



**United Nations  
Conference  
on Trade and  
Development**

Distr.  
GENERAL

TD/B/COM.1/62  
16 December 2003

Original: ENGLISH

TRADE AND DEVELOPMENT BOARD  
Commission on Trade in Goods and Services,  
and Commodities  
Eighth session  
Geneva, 9–13 February 2004  
Item 4 of the provisional agenda

**TRADE IN SERVICES AND DEVELOPMENT IMPLICATIONS\***

Note by the UNCTAD secretariat

**Executive summary**

The role of developing countries in international trade in services has been increasing in terms of exports and imports. Public policies, including development of the regulatory framework and competitive business environment, and sequencing of the liberalization process, are crucial in ensuring development gains from liberalization of trade in services. Outsourcing of services to developing countries has created new trading opportunities in services. Regional integration, involving developing and least developed countries in all regions, has been increasingly expanding to include services. Liberalization of trade in infrastructure services can bring economic benefits; however, the necessary conditions have to be put in place to ensure domestic supply capacity building and competitiveness, affordability and universal access to these services. Given interlinkages among the GATS modes of supply, there is a need to have a balanced approach to their liberalization in order to ensure their maximum contribution in generating employment, growth and development. Ongoing negotiations under the GATS could reinforce the increasing participation of developing countries in trade by delivering commercially meaningful commitments by their major trading partners particularly in Mode 4. The elaboration of disciplines on GATS rules and domestic regulations with appropriate flexibility for developing countries needs to be completed.

\* This document was submitted after the normal submission deadline had passed.

## INTRODUCTION

1. The present note has been prepared as a contribution to discussion of agenda item 4 (Trade in services and development implications). It reflects on the challenges facing developing countries in the international trade-in-services and reviews experience accumulated by them in the ongoing multilateral trade in services negotiations, as well as on conclusions and recommendations formulated by private and public actors during the most recent UNCTAD Expert Meetings. The latter's findings and discussion of these issues would directly contribute to shaping UNCTAD XI agenda and provide an additional insight into its sub-themes, especially "Assuring development gains from the international trading system and trade negotiations".

### I. RECENT DEVELOPMENTS AFFECTING THE GLOBAL SERVICES ECONOMY

2. International trade in services has become a key factor driving structural change in the world economy. Total exports of services quadrupled, growing from US\$ 400 billion in 1980 to about US\$ 1.6 trillion in 2002, while the share of services in total trade grew from 16.2 per cent to 19.4 per cent.<sup>1</sup> International trade in services is dominated by developed countries, which account for the bulk of services imports and exports and run a surplus in their balances of trade in services vis-à-vis developing countries. However, the role of developing countries in international trade in services has been increasing, and their global deficit in trade in services has been shrinking. Developing countries' share of total trade in services grew from 18 per cent in 1980 to 23 per cent in 2002, while their share of world services imports fell from 31 per cent in 1980 to 25 per cent in 2002.

3. These global figures mask quite divergent trends among major country groupings and regions. By 2002, the European Union ran a small deficit in its trade in services. Countries in North America, however, saw their services trade surplus increase, constituting over a quarter of their total exports, and thus partially compensating for the region's structural deficit in its balance of trade in goods. For instance, North America's net surplus arising from trade in services exceeded US\$ 60 billion in 2002 compared with its deficit in trade in goods, which reached US\$ 480 billion. It is interesting to observe that in 1980 major petroleum exporters ran a huge deficit in services that accounted for 12 per cent of the world total, but by 2002 their share of world imports of services had shrunk to only 4 per cent. Asia's share of world services exports rose from 10 per cent in 1980 to 17 per cent in 2002, while the relative positions of developing countries in Latin America and Africa stagnated: their shares of world services exports remained at 4 and 2 per cent respectively in 2002, while imports of services shrank to 5 and 4 per cent respectively in 2001.

4. The above experience reflects the importance of public policies, which varied between Latin America, Asia and Africa and reveal the possible negative outcomes that can result when liberalization proceeds too rapidly for local actors to successfully develop their services industries against an abrupt flow of services imports. These negative impacts were more pronounced where an adequate regulatory framework was lacking, and Governments could not ensure a competitive business environment. Despite the important role that developing country Governments could play in their public, trade and industrial policies, their ability to implement necessary measures may be

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<sup>1</sup> Data in this section are drawn from the *UNCTAD Handbook of Statistics 2003*.

limited by the increasing pressures of public debt, which rose to above average of 70 per cent of gross domestic product (GDP) by the end of 2002 in developing countries.<sup>2</sup>

5. As a new development in international trade, outsourcing has become a significant factor necessitating adjustment in industrial structures, shifting employment patterns and leading to an increase in the overall efficiency of production. This may be a positive sign that developing countries are likely to assume the same competitive position in some areas of services as they have achieved in selected areas of manufacturing.

6. By limiting the free movement of consumers, security measures introduced internationally have had direct implications for global services trade in such areas as tourism, education and health services, thus undermining trade in these sectors. In many cases, these security measures have also, restricted access for the temporary movement of natural persons supplying services under the General Agreement on Trade in Services (GATS), and also logistics services. For shippers and transport providers exporting to the United States, additional costs and liabilities arise from the new regulations and legislation under which they have to provide more detailed and timely information on goods carried, and they may face shipping delays as a result of new measures to screen equipment and personnel. Developing countries face important difficulties in compliance with these requirements.

