

Trade in Services, Development and Economic Partnership Agreements

Paul Brenton and Nora Dihel

World Bank

Poverty Reduction and Economic Management

Africa Region

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This presentation is based upon a draft report on Trade in Services in Africa and Economic Partnership Agreements. The presentation is part of a consultation process prior to the competition of the final report and should not be quoted, comments are welcomed.

Key features of (interim) EPA

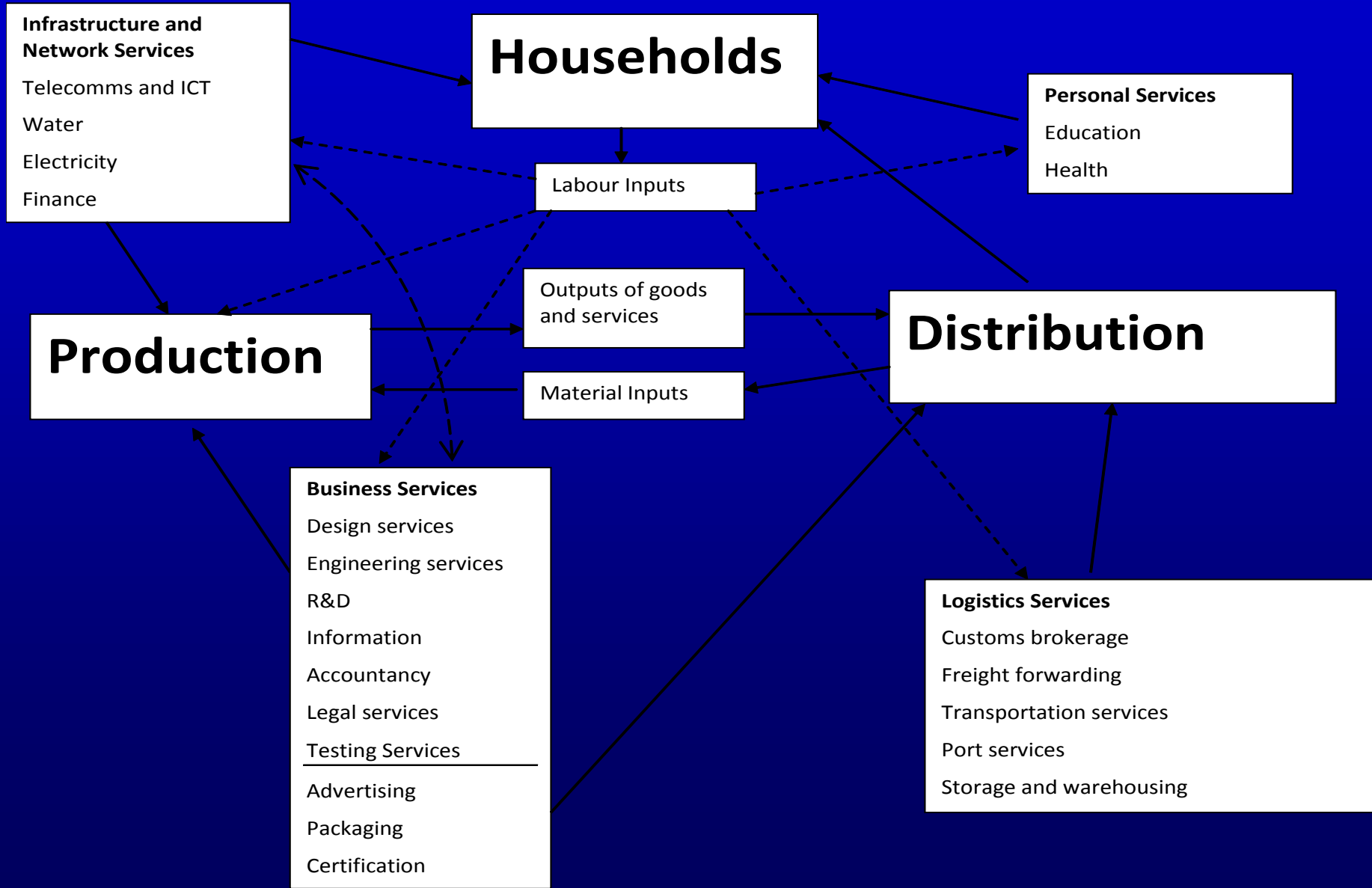
- 100 percent DFQF access to the EU market with transition periods for rice and sugar.
- Progressive opening in ACP to imports from EU
 - Example - EAC to liberalize 82 percent of imports (64% in 2 years, 80% in 15 years, rest in 25 years).
- Less restrictive ROOs for textiles, clothing, fish and a few agricultural products.
- An MFN clause
- A standstill clause on new customs duties on trade between the parties
- Development assistance, or “Aid for Trade”, from EDF
- Commitment to negotiations on **services** trade, investment, competition and govt procurement.

Why negotiate services in an EPA?

