



Reflections on the Preferential Liberalization of Services Trade

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Services PTAs: A factsheet

- There were 81 agreements in force before the year 2000
- Only 11 of these covered services
- Since then, 74 of the 147 PTAs agreements in force have involved services
- 62% of services PTAs feature an OECD Member; 13% are N-N, 49% N-S and 38% are S-S – yet 74% of services trade is N-N (no EU-US PTA in services)
- Such trends broadly mirror specialization patterns in services trade





Broad results from literature

- Even as the Vinerian approach to estimating the welfare effects has lesser analytical relevance...
- ...there are lower costs of trade diversion from preferential access than in the case of goods trade
- However, the sequence of liberalization may matter more in services trade esp. in sectors with network externalities...
- ...because location-specific sunk costs of production are important so that even temporary privileged access for an inferior supplier can translate into durable longer-term market advantage deterring future market contestability

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We know little about preferences and their possible erosion in services trade...but preference margins are real (if possibly theoretical)

- The scope for – and political economy of – preference erosion in services trade is understudied and hard to gauge
 - Do PTAs entrench regional preferences or facilitate WTO commitments? (This remains an important empirical question to which the end of the DDA will provide measurable answers)
 - There is considerable “water” both in GATS commitments and the latest DDA offers (This may be entirely tactical and linked to the DDA’s state of play on agriculture and NAMA)

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GATS vs PTAs: Modal Differences in Levels of Liberalization and Margins of Preference

	GATS	DDA Offer (0 to 100)	PTAs	GATS/PTA %	DDA/PTA %	PREF. MARGIN %
Total score	27	34	63	38	54	46-62
Mode 1	24	30	59	41	51	49-59
Mode 3	30	38	67	45	57	43-55
OECD						
Mode 1	43	51	59	73	86	14-27
Mode 3	53	59	67	79	88	12-21
Non-OECD						
Mode 1	18	23	60	30	38	62-70
Mode 3	23	32	67	34	48	52-66

Source : Author calculations based on Marchetti and Roy (2008).




Comparing the level of services trade and investment liberalization across sectors

Sector	GATS	DDA (0 to 100)	PTA	GATS/PTA %	DDA/PTA %	Pref. Margin %
Professional	30	39	67	44,8	58,2	41,8 – 55,2
Computer	55	74	93	59,1	79,6	20,4 – 40,9
Postal/Courier	14	20	53	26,4	37,7	62,3 – 73,6
Telecom	51	58	80	63,8	72,5	27,5 – 36,2
Audio-visual	17	20	50	34,0	40,0	60,0 – 66,0
Construction	40	46	75	53,3	61,3	38,7 – 46,7
Distribution	32	41	76	42,1	53,9	46,1 – 57,9
Education	18	25	57	31,6	43,9	56,1 – 68,4
Environmental	20	30	62	32,3	43,4	56,6 – 67,7
Financial	36	40	53	67,9	75,5	24,5 – 32,1
Health	8	11	34	23,5	32,4	67,6 – 76,5
Tourism	51	61	83	61,4	73,5	26,5 – 38,6
Maritime	12	23	57	21,1	40,4	59,6 – 78,9
Rail	14	20	52	26,9	38,5	61,5 – 73,1
Road	16	18	56	28,6	32,1	67,9 – 71,4
Auxiliary transport	21	24	58	36,2	41,4	58,6 – 63,8

Source: Author calculations based on Marchetti and Roy (2008)



But what about rules of origin?

- The restrictiveness of rules of origin determines the extent to which non-members can benefit from trade preferences negotiated in agreements
- Given that a majority (62%) of WTO-notified agreements involve a developed country member, the majority of PTAs covering services adopt the most liberal (i.e. substantial business operation) rule of origin, with a view to promoting third country FDI inflows into the integrating area and extending the benefits of integration to all investors that are established in one of the PTA Parties. **In such instances, the preferential liberalization of Mode 3 largely approximates MFN liberalization**
- **South-South PTAs make increasing use of the space afforded them under Article V** to adopt more restrictive rules of origin aimed at limiting benefits to insiders (e.g. Andean Pact, Mercosur, ASEAN). The TPP, on the other hand, would adopt liberal RoO given its N-S membership
- Rules of origin targeting cross-border supply (Mode 1) remain largely unaddressed (and weakly enforceable), those on Mode 2 are largely immaterial and rules of origin for Mode 4 trade tend to be highly restrictive, typically bestowing temporary entry benefits only to citizens or permanent residents of PTA partners

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So do preferences really matter? Are they more theoretical than real?

- Feasibility constraints in enforcement-poor regulatory settings – many developing and most least developed countries do not have the regulatory means to enforce preferences, least of all overlapping ones
- The dubious practicality of maintaining parallel regulatory regimes
- Tepid advances can be reported on MRAs in most PTAs. How effectively trade facilitating have MRAs proven to date under AFTA?
- Preferences appear weakly enforceable for many Mode 1 transactions and are of least relevance for Mode 2 trade
- Article V.6 all but multilateralizes preferential liberalization for Mode 3 for N-N and N-S PTAs (these PTAs account for the bulk of services trade)
- Preferences appear most feasibly enforceable where the border matters, such as for Mode 4 trade (but this concerns the smallest share of trade and of commitments, <5%)

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Moreover, some issues are thorny still for PTAs

- **Sensitive sectors tend to be the same across negotiating settings** despite the fact that in almost all instances, PTAs have generated forward movement (especially true of N-S PTAs and those involving the US)
- **Progress on Mode 4 trade remains uneven and generally limited even in PTAs**, though the possibility to contain MFN leakage helps to raise comfort levels at the trade-migration interface (arguably treated more effectively in non-trade bilateral migration agreements, especially for lower-skilled temporary worker movement)
- **Sectors such as land transport/logistics, MRAs in professional services lend themselves more readily and easily to “neighbourhood” approaches**

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Bottom line

- Even as the potential downsides of preferential services liberalization may be less ominous...
- ...preferential access does result in significant first-mover advantages, which can be used to deter entry for more efficient third-party suppliers
- Also, PTAs are here to stay...
- ...even though one cannot deny that the gains from multilateral liberalization are likely to be larger

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Multilateralizing services preferentialism

- Mandating the pursuit of MRAs under the open regionalism logic of Article VII rather than the closed properties of Article V of GATS
- Making preferences in services trade time-bound (with differentiated transition periods by level of development of WTO Members)
- Requiring that any PTA featuring a member that accounts for at least 1% of world trade adopt the most liberal rule of origin for Mode 3 trade
- Showcasing PTAs with liberal denial of benefits provisions as best practice accords
- Negotiating voluntary best practice guidelines for preferential services agreements

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Thank you!

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