7. One of the salient features of the new regionalism evolving worldwide is the incorporation of services trade liberalization in regional trade agreements. Almost every new such agreement includes provisions on services, where countries find themselves negotiating simultaneously different initiatives to liberalize trade in services. Two main types of agreements on services have evolved: the "top-down" approach and the GATS-type, or "bottom-up" approach. The first incorporates liberalizing principles as general obligations with a negative listing of reservations and exceptions to commitments; the latter incorporates limited general obligations with a positive listing of specific liberalization commitments. The Mercosur Protocol of Montevideo, the ASEAN Framework Agreement on Services, the Chile–EFTA agreement and the approach considered for services negotiations in SADC have followed a GATS-type model with a positive listing of specific commitments. The NAFTA and the NAFTA-type agreements, including those signed between Mexico and a number of countries in the Western Hemisphere, CARICOM services trade liberalization, the Canada–Chile agreement and those agreements promoted by the United States, including with Singapore and Chile, all followed a negative listing approach. In the ongoing negotiations in the Free Trade Area of the Americas the approach to services liberalization has yet to be resolved and countries could submit initial offers through either a negative listing or a positive listing. The European Communities have followed a differentiated approach in different agreements covering trade in services.

## **II. TRADE IN SERVICES AND SUPPLY CAPACITY BUILDING**

### **The role of infrastructure services**

8. Infrastructure services play the important role of linking different parts of the economy in the most cost-efficient manner, while Governments seek to ensure their affordability and universality of access by the populations at large. These services are important contributors to development and GDP, acting as generators of employment and income, and are key sectors of international trade in

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<sup>2</sup> Public Debt in Emerging Markets: Is it Too High?  
[www.imf.org/external/pubs/ft/weo/2003/02/pdf/chapter3.pdf](http://www.imf.org/external/pubs/ft/weo/2003/02/pdf/chapter3.pdf)

services. They are critical for the development of the whole economy, acting as the engine for development when present or as a major barrier to development where local supply capacity is low or non-existent. They may determine the structural characteristics of the economy, and also will influence patterns of trade, including in goods. The availability of competitive infrastructure services would ensure that developing countries realize their comparative advantages in the international markets.

9. In a relatively short time the market structure and behaviour of **telecommunications services** have experienced a profound transformation worldwide. Both in developed and increasingly in developing countries competition has been introduced into that sector through deregulation, the establishment of independent regulatory bodies, privatization and trade liberalization. Experience shows that integrating robust competition policies and adequate sectoral regulation and enforcement capabilities are pre-conditions for liberalization to yield benefits. Sequencing of the reform may also have a significant impact on the final outcome. Active policy intervention might be necessary, in the context of the reform, to guarantee improved access to telecommunications services for the poor. Telecommunications markets have also been significantly impacted by the rapid introduction of new technologies. Advanced telecommunications infrastructure furthers economic growth through various channels, increasing the overall competitiveness of economies. Communications costs may also have a significant influence on a country's trade patterns. Moreover, efficient telecommunications services are a necessary condition for facilitating the liberalization and trade of a wide range of other services, including information and technologies, and in particular in promoting and making possible the international outsourcing of services, which is experiencing rapid growth. Therefore, telecommunications services have been treated as the prime target for liberalization both in the context of the GATS and in regional agreements. The requests in the current GATS round of services trade negotiations aim at further improvement of commitments in the telecommunications sector in Mode 3 (i.e. commercial presence) and outsourcing through Mode 1 (i.e. cross-border trade).

10. **Financial services** play a central role in economic development since economic growth and financial development are mutually interdependent factors. Rapid capital accumulation in developing countries propels economic growth, especially through productivity growth, while a weak financial system and associated lack of capital would act as barriers to trade and development. In the context of the ongoing GATS negotiations, two pervasive concerns have dominated discussions so far: developed countries seek increased market opening, tighter rules for policy measures and stricter transparency requirements, while developing countries wish to ensure the compatibility of further liberalization with financial stability to avoid the potentially destabilizing effects of international capital movements. Strengthening of the regulatory framework at the national level before engaging in the liberalization efforts ensures appropriate pacing and sequencing of liberalization and gradualism of the reforms, which is of prime concern to developing countries. The discretion left under the GATS Annex on Financial Services, which recognizes the right of countries to take *“measures for prudential reasons, including for the protection of investors, depositors, policy holders or persons to whom a fiduciary duty is owed by a financial service supplier, or to ensure the integrity and stability of the financial system”*, has failed to reassure many developing countries that further liberalization in the GATS context would not create uncertainties in their financial markets. One reason for this is that by undertaking full commitments in all financial services a country would be engaging in comprehensive liberalization of the capital-account transactions.

11. The challenge facing most developing countries would be their limited ability to predict the associated flows and size of the entry and exit of capital. It should be noted that the standard-setting bodies, such as the Basel Committee on Banking Supervision and the International Organization of Securities Commissions, have a limited membership. Introduction of internationally established

financial standards for prudential purposes, which would adequately reflect the interests of the developing countries, is of recognized importance. However, the adoption of international standards and developing supervisory capacity remain resource- and time-intensive in terms of effective implementation and adequate human resources and institutional infrastructure. Special measures need to be taken so that developing countries are enabled to develop robust prudential regulation and supervisory capacity.

12. The importance of multimodal transport and **logistics services** in trade equals that of custom tariffs or the exchange rate in affecting the magnitude and direction of trade flows.<sup>3</sup> The geographical location of countries has become less important than the availability of transport and logistics services. Through their direct impact on costs of trade, logistics services may influence inflation, per capita income, costs of production, and export earnings, and even lead to loss of export markets. Logistics services include management, provision of packaging, warehousing, information and transport services within the supply chain and where the transport share in the overall logistics cost has been increasing in recent years. Multimodal transport has become the predominant method for delivery of goods, and multimodal transport operators are the leading players in providing door-to-door transportation. These new developments pose challenges for developing countries in the use and provision of logistics services. For developing countries, their geographical situation, small trade volumes and trade imbalances are the cause of a difficult starting position for quality and inexpensive international logistics services. While expanding volumes of trade lead to falling unit costs of transport, lack of trade would discourage the supply of transport services, in turn becoming a barrier to trade. Thus, trade balances, available transport mode options and economies of scale are the main determinants of the cost of transport services. Coherent trade and transport facilitation measures, necessary for the development of international logistics and multimodal transport services, may be successfully addressed in developing countries through bilateral and regional arrangements, while the need to help improve the ability of developing countries to meet existing standards would need to be addressed as a priority through international action.