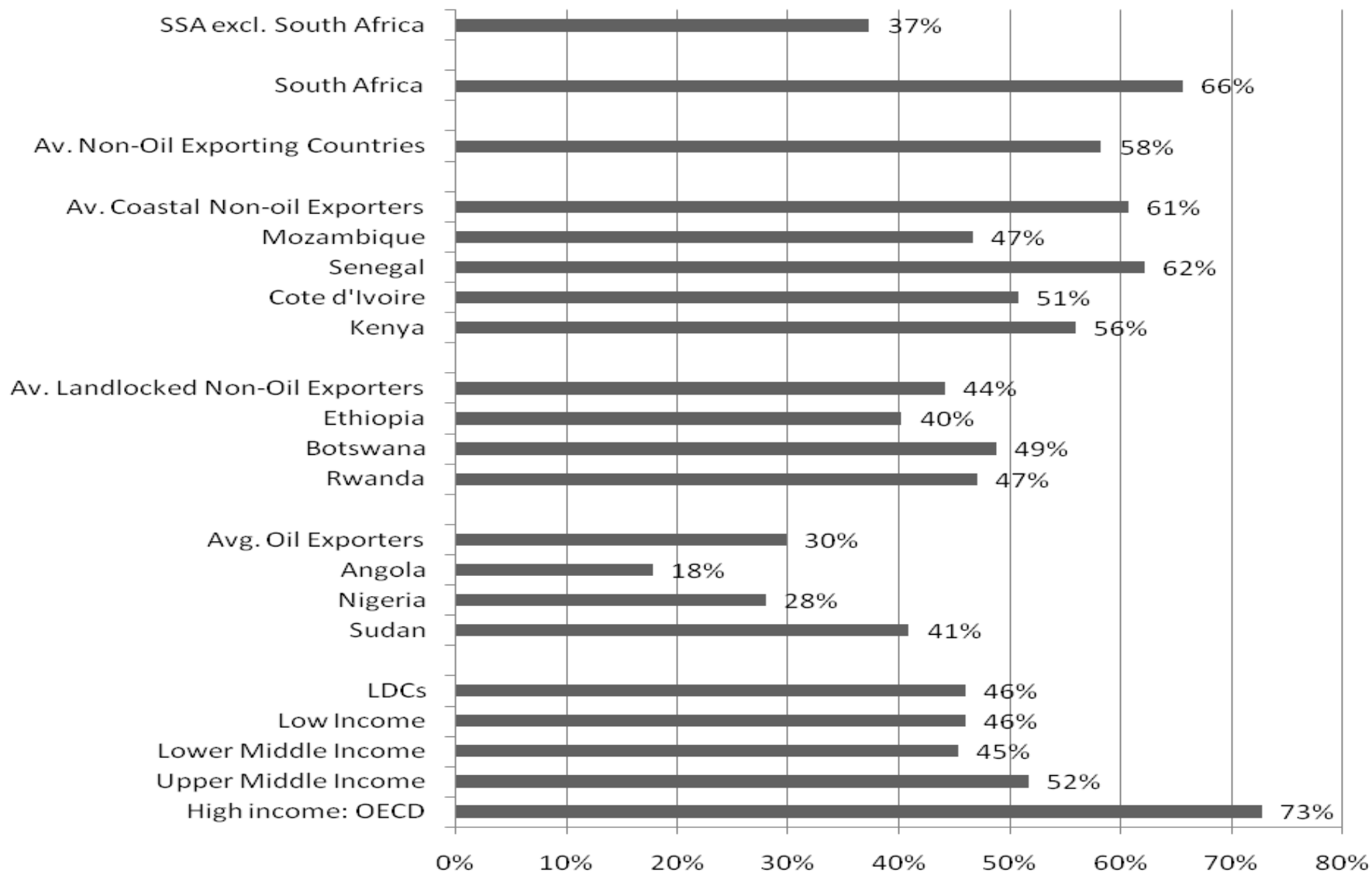
- No obligation at WTO to include services
- Services critical for development
- Opportunities from EPA
 - Accelerate trade and regulatory reforms
 - Enhance regional integration in services
 - Leverage financial resources and expertise from EU to build regulatory capacity?
- Risks from EPA
 - Too much focus on market access without coordinated regulatory reform and capacity building

