

# Services and Development

## The Scope for Special and Differential Treatment in the GATS

Arne Melchior

with contributions by Christopher Stevens and Åshild Johnsen



Norsk Utenrikspolitisk Institutt  
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Norwegian Institute of International Affairs

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## Preface

This report presents the results from a research project undertaken by the Norwegian Institute of International Affairs during 2009–2010, with funding from the Norwegian Ministry of Foreign Affairs. Results from the project have been presented to the ministry at various stages and this report presents an edited collection of the various outputs, including some new material. Hence the report is not a monograph and the chapters can generally be read separately. In the summary, a brief overview of the report is also provided.

At NUPI, Arne Melchior has been the main responsible and project manager, with Åshild Johnsen as Research Assistant during the autumn of 2009. Christopher Stevens, Overseas Development Institute, London, has written Chapter 3 and we thank him for his contribution. Åshild Johnsen contributed to Chapter 2 where she is included as a co-author, and the remaining parts were written by Arne Melchior.

In December 2009, Johnsen and Melchior visited Geneva and had meetings with various developing country representatives as well as staff members from the WTO and UNCTAD. We thank those who spent time sharing with us their valuable knowledge and views. We also thank the Ministry of Foreign Affairs for the financial support, for practical assistance in Geneva and for their comments to material presented from the project earlier. As usual, the responsibility for remaining errors remains with the authors, and the views and assessments are those of the authors and not the Ministry of Foreign Affairs.

Arne Melchior  
Senior Research Fellow and Project Manager, NUPI

## Abstract of policy conclusions

### Based on Chapter 2 and the report in general

While non-discrimination across trade partners is a core principle in the international trading system, exceptions are allowed in some cases (e.g. free trade agreements). For trade in goods, it has also been allowed since 1971 to give better market access to developing countries in order to promote development. In the current negotiation round of the WTO (World Trade Organisation), it has been suggested to introduce similar discrimination for trade in services. A waiver (temporary exemption) from WTO rules may allow discrimination to the favour of the Least Developed Countries. This report examines the implications.

Services can be traded across borders or via FDI or temporary movement of the service providers. In this report, we therefore undertake a study of global service trade flows of all types in order to assess the impact of preferences.

While developing countries are now net exporters of manufactured goods, developed countries have a comparative advantage for services, in the form of cross-border trade as well as FDI. In spite of India's success in information technology services, the export performance of developing countries is generally weaker for services than for goods. The dominance of developed countries is particularly large for skill-based services. LDCs are marginal services suppliers in most areas.

Norway has relatively large services trade due to shipping and imports of business services from Europe, but trade with developing countries is relatively small due to Norway's proximity to and integration with Europe. Registered services imports or FDI from the LDCs into Norway are close to zero.

Due to the limited services trade with LDCs, the assessment of the report is that better market access for LDCs in Norway will have modest economic impact. A possible exception is Mode 4 trade, which may be increased especially if access for less-skilled service providers from LDCs is allowed.

Due to the limited impact of preferential market access for LDCs, Special and Differential Treatment (SDT) should not rely too much on such discrimination, but include other approaches such as trade-related aid. FDI in the tourism sector of LDCs may also help, but this cannot be stimulated by market access in Norway.

Since Norway is a marginal export market for the exports of services from LDCs, the economic impact of a waiver will largely depend in its implementation in large nations such as the USA, or the EU. In the report, we show how the EU has granted better market access to Caribbean countries in one of its recent trade agreements.

Trade preferences for services are technically more complex than for goods and the actual future implementation of a waiver is uncertain. The overall impact of a waiver is therefore difficult to assess in advance, and a waiver should be considered as a temporary experiment in order to develop new ways of promoting development through services trade.

## **Abstract, Chapter 3:**

### **The potential role of services trade preferences in fostering export diversification in low income states**

Preferences for services trade in the WTO represent a new concept where the practices as well as the consequences are little known. Such practices in regional and bilateral agreements on services may therefore provide useful knowledge about how to shape preferences, and their consequences. Chapter 3 therefore examines the recently concluded CARIFORUM-EU EPA (Economic Partnership Agreement), which is the only EPA with a fully developed services agreement.

