Policy Dimension of Trade in Services and Economic Transformation

by

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The views expressed are those of the author and do not necessarily reflect the views of UNCTAD.
INTRODUCTION

- Debate on economic transformation (ET) centres on transforming agriculture and moving into manufacturing, services remain an unexplored component.
- Many policy makers in low-income countries (LICs) do not regard services, even less trade in services, as a focus of action on ET.
- Sceptical view suggests that services follow rather than lead ET.
- However, Balchin et al (2016) finds that
  - Productivity differentials are large and occur across countries, across services and other sectors and between firms within services sectors.
  - Services play a key role in aggregate productivity change and successful countries have seen productivity change in services and other sectors at the same time (Balanced growth).
  - Services are embodied in goods trade – developing manufacturing without quality services is difficult if not impossible.
• Policy (including policy directly affecting trade in services) can have major impact in terms of raising the contribution of services for ET
• Even when promoting manufacturing exports is priority, the answer can be found in trade in services policy
• In policy designing, important to recognise the heterogeneity in the impacts of different services sectors on ET.
• Some services are important revenue and foreign exchange earners (hydropower, tourism, information and communication technology (ICT))
• In others, linkages with the rest of the economy are more prominent (e.g. suppliers in the tourism sector).
• Some sectors are key for supporting productivity/trade in other sectors (e.g. ICT, logistics, finance) and these linkages are perhaps less visible
TARGETED TRADE POLICY IN LICS

• Openness is related to transformative effects in the services sector.
• Export promotion is important for services producers and economic transformation more generally.
• Imported services are a key part of the value added embedded in a country’s goods exports: necessary to remain open towards imports in services.
• Openness to FDI: the effect of foreign ownership on labour productivity is large and positive in the services sector in LICs, although heterogenous.
• Trade policy plays a crucial role in opening markets, regionally as well as internationally (e.g. in airline services).
• An open service sector will increase competition and help domestic services firms become more competitive.
FRAMING POLICIES

- Liberalisation, however, need to recognise the complicated nature of the regulations that affect trade in services.
  - Many regulations are embedded in the domestic regulatory frameworks and they may be justifiable by addressing certain standards of quality (i.e. certification of medical practitioners).
  - But they can constitute a impediment to trade in services, constraining the policy space and requiring more innovative approaches

- Some services sectors in countries have managed to overcome constraints to liberalisation and implemented domestic regulatory frameworks that are non-trade-distorting.
  - Mauritius, South Africa and Uganda have begun to liberalise air access to support tourism services
  - Senegal and Mauritius have also liberalise their telecommunications sector, improving efficiency and making ICT services sectors more competitive.

- There is a range of mechanisms available to negotiate better access for developing countries’ services exports.
  - Plurilateral level (WTO General Procurement Agreement)
  - Regional level: they facilitate mutual recognition of services sector qualifications (South-East Asia)
  - Bilateral: facilitated access for mode 4 from developing countries (Chile-US FTA)
• Basic factors are key for success in some services sectors (e.g. natural resources/endowments for hydropower (Lesotho, Nepal) and tourism (Mauritius, Tanzania) or a skilled workforce and telecommunications infra for ICT).

• Active services policy play an important role in promoting exports of services (e.g. software technology parks (India) and a cyber city (Mauritius) to support ICT services).

• Iterative, adaptive and flexible approaches have proven successful in setting up mechanisms to coordinate investment in certain services sectors (e.g. hydropower in Nepal).

• An appropriate regulatory framework for services promotes competition and improve efficiency, ensuring services exports are competitive in int’l markets (e.g. liberalisation of telecommunications in Senegal/Mauritius).

• Regulation and political economy considerations are particularly important in large services sectors.

• Productivity of services firms in LICs that supply exporters is low on average: ET potential by raising their productivity, which will have knock-on effects on trade in goods and services, etc.
CASE STUDIES

• Financial services in Africa: Higher degree of financial deepening in Kenya than in Nigeria.
  – Policy-led integration with EAC has boosted Kenya’s trade in financial services.
  – Lack of integration and sectoral development strategy have hampered the development of the sector in Nigeria.

• Tourism in Mauritius and Tanzania. Improvement in liberalisation air travel in both countries
  – Diversification of offer in Mauritius (medical and business tourism) and improvement of infrastructure.
  – Deficiencies in the availability and quality of tourist-related infrastructure and a shortage of relevant skills in the domestic economy in Tanzania

• IT in India, Mauritius and Senegal. Key good internet connectivity and liberalised telecoms sector
  – Basic factors need to be in place to develop exports of ICT services, including a skilled workforce and telecom infra.
  – Clusters are also important (Cyber City in Mauritius and Software parks in India)

• Airlines: Location is key. Key is the negotiation of bilateral regular services agreements
  – Kenya and Ethiopia capturing traffic between Asia-Europe-Africa. Is there space for other local players? (e.g. Rwanda air)
  – Ethiopia more successful in developed horizontally (e.g. cargo) and vertically (e.g. MRO services)
FINAL COMMENTS

• Services play a key role in productivity change and successful countries have seen simultaneous productivity growth in services and other sectors (Balanced growth).

• Policy (including policy directly affecting trade in services) can have major impact in terms of raising the contribution of services for ET.

• Even when promoting manufacturing exports is the top priority, trade in services policy can be instrumental.

• Export promotion and liberalisation of import of services are key: Services are an increasing part of the value added embedded in a country’s goods exports. Openness to FDI also important.

• Liberalisation, however, need to recognise the complicated nature of the regulations that affect trade in services.

• Certain policies act as enablers and they unlock the transformational effect of trade policies in the service sector.

• Case studies in LICs suggest the roles that different services have had on ET and the policies that support them.
The Supporting Economic Transformation (SET) is an ODI programme funded by UK DFID to support countries in their quest for economic transformation through data and policy analysis and convening. The views expressed are those of the researchers and do not necessarily represent the views of ODI or DFID.

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