Services in the modern economy

Figure A1. Infrastructure, Business, Logistics and Personal Services

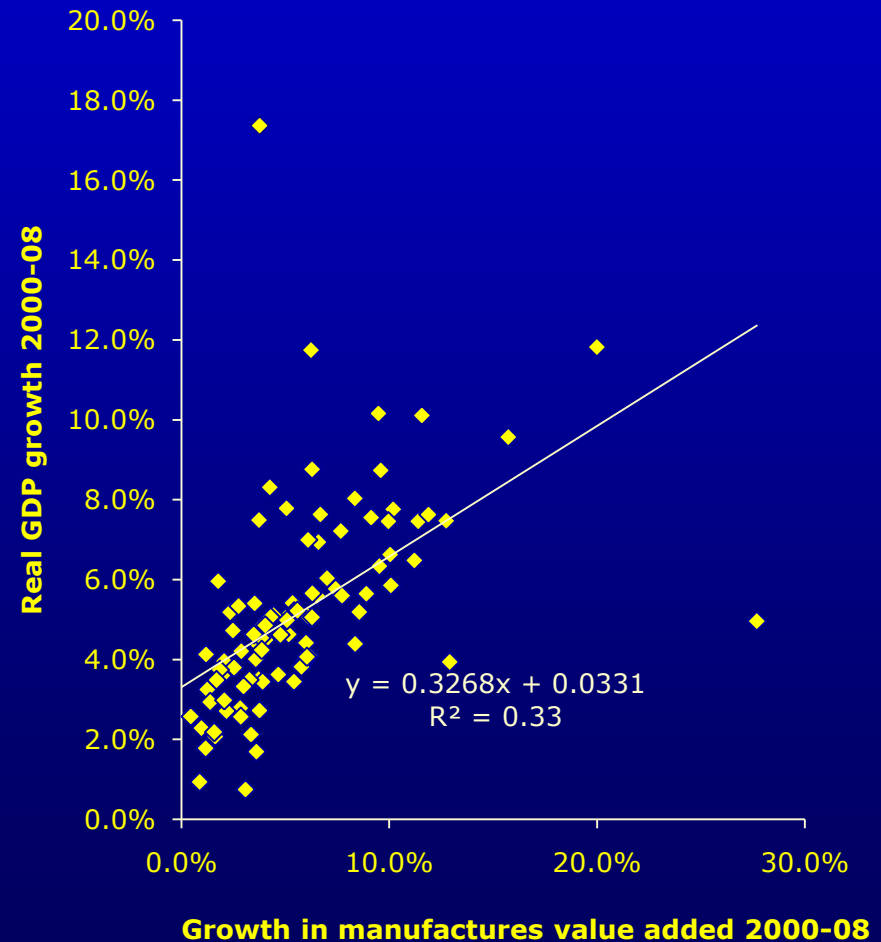
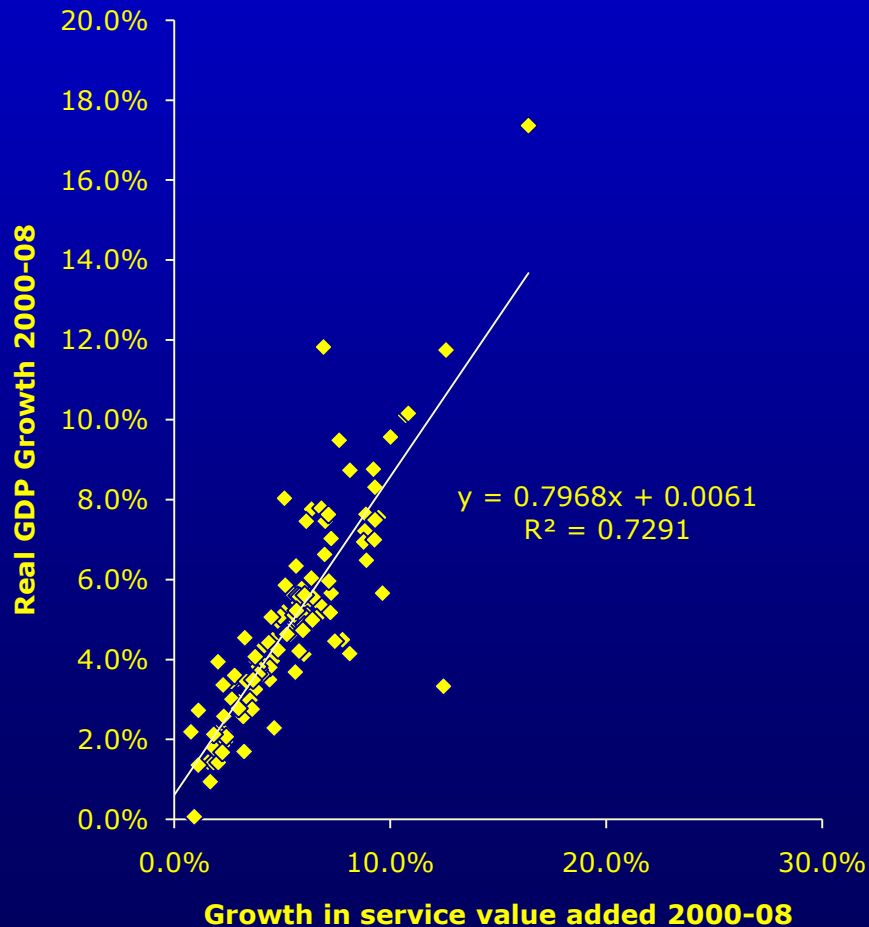


Services - large share of GDP



Services matter for growth

- Growth sectors in their own right
- Key inputs into production of goods and other services



Services a new route to development in Africa?

