contribution to GDP Growth  
(OECD Economies, 2000-2006)**



Source: Tcha (2011)

Evidence is emerging that “multi-factor productivity”, which used to be the immeasurable residual once called “technological change”, is now becoming better understood as “services innovation”. Services innovation appears to contribute importantly to productivity growth and to services exports performance. Most research and development (R&D) is now taking place in the services sector compared to manufacturing as seen in Figure 8. However, R&D is only one component, and a declining one, of total firm expenditure on innovation (which also includes design and business process restructuring). For example, in China’s manufacturing sector, R&D expenditure is only about one third of firms’ total expenditure on innovation (Tcha 2011).

**Figure 8** Share of R&D Conducted by the Services Sector (OECD, 2000-2008)



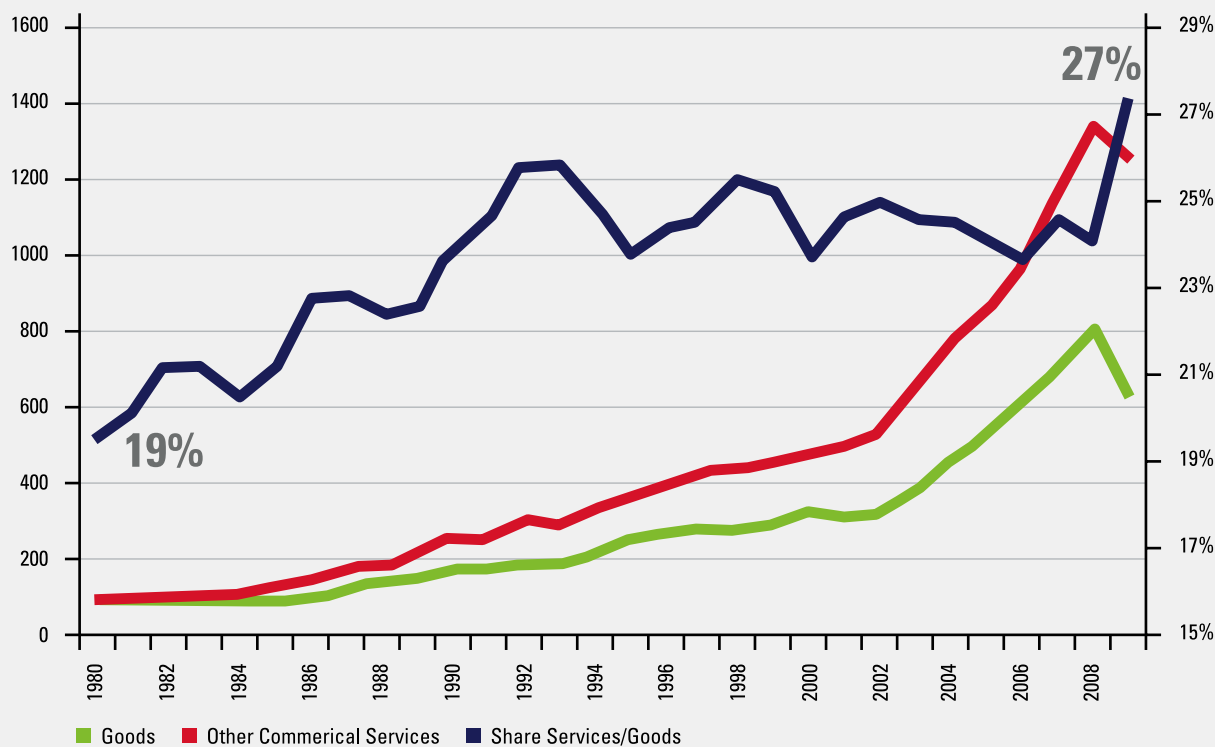
Source: Tcha (2011)

The concept of supply chains in manufacturing is well-understood in trade policy literature and even in official policy discussions. The role that services plays in facilitating the smooth flow of components along the nodes of the chain, in terms of warehousing and logistics, is also addressed in trade policy discussions. However, missing from the policy discussion is the concept of services supply chains. In new business models, services firms, like goods firms, are seeking to go up the value chain and to outsource non-core services functions. This section addresses the challenges in understanding services supply chains.

#### *Trade in Services*

Global services trade remains small compared to goods trade, but its growth since 1980 has outstripped that of goods trade. Services trade, as measured by the balance-of-payments, now accounts for around 27 percent of global exports (Figure 9).

**Figure 9** Trend in Global Share of Services to Goods Exports

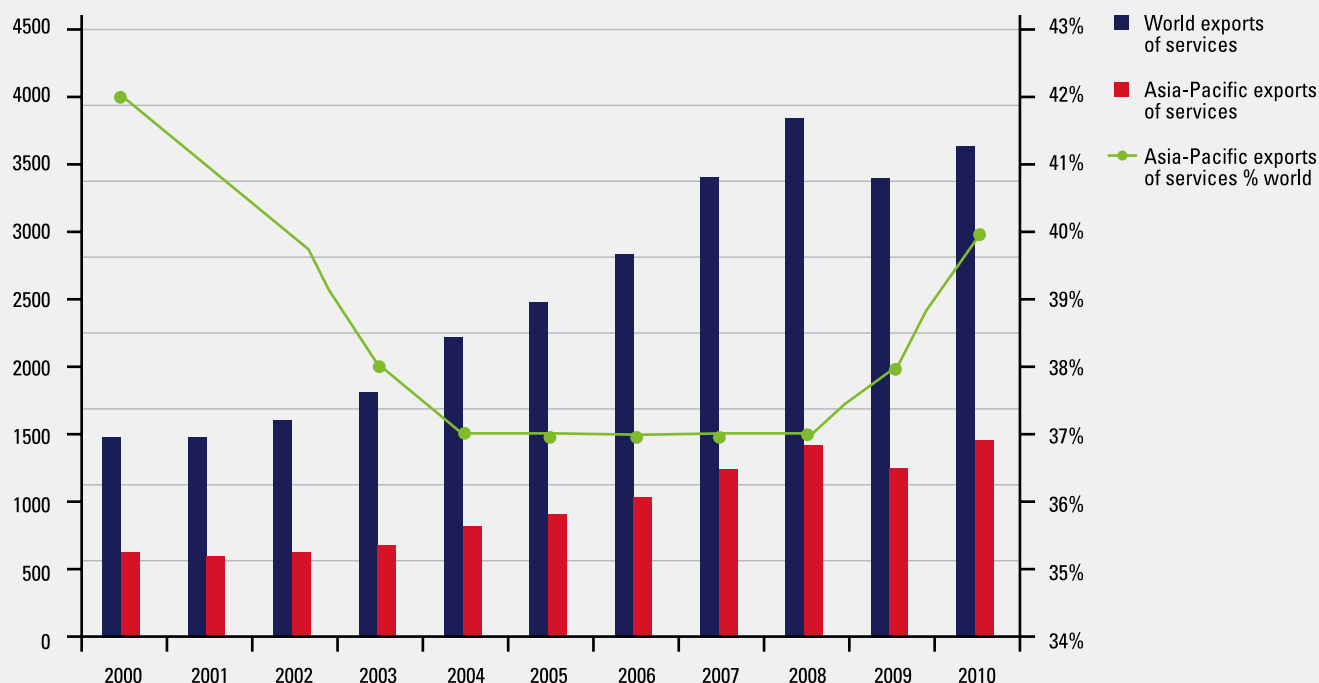


Source: Saez (2011)

Research results consistently suggest, however, that adding in mode 3 transactions (commercial presence) could roughly double this figure. All APEC economies are successfully exporting services of one kind or another, although in the early part of the last decade, the rate of growth of the APEC region's exports of services lagged behind the global average. Figure 10 shows that APEC economies' share of global services exports dropped from 42 percent in 2000 to a low of 38 percent in 2007. However, global and regional trade in services proved more crisis-resilient than trade in

goods. Indeed, the APEC region experienced even less of a decline in services exports than the global average, the outcome being that APEC economies gained in percentage share of global services exports in 2009, a trend that intensified into 2010. In 2010, the APEC region accounted for 41 percent of global services exports, almost making up for the earlier decline.