13. **Distribution services** are central in the logistics chain and for trade in goods and other services. In the GATS negotiations access to and ownership of distribution networks, wholesaling outlets and particularly retailing have dominated the debate. Distribution services are a highly concentrated activity worldwide. In retail services the top 100 retailers account for 25 per cent of worldwide retail business, with the leading 30 retailers accounting for 10 per cent. By 2002 the world's top 30 retailers were active in 88 countries, nearly 70 per cent more destinations than in 1997, and the overseas expansion of major retailers is constantly increasing. All but one of the world's leading retailers are from developed countries. However, some companies from developing countries, for example Kenya, South Africa and Chile, have established operations in other developing countries. The retail sector in developing countries is dominated by a large traditional sector composed of small retail outlets, street vendors and local-government-run district markets, with a modern retailing sector catering to high-income segments of the population representing a small proportion of total retail business. Large retail chains in the majority of developing countries accounts for example, for 16 per cent in Argentina, 19 per cent in Brazil, 23 per cent in Mexico, and 15 per cent in Indonesia. In developed countries retailing is a mature industry facing a saturated market, and the growth in the number of retailers is taking place mainly through mergers and acquisitions, resulting in growing concentration in the sector. The transformation of the retailing sector has raised some concerns in many developing countries in respect of its impact on traditional retailers and the social

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<sup>3</sup> A detailed discussion of this sector is presented in TD/B/COM.3/EM.20/2.

consequences, including unemployment, as mentioned in WTO submissions by Thailand and China<sup>4</sup> on assessment of trade in services. Also, major concerns regarding competition issues have been raised with respect to large chains entering their markets and increasing concentration of the industry. An adequate regulatory and investment framework is a precondition for achieving better outcomes in terms of efficiency and tangible benefits for consumers as well as providing solutions for anti-competitive behaviour and addressing social concerns.

14. The importance of **energy** for economic and social development, given the disparity of physical infrastructure in developing countries, gives rise to the “access divide”. The increasing demand for energy, the liberalization of energy markets and the introduction of new technologies would combine to create dynamism in trade and investment in the energy sector even greater than that experienced by the telecommunications sector in the last decade. In this sector developing countries are faced with the challenge of, on the one hand, achieving more reliable and efficient access to energy, and on the other, of obtaining a greater share of the energy “business”. The pursuit of both goals requires access to knowledge, expertise, technology and managerial know-how. Additional conditions such as promoting transfer of technology and training, reflecting the specificity of energy services and their relevance for development, could be attached to the liberalization commitments to ensure the achievement of development policy goals. Concerns regarding sovereignty over energy resources have been raised by several energy rich countries.

15. The trend towards harmonizing national environmental standards, adopting global environmental targets (especially through the implementation of multilateral environmental agreements) and privatizing utilities is making the industry more trade-oriented. While the developed countries – mainly the United States and countries in Western Europe – account for 85 per cent of the environmental services market, they have collectively represented only 2–3 per cent of annual growth in recent years and seem to face stagnation in demand. The public infrastructure services of drinking water, waste-water treatment and waste management are the core and most traditional environmental services.

16. Privatization and liberalization of the **water sector** are gradually taking place across the globe, with developed countries accounting for 20 per cent of large-scale private water operators and developing countries only 2 per cent.<sup>5</sup> Issues of equity, access of the poor and political acceptability remain key considerations in proceeding further in privatizing water resources and services given the limited purchasing power of the majority of the populations in developing countries. Developing countries rely to a larger extent – nearly half of their needs – on small-scale providers who often operate with minimal investments and low-technology solutions in a predominantly informal rural sector serving the needs of the small communities. Developing countries would benefit more if issues regarding how to build engineering partnerships and address barriers to technology transfer were addressed in this context. In addition, public intervention is bound to remain significant to ensure that provision of essential services such as water is socially equitable. Policies and reforms at the institutional level need to support protection of consumers in the provision of basic environmental services, including water.

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<sup>4</sup> WTO Communications from Thailand, 22 July 2002, TN/S/W/4, and from the People's Republic of China, 19 December 2002, TN/S/W/9.

<sup>5</sup> UNCTAD Expert Meeting on Definitions and Dimensions of Environmental Goods and Services in Trade and Development, 9–11 July 2003.

## **Importance of different modes of supply in trade in services**

17. GATS defines trade in services by introducing the concept of four modes of supply of services. A mode-wise approach in the negotiations does not fully reflect the economic reality of simultaneously supplying services through multiple modes and the linkages between modes of supply for the delivery of services. Barriers to one mode translate into actual/potential barriers to other modes. For developing countries barriers to Mode 4 most affect their ability to effectively use the other three modes to their advantage. In addition, the participation of small and medium-sized enterprises in international trade in services depends predominantly on two types of modalities, namely cross-border trade and associated information and telecommunications technology, and the temporary movement of natural persons supplying services under the GATS, namely Mode 4.