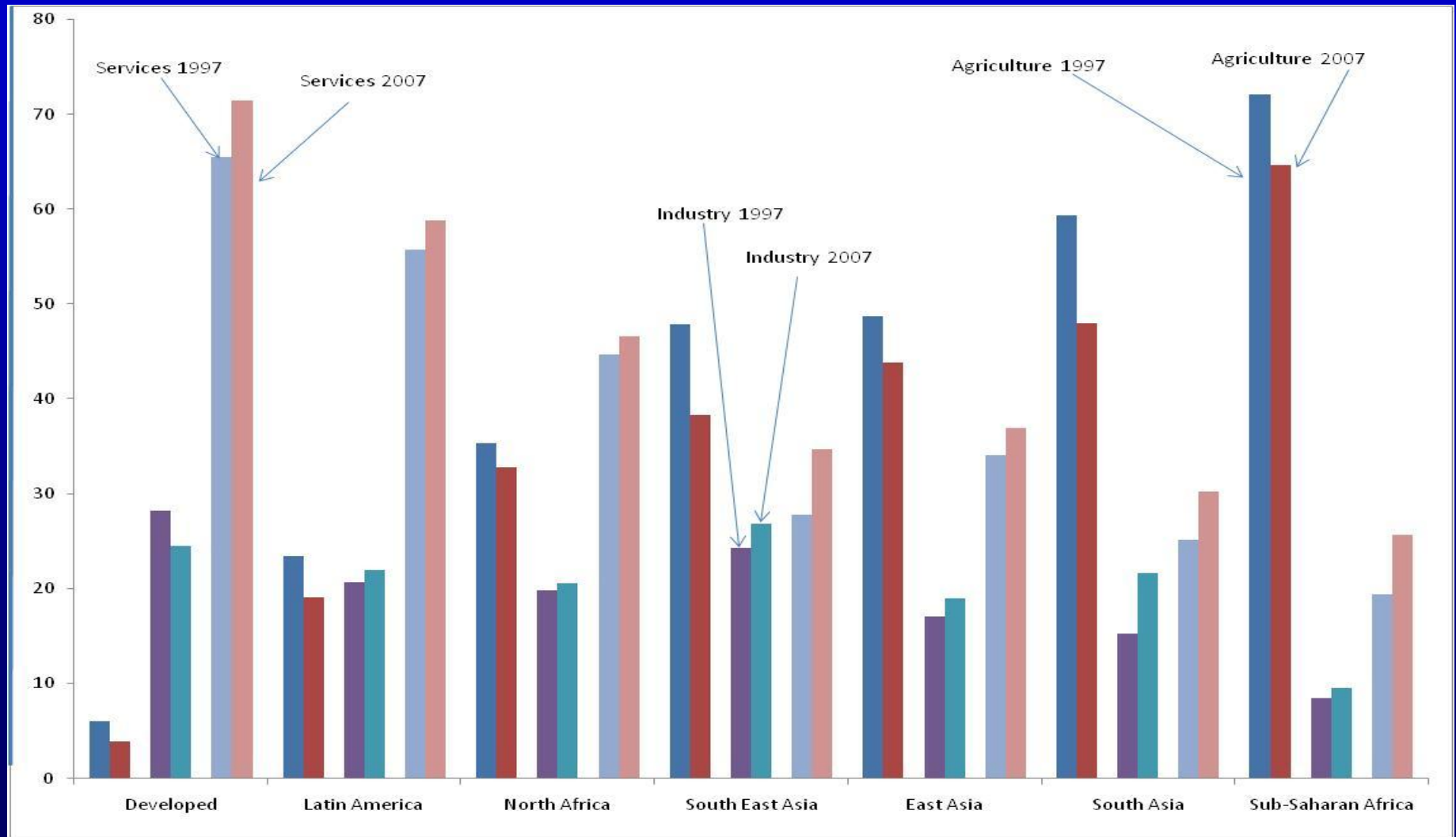
- Productivity growth in services can be higher than in manufacturing
- Many services thought to be non-tradable can now be exchanged across borders
 - banking, insurance, telecomms and also business services, education and health.....
- Technological change important for services
 - Enormous potential for catch-up in Africa
- Significant learning and knowledge spillovers through clustering.
 - easier for of services firms to cluster than manufacturing firms; they require less space and cause less congestion and pollution

Services and poverty reduction

- Water, sanitation, electricity are key services for raising standard of living of the poor
- Telecommunications and transportation link the poor to markets and to a route out of poverty
- Access to finance is essential to allow the transition out of poverty.
- Poverty reduction more strongly correlated with growth of services than with growth of manufacturing
 - Services largest contributor to job creation
 - High employment rates for women

Services drive employment growth

Shares of Employment in Agriculture, Industry and Services, 1997 and 2007



Trade policy in services matters

- Exports of services can diversify exports and be new dynamic source of growth
 - Potential 18 million new jobs in developing countries from offshoring of services (each job generates a further 3 jobs)
- Imports of services and FDI can lead to greater competition, lower prices, higher quality and more variety
 - Impact magnified since services important inputs into production of goods and services
- Openness key element of good regulatory policy and can support achieving public policies (eg education)

Kencall - example of successful African services exporter

- Operational since 2005
- Strong growth - 600+ employees
- High profile clients in East Africa and abroad
- Management team with vast international and domestic experience
- Intense focus on quality
- Established processes and tools
- World-class facility in Nairobi
- Global award winner
 - CCF rated **best non-European Call Center** 2008,
 - KPMG - **Fastest growing Kenyan Top 100 company**



Trade liberalization and competition

- Competition is essential to increase efficiency
 - Competition leads to lower prices+better quality services.
 - Competition pushes service suppliers to reduce waste, improve management and reduce operating costs
 - forces suppliers to pass on cost savings to consumers in the form of lower prices.
 - Competition undermines costly rent-seeking activities
- Use trade liberalization to increase competition and attract FDI
 - Small national markets in Africa cannot generate level of competition needed to drive efficiency and adoption of new technologies.
 - Small size means attracting investment from overseas is important for key infrastructure services.