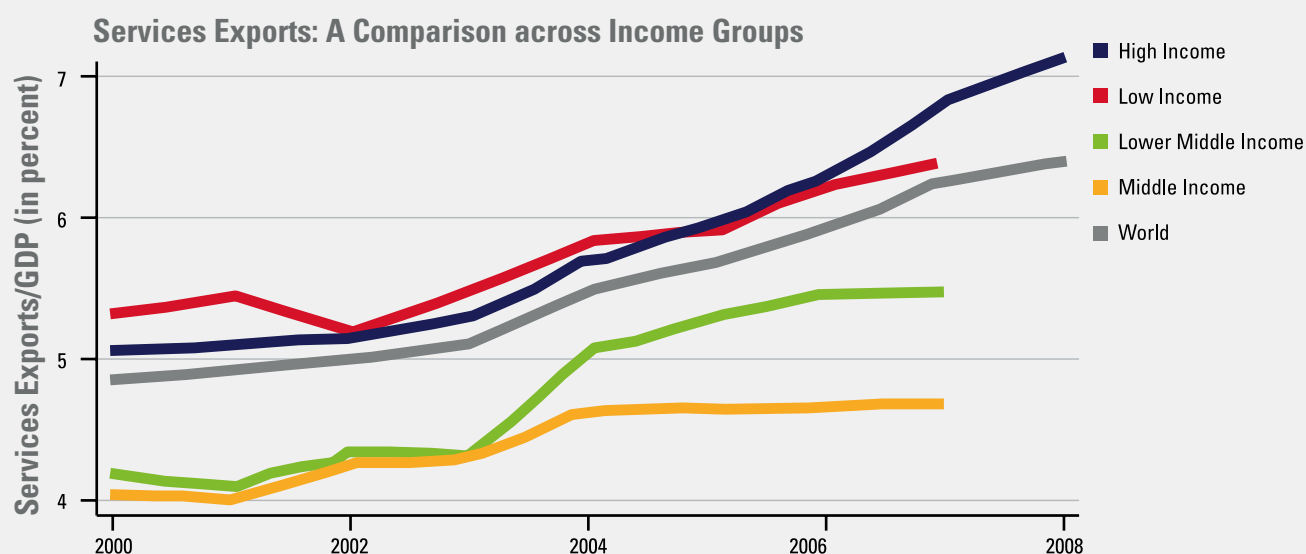
**Figure 10** Decade of Global and Regional Growth in Services Exports (US\$bn)



Source: Statistics APEC, World Trade Organization, Time Series on International Trade

While the world average ratio of services exports to GDP has grown from less than 5 percent in 2000 to around 6.5 percent in 2008, there are significant differences in the trend for economies in different income level groups. Services exports are already contributing over 7 percent of GDP for high income economies, but still well below 5 percent for middle income economies (Figure 11). Importantly, services exports are making higher contributions to GDP for low-income economies than for middle-income economies; just under 6 percent for lower middle income economies and just over 6 percent for low-income economies (Saez 2011).

**Figure 11** Services Exports as a Contributor to GDP at Different Levels of Development



Source: Saez 2011 from World Bank, World Development Indicators

This suggests that the services sector offers a viable alternative development route to manufacturing, enabling poorer economies to “leapfrog” over manufacturing.

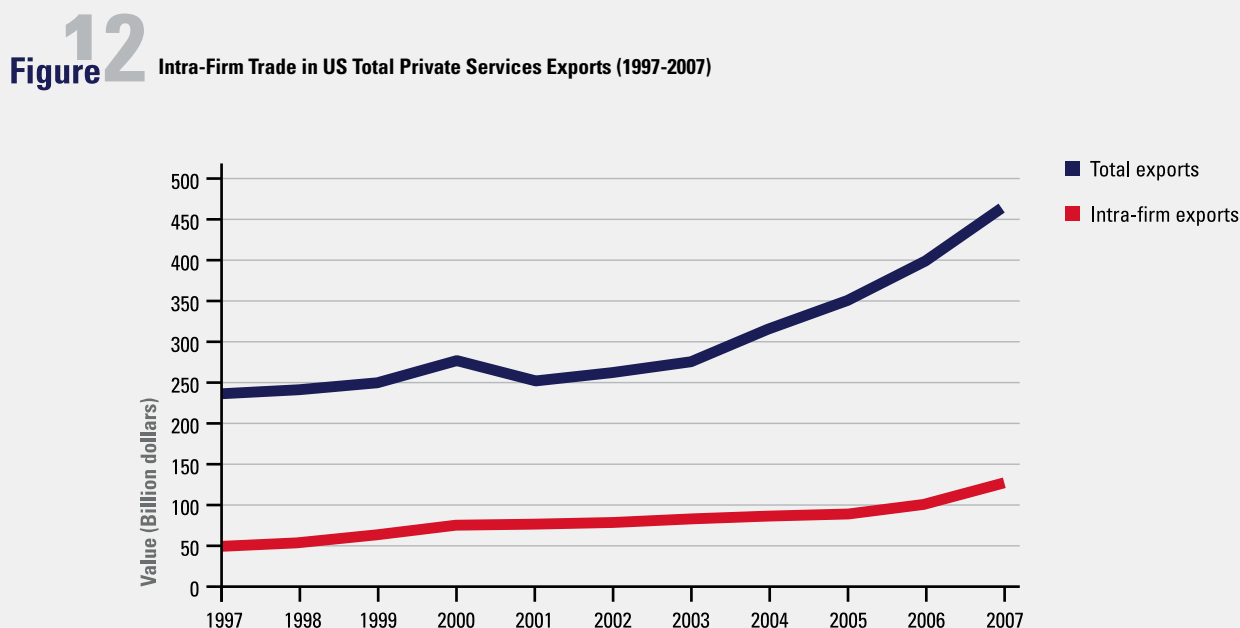
### Trade in Tasks and Services Value Chains

There has been much attention in the trade policy conversation to global supply chains for goods, and there is improved understanding that for many elaborately transformed manufactures (such as the iPhone), the highest value-add is contributed by services inputs, often at the R&D and design phase or at the logistics/distribution phase. All kinds of tasks along the intermediate phases of the supply chain between these two high value-added ends are increasingly being outsourced to wherever each individual task can be most efficiently performed. This intermediate or intra-firm trade is being described as “trade in tasks”.

The role of services in facilitating “trade in tasks” by providing the “glue” at each point in the goods supply chain is increasingly recognized. It is also a fact that the “embodied” services component of production and trade, especially of elaborately transformed manufactures, can account for a very high percentage – sometimes over 50 percent – of the total value of the good. What remains much less well understood is that value chains, including global value chains, exist not only in the goods sectors but also in the services sector itself (Maurer and Tschang 2011). In new business models, services firms, like goods firms, are seeking to go up the value chain and to outsource non-core services functions. This leads to services becoming “embodied” not only in goods exports but also in final services exports. “Trade in tasks” describes all these phenomena but initial surveys on international sourcing suggest that this trend is not yet as well developed in services as it has been in the manufacturing sector (Maurer and Tschang 2011).

There is now innovative work being undertaken to look at how services firms organize, what determines their global distribution of work (offshoring), what the implications are and how trade flows take place. This area is much more challenging than the global value chain approaches to manufacturing due to the paucity and inconsistency of services data collection. Methods of measurement, moreover, especially for services delivered through modes 3 and 4, are complex. Such data collection and methodology issues lead to an understatement of the importance of services in supply chain development.

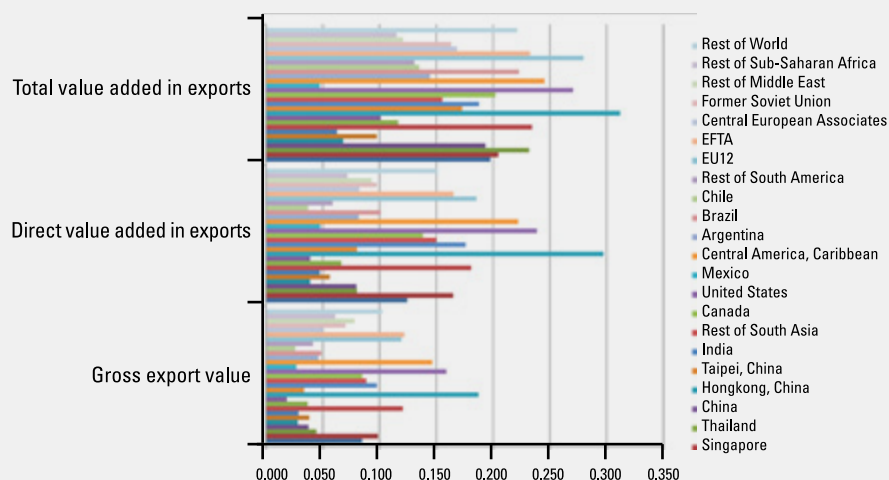
In the case of the US, growth in intra-firm trade has been a major contributor to exports of services. The US has recorded an increasing share of trade between US-based firms and their majority-owned foreign affiliates, growing from 22 percent to 28 percent a decade later in 2007 (Figure 12) (Maurer and Tschang 2011).



Source: Maurer and Tschang (2011)

Taking account of intermediate services inputs to goods trade would nearly double the services share of global trade. Figure 13 shows services as closer to 50 percent of world trade, and that is still without taking into account the dominant component of international services transactions, namely commercial presence or mode 3 (Christen, Francois and Hoekman 2011).