### **Mode 4**

18. For developing countries commercially meaningful Mode 4 liberalization is a litmus test for the development content of the Doha Work Programme and its claim to being called the Doha Development Agenda. Economic analysis shows that if quotas were increased by an amount equal to 3 per cent of developed countries' labour forces, there would be an increase in world welfare of \$US 156 billion per year.<sup>6</sup> So far, specific commitments in the WTO have been asymmetrical in terms of limited coverage of Mode 4. The fact that in the services negotiations Mode 4 has so far been treated as an orphan gives rise to concerns about a development deficit in the services negotiations, just as lack of progress in agriculture has caused frustration in the larger context of Doha negotiations. Liberalization of Mode 4 could be a win-win welfare situation for developed and developing countries given the right policy and regulatory framework at the national and international levels.

19. The most evident way in which trade in Mode 4 benefits developing countries is through the provision of a steady and continuous inflow of remittances, which amount to US\$ 60 billion a year and exceed the current level of official development assistance. The total amount of resources remitted may, however, be two or three times greater since a large number of transactions are effected through informal channels. Movement of natural persons supplying services under the GATS exceeds its purely static economic, trade and competitiveness benefits for developing countries. Dynamic gains for the home country are significant, because they increase investment and domestic savings, promote development of other sectors of the economy and trade, ensure transfer of technology, entrepreneurship and knowledge, and build human capacities. Movement of natural persons is a new source of ideas and creativity for destination countries, and business and trade opportunities through networking for both trading parties. There is therefore a strong political and economic case in favour of more comprehensive and commercially meaningful market access commitments in Mode 4. This is an important development benchmark of the Doha Work Programme, which would make the international trading system more equitable and balanced from a developing country's perspective.

20. One of the ways to correct existing asymmetries and enhance Mode 4 liberalization under the GATS could be the adoption of the model schedule approach, under which specific commitments for natural persons with certain skills on short-term intra-company visits and short-term visits to fulfil contracts could be undertaken. "Short-term" could be defined in each case as a stay of less than a year. Reflecting these classes of movement as a Service Provider Visa in the national migration laws

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<sup>6</sup> LA Winters, The economic implications of liberalizing mode 4 trade. Paper prepared for the Joint WTO–World Bank Symposium on "The Movement of Natural Persons (Mode 4) under the GATS", Geneva, 11–12 April 2003.

would help streamline temporary entry.<sup>7</sup> A set of additional commitments would be made under Article XVIII of the GATS, which would aim to enhance the transparency of visa procedures and limit the trade-impeding impact of measures such as qualifications requirements and administrative procedures. The emphasis in this model schedule would be on broad horizontal commitments ensuring a basic minimum level of access across all sectors, supplemented by sector-specific commitments where deeper liberalization is possible. The lack of recognition of qualifications, skills and experiences remains one of the pervasive barriers in the area of professional services and affects the movement of natural persons in more than one way: it either denies market access to service providers of other countries or induces a service provider to perform in a capacity below his or her level of qualifications. Article VII of the GATS permits members to deviate from the most-favoured-nation (MFN) principle and enter into bilateral or plurilateral mutual recognition agreements (MRAs). Developing countries could benefit from bilateral technical and financial support in promoting the establishment of professional bodies and associations and facilitating accession of developing countries to MRAs.

### ***FDI in services***

21. Net flows of foreign direct investment (FDI) are not equally distributed across all services sectors and have pronounced regional differences. At the same time, in most countries FDI in services sectors is the largest in terms of FDI stock and output<sup>8</sup>. With recent trends of privatization of monopoly services providers, for example in the area of energy or telecommunications, across many countries, the role of FDI has been increasing, and this calls for the strengthening of regulatory frameworks, institutions and effective competition policy. Financial services have been attracting the largest share of FDI so far and account for half of the total stock of FDI worldwide, followed by FDI in services linked to trade in goods, including business services, distribution and utilities. More than two thirds of all privatization deals in developing countries involved foreign investors as a way to obtain capital, technology and managerial expertise. The positive contribution of FDI has been noted in increasing competitiveness in the host economy. Availability, access and quality of services are to be emphasized as objectives in promoting FDI, as well as its contribution to sustained productivity growth. Performance requirements such as partnerships and foreign equity limitations, local content, transfer of technology, and employment and training requirements could be seen as a way to ensure that foreign investors enter into joint ventures with domestic partners and provide access to technology, particularly soft technology and management techniques.

22. Privatization and liberalization of services has raised concerns about the risk of the abuse of monopoly power and the resulting distribution of benefits or impact on employment. Governments need to define the boundary line of what to privatize and what to retain in the public domain as a better way to pursue broader social objectives, and then decide whether or not to involve foreign investors in industries that are privatized. But given the power and superior capabilities of many transnational corporations, as compared with local firms in these countries, there are fears that foreign investors will crowd out local players and interests, abuse monopoly power with adverse effects on competition and consumer welfare and pursue their own interests, not sufficiently taking into account the concerns of host economies.

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<sup>7</sup> Communication from Argentina, Bolivia, Chile, the People's Republic of China, Colombia, Dominican Republic, Egypt, Guatemala, India, Mexico, Pakistan, Peru, Philippines and Thailand, TN/S/W/14, 3 July 2003.

<sup>8</sup> For more detailed discussion on FDI in services, see TD/B/COM.2/EM.14/2.

### **ICT and services**

23. Information and communication technologies (ICT) have driven the convergence of specific sectors, with profound impacts on the service economy and the growing importance of e-commerce and outsourcing of services to developing countries.<sup>9</sup> The information industry, including audiovisual services, telecommunications and the computer-related industry, is at the core of this trend. Services are always embedded in e-commerce by providing a platform through telecommunications and distribution services where goods are traded. In the case of cross-border trade in services, tourism, audiovisual services, including music and news agency services, and also software and other computer-related services remain at the forefront. E-commerce is important in its cost-reducing effect and in stimulating economic activity. Banking transactions via the Internet cost 27 times less than using an automated teller machine or 52 times less than over the phone; similarly, processing airline tickets costs eight times less over the Internet than through a travel agency. Efficient telecommunication systems and telecommunications technology and transport logistics infrastructure are required for the successful implementation of e-commerce. Development of the financial environment is required in order to allow for e-payments and the use of credit cards. Transportation and delivery systems, as well as entrepreneurship and business skills, are also essential. On the policy side, there is a need to adapt national and legal regulatory frameworks to foster e-business, allowing for e-signatures and data protection. The Government's role in promoting digital awareness and digital literacy through special programmes can help ensure long-term competitiveness and wider distribution of benefits arising from e-commerce and ICT services.