Trade liberalisation and services

– empirical evidence

- Countries with open financial and telecomms sectors grow faster than countries that are less open (Mattoo et al 2006)
- Greater openness to trade in services enables better exploitation of comparative advantages in labour intensive manufactures (Nordas 2008)
 - In addition to inputs of basic infrastructure services, labour intensive activities require a range of supporting services, such as accounting, legal, marketing and other professional services.
- Trade barriers in services slow down technology diffusion (OECD 2006)

Many services require regulation

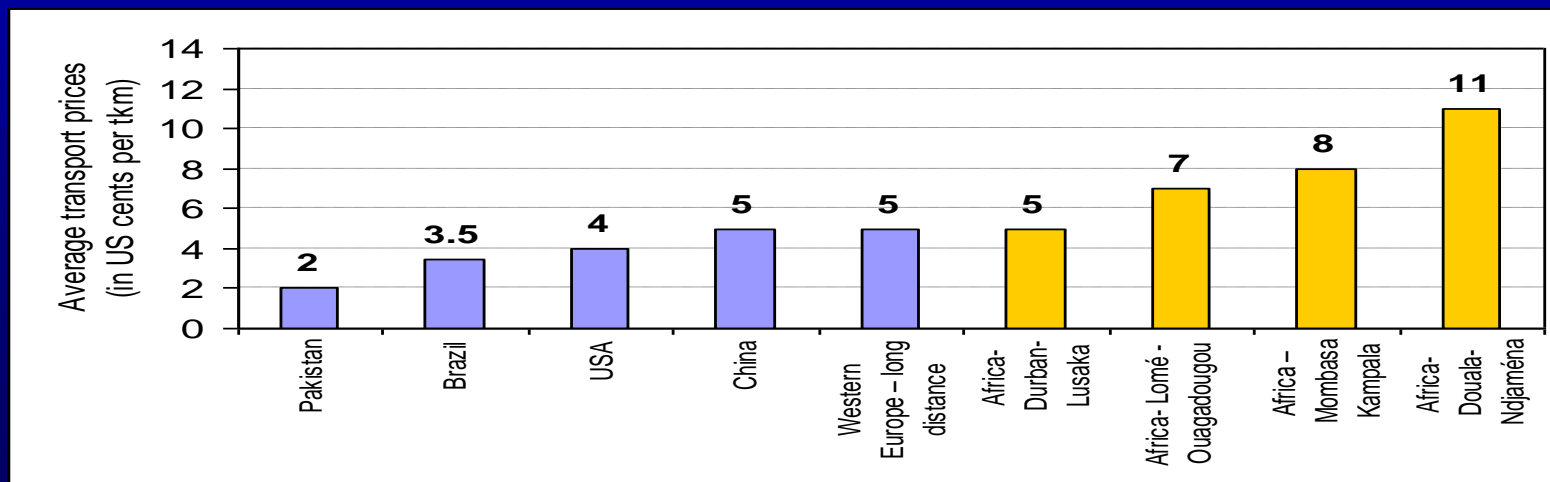
- Market failures in many services sectors can impact on both efficiency and equity.
 - natural monopoly, systemic risks, asymmetric information, and externalities require regulation.
- Example -network and infrastructure industries
 - highly capital intensive with sunk costs, substantial economies of scale can lead to natural monopolies.
 - consumers may need to be protected from abuse of monopoly positions by service providers
 - investors may need to be protected from govts to keep prices at level of operating costs.
 - existing users seek to keep prices low which may come at expense of those not yet connected.

Effective regulation and capacity

- Regulation can be complex
- In electricity need to monitor and consider:
 - *Output and consumption* (access levels, Consumption levels and growth, unsatisfied demand);
 - *Efficiency* (Productivity levels and growth, Cost levels and changes, Capacity and utilization, losses);
 - *Quality of supply* (Continuity, Quality, customer service)
 - *Financial performance* (Financial surpluses and losses, rates of return, indebtedness and interest burden);
 - *Capacity, investment, and maintenance* (Capacity levels and margins , investment , maintenance expenditure);
 - *Prices* (prices and full economic costs, efficiency of subsidies Tariff design and technical and economic efficiency);
 - *Competition* (Well-functioning bid auction markets , Well-functioning and competitive generation and supply markets)
 - *Social indicators* (Affordability especially for low-income consumers, Impacts on development)