- Due to their extreme export specialisation, many of the Least Developed Countries (LDCs) have been particularly vulnerable to fluctuations in international markets and the global financial crisis. This has earlier been well known for LDC commodity exporters, but it has recently become clear that vulnerability also applies to services exporters. Some LDCs rely heavily on tourism, which has been hard hit by the crisis. Services trade preferences for LDCs could promote diversification and thereby reduce their vulnerability.
- Trade preferences for services are only effective where trade is impeded by government regulations rather than business practices. Furthermore, qualification or accountability requirements are often motivated by non-trade concerns and therefore not subject to international negotiations or suitable for discrimination across countries. For such reasons, services trade preferences should be more case-specific than for goods, and focus on cases where it is likely that such government measures will generate more exports.
- The services chapters of the CARIFORUM EPA cover 13 non-LDC states. Compared to LDCs, these countries are one step up the ladder and therefore represent a “best case” in terms of services trade potential. The agreement contains specific “positive lists” for each CARIFORUM country with increased market access for specific sectors and modes in services, in addition to some “horizontal” offers that apply to all countries. Commitments also vary across EU members so the agreement is complex with 13x27 schedules.
- For GATS Mode 4, the CARIFORUM EPA mainly provides liberalisation for skilled labour, and the EU has opened 29 sub-sectors for temporary visits of “contractual services suppliers”. There are no quotas or ceilings, but individual EU countries may apply economic needs tests.
- While the economic impact of services preferences is somewhat uncertain and difficult to quantify in advance, such preferences may be a useful supplement to other measures. If such preferences also provide help to conclude the Doha Development Agenda, this would have an additional value which should not be underestimated.



## Abstract, Chapter 4

### Development and comparative advantage in services

Since the purpose of services trade preferences is to promote development and reduce poverty, it is important to know how services trade is related to development. Trade in services takes place according to the four supply modes defined by the WTO, and the analysis therefore addresses FDI and temporary migration as well as ordinary services trade.

- According to WTO data, international trade in goods and services have grown at the same pace during 1990-2008. International FDI has grown almost twice as fast during the same period. Cross-border trade (Mode 1 of the GATS) and commercial presence (Mode 3, including FDI) are the most important modes of supply.
- Rich countries have larger services sectors and are on average net exporters of services as well as net suppliers of FDI. While developing countries have developed a significant trade surplus for trade in goods, they are on average net importers of services as well as FDI. For migration, net flows go in the opposite direction: from poor to rich countries. For services, there is a lot of two-way trade between rich countries.
- During 1990-2007, lower middle income countries had continuous growth in their income levels and their share of world trade, and their trade in goods grew faster than trade in services. The Least Developed countries experienced growth during 2000-2007, and their goods trade and services imports increased considerably. While their exports of goods grew fast, their services exports lagged behind. Probably due to aid, LDCs have relatively high services imports.
- At the more disaggregated level, there are considerable differences across services sectors: Rich countries tend to be net exporters of skill-based services; developing countries do better for passenger travel and tourism; and construction and freight are intermediate cases. The ranking across sectors is mostly similar for LDCs and other developing countries. The notable exception is computer and related services, where India's export success has boosted developing country performance. This is however still the exception rather than the rule. For LDCs, tourism is the most important services activity.
- Developed nations have 80% of outward and 2/3 of inward FDI. LDCs have a significant share of inward FDI but almost no outward FDI. About 2/3 of world FDI is in services, with financial services and business services as the leading sectors.
- Temporary movement (Mode 4 trade) has also increased but current data availability is very limited. Such trade is estimated to represent 1-2% of total services trade but the figure is uncertain. Mode 4 trade is much more restricted than Modes 1-3 and with a more liberal regime, such trade could increase.

## Abstract, Chapter 5

### Norway's services trade and the potential impact of trade preferences

If the scope for trade preferences for services is increased, current trade patterns may indicate where such preferences may be successfully applied if they are to be effective. The analysis below shows that Norway's trade pattern partly conforms to the global patterns shown in Chapter 4. But due to the proximity and integration with Europe, Norway's services trade with developing countries is more limited than for the world at large.