24. Ensuring full market access and national treatment commitments under all subsectors of computer and related services in Modes 1, 2 and 3 granted to developing country suppliers would enhance their ability to supply ICT services. Ongoing negotiations on services would need to ensure also that in the area of Mode 4 members undertake specific commitments free of the application of the economic needs test for computer professionals and computer associate professionals. In addition, as part of ensuring the increasing participation of developing countries in trade in services, WTO members should contribute to measures in developing countries aimed at development of the ICT sectors in order to promote their economic and social development.

## **III. TRADE IN SERVICES AND HUMAN DEVELOPMENT**

### **Trade in services and poverty alleviation**

25. Eradication of extreme poverty and hunger is the first Millennium Development Goal, where trade in services could play an important role. Most services sectors are typically of a dual nature: in addition to the purely commercial side, they are important in their social, cultural, welfare-enhancing role and pro-poor policies, which may have a different dimension in developing countries. Translating countries' success in services trade towards poverty alleviation is not an automatic process. It depends largely on government policies aimed at promoting domestic employment at lower skill levels (e.g. in tourism), ensuring availability and accessibility of essential services to the poor (e.g. in health and education), and investments in the building of efficient and accessible infrastructure services (e.g. telecommunications, transportation, and water and sanitation). As exporters of services developing countries have demonstrated their comparative advantage in trade through temporary movement of natural persons at all skill levels. However, they continue to face the greatest market access restrictions in this area. As an effective trade instrument, Mode 4 ensures that benefits accrue directly

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<sup>9</sup> For example, see communications by Costa Rica, S/CSS/W/129, 30 November 2001, by Mercosur, S/CSS/W/95, 9 July 2001 and by India, S/CSS/W/141, 22 March 2002.

to people and thus alleviate poverty. Many developing countries have sought to promote trade in services through privatization and liberalization, aiming to obtain technology, enhance efficiency and ensure growth in productivity and thereby generate the economic conditions needed to promote employment and development and reduce poverty. To ensure competition in local markets, this process has to be supported by an adequate regulatory framework, and institutional and human infrastructure, all of which are weak in most developing countries. Economic transformation puts downward pressures on employment, especially for unskilled labour, with a resulting disparity in income that accentuates poverty among the poorest segments of the population. Promoting trade in services in sectors with a particularly pronounced social dimension, if supported by regulatory measures to ensure cohesion of social fabric and needs, can guarantee basic access to services by the poor.

### **Trade in services and cultural industries**

26. The influence of globalization and trade has extended itself to the world of cultural industries, which is particularly sensitive to convergence of cultural and economic considerations. Creative industries are the backbone of sustainable human development and a nation-building instrument promoting respect for cultural diversities, traditions, national values and heritage. Cultural diversity is essential for humanity in the shaping of its future: “as a source of exchange, innovation and creativity, cultural diversity is as necessary for humankind as biodiversity is for nature”.<sup>10</sup> Further development of trade in this area should ensure access, diversity, and an environment favourable to the flowering of creative diversity, to freedom of choice among an abundant supply of cultural products and to the development of critical thought and critical pluralism.

27. At the same time, creative industries have become a pillar of the new economy because of their increasingly important contribution to economic development, especially in terms of generation of employment and as a way of opening up opportunities for economic diversification in non-traditional sectors and successful integration into the global economy. They represent an emerging cluster of economic activities. There are a number of preconditions for countries to be successful in ensuring economic and creative interdependence and in promoting the development of creative industries: an appropriate legal and regulatory framework at the domestic level; a dynamic cultural policy; the availability of a critical mass of quality products; the availability of qualified professionals and entrepreneurial capability all along the production and distribution chain; and access to the distribution networks. A participatory approach involving the private and public sectors and civil society can ensure that the objectives of social cohesion, overcoming social exclusion and achieving creative diversity are fully taken into account.

### **Trade in services and gender**

28. Trade may play an important contributory role in promoting gender equality and empowerment of women, which forms the third Millennium Development Goal. Most of the firms in services activities are traditional employers of women, including government, which retains its role in providing services in many developing countries. Regional trade and international trade play an important role in the development of efficient services sectors in developing countries. Many developing countries have recognized the importance of temporary movement of persons supplying services, where women play an important role, especially in such areas as nursing and health care, which can be delivered only by ensuring proximity between provider and consumer. The temporary

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<sup>10</sup> UNESCO Universal Declaration on Cultural Diversity, Article 1, “Cultural diversity: The common heritage of humanity”, [http://www.unesco.org/culture/pluralism/diversity/html\\_eng/index\\_en.shtml](http://www.unesco.org/culture/pluralism/diversity/html_eng/index_en.shtml)

movement of women abroad would tend to increase the return on education and would send a positive signal to young women for investing in human capital in the home economy and, thus, ensuring the continued availability of skills domestically, which is an important factor in the area of health services. Where movement involves other than skilled women, it is likely to produce a positive impact on the wages of less skilled women in the home economy owing to a change in ratio between skilled and less skilled labour. Because of the limited domestic employment opportunities and the long period necessary for a structural change in the economy, the movement of women abroad emerges as an option in the immediate term to provide domestic employment opportunities for women.