Weak regulation leads to less competition and higher transport costs

	Average transport price per ton-km (in US cents)	Average yearly mileage (in kilometers)	Average truck fleet (in years)
Southern Africa (North-South Corridor)	4-5	100,000-144,000	5
West Africa (Lomé-Ouagadougou)	6-8	40,000-50,000	Over 12
East Africa (Mombasa-Kampala)	8	100,000-144,000	7
Central Africa (Douala-Chad)	10-25	60,000-70,000	12

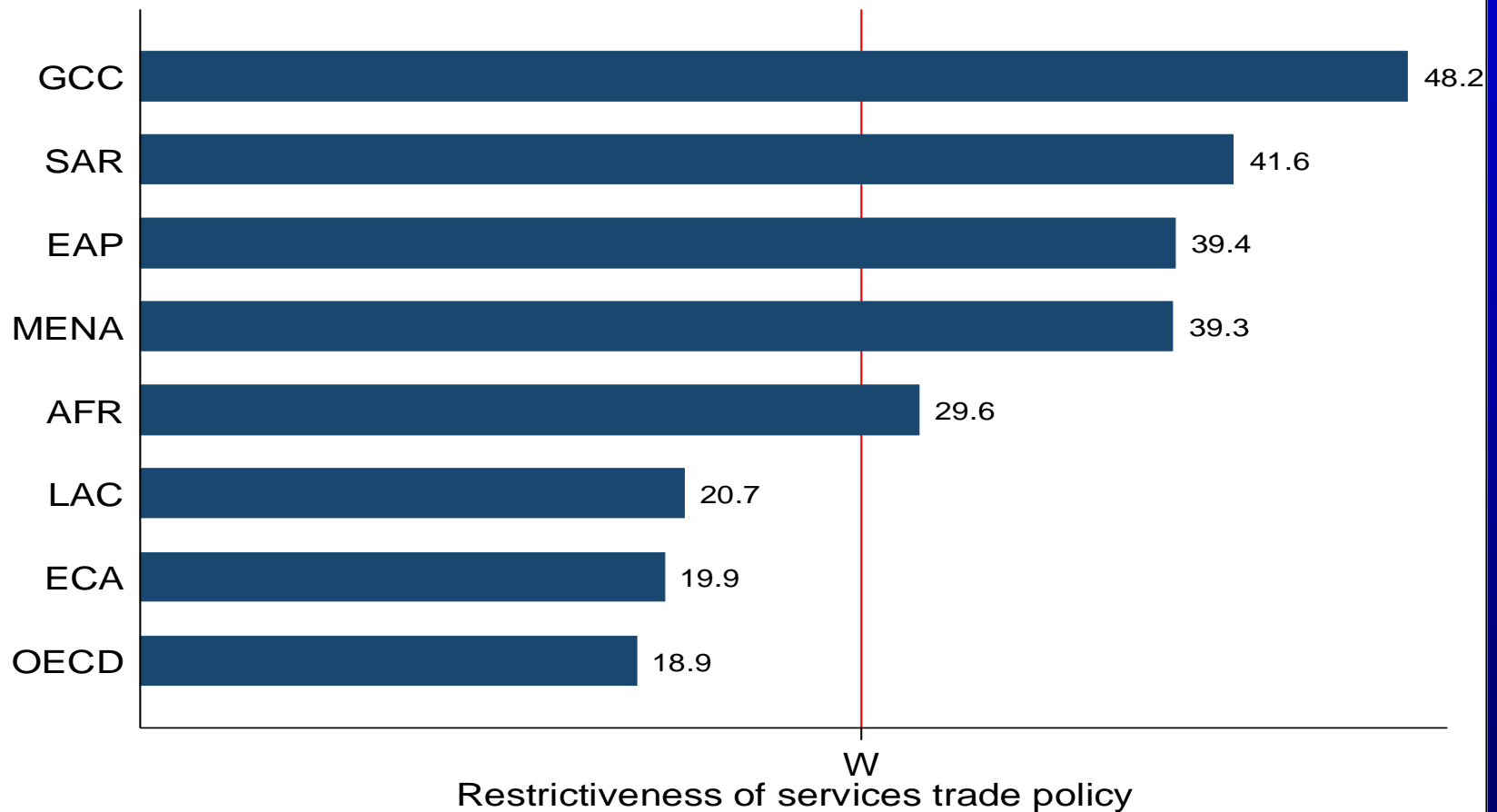


■ Source: "Transport Prices and Costs in Africa", Raballand and Tervaninthorn, (World Bank, 2008)