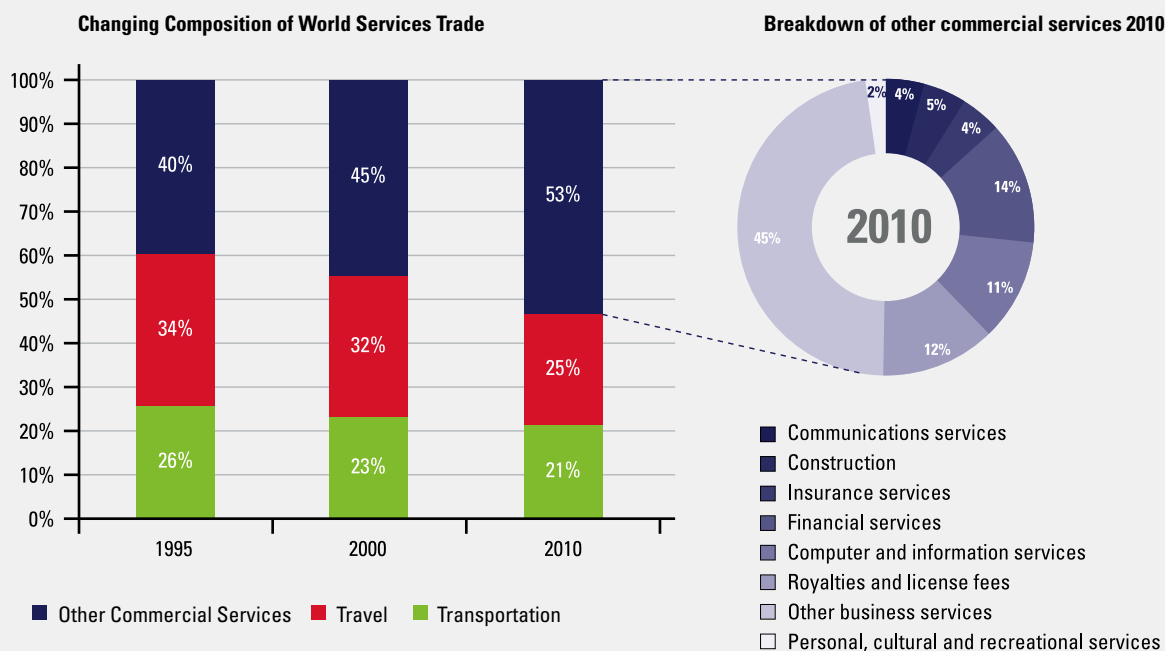
**Figure 13** Adding Indirect Production and Trade in Services



Source: Christen, Francois and Hoekman (2011)

The development of services supply chains has resulted in the composition of services exports undergoing significant change. "Other commercial services" are becoming more important than the traditional "travel" and "transport" components of world services trade. The biggest contributors to the recent growth have been the knowledge-intensive business services such as telecommunications, computer and IT services, R&D services, financial services, legal, accountancy, management consultancy services, architecture, engineering and other technical and professional services, as well as market research, advertising, media, energy and environmental services (Figure 14).

**Figure 14** Changing Composition of World Services Trade



Source: World Trade Organization, Time Series on International Trade, adapted from Saez 2011

There may also be potential benefits in using a value-added approach to measure international services trade flows. As international merchandise trade statistics are established from customs documents at the border, they assign the full gross value of an international transaction to the immediate economy of origin. But the economy of origin may only be the last assembler in a long supply chain, and it may not have created nor benefited from the full value-add included in the final good. The value-add necessary to produce the product may be spread across several economies forming the supply chain, as illustrated in Table 2 for the iPhone.

**n2**  
**Table** 2009 US Trade Balance in iPhones (US\$m)

	China	Japan	Korea, Rep. of	Germany	Rest of world	World
<b>Traditional measure</b>	-1,901.2	0	0	0	0	-1,901.2
<b>Value added measure</b>	-73.5	-684.8	-259.4	-340.7	-542.8	-1,901.2

Source: Miroudot, S., *Global Forum on Trade Statistics*, 2-4 April 2011, from Maurer and Tschang (2011)

One big question is whether there is also a need for a value-added approach to measuring trade in services developments, and if so, how to achieve it, given the paucity of bilateral services trade data.

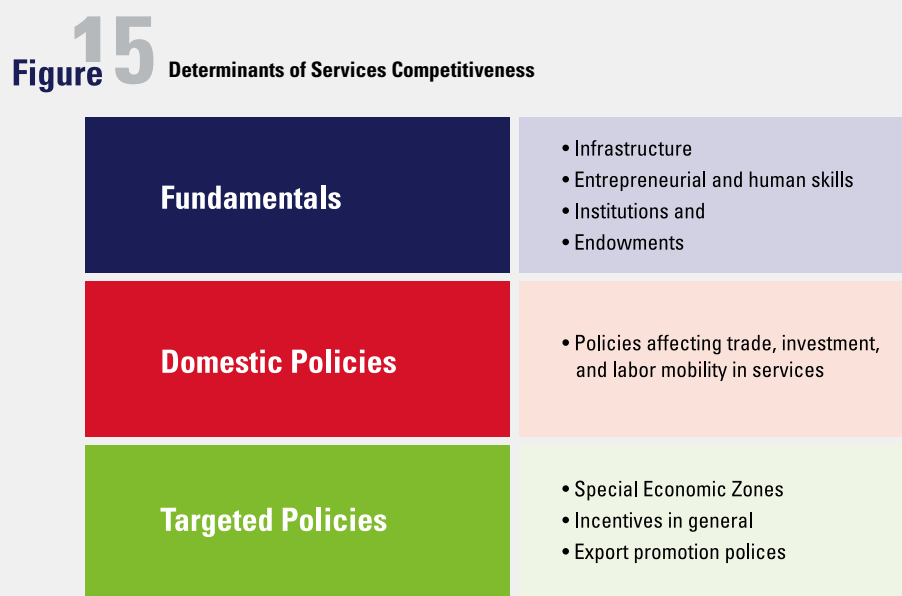




Trade barriers can have both rent-creating and cost-creating effects. Rent-creating effects arise from limiting market entry while other kinds of barriers are cost-creating in their impact (for example regulatory compliance costs). Removing cost-escalating barriers can generate relatively larger welfare gains and benefit both domestic and foreign producers. In goods trade, the barriers tend to be rent-creating, while in services trade, many more barriers are cost-escalating. Therefore, services trade reforms oriented to cutting costs should have a positive impact of a genuinely “win-win” nature for both domestic and foreign services providers. A number of empirical studies confirm that the primary feature of services trade liberalization is a rise in the level of domestic productivity. Hence, there is a strong linkage between the degree of openness to trade and investment in the services sector, and the achievement of international competitiveness in services. As a result, economies with more open regimes for services are more likely to do well in global services markets.

#### *Determinants of Services Competitiveness*

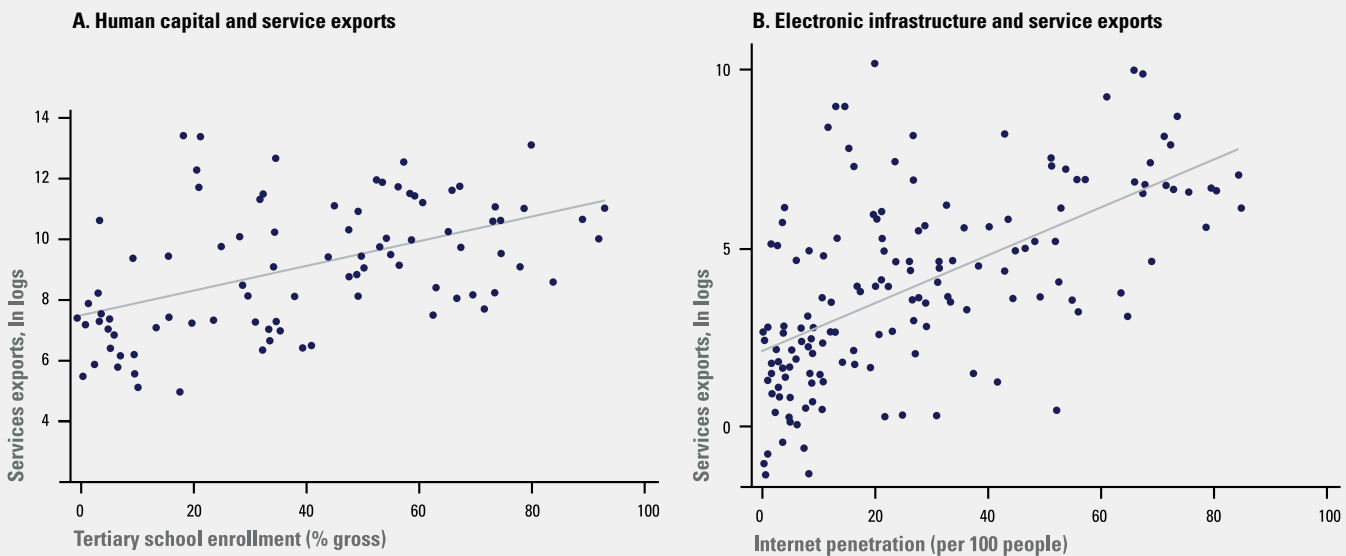
Developing economies are adopting a variety of strategies for growing their services sector. Figure 15 illustrates the main factors identified as determinants of services competitiveness.



Source: Saez 2011

There is strong evidence of a correlation between human capital (as measured by tertiary school enrolments) and services exports and between electronic infrastructure (as measured by internet penetration) and services exports (Figure 16).

**Figure 16** The Importance of Human Capital and Digital Infrastructure



Source: Saez 2011

Human resource inputs are overwhelmingly important for certain businesses, such as IT service firms. Decisions on where to source work, and at what level of value-add, depend on a firm's access to trained workers, the quality of training, and the associated wage structures.