29. Women play an important role in the economies of developing countries, and creating economic opportunities for them in the area of international trade in services would help eliminate gender inequalities in social and economic life and act as an important factor stimulating economic growth and development. Active pursuit of policies that promote gender equality and empowerment of women through targeted programmes, activities and projects at the national and subregional levels is necessary, including specialized training in information technology and in other modern skills.

#### **IV. BRINGING DEVELOPMENT ISSUES INTO THE TRADE IN SERVICES NEGOTIATIONS**

##### **Overview of the ongoing GATS negotiations on services**

30. Since 2000, the negotiations on services have proceeded in accordance with Article XIX (Negotiation of Specific Commitments) of the General Agreement on Trade in Services (GATS), and were subsequently incorporated into the Doha Work Programme (DWP). The WTO Doha Ministerial Declaration (paragraph 15) provides for negotiations on trade in services to be conducted with a view to promoting the economic growth of all trading partners and the development of developing and least developed countries. It reaffirms the Guidelines and Procedures for the Negotiations<sup>11</sup> as the basis for continuing the negotiations with a view to achieving the objectives of the GATS, as stipulated in its Preamble, Article IV (Increasing Participation of Developing Countries) and Article XIX (Progressive Liberalization).

31. The DWP called for initial requests for specific commitments to be submitted by 30 June 2002, and for initial offers to be submitted by 31 March 2003. Bilateral consultations on requests for market access began in July 2002. To date, 39 offers have been tabled of which 19 were presented by developing countries and one by a least developed country (LDC). Most developing countries are still in the process of identifying their specific sectoral and modal interests, the barriers to their services exports, the impact of requests by developed countries on their services sectors, and ways and means of overcoming supply constraints through implementation of GATS Articles IV and XIX.2. Services are particularly important in the DWP given (a) their role in the growth and development of the whole economy, (b) their linkages with other market access negotiations, and (c) the overall balance of negotiations. Some developing countries have stressed that there is no reference in the Draft Ministerial Cancun texts to the Guidelines and Procedures for the Negotiations and GATS Articles IV and XIX.2, and that, in their view, some issues have not been adequately addressed – for example, assessment of trade in services, and review and evaluation of progress in negotiations as provided for in paragraph 15 of the Guidelines.

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<sup>11</sup> WTO document, S/L/93, 29 March 2001.

### ***Developments under GATS Article XIX.3***

#### *Assessment of trade in services*

32. Assessment of trade in services should have been completed before adopting the negotiating guidelines were adopted, but this did not happen. The discussion on assessment of trade in services, which has been continuing since 1999, has not yet led to adoption by the Council of conclusions, including with respect to the contribution of GATS to increasing the participation of the developing countries. The *Guidelines and Procedures for the Negotiations on Trade in Services (S/L/93)* clearly indicated in its paragraph 14 that the objective of assessment is to adjust the negotiations in the light of the results of the assessment with reference to the objectives of Article IV.

33. A number of common observations<sup>12</sup> have emerged from the developing country submissions on assessment. These include developing countries' recognition that: (a) an overall balance of rights and obligations for all WTO Members has not been attained, this refers to a lack of meaningful concessions by developed countries; (b) the increase in share of world services exports has been small for developing countries; (c) the objectives of Article IV have not been achieved owing to critical trade barriers faced by developing countries and supply constraints; (d) benefits from privatization and liberalization are not automatic without appropriate preconditions, including technological capacity-building and complementary policies; (e) there is a need for policy flexibility and proper sequencing of liberalization; (f) priority attention needs to be given to ensuring access to universal and essential services; and (g) nascent services sectors and small and medium-sized enterprises of developing countries require capacity-building assistance from developed countries. The assessment of developing countries would need to be reflected and effectively addressed in the results of the market access negotiations. Opening up of the markets may need to be re-evaluated and perhaps re-regulated depending on the assessment of evolving market realities. Ongoing efforts on assessment are necessary at the national, regional and multilateral levels for obtaining insight into the impact of trade liberalization on developing countries.

#### *Modalities for the Treatment of Autonomous Liberalization*

34. The Modalities for the Treatment of Autonomous Liberalization adopted in March 2003 were a step forward, although they do not create any legal obligations or establish any automatic right to credit or recognition. They provide that an autonomous liberalization measure of a Member eligible for credit should, *inter alia*, have been undertaken by the Member unilaterally since previous negotiations. A positive factor is that this includes liberalization undertaken as part of structural adjustment programmes under the aegis of the IMF and the World Bank.

#### *Modalities for Special Treatment of LDCs*

35. WTO Members agreed on modalities for special treatment for LDCs in accordance with the provisions of Article XIX.3. The latter provides, *inter alia*, that developed countries shall exercise restraint in seeking commitments from LDCs; LDCs shall not be expected to offer full national treatment, nor are they expected to undertake additional commitments under Article XVIII of the GATS on regulatory issues that may go beyond their institutional, regulatory and administrative capacities; LDCs may make commitments that are limited in terms of sectors, modes of supply and scope; and WTO Members shall, to the extent possible, and consistently with Article XIX of the GATS, consider undertaking commitments to provide access in Mode 4, taking into account all

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<sup>12</sup> M. Mashayekhi and M. Julsaint, *Assessment of Trade in Services in the Context of the GATS 2000 Negotiations*, South Centre, Working Paper 13, p. 39.

categories of natural persons identified by LDCs. These modalities would need to be effectively operationalized and to serve as a basis for negotiations and building supply capacity for the LDCs