Coordination of trade and regulatory reform in services sectors

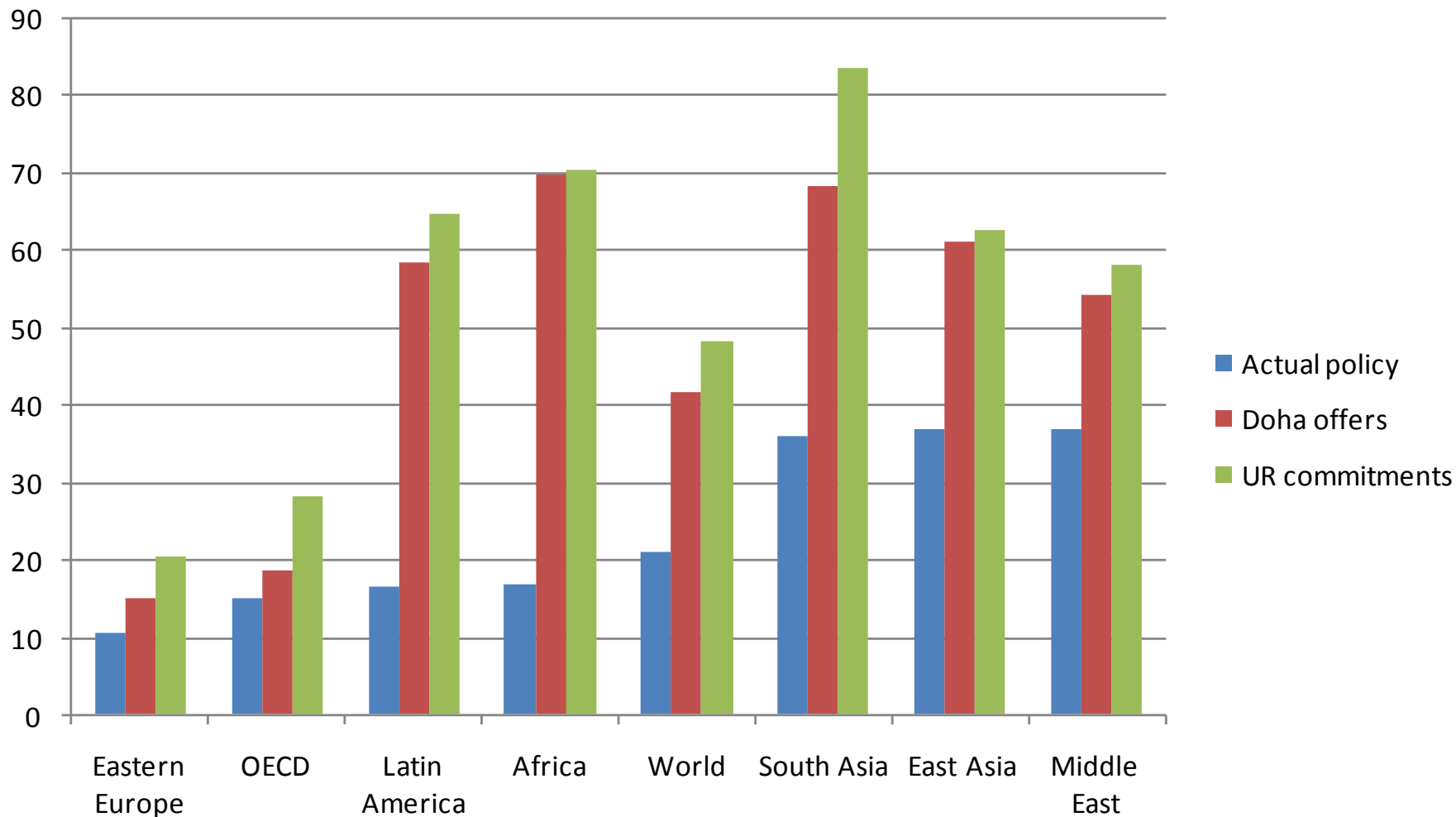
- Appropriate regulations may be necessary to realize benefits of trade liberalization
 - A regulatory framework that emphasizes competition, sound regulation and wider access
 - Trade brings new technology which may require change to regulatory approach
- Trade opening with inappropriate regulations can result in adverse outcomes
 - e.g foreign monopoly
 - But trade opening may be necessary to break regulatory capture that prevents regulatory reform
- Need for capacity to design and implement appropriate regulations and monitor impact
- Trade liberalization and regulation
 - a dynamic process – no strict sequencing