**Figure 17** Skills are Relevant to Competitiveness in Services

Economy	Salary of Graduates US\$ p.a.	Total Number of Graduates p.a.	Offshore location: India offers the best package USD p.a. (ongoing costs), per employee					
			India		Philippines	Malaysia	China	Russia
India	2400	2,000,000	People <ul style="list-style-type: none"><li>• Agent and management costs</li><li>• Recruitment and training</li></ul>	5,300	5,500	11,000	7,700	14,450
China	2000	950,000		211	232	232	232	580
Philippines	2900	380,000	Infrastructure <ul style="list-style-type: none"><li>• ICT and utility</li><li>• Facility</li></ul>	992	1,476	1,584	1,584	1,000
Mexico	1400	137,600		1,520	1,605	1,900	1,900	2,600
Ireland	19500	43,200	Tax <ul style="list-style-type: none"><li>• Tax</li></ul>	0	0	0	0	3,350
Malaysia	7200	30,000						
Singapore	16500	12,500						
Total				8.023	8.813	14.716	11.416	21.980

Source: Chanda and Pasadilla (2011)

While there is some focus on developing services exports, the openness of the regime including trade, investment (inwards and outwards) and labor mobility in services are all important for the sector's own performance and for the rest of the economy. This is a very significant comment that has also been stressed by ABAC. While there remain concerns in some economies that a more open services regime may lead to significant adjustments in domestic services providers' structure of activities, the consequences of greater openness for the competitiveness of the sector as a whole are important. Services providers are themselves significant users of other services, for example, tourism and air transport, or telecoms services used in business processing. A more open sector also offers more variety to users of services. Furthermore, a more competitive services sector contributes to productivity growth elsewhere in the economy. Research is now being done to establish the links between services sector reform and manufacturing sector productivity (McCredie and Findlay 2011).

Another important factor in services sector performance is institutional quality, as measured by the degree of corruption in government processes, the extent of rigidity in employment law, the economic freedom index, the scope for active private sector policy advocacy and their input in policy making. Institutional quality matters because of the support it provides for structural change, the reduction of uncertainty around contracts, as well as the opportunities and costs of setting up new businesses (Saez 2011).

Differences in services competitiveness between economies in all of these dimensions are not static and can evolve depending on the policy choices an economy makes.

Regulatory simplicity and efficiency, including predictability and coherence, are also very important determinants of services competitiveness, as is the support for services innovation and Small and Medium-Sized Enterprises (SMEs) (McCredie and Findlay 2011).

As many of the constraints to services trade are behind-the-border measures, the regulatory reform agenda is important not only for domestic services efficiency but also for services trade. Regulatory reforms for services have direct effects on:

- markets and trade,
- access and entry of new services providers (both domestic and foreign),
- the scope of business operations,
- the sector's overall growth and performance,
- manufacturing firms that rely heavily on services.

Eventually, regulatory reform agenda is also a trade agenda item. It is hard to disentangle one from the other, especially in the case of the services sector.

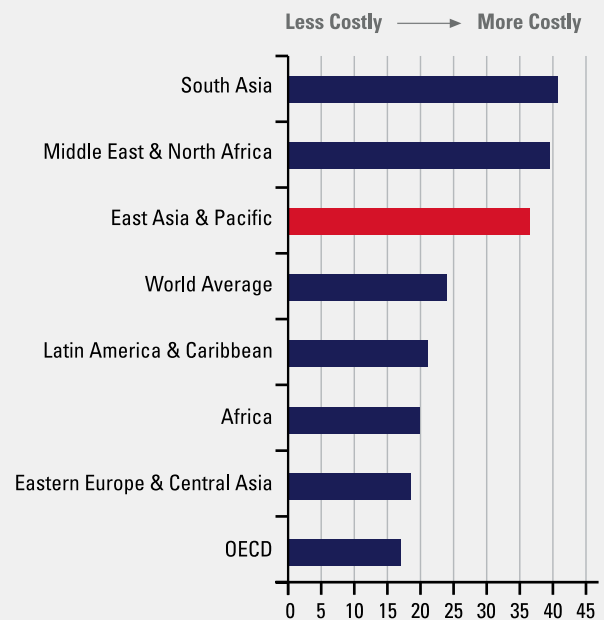
Most services firms are "multi-modal" and thrive best in a regulatory environment that allows maximum flexibility to switch between modes. Face-to-face contact between a services provider and a client is consistently described by services firms as essential, even for firms operating chiefly via mode 1 or mode 3

(cross-border trade and commercial presence respectively). This means that ease of operating via mode 4 (movement of natural persons) always matters for international business in services.

#### *Impact of Regulatory Barriers*

Both OECD and the World Bank are currently compiling their Services Trade Restrictiveness Indices, which are expected to become available during the first half of 2012. Meanwhile some initial aggregate data is presented in Figure 18. This chart shows that services policies in "East Asia and the Pacific" are relatively restrictive compared with other regions and even compared to the world average. Everywhere in the world, professional services are by far the most restricted.

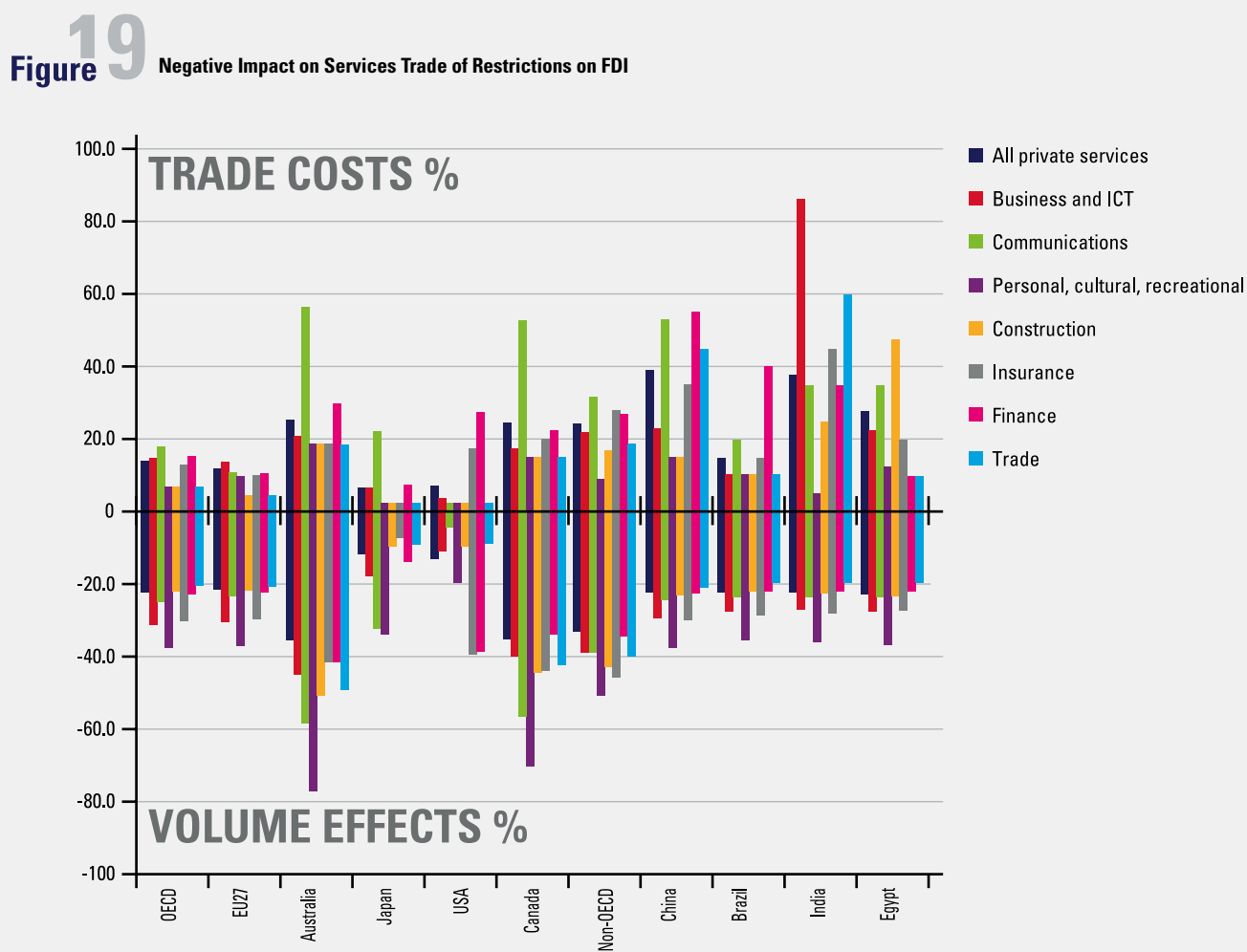
**Figure 18** Costliness of Policies Affecting Services Trade



Source: Gootiiz and Mattoo (2009)

The World Bank data provides some breakdown into financial services, telecommunications, maritime transport, retail and professional services. In all of these services, "East Asia and the Pacific" is more restrictive than the world average. Everywhere in the world, professional services are by far the most restricted.

Figure 19 shows the impact of restrictions on FDI on different services sectors. It shows that restrictions implies positive trade costs and decreased trade volume.



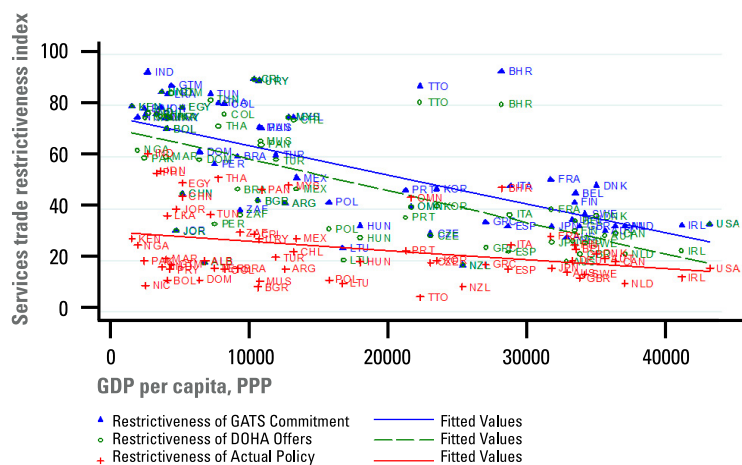
Source: Christen, Francois and Hoekman 2011

*Multilateral Trading System*

In terms of the multilateral trading regime, the World Bank's Services Trade Restrictiveness Index shows relatively little progress in bound commitments in services. Furthermore the proposed DDA improvements over Uruguay Round commitments make little headway in reducing the "water" between bound and applied policies on services (Mamdouh 2011, referring to Borchert, Gootiiz and Mattoo, 2010). This leaves businesses in a state of uncertainty when considering investments overseas. Figure 20 shows the applied regime (in red), the GATS commitments (in blue), and the current DDA offers (in green).