- Norway has traditionally had large services trade, with shipping exports as a driving force. In spite of the rising importance of the oil and gas sector, services trade is still important, with a share of GDP that is higher than for the Euro area.
- Norway is currently a large net exporter of maritime services and other transport and communication services, and a significant net importer of travel services. The USA is a significant market for shipping and 29% of services exports go to North America. For services imports, 80% comes from Europe.
- Norway's imports of services from developing countries is very limited, and large countries such as China, India and Brazil have much lower shares in Norway's imports of services than for goods. According to the data available, Norway recently did not import services from LDCs. Some imports of tourism may however be unregistered.
- At 50%, the share of services in FDI is somewhat lower for Norway than for the world, due to FDI related to oil and gas. Almost all inward FDI was from OECD or Offshore Financial Centres, while 15% of outward FDI was directed to developing countries. There was virtually no inward FDI from LDCs, and the outward FDI to LDCs was mainly related to oil.
- We have no data on Mode 4 services trade, but since current Mode 4 trade is linked to FDI, the FDI evidence indirectly shed light on Mode 4 as well. In addition, we use migration data to illustrate the geographical distribution of migrants. A large share of immigration into Norway is from developing countries, and 14% of the inward migrant stock was from the LDCs.
- Since Norway's registered services imports from LDCs are close to or equal to zero according to the analysis, the short-term material impact of preferential market access for LDCs in Norway is likely to be limited. For Mode 4, there may be scope for an increase if market access is improved for less skilled workers. This is however a politically controversial issue and the impact will depend on the measures taken. In order to help the LDCs develop their services sectors, the analysis suggests that aid and investment will be more important than market access discrimination. Hence a wider perspective on SDT (Special and Differential Treatment) is needed.

## Abstract, Chapter 6

### International Migration, the Least Developed Countries and the WTO

The chapter provides a survey with some new evidence on aspects of international migration. While Mode 4 trade constitutes a very small share of international migration, this broader evidence sheds light on some aspects that are also relevant in the GATS context.

- International migration, especially South-to-North migration of skilled labour has increased rapidly in recent decades and migrants now constitute 9% of the population in the OECD. 44% of international migration is South-South. The poorest countries have lower emigration rates and for the LDCs, 61% of outward migration is to low-income countries. International migration and Mode 4 in the GATS are therefore not North-South issues but global issues.
- Emigration of skilled labour contributes to a “brain drain” but in some cases, the prospect of emigration can lead to more investment in education and the net result may be a “brain gain”. This is more likely for large countries such as India, but for poor countries with limited skills the brain drain can be a real problem. In spite of this, some LDCs consider skilled emigration as a future prospect. For temporary migration, the brain drain problem is more modest.
- According to current practice, GATS covers foreign individuals and foreign firms delivering services, but not foreigners employed by host country firms. There is however some ambiguity in the GATS legal text and a future option is to allow the latter category and thereby recruitment of temporary workers by host country firms. If the LDCs are granted new special provisions in the GATS, one option is to extend the scope of GATS in this way only for the LDCs, in addition to providing more or deeper commitments.
- Temporary migration may easily become permanent and current regimes for temporary migration in the OECD are generally based on strict implementation regimes. These are in several cases based on bilateral cooperation where source countries also have responsibility for screening, return and control. Mode 4 liberalisation without appropriate control regimes is likely to be an illusion, and a waiver should therefore extend flexibilities on implementation and allow bilateral arrangements.



# **1. The Doha Development Agenda (DDA) and the issue of SDT in services: Background and overview of the report**

**Arne Melchior**

The chapter briefly presents the trade policy context of the issues examined in the report, and the content of later chapters.

## **1.1. Introduction: The DDA and services**

The establishment of GATS (the General Agreement on Trade in Services) from 1995 was one of the main achievements of the Uruguay round of the WTO (the World Trade Organisation). GATS secured a new legal framework for services trade and linked it to the common dispute settlement system; and it provided a framework for future liberalisation. In terms of actual liberalisation, the Uruguay Round was less impressive, and most analysis suggests that what was done was more to put on paper the status quo rather than to provide real improvements in market access (for an analysis of current commitments, see e.g. Adlung and Roy (2005)). Recently, Gootiiz and Mattoo (2009) have presented new evidence that compares GATS commitments with current actual market access. According to their analysis; if actual market access is set equal to 1, current commitments are on average at 2.3. For trade in goods, it is well known that WTO tariff ceilings are often far above the currently applied tariffs (so-called “water in the tariffs” in the WTO jargon), and there is apparently a similar slack in the GATS.