Services trade policies appear to be less restrictive in Africa



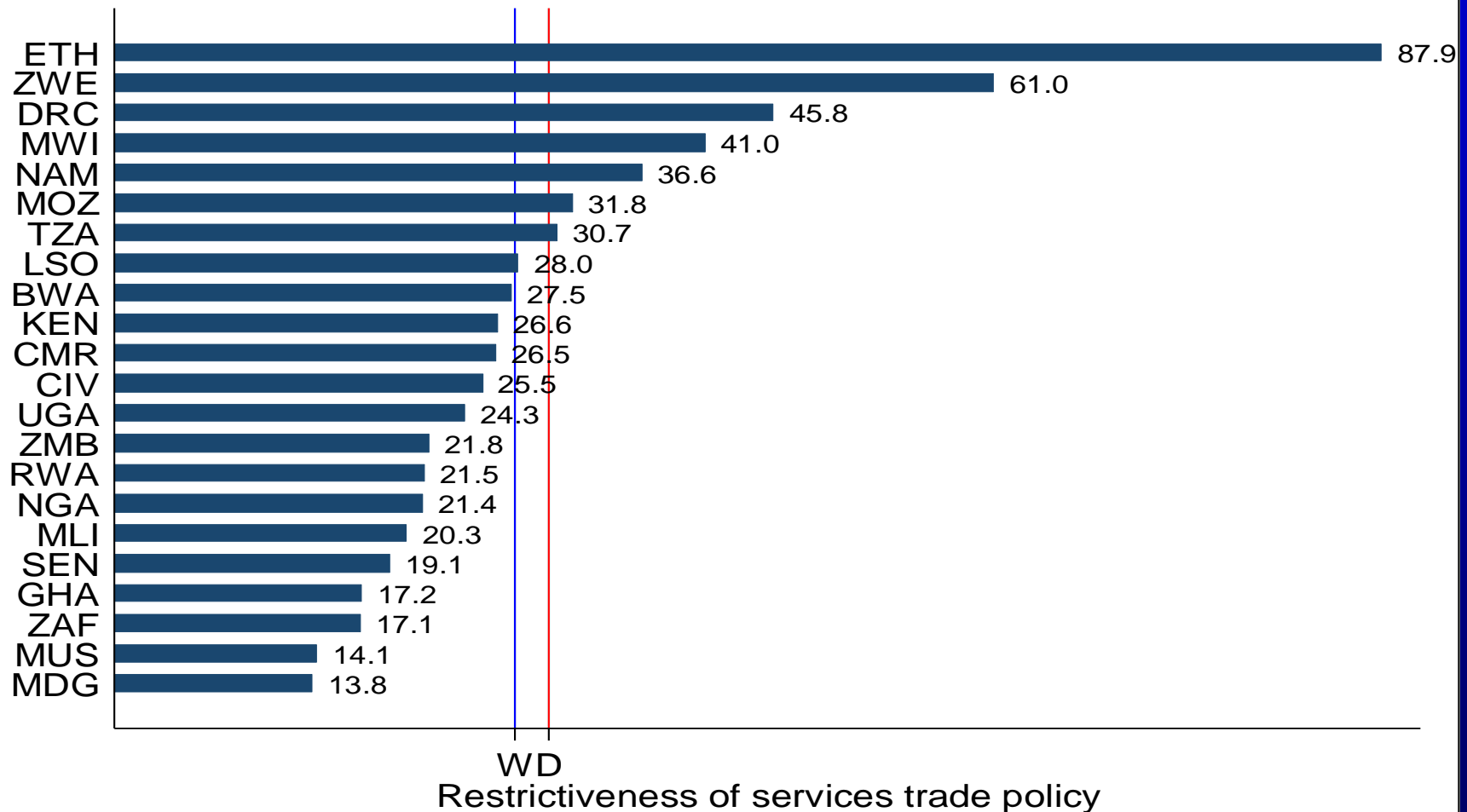
■ Source: Gootiz and Mattoo (2009)

But Africa has not bound this openness at the WTO



■ Source: Gootiz and Mattoo (2009)

Services trade policies vary across Africa



Note: D is average STRI of developing countries, W average STRI of 102 countries

Issues in liberalising trade in services

- Liberalization of Applied Policies and Regulatory Reform
 - Is further reform of applied trade policies required?
 - Is current policy stance on openness credible?
 - Is more pressing need for reform of domestic regulations and regulatory capacity?
- Complementary Role of Trade Agreements
 - GATS may not provide a strong commitment mechanism for small developing countries.
- Complexity of the Reform Process and Capacity Building.
- A Phased Sector-by-Sector Approach to Reform.
 - May need to address political economy issues

Regional integration and services

- Risks from preferential liberalisation – MFN dominates – especially in network industries
 - Preferential liberalisation can be important to allow for learning effects
 - But can give first-mover advantage to less efficient firm
- But potential gains from mutual recognition etc
 - Move faster at the regional level than in EPA or multilateral in sectors with similar standards and regulatory approaches
- Opportunities from regional regulatory cooperation
 - Avoid regulatory capture
 - Can allow for faster reform
 - Pooling of technical capacities for regulation

Enormous scope for further development of services in Africa

- In general, services in Africa are less efficient, more costly, and less widely available than in other regions
- Lack of data on output, production and regulatory policies
- Lack of capacity to design and implement effective regulations
- Key constraint to competitiveness in both goods and services
- How to catalyse coordinated regulatory and trade reform and required capacity building?

What can EPA contribute?

- Provide credibility to reform process
 - May be necessary to encourage FDI
- Improvement in access to EU
 - Especially mode 4 beyond skilled workers
- Provisions on regulatory issues of particular importance to Africa
 - Tourism - Shipping?
- Financial and technical assistance
 - Should not be linked to EPA - Establish fund for aid for services trade
 - Link to outcomes and increase credibility of commitments

Approach for a development-oriented services EPA for Africa

- A coordinated sector-by-sector regulatory-reform/trade-opening process
 - Establishment of a trade reform and regulatory coordinating committee to drive reforms in Africa
- Flexible approach to timing of reforms and a phased strategy towards implementation.
- An emphasis on locking in non-discriminatory liberalization of services imports
- Simultaneous development of regional regulatory cooperation – especially in professional services
- EPA a process not an end-point