It is clear from the Figure that the offered reductions in bound levels of intervention, which the DDA might achieve, deliver no new actual liberalization in the marketplace. Even in OECD economies, where the Doha offers do cut into the "water"<sup>3</sup>, the offers, if reaped, would not provide any new market access opportunities.

**Figure 20** Uruguay Round Commitments, DDA Offers and Actual Policies

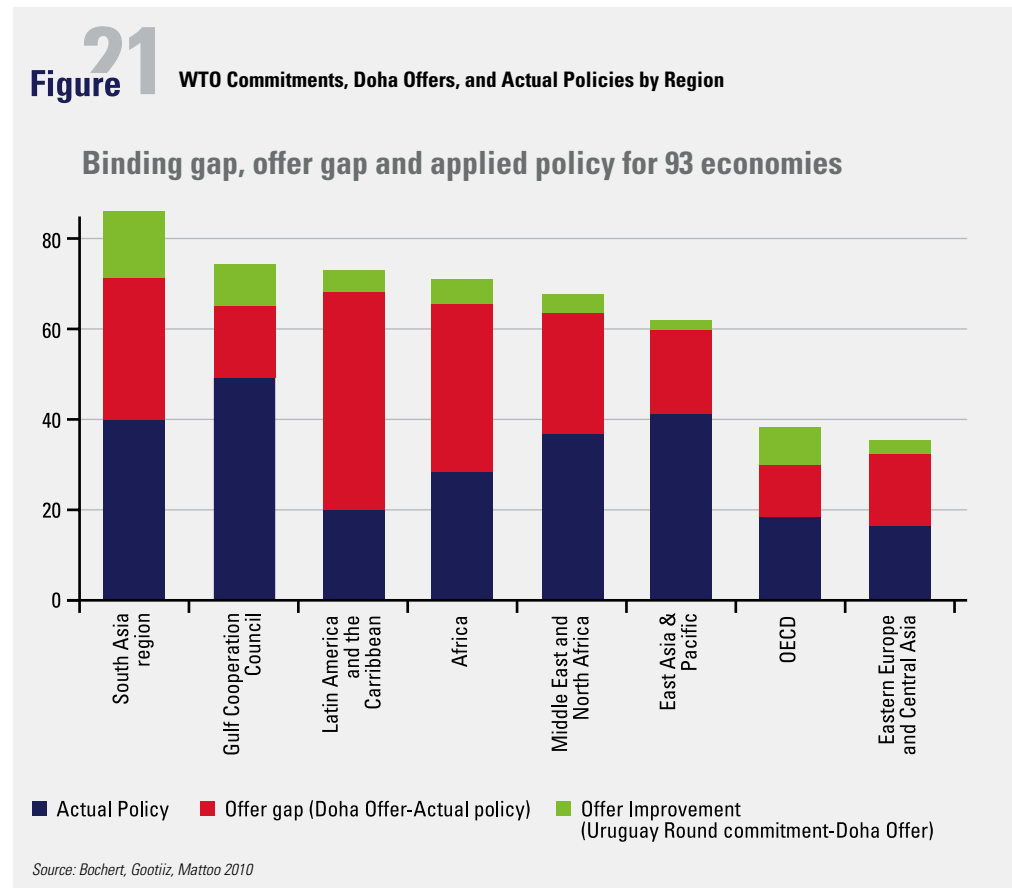


STRI for 61 economies, excluding Qatar and 31 economies that did not submit offers

Source: Borchert, Gootiiz and Mattoo, 2010 in Mamdouh (2011)

<sup>3</sup> Referring to the gap between actual or current levels of protection and bound commitments.

Figure 21 presents the same information in a slightly different format, showing quite clearly that the current services offers on the table in the DDA will not deliver new market openings.



If services sector reform involves a win-win situation that brings positive impact for all economies, as is argued in this report, why has there been so little progress in the negotiations? Some of the contributing factors are:

- a relative lack of information among governments on the services economy and their own commercial interests in services;
- an absence of coordinated domestic strategies for services development;
- consequent policy uncertainty and defensiveness, particularly given the implications of reform for the operation of domestic regulation and its effectiveness;
- a lack of domestic impetus, therefore, for regulatory reform;
- inadequate private sector stakeholder consultation;
- the absence of international support for domestic regulatory transparency institution building.

The nature of a multilateral “round” and the WTO concept of a “single undertaking” are also seen as having negative impact on the prospects for the services sector, given that the negotiating focus to date in the DDA has been on agriculture and manufacturing. Aspects of the GATS and the GATS negotiating modalities are also identified as problematic, for example:

- the technical complexity of GATS schedules;
- the unintelligibility of the GATS itself and its disconnect from business reality;
- uncertainties in GATS interpretation given the relative absence of dispute settlement case law;
- the absence of any “formula” by which to quantify progress in reducing barriers in the services sector.

The unduly mercantilist “request-offer” nature of the negotiations and the public opacity of services offers are also contributors to the lack of progress in this area so vital to development (Drake-Brockman 2011). The fact that “behind-the-border” services barriers relate to core aspects of

domestic legislation leads to additional problems, intensified by the absence of regulators from the negotiating table and the lack of global support for international regulatory dialogue.

This situation has immediate implications for businesses which consider the content and coverage of the current GATS negotiations increasingly outdated. The DDA excluded key services-related topics such as investment, competition policy and mutual recognition of regulatory authorities. It is increasingly important for services negotiations to cover a range of “21st century” issues, including global supply chain interoperability. When the OECD and the World Bank’s Services Trade Restrictiveness Indices are released in 2012, they can be expected to trigger more widespread business advocacy for an intensified push on services trade reform.

### *Plurilateral Approach*

One solution to this is that a plurilateral approach might be more effective, noting that less than a third of WTO members have in any case submitted a DDA services offer (Stephenson and Robert 2011; Drake-Brockman 2011). This idea has been articulated in other reports, including an earlier World Bank Policy Research Paper<sup>3</sup>, the Warwick Commission Report on the Future of the WTO<sup>4</sup>, and the work of the Australian Services Roundtable<sup>5</sup>.

Continued negotiations on services are already mandated as part of the built-in agenda from the Uruguay Round, and political will to do so can recommence them. The ITA has been cited as an example of a “critical mass” plurilateral model, where benefits are extended on an MFN basis. Other models cited include the WTO Agreement on Government Procurement (GPA), under which the benefits are applied on a reciprocal basis only to the signatories; and outside the WTO context, the Anti-Counterfeiting Trade Agreement (ACTA).

In an inclusive MFN-based approach, market forces might provide the natural incentives for economies that have initially opted out of a plurilateral agreement, to eventually come on board. In the case of services, where reform of inefficient regulations improves productivity, being a party to a plurilateral agreement will help an economy compete effectively for inward foreign investment in services (Drake-Brockman 2011). By way of example in the telecoms industry, research has shown that economies that have not signed the WTO Basic Telecommunications Reference Paper have failed to attract telecoms investment<sup>6</sup>.

Another reason for considering the MFN approach is that there are practical difficulties inherent in implementing reform of behind-the-border services regulation in any manner, other than using the MFN-based approach. This has been the experience in implementing Free Trade Agreements (FTAs) (Stephenson and Robert 2011).

Therefore, a plurilateral negotiation that attracted a “critical mass” of major players could be expected to place economic pressure on non-participants to cooperate or face significant competitive disadvantages. To support the application of the principle of MFN in this arrangement, any such “critical mass” negotiations should be within the WTO framework. Full participation of APEC members would likely be sufficient, as it was in the case of the ITA, to generate a broad “critical mass” of WTO members. Participation on the part of the European Union (EU) would be essential given the weight of EU-based firms in services trade (Table 3).

<sup>3</sup> Referring to the gap between actual or current levels of protection and bound commitments. <sup>4</sup> Gootiiz, B. and Mattoo, A. (2009) <sup>5</sup> The Warwick Commission (2009)

<sup>6</sup> Australian Services Roundtable (2008) <sup>7</sup> Economies with substantial liberalizing WTO telecoms commitments have experienced a more rapid rate of growth in telecoms sector revenues (and consumer benefits) than those without such commitments. In low-income economies in Europe and Central Asia, telecoms sector revenue in economies with liberalizing WTO commitments grew from 1.5 percent to more than 4 percent of GDP in the years following the WTO Agreement on Telecoms (1997-2002), while the Figure was essentially flat during the same period for economies that made no liberalizing commitments. Telecoms investment and usage has surged in economies that have liberalized this industry, and the costs of both local and long distance calls have fallen dramatically. World Bank statistics underscore the correlation between availability of telecoms services – and standards of living. For every 10 percentage-point increase in the penetration of broadband services, there is a 1.3 percentage-point increase in economic growth. Source: Global Services Coalition (2010)



### Table 3 Global Trade in Commercial Services 2010

Rank	Exporters	%Share	Rank	Importers	%Share
1	United States	14.1	1	United States	10.2
2	Germany	6.3	2	Germany	7.3
3	United Kingdom	6.2	3	China	5.5
4	China	4.6	4	United Kingdom	4.5
5	France	3.8	5	Japan	4.4
6	Japan	3.8	6	France	3.6
7	Spain	3.3	7	India	3.3
8	Singapore	3.0	8	Netherlands	3.1
9	Netherlands	3.0	9	Italy	3.1
10	India	3.0	10	Ireland	3.0
11	Hong Kong, China	2.9	11	Singapore	2.7

Source: Hong Kong Coalition of Services Industries, "Services Sector in Hong Kong", Statistical Card 2011, Hong Kong General Chamber of Commerce, September 2011

In thinking about new approaches to trade negotiations, modalities should be structured to avoid the difficulties of past "request-offer" negotiations. This might require a simple multi-modal services accord, for example a standstill and rollback-type deal, without individual schedules, or with negative, if any, listings. It would be important to cover all services, as well as to permit internal trade-offs and to regain widespread business confidence.