## ***Developments in the area of GATS rules***

### ***Emergency Safeguard Measures***

36. Developing countries have emphasized the need for the disciplines on Emergency Safeguard Measures (ESM) in the context of the mandated negotiations under GATS Article X. In comparison with trade in the area of goods, trade in services liberalization has only recently been assimilated by most developing countries, including their private sectors. Owing to its temporary nature, imposing a window of time for implementing necessary adjustment by local suppliers of services and to address employment concerns, ESM becomes a means to deflate opposition to liberalization while possibly allowing an opportunity for affected industries to restructure. The importance of ESM is based on the understanding that liberalization involves adjustment costs and recognizes that imperfection in factor mobility may negatively affect resource allocation. ESM would apply in cases where surges of imports, as measured by value or volumes, threaten to cause injury to a domestic sector or provider. They would address the supply of new services or service suppliers or for expanding supply (new branch or new contract) for those already present in the country applying ESM. The role of ESM is of particular relevance in those sectors where GATS commitments have been made, where it could take the form of suspension of specific commitments or adoption of positive measure in favour of domestic suppliers. Since multilateral assessment of the implications of liberalization in trade in services has not been completed, Governments remain cautious in the presence of uncertainties about its potential impacts. At this early stage of GATS' existence, it would be preferable to come up with a horizontal set of disciplines that could gradually gather sectoral specificities from concrete cases.

### ***Subsidies***

37. Little progress has been achieved in the discussions under GATS Article XV concerning the need for and possible scope of disciplines on subsidies. WTO Members have not been forthcoming in contributing to the exchange of information mandated by Article XV on subsidies which may have trade-distorting effects. However, available information suggests that government support measures are prevalent in many services activities and their possible trade-distorting effects cannot be discarded a priori. The provision of some services is highly subsidized. In rail transport the rate of support varies between 15 and 180 per cent of total value added.<sup>13</sup> In the OECD countries government support to private tertiary education amounts to 0.24 per cent of total GDP. The airline industry receives State support amounting on average to more than US\$ 7 billion a year.<sup>14</sup> Audiovisual production is supported worldwide with more than US\$ 2 billion of State resource transfers.<sup>15</sup> Support to R&D in services in OECD countries represents in some cases up to 50 per cent of total investment in R&D by the services sector, and in general a significantly higher proportion than in the case of other economic activities. Conceptually, there is no compelling reason not to accept the notion that subsidies in services could distort trade just as in the case of trade in goods. Further work is required to identify services-related State support measures that could be considered as subsidies and in particular to analyse their effect on trade in services. Measures could be classified under three main categories: *export-enhancing subsidies*, through which a country would attain a larger market share in

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<sup>13</sup> B Hoeckman and C Primo Braga; Protection and Trade in Services, Policy Research Working Paper, World Bank, April 1997.

<sup>14</sup> ICC, State Aid to Airlines, Document No 310/430 rev.2, 13 June 1995.

<sup>15</sup> L Abugattas. Working Paper (in progress), November 2003.

comparison to that in the absence of the measure; *import-displacement subsidies*, through which a country would import less than in the absence of the measure; and finally, *investment-diverting subsidies*, which distort the flows, volume and direction of FDI in relation to what would have been expected in the absence of the measure. The desirability of disciplines on subsidies cannot be decided solely on the basis of whether or not they are needed today on the basis of the extent of current subsidization and effect on trade in services, but should govern the possible future behaviour of governments.

### ***Government procurement***

38. Article XIII exempts from the MFN, market access and national treatment provisions of GATS all services purchased by governmental agencies for governmental purposes and without a view to commercial resale, or with a view to use in the supply of services for commercial resale. The same article provides that there shall be multilateral negotiations on government procurement of services within two years of entry into force of the WTO (i.e. beginning in 1997), but these have not yet produced any concrete results. Some services have been included in the schedules under the plurilateral Government Procurement Agreement (GPA), to which few developing countries are parties<sup>16</sup>. Most developing countries do not wish to participate in the GPA because of the lack of effective special and differential treatment provisions and costs of implementation. This also is because of the general perception that by opening their government procurement to international tendering they will allow foreign firms to capture a significant part of their domestic business while their firms will be precluded from gaining access to foreign government procurement markets owing to financial and technological weaknesses or owing the various other barriers (i.e. those mentioned above).<sup>17</sup> However, this is also used as a means to promote development of domestic industry or technology and to support the competitiveness of small and medium-sized enterprises. They have been reluctant to embrace the initiative to establish disciplines on transparency in government procurement because they are concerned that this may prejudice their use of government procurement as a tool for pursuing social and development objectives, and also because of the high cost of implementation of such an agreement.

### ***Domestic regulation***

39. Regulatory reform is of key importance to developing countries and they have emphasized that the pace of services liberalization needs to be adjusted to take into account Governments' supervisory and regulatory capability. Another important area of work relates to Article VI.4 disciplines on domestic regulation, taking into account the right of Members to regulate, and to introduce new regulations, on the supply of services within their territories in order to meet national policy objectives. Given the existence of asymmetries with respect to the degree of development of services regulations in different countries, the particular need of developing countries to exercise this right has been recognized in the preamble of the GATS. The *Guidelines and Procedures for the Negotiations on Trade in Services* provide for the conclusion of negotiations on Article VI.4 prior to the conclusion of the negotiations on specific commitments. The work of the Group on Domestic

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<sup>16</sup> Some developing countries that have recently acceded to the WTO have consented to enter into negotiations to adhere to the GPA.

<sup>17</sup> The counterpoint to this argument is that the services so obtained would be provided at more competitive prices than local firms could achieve (otherwise the local firms would win the contracts), thus stimulating development and growth elsewhere in the economy. Where the balance between these two concerns lies is a matter for judgement by each country.

Regulation has not made much progress, as countries' positions are not converging on the issues under consideration.