Will the “commitment slack” be removed through the DDA? Services negotiations in the DDA have moved slowly and been partly in the shadow of the negotiations on agriculture and goods trade (the so-called NAMA – Non-Agricultural Market Access negotiations) (see e.g. Adlung 2009). According to Mattoo (2005) “The negotiation process has resulted in a low-level equilibrium trap where little is expected and less offered”. Some progress has been made since then. The more recent assessment of Gootiiz and Mattoo (2009) is that the DDA liberalisation prospects can be quantified at 1.9, compared to the figures above.

A general pattern in the GATS is that developing countries have accepted less “commitments” than developed countries. Countries in Asia and the Middle East have the most restrictive current trade policies for services (ibid.); especially for cross-border trade (Mode 1) and commercial presence (Mode 3). For services delivered

through temporary migration, or “movement of natural persons” as it is called in the WTO, most country groups are restrictive.

The asymmetry between developed and developing countries is partly a feature of the WTO rules; developing countries and particularly the LDCs are expected to liberalise less. If trade is good for development, this rule is paradoxical but it is nevertheless one of the “advantages” of developing countries in the WTO as well as the GATS. In the DDA, negotiations have developed on how SDT may be developed further.

## 1.2. New proposals for preferential trade policies

For trade in goods, preferential trade policies for development purposes have been pursued ever since the 1960s, and “Special and Differential Treatment” (SDT) of developing countries has become an accepted policy objective in the WTO. In the current WTO negotiations (the Doha Round or Doha Development Agenda – DDA), SDT is one of the major buzzwords, and one proposal is that preferences for trade in services should be strengthened.

For trade in goods, SDT has been provided in four different shapes:

- *Non-reciprocity* in negotiations; whereby developing countries are allowed to liberalise less than rich countries.
- *Technical assistance*; whereby poorer WTO members are given aid-for-trade (AfT) in order to promote trade, enhance their negotiating capacity or strengthen institutions.
- *Transitional arrangements*; whereby developing countries are given longer time to phase in trade reforms.
- *Preferential market access*; especially in the form of the GSP (Generalised System of Preferences) that was established in the late 1960s and allowed rich countries to have lower tariffs on imports from developing countries.

For trade in goods, all these four types of SDT have been granted and accepted and this is reflected in the GATT Agreement. In the case of services, however, there is no agreement on preferential market access and only the first three types have been provided.

In the field of goods, GATT/WTO negotiations have aimed at sweeping tariff cuts applying to many sectors. For example, the DDA negotiations for manufactured goods aim at cuts according to a formula that would apply equally to all manufacturing sectors. For services, however, market access negotiations are undertaken in a step-wise manner based on requests and offers for particular services sectors and particular modes of supply. In the context of GATS, a fifth type of SDT has therefore been added:

- *Preferential coverage*: In this case, liberalisation for each sector/mode of supply is undertaken without discrimination, but the selection of sectors and modes is made in a way that favours developing countries.

For trade in goods, preferential coverage has not been important as a principle. On the contrary, preferential market access has been partly nullified by adverse selection of sectors. For example, the GSP systems of rich countries have been more limited for textile goods which have frequently been considered as “sensitive” and exempted from tariff reduction. Hence for sectors of particular interest to developing countries, market access has not been better, but on the contrary more limited.

The GATS Agreement refers to non-reciprocity and preferential coverage as well as technical assistance. Article IV paragraph 2 stipulates that increased participation by developing countries in world services trade should be promoted by (i) strengthening their services capacity and competitiveness through e.g. access to technology on a commercial basis; (ii) improved access to information and distribution channels (which may include technical assistance); and (iii) liberalisation in sectors and modes of supply of particular interest to developing countries (i.e. what we have called preferential coverage). Developed countries should establish “contact points” to improve the developing countries’ access to information (IV.2) (also implying technical assistance). With respect to both paragraphs, special priority should be given to the Least Developed Countries (LDCs), and for the LDCs the principle of non-reciprocity is also stated (IV.3).