In seeking to broaden the negotiating content, it would be important to apply the many lessons learned from the last decade on bilateral services trade and investment negotiations. Bilateral efforts to liberalize services have used various types of architecture. Some have followed the GATS architecture but others have departed from it significantly through recourse to the powerful negative list approach and use of "ratchet mechanisms". Others are explicitly "living agreements" that cater for continuous content enhancement through ongoing negotiations, accompanied by regulatory benchmarking and stakeholder consultation. These principles of continuing reform are important to adopt (Drake-Brockman 2011 and Stephenson and Robert 2011).

International regulatory benchmarking and dialogue, both on a regional and global basis, are critical to improving the governance of services trade. The GATS does not interfere with the domestic regulatory agenda nor does it provide much guidance either on how to pursue a sound regulatory approach. The development of a set of regulatory services sector guidelines might be a feasible option to provide consistency in how services are regulated (Mamdouh 2011). This could take the form of a generic cross-sectoral "Services Reference Paper", modeled on the WTO Telecoms Reference Paper, setting out pro-competitive principles for services regulation. This could be accompanied by global capacity-building support for intensified domestic attention to regulatory audit, and regulatory institution building (Drake-Brockman 2011).

In PECC's annual survey of over 400 opinion leaders in the Asia-Pacific, 72 percent of all respondents agreed that "APEC members should take the lead in promoting a plurilateral agreement on services", while only 5 percent disagreed; 70 percent of government officials responded positively and 76 percent of business leaders also did so. In every region, a large majority responded in favor of

services plurilaterals. Support was strongest in South America (81 percent) followed by Southeast Asia (73 percent) with Oceania and North East Asia both at 71 percent and North America the lowest at 65 percent<sup>8</sup>.

### *Regional Arrangements*

Since the early 1990s, regional trade arrangements (RTAs) covering trade in services have proliferated, with 95 RTAs covering services notified to the WTO as of May 2011. Although RTAs sometimes provide a deeper level of market opening and greater transparency for services commitments, on the whole RTAs weaken the governance function of the multilateral trading system by diverting attention away from the GATS, providing parallel and competing architecture and developing new alternative rules and disciplines (Stephenson and Robert 2011). Hence, it would be valuable for the WTO to have strengthened its oversight of the diverse universe of RTAs. The WTO should also exercise greater flexibility in incorporating some of the innovative elements in RTAs into the GATS, perhaps via plurilateral agreements that can push the envelope of services liberalization further among smaller groups of like-minded economies.

One agreement currently being negotiated is the Trans-Pacific Partnership (TPP) that seeks to address “ambitious 21st century” benchmarks for “post Doha” services negotiations in the WTO. For regional businesses to see it as commercially relevant to meeting the business challenges of a fast globalizing services economy and genuinely helpful in building a seamless, integrated regional business environment, the TPP would need to break significant new ground. The TPP should have more GATS-plus features than earlier FTAs. This would mean having more GATS-plus features than the NAFTA-styled template, which set a classic benchmark in the region for “high-standard” bilateral services governance in the 20th century.

Given the changes taking place in services supply chains discussed earlier in this report, businesses require:

- new disciplines in future trade agreements on standards and interoperability for cross-border data-transfer and data-storage;
- clear rules on the role of state-owned and state-linked enterprises in competitive markets; improving the conditions for commercial presence;
- avoidance of discriminatory and unreasonable localization requirements on global business activities;
- reduction of choke points in supply chain connectivity through trade facilitation and more efficient logistics and other services;
- improvements in rules on the movement of services business people, including professional recognition.

Other issues mentioned include the need for regulatory coherence, best practice principles, facilitation of SME engagement in services innovation and export and disciplines on services sector subsidies (Vastine 2011).

Another regional agreement under which innovative approaches are being used to progress services negotiations is ASEAN’s Economy Community Blueprint. This involves consecutive rounds of negotiations being held every two years until 2015. The negotiations are designed to achieve the following goals:

- commitments in a minimum of ten new sub-sectors by 2008, 15 by 2010, 20 in 2012, 20 in 2014 and another 7 in 2015
- no restrictions in modes 1 and 2, other than for bona fide regulatory reasons such as public safety.

<sup>8</sup> PECC (2011)

- Mode 3 targets for lifting of foreign equity limits (to be phased in); 70 percent foreign equity participation to be achieved by 2013 for priority sectors (such as logistics) and by 2015 for other sectors. Other mode 3 market access limitations to be progressively removed by 2015.
- liberalization of national treatment restrictions under mode 3, as well as liberalization of horizontal limitations on mode 4. An ASEAN Agreement on Movement of Natural Persons is currently under negotiation.

The ASEAN agenda is a bold one. Services sector liberalization, while an important driver of regional economic integration, is not a simple task in ASEAN, as in many other parts of the world. It is still unfamiliar territory compared with goods trade liberalization and inherently very different, governed by a myriad of domestic rules and regulations (some of which are of a constitutional nature) involving a diverse range of sectors and numerous government ministries and agencies (Tan Tai Hiong 2011).

Given the impediments to progress in services reform, circuit breakers are required. An important foundational tool for progress could be the adoption of a cross-sectoral “Services Reference Paper” (modeled after the WTO Telecoms Reference Paper) setting out pro-competitive principles for services regulation, accompanied by capacity-building support for intensified domestic attention to regulatory audit and institution building. ASEAN could take a lead position for the achievement of its own goals in the development of such a paper.

The European Union’s (EU) recent experience in implementing the EU Directive on Services among its 27 member states is also relevant and important. The first mutual evaluation of the EU Single Market for Services is underway in 2011 and 2012. Like in other parts of the world, within the EU, trade barriers hit services harder than goods. And SMEs, in particular micro-enterprises (comprising 95 percent of all services providers in the EU), are hit harder than larger firms. Many of the barriers arise from administrative burdens, legal uncertainty associated with cross-border activity and the lack of mutual trust among member states. Even within as deeply integrated a region as the EU, the challenge of creating a single market is a “never-ending story” given the rapidity of technological developments and changes in business models (Arkell 2011).

*For Research*

Ten years ago, there was relatively little information available on international trade in services. Over the last decade, international institutions, along with individual researchers, have pushed the envelope forward significantly, stimulating research interest in services trade in many new quarters. Research in this area has mushroomed, including that commissioned by various governments and most recently by the APEC PSU. New research results are now coming on-stream, and all these have extended and enriched the literature at a remarkable rate.

Nevertheless, there are still many unanswered questions. There remains an imperfect understanding of even the most basic issues, such as the share of services in GDP. Some economies continue to exclude construction, energy and other utilities from the published aggregate for services, leading to difficulties in comparing one set of national aggregate statistics with another and leading to underestimation of the size of the global and regional services economy. Up to date GTAP<sup>9</sup> data on services are not available for all Asia-Pacific economies. Modeling techniques are imperfect and under-practiced.

The implementation of the 6th edition of the Balance of Payments (BMP6) and the 2010 revision of the Manual for Statistics on International Trade in Services (MSITS) will generate many questions that may need public explanation and may lead to further research and analysis. (Maurer and Tschang 2011) One new feature is the stricter application of the ownership principle, which sees certain items reclassified from trade in goods to trade in services and vice versa. For example, goods sent abroad for processing, without any change in ownership of the inputs, are now reclassified as "Manufacturing Services on physical inputs owned by others" (this includes oil refining, liquefaction of natural gas, assembly of clothing and electronics, assembly, labeling, and packing). Repair and Maintenance costs are also reclassified as services. In contrast, "merchanting" (i.e. the purchase and onward resale of goods, where an ownership change takes place, although the goods never enter the economy of the merchant) is now reclassified as trade in goods.

The research community and the business community alike continue to attach high priority to improving national collections of services sector statistics. The implementation of BPM6 is expected to highlight some statistical problems for certain APEC members. It is also expected to require some public explanation and capacity-building activities to implement properly.

When it comes to measuring the barriers to trade, the World Bank and the OECD Services Trade Restrictiveness Indices will also generate another big new policy research agenda.

Debate is still active on key questions in relation to services productivity. There is evidence, in different APEC economies, of both higher than average and lower than average labor productivity, and total factor productivity, in services sector activities as compared to the goods sectors. More work also needs to be done to collect data on relative wage rates in services activities, for both male and female workers. And the jury is still out on the impact of targeted policies for growth in services sector activities, as the World Bank research on this matter remains at best inconclusive.