40. It is understood that measures in the area of domestic regulation are non-discriminatory, and should ensure that what regulators impose for reasons of public policy and legitimate objectives does not act as an unnecessary barrier or barriers to trade in services. One of the roles that disciplines in the area of domestic regulation may play is to make specific commitments more effective. Developing countries have also highlighted the fact that they would prefer to deal with disciplines on domestic regulations multilaterally as provided for in Article VI rather than on a bilateral basis in the request/offer exercise. Some developed countries have proposed adoption of least trade restrictive regulations based on a strict "necessity" test/proportionality principle as well as transparency obligations extending to prior consultations on new legislation. Of crucial interest to developing countries are issues relating to maintaining their right to regulate and the flexibility to undertake policy/regulatory reform, pursuit of public policy objectives ensuring access to universal services and full transparency of the regulatory and administrative framework on Mode 4.

### ***Review of the initial offers***

41. The ongoing request/offer process within the GATS poses challenges to developing countries in evaluating the requests and offers submitted to them by developed country trading partners, and the formulation of their own requests and offers, which is a particularly complex task, since they need to determine clearly their national policy objectives and the competitiveness of each sector/subsector, and evaluate *inter alia* the proper sequencing of liberalization, the capacity of domestic firms to provide particular services and whether this capacity would be positively or negatively impacted by further competition in the market. Other elements of such an evaluation relate to impact on investment, infrastructural services, the impact on employment and access to high-quality and more efficient imports of services.

42. In line with the provisions of the GATS, the increasing participation of developing countries in the international trade in services will be facilitated through negotiated specific commitments by WTO Members in the services sectors and modes of supply of export interest to developing countries. Developing countries as a group maintain their trade interests in nearly all services sectors; however, some of these sectors have attracted more attention in the ongoing negotiations, including business, computer-related, communication, financial, construction and transport services. At the same time, progress in the area of Mode 4 supply of services retains its particular importance as the area of direct export interest for majority of the developing countries.

43. Concerns have been expressed by developing countries regarding the lack of commercially meaningful initial offers submitted by their major trading partners. Changes introduced in the initial offers concerning classification of services or replacing one type of measure by another, have made it difficult to assess effective liberalization in each of the areas affected by these changes, leading in some cases to a narrowing of the scope of the specific commitments.<sup>18</sup> Emergency safeguard-type provision have been retained in selected sectors by some countries in their schedules of commitments, while progress has not been achieved in the area of GATS rules multilaterally. While GATS seems to clearly recognize the right of its Members to regulate in order to meet public policy objectives, as well as to exclude from its scope measures taken by the Government in exercise of its authority, some Members felt the need to reconfirm this right through excluding from their initial offers public or

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<sup>18</sup> Communication from Brazil, JOB(03)/186.

publicly funded services as well as services supplied under governmental authority from their consideration in the trade in services context.

44. Concerning new offers in the area of Mode 4, Norway has scheduled a broad commitment, while the EC has made a commitment to some liberalization. In principle, the European Communities (EC) and Canada have made market-opening offers of an equal order. As its most significant improvement the EC have removed the requirement to comply with the economic needs test for intra-corporate transferees and for contractual services providers, including independent professionals within the established quota. Among initial offers submitted by developed countries, Australia, the United States of America and Iceland have made no improvements. The specific liberalization commitments continue to cover measures regulating commercial presence substantially more than measures regulating the movement of natural persons. In general, these initial offers have not achieved balanced coverage and economically meaningful commitments with respect to all modes of supply. The liberalization commitments in the initial offers of Norway, the EC, Canada and other countries are a positive step that contributes to creating a momentum in Mode 4 liberalization negotiations that needs to be further pursued.

## V. CONCLUSIONS

45. Sustained growth of the services economy is crucial for maximizing positive development implications in terms of opportunities for developing countries to improve national socio-economic dividends and achieve trade benefits. Liberalization of trade in infrastructure services can bring economic benefits; however, preconditions have to be put in place to ensure appropriate sequencing, domestic supply capacity building and competitiveness, affordability and universal access. Growing trade in services can provide immediate development benefits to the extent that it leads to the development of efficient and competitive services sectors, access to essential services, better employment opportunities, poverty alleviation and improvement of human development, including positive gender outcomes and leading to raised living standards. In the context of the Doha Work Programme, the outcome of services negotiations should ensure better prospects for developing countries in terms of balanced and equitable distribution of benefits from trade liberalization. To the extent that scope is preserved in the international trading system for an increase in services supplied by developing countries, trade liberalization can be supportive in overcoming poverty. This is particularly evident in Mode 4 and sectors such as tourism, which remain the primary source of export revenues for many developing countries. Similarly, in other sectors such as construction, environment, health, education, telecommunication and energy services, trade liberalization should be supportive of the priority national policy objectives of developing countries, with special consideration given to the needs of the large populations living in poverty.

46. To achieve a balanced outcome of negotiations and effective participation of developing countries, conditions and limitations may need to be maintained in providing market access in developing countries to address strengthening of the competitiveness of their suppliers and development needs. At the same time, market opening in developed country markets would need to ensure fair opportunities for suppliers from developing countries. In addition to effective market access and national treatment, additional commitments need to be sought by developing countries as a way to implement GATS Articles IV and XIX.2 (which allows developing countries to attach access conditions to their markets) to ensure supply capacity building. Furthermore, paragraph 15 of the Guidelines and Procedures for the Negotiations on Trade in Services requires that in the review of progress in negotiations the extent to which Article IV is being implemented be considered and that ways and means of promoting the goals therein be suggested. In this context, commercially

meaningful commitments need to be made by developed countries in specific sectors and modes of export interest to developing countries as reflected in their requests, particularly in Mode 4.

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