The implementation of GATS Article IV has however not been fully clear, and this is therefore an issue in the Doha Round. In 2003, a set of guidelines (“Modalities”) were agreed upon regarding how the promised favourable treatment for LDCs should be addressed in negotiations.<sup>1</sup> Non-reciprocity, preferential coverage and technical assistance are again the main approaches. In 2005, the European Communities issued its own statement on LDC preferences in services where these three principles were endorsed. In this context, the EU explicitly rejected the option of preferential market access: “... quotas for LDCs would appear to contradict the principle of MFN treatment enshrined in the GATS”.<sup>2</sup> In 2006, however, the LDCs tabled their own DDA proposal on how to implement Paragraph IV.3 in GATS, including preferential market access.<sup>3</sup> Some countries including Norway have shown sympathy for this idea, but the Doha Round, in particular the services negotiations, have moved slowly so no agreement has been established.

<sup>1</sup> See WTO document TNS/S/13 of 5 September 2003, included in Appendix C.

<sup>2</sup> WTO document TN/S/W/54 of 3 October 2005. MFN = Most Favoured Nation.

<sup>3</sup> WTO document TN/S/W/59 of 28 March 2006, included in Appendix B.

If preferential market access is to be granted to LDCs, it will be contrary to the MFN principle of WTO, and a legal mechanism for this purpose therefore has to be established. For trade in goods, GSP was initially allowed under a temporary exemption from the MFN principle (a “waiver”), and later under the so-called “enabling clause”; a GATT decision from 1979.<sup>4</sup> In the DDA negotiations, a waiver has been proposed and it now seems likely that it will be part of the final result. When Director-General Pascal Lamy of the WTO presented the road map for further DDA negotiations on 24 July 2009, he stated “The implementation of LDC modalities has always been an important topic in the services negotiations and consultations are continuing on an anticipated submission regarding an LDC Waiver mechanism.”<sup>5</sup> A waiver related to services is one of the elements that may contribute to a completion of the DDA, and therefore has significance beyond the direct economic effects that may follow from the waiver itself. Given that a waiver is about to be decided, we examine in this report the potential impact and implementation.

### 1.3. Trade preferences for goods vs. services

The proposal for a waiver for LDCs in the GATS could be seen as a parallel to the early history of preferences for trade in goods: When the GSP (Generalized System of Preferences) was initiated, it implied a violation of the MFN (Most Favoured Nation) principle of the GATT, and a special legal exemption was needed. In May 1971, therefore, the GATT Council decided that “the provisions of Article I shall be waived for a period of ten years” in order to grant tariff preferences in favour of developing countries (GATT 1972, p. 24ff.).

The waiver proposed for the LDCs in GATS is legally a parallel to the GSP waiver in 1971 but there are some differences: The GATT waiver in 1971, as well as the GSP system later, was for developing countries in general while the GATS proposal is only for LDCs. While Special and Differential Treatment exists in the GATS also for other developing countries, the rights under a waiver may not.

Preferential treatment is technically easier for goods tariffs since the MFN barrier is a simple figure: If the MFN tariff is 25%, the GSP tariff can be 10% or zero. Rich countries have also bound most of their tariffs whereas for services, GATS commitments have been made only for a fraction of the sectors and modes. Preferences may then be granted by adding new commitments, and one possible interpretation of a waiver is that more commitments may be given to LDCs. This creates a risk that preferences in services may contribute to a very complex trade system.

<sup>4</sup> “Differential and more favourable treatment, reciprocity and fuller participation of developing countries”, GATT Decision of 28 November 1979, document L/4903, p. 202ff in GATT (1980).

<sup>5</sup> See [http://www.wto.org/english/news\\_e/news09\\_e/tnc\\_dg\\_stat\\_24jul09\\_e.htm](http://www.wto.org/english/news_e/news09_e/tnc_dg_stat_24jul09_e.htm).



If a commitment has been made on an MFN basis, LDCs may be granted a more far-reaching commitment. In some cases this would be clear: For example, if there is an immigration quota, an additional quota could be granted to LDCs, or additional occupations could be added. But e.g. for regulatory issues, it would not always make sense with “deeper commitments”. For example, if a specific education is required for accountants, it would not be plausible to drop this requirement for LDCs. Regulatory barriers play a larger role for services; especially for skill-based services where licensing and qualification requirements are the main barriers. In most cases, SDT in the form of less stringent qualification requirements is not an option that makes sense.