*For Business*

Several business representatives left the Conference evidently determined to put their weight behind

<sup>9</sup> Global Trade Analysis Project – see [www.gtap.org](http://www.gtap.org)

efforts to lift the profile of services not only in APEC but also in other domestic, regional and global policy contexts. Initial ideas arose on the sidelines of the Conference, leading rapidly afterwards to the commencement of an ABAC project on trade and investment in services.

Several of the business associations at the Conference participate in the Global Services Coalition. This set of industry associations together issued a joint media release after the Conference, making a concerted call for the first time for a services-only negotiating approach. The Global Services Coalition also called on governments to address the following issues:

- improving timeliness and conditions associated with cross-border transfer and storage of data;
- improving the movement of services business people;
- better and clearer rules on the role of state-owned and linked enterprises;
- improving the conditions for commercial presence for foreign companies; and
- developing of a set of principles providing best practice regulation.

Some business representatives took subsequent opportunities, including with the Director-General of the WTO, Mr Pascal Lamy, to raise business advocacy issues arising from the Conference; in particular, the business community's increasing interest in finding ways to build momentum, following the PECC/ADB I Conference, for a critical mass of support for stand-alone services negotiations.

#### *For Policy-makers*

Government representatives left the Conference with no doubt that the business community, in developed and developing APEC economies alike, does understand and care about the WTO, and the GATS and is deeply concerned by the lack of progress in binding government commitments to liberalize services trade and investment. It is evident that the business community does not attach much commercial value to the existing services offers on the table in the DDA. Nevertheless, the business community would prefer at least these offers to be adopted as soon as possible, even though they will not be enough to excite much business interest. More progress will clearly be needed. The government representatives also heard business messages to the effect that the progress made to date in the context of FTAs is similarly insufficient. It is clear that very high standards are expected of future new agreements, including the TPP.

Given that the business community is expressing strong interest in finding new approaches to deal with global and regional services trade and investment governance, the Conference generated active discussion on a number of new approaches that are worthy of further examination at policy level. PECC and ADB I had the opportunity to report on the Conference discussions to the APEC Group on Services, the APEC Economic Committee, the APEC Committee on Trade and Investment, and the Senior Officials Meeting during the APEC cluster of meetings in San Francisco in September 2011. The Task Force also led a concurrent session on Trade in Services at the PECC General Meeting in Washington in September 2011. The proceedings of this session can be found at [www.pecc.org](http://www.pecc.org).

There is widespread support among all groups of participants for the idea of continued joint discussion to operationalize the concept, at least informally, of a regional "services knowledge platform". The idea is for a forum through which the business and policy communities could continue to interact with the wider knowledge community. This will enhance understanding of the services economy and the contribution of services trade and investment to growth, development and poverty reduction.

The proposals that were put forward during the Conference stimulated engaging discussions. They were considered by the Task Force to deserve further sustained policy attention. These proposals clustered around two big ideas for improving regional and global governance in the services sector, both of which have implications for APEC.

#### *Regulatory Principles for Services*

The first big idea is that governments should develop a set of regulatory principles for the services sector. One specific suggestion was for development of a generic cross-sectoral “Services Reference Paper”, setting out pro-competitive principles that might have application to all services.

There are many potential sources from which such work may draw inspiration, including:

- the WTO Telecommunications Reference Paper;
- the OECD/APEC Integrated Checklist on Regulatory Reform;
- the Insurance Principles developed by the services business community during the GATS negotiations on Financial Services;
- the work over many years of the APEC Group on Services.

Regulatory regimes for network services might differ in some aspects from regulatory principles applicable to natural monopolies or to services affected by information asymmetries. However, with some economic analysis and some conceptual imagination, it should not be difficult to arrive at a useful set of principles with relevance across the services sector economy.

APEC should initiate inter-governmental discussion, drawing in their discussion on inputs not only from policymakers and regulators, but also from the knowledge community, on principles for all-of-services regulation, with a view to generating global interest in developing such principles. It was suggested that APEC should experiment with new ways of bringing services regulators together with trade officials, both sector-by-sector and at whole-of-services level. This will facilitate sharing of regulatory experience, raising awareness of regulatory incoherence and promoting discussions on options for improving regional practice, as well as encourage domestic regulatory audit and benchmarking of progress.

To build regional momentum for this idea as well as to generate interest beyond the region, it would be valuable to further develop the idea of a “services knowledge platform”. This may be done by building on the foundations of this inaugural Conference to seek broader cooperation and input from the relevant regional institutions. APEC could lead this process, as the task is consistent with its own goals and systems. However, as this Conference has demonstrated, connections with ASEAN, the EU and throughout the Americas are critical. Some commentators<sup>10</sup> have recently suggested that the G20 might provide a forum in which this kind of inter-institutional cooperation could be given a more formal mandate.

There was also evident support for the suggestion that governments should consider designing practical regulatory mechanisms, in consultation with the business community, to increase recipient economy confidence specifically on mode 4.

#### *Stand-alone Negotiations on Services*

The second big idea is that governments might have a higher degree of inter-governmental

<sup>10</sup> Hoekman and Messerlin (2011)

negotiating success than has been achieved to date, if they were to pursue services negotiations within a new set of arrangements. There are three components to this structure – stand-alone, plurilateral and new formats for commitments.

First, services negotiations could be organized on a stand-alone basis, i.e. independently of the additional complexities of negotiations on agricultural and manufactured goods. This option is already open to WTO members. Stand-alone services negotiations are mandated in the Uruguay Round built-in agenda and these could and should be recommenced, irrespective of developments in the DDA. A number of economies in the region have significant experience in this: under the ASEAN Economic Community Blueprint, consecutive rounds of negotiations take place every two years until 2015 which are designed to achieve commitments in a minimum of 10 new sub-sectors by 2008, 15 by 2010, 20 in 2012, 20 in 2014 and another 7 in 2015.

Second, given that less than one third of the WTO members have made services offers in the DDA, new negotiations could commence plurilaterally. In contemplating the possibility of services plurilaterals, Conference participants expressed their preference for a “critical mass” MFN-based approach. They also attach importance to ensuring that the resulting regulatory reforms are implemented simply and efficiently, without introducing new distortions.

Third, as the “request-offer” process has effectively failed, consideration needs to be given to the alternative possibility of a new multi-modal framework accord, such as a standstill and rollback-type deal (with or without individual schedules of commitments, on either a positive, negative or hybrid list basis).

Progress will eventually depend on the effective use of the burgeoning body of research on services policy and on close consultation with the services business community. There will be widespread interest in exploring ways in which services negotiations might benefit from the insights from soon-to-be-published works on the services sector trade restrictiveness measurement. These include works by the OECD and the World Bank, and also recent work commissioned by the APEC PSU. ABAC’s work on services, as well as that of the Global Services Coalition, will also be instructive.

#### *APEC Leadership Role*

APEC was seen as uniquely well-placed to build a “critical mass” of political will for stand-alone services plurilaterals, just as it did in the case of the ITA. From the outset the intention should be to extend the thinking beyond APEC. The wider co-operation proposed above in regulatory capacity building helps draw in a wider set of participants.

It is the hope of the task force that APEC members will take heed of these two considered recommendations and take the opportunity that APEC as an organization provides, to incubate these new ideas.

There are different ideas on the form such a stand-alone services trade discussion should take. A study group in APEC could be created to better understand the ramifications of a services agreement and the incentives for economies.

APEC must have concrete outcomes visible to businesses if it is to sustain regional business interest. A services trade initiative from APEC would achieve this objective, especially if it is linked, as ABAC has suggested, to dealing with the choke points in regional supply chain operations. The initiative should bring new depth and energy to APEC work on regulatory cooperation, including specifically to develop principles for regulatory coherence in services.

Meanwhile, APEC should look beyond the DDA and open the way forward for considering fresh negotiating processes and for exercising flexibility with respect to negotiating modalities, specifically in services. This is a way for APEC to show its leadership on the global issues that have most impact on creating jobs for future generations.

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All other sources referred to in this Report are papers presented by contributors to the Conference in Hong Kong in June 2011. The speakers programme is attached and the full set of the papers and presentations is available at <http://www.pecc.org/component/eventlist/details/194-pecc-adbi-services-trade-new-approaches-for-the-21st-century> and <http://www.adbi.org/event/4375.adbi-pecc.regional.trade.investment.services/events.resources.php?TypeID=21>







In conjunction with the Hong Kong General Chamber of Commerce

**SERVICES TRADE: NEW APPROACHES FOR THE 21ST CENTURY**

Hosted by the Institute of Global Economics and Finance and  
the Economic Research Centre of the Hong Kong Institute of Asia Pacific Studies, CUHK

1 June 2011	American Club, Exchange Square 2, Central
2-3 June 2011	Cho Yiu Hall G/F University Administration Building, CUHK Sha Tin, New Territories, Hong Kong

**1 June 2011, American Club, Exchange Square 2, Central**

**1800 Registration for Welcoming Reception**

**1830 Welcoming Remarks**

**Anthony J. L. Nightingale** (Managing Director, Jardine Matheson Ltd, Chair of APEC Business Advisory Council Action Plan and Advocacy Working Group)

**1840 Panel of speakers (Moderator: Alex Fong, CEO, HKGCC)**

**Hamid Mamdouh** (Director, Trade in Services Division, WTO Secretariat)

**Kaaren Koomen** (Government Relations, IBM Australia and President, Australian Services Roundtable)

**Tan Tai Hiong** (Services and Investment Division, ASEAN Secretariat)

**Dale Andrew** (Head of Trade Policy Linkages and Services Division, OECD Secretariat)

**Stewart Forbes** (Executive Director, Malaysian International Chamber of Commerce and Coalition of Services Industries)

**Ta-Chung (Jack) Chia** (Secretary General, Taiwan Coalition of Services Industries)

**1945 Vote of thanks and Commencement of Reception**

**Bernard Pouliot** (Chairman and CEO Quam Ltd, Director, Pacific Basin Economic Council (PBEC))

**0830-0900 Registration**

**0900-0930 Official Opening**

Chair	<b>Sung Yun-wing</b>	Associate Director, Hong Kong Institute of Asia Pacific Studies, CUHK, and Chair, Hong Kong PECC
Opening Address	<b>Sir James Mirrlees</b>	1996 Nobel Laureate in Economic Sciences, Distinguished Professor-at-Large and Master, Morningside College, CUHK
	<b>Charles E. Morrison</b>	President, East-West Center and International Co-Chair, PECC
	<b>Masahiro Kawai</b>	Dean, Asian Development Bank Institute
	<b>Maria Kwan</b>	Director-General, Hong Kong Trade and Industry Department

**0930-1115 Session 1 Theme 1: Behind the Border: Enhancing the Competitiveness of Services**

Chair	<b>Masahiro Kawai</b>	Asian Development Bank Institute
Presentation 1	<i>An Explanatory Framework for Measuring Services Value-added</i>	
	<b>Andreas Maurer</b>	World Trade Organization
	<b>Ted Tschang</b>	Lee Kong Chian School of Business, Singapore Management University
Discussant	<b>Julian Arkell</b>	International Trade and Services Policy
Presentation 2	<i>Determinants of Competitiveness and Factors affecting Productivity in Services</i>	
	<b>Andrew McCredie</b>	Australian Services Roundtable
	<b>Christopher Findlay</b>	University of Adelaide
Discussant	<b>Moonjoong Tcha</b>	Korean Development Institute
Presentation 3	<i>Benchmarking Competitiveness in Services</i>	
	<b>Sebastian Saez</b>	World Bank
Discussant	<b>Jane Drake-Brockman</b>	JDB Solutions

**1115-1130 Tea Break**

**1130-1230 Session 2 Theme 1: Behind the Border: Enhancing the Competitiveness of Services (continued)**

Chair	<b>Charles E. Morrison</b>	East-West Center and PECC
Presentation 4	<i>Policy and Regulatory Priorities for Developing Efficient Services Industries</i>	
	<b>Soonhwa Yi</b>	World Bank
Discussant:	<b>Bapak Bachrul Chairi</b>	Ministry of Trade, Jakarta
Presentation 5	<i>China's Services Policy Reform: Pre and Post Global Financial Crisis</i>	
	<b>Ying Fan</b>	University of International Business and Economics, Beijing
Discussant	<b>Fukunari Kimura</b>	Keio University

<b>1245-1415</b>	<b>Luncheon</b>	<b>LuMing Room, Benjamin Franklin Building</b>	
	Luncheon Address	<i>Tool kits for Promoting Services Exports</i>	
		<b>Fred Lam</b>	Hong Kong Trade Development Council
<b>1415-1600</b>	<b>Session 3</b>	<b>Theme 2: At the Border: Realizing the Benefits from Services Liberalization</b>	
	Chair	<b>Sung Yun-wing</b>	Hong Kong Institute of Asia Pacific Studies, CUHK, and Hong Kong PECC
	Presentation 1	<i>The OECD Services Trade Restrictiveness Index: Progress on the Regulatory Database</i>	
		<b>Dale Andrew</b>	Organization for Economic Cooperation and Development
		<b>Massimo Geloso-Grosso</b>	Organization for Economic Cooperation and Development
	Discussant	<b>Christopher Findlay</b>	University of Adelaide
	Presentation 2	<i>Overview of Policy Planning Techniques, Data Constraints and Results to Examine the Benefits of Services Trade and Investment Liberalization</i>	
		<b>Joe Francois</b>	University of Vienna
	Discussant	<b>Hikari Ishido</b>	Chiba University
	Presentation 3	<i>Dissecting the Gains from Services Liberalization for Developing APEC Economies</i>	
		<b>Raymond Atje</b>	Centre for Strategic and International Studies
	Discussant	<b>Fernando Gonzalez-Vigil</b>	Universidad del Pacifico
<b>1600-1615</b>	<b>Tea Break</b>		
<b>1615-1800</b>	<b>Session 4</b>	<b>Theme 2: At the Border: Realizing the Benefits from Services Liberalization (continued)</b>	
	Chair	<b>Ted Tschang</b>	Lee Kong Chian School of Business, Singapore Management University
	Presentation 4	<i>Employment and People-Movement Impacts of Services Trade Liberalization</i>	
		<b>Gloria Pasadilla</b>	Asian Development Bank Institute
		<b>Rupa Chanda</b>	Indian Institute of Management
	Discussant	<b>Deunden Nikomborirak</b>	Thailand Development Research Institute
	Presentation 5	<i>Assessing the International Regulatory Framework applicable to Capital Movement and the Link between Capital Movement and Trade in Services</i>	
		<b>Federico Lupo Pasini</b>	CUTS International
	Discussant	<b>Bryan Mercurio</b>	Faculty of Law, CUHK
		<b>David A. Katz</b>	VISA Worldwide Pte Ltd
	Presentation 6	<i>Mapping the Universe of Services Disciplines in PTAs: The Indian Contribution</i>	
		<b>Biswajit Nag</b>	Indian Institute of Foreign Trade
	Discussant	<b>Rajesh Sharma</b>	School of Law, City University of Hong Kong and Hong Kong WTO Research Institute.

<b>1830</b>	<b>Conference Dinner Meraviglia, No. 10 Science Park West Avenue, Phase 2</b>
Guest speaker	<b>William Fung</b> Deputy Chair, Li and Fung Ltd <b>Nicholas Brooks</b> Chairman, Hong Kong Science and Technology Parks Corporation
Q&A	Led by <b>Bob Vastine</b> CEO, US Coalition of Service Industries

### 3 June 2011, Friday (Cho Yiu Hall, CUHK)

<b>0900-1000</b>	<b>Session 5</b>	<b>Theme 3: Improving the Governance of Services</b>
	Chair	<b>Jesus Seade</b> Lingnan University
	Presentation 1	<i>What is the WTO delivering for Services</i> <b>Hamid Mamdouh</b> World Trade Organization
	Discussant	<b>Bob Vastine</b> US Coalition of Service Industries
	Presentation 2	<i>Developing More Effective Negotiating Modalities and Narrowing the Governance Gap for Services at the WTO</i> <b>Jane Drake-Brockman</b> JDB Solutions
	Discussant	<b>Sergio Marchi</b> International Centre for Trade and Sustainable Development

### 1000-1015 Tea Break

<b>1015-1115</b>	<b>Session 6</b>	<b>Theme 3: Improving the Governance of Services (continued)</b>
	Chair	<b>Chin Leng Lim</b> Faculty of Law, Hong Kong University
	Presentation 3	<i>Evaluating the Contributions of RTAs to Governance of Services Trade</i> <b>Maryse Robert</b> Organization of American States <b>Sherry Stephenson</b> Organization of American States
	Discussant	<b>Shujiro Urata</b> Waseda University
	Presentation 4	<i>The Services Components of TPP and a Possible FTAAP</i> <b>Bob Vastine</b> US Coalition of Service Industries <b>Robert Scollay</b> University of Auckland
	Discussant	<b>Jane Drake-Brockman</b> JDB Solutions

<b>1115-1215</b>	<b>Session 7</b>	<b>Theme 3: Improving the Governance of Services (continued)</b>
	Chair	<b>Terence Chong</b> The Institute of Global Economics and Finance, CUHK
	Presentation 5	<i>Challenges in Building an EU Single Market for Services</i> <b>Julian Arkell</b> International Trade and Services Policy
	Discussant	<b>Pascal Kerneis</b> European Services Forum
	Presentation 6	<i>Challenges in Building the ASEAN Framework Agreement on Services</i> <b>Tan Tai Hiong</b> Services and Investment Division, ASEAN Secretariat
	Discussant	<b>Fajar Hidayat</b> European Commission, Jakarta Office <b>Mia Mikic</b> United Nations Economic and Social Commission for Asia and the Pacific

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**1215-1330 Luncheon Discussion: Chung Chi College Staff Centre**

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**1325-1500 Policy Seminar (Chung Chi College Staff Centre)***How Services can promote integration in the Asia-Pacific*

Moderator	<b>Anthony Nightingale</b>	Jardine Matheson Ltd, APEC Business Advisory Council Action Plan and Advocacy Working Group
Key Note	<b>Paul Tighe</b>	Australia's APEC Senior Official
Panel	<b>Jesus Seade</b>	Lingnan University
	<b>Pascal Kerneis</b>	European Services Forum
	<b>Stewart Forbes</b>	Malaysian International Chamber of Commerce and Coalition of Services Industries
	<b>Matt J. Matthews</b>	US Deputy Consul, Hong Kong
	<b>Jack Chia</b>	Taiwan Coalition of Services Industries
	<b>Kaaren Koomen</b>	IBM Australia/New Zealand
	<b>Carlos Kuriyama</b>	APEC Secretariat, Singapore

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**1500-1515 Wrap Up and Closing Ceremony**

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