#### **1.4. Overview of the report**

The analysis of services trade preferences is more complex since services trade can occur in different ways, according to the four GATS modes of supply (cross-border trade, consumption abroad, commercial presence and temporary movement of service providers). To the extent that time and statistics allow, the report examines all the four modes:

- Modes 1 and 2 are in principle included in the available statistics on services trade; although it is likely that Mode 2 trade is under-reported. For example, registered services imports from LDCs into Norway are negligible but there may be Mode 2 trade in tourism that is not reflected in the statistics.
- For Mode 3, FDI data capture most of the trade and are also available for services.
- For Mode 4, there is a severe data gap and we have to use round-about ways to address the issues. In current WTO practice, market access has been granted particularly for FDI-related movement of service providers and FDI evidence therefore also tell something about Mode 4 trade, or at least a component of it. The migration literature and evidence also addresses issues relevant to Mode 4, and we therefore also use migration data to shed light on general issues related to Mode 4. In this context, it should therefore be recalled that Mode 4 trade is just a tiny sub-component of migration.

Chapters 4-6 contain empirical analysis of international services trade (Chapter 4), Norway’s services trade (Chapter 5) and aspects of international migration (Chapter 6). To some extent, and particularly in Chapter 6, we also include a survey of relevant literature.

Preferences for services trade in the WTO represent a new concept where the practices as well as the consequences are little known. Such practices in regional and bilateral agreements on services may therefore provide useful knowledge about how to shape prefer-

ences, and their consequences. Chapter 3 therefore examines the recently concluded CARIFORUM-EU EPA (Economic Partnership Agreement), which is the only EPA with a fully developed services agreement.

Each of these four chapters includes an own abstract, and they constitute a basis for the overall policy assessment included in Chapter 2. Chapter 2 draws on the analysis undertaken later and also summarises particularly relevant aspects.

The Appendix of the report includes supplementary material for the different Chapters. Appendix A contains additional statistical tables related to Chapters 4 and 5. Appendix B contains core WTO documents on SDT in the current GATS negotiations. Appendix C includes fact sheets for aggregate services trade as well as 14 sub-sectors, as a supplement to Chapter 4.

## **2. Special and differential treatment in services: An overview and assessment**

**Arne Melchior and Åshild Johnsen**

### **2.1. Introduction**

1. Special and Differential Treatment (SDT) for developing countries has been implemented for trade in goods since the 1960s. This is reflected in the outcome of GATT negotiations as well as the GSP (Generalised System of Preferences). For services, some forms of SDT exist in the current GATS Agreement. In the ongoing WTO negotiations, the Doha Development Agenda (DDA), developing countries have asked for extended SDT and guarantees for its implementation. A waiver (temporary exemption) has been proposed that allows discriminatory market access in favour of the Least Developed Countries (LDCs).
2. LDCs are weak suppliers in many services sectors and one could easily think of forms of SDT that have little effect beyond their symbolic content. For example: financial services are skill-intensive; FDI is a major mode of “trade”; and the LDCs are not significant export suppliers. Providing SDT in the form of preferential market access for LDCs in financial services, FDI would therefore be of modest value. As a principle, SDT should be provided in a way that is feasible, credible and possible to exploit. SDT as mere “symbolic policies” with little real effect amounts to tampering with the global trade system; even with a risk of harming it. A characteristic feature of services trade is that liberalisation has to a limited extent been discriminatory, as has been the case for trade in goods. Introducing more discrimination for services also has a cost in terms of discrimination and complexity, and this cost should be borne only when the gains from such measures are even larger.
3. The question of more development-friendly trade rules for services is one of the issues that have to be solved in order to obtain a successful conclusion of the current WTO negotiation round; the Doha Development Agenda (DDA). If a waiver for services can contribute to concluding the DDA, it will therefore have a development impact far beyond its own field.
4. Services sectors are extremely heterogeneous in several respects: skill levels, modes of trade and linkages to other sectors. In order to provide SDT in a way that is efficient in terms of promoting de-

velopment, one has to consider this heterogeneity (cf. the financial sector example) and the particular characteristics of the main sectors and modes. In the study, we therefore undertake an examination of trade flows, specialisation and modes of supply at the aggregate and partly at the sector level. Since market access discrimination has not yet been allowed at the multilateral level, we also look at regional trade agreements in order to draw on the experience from these agreements, for example with respect to the technical implementation of discriminatory policies.

## 2.2. Comparative advantage and trade in services

5. Services can be delivered via cross-border trade (GATS Mode 1), consumption abroad (Mode 2), commercial presence (Mode 3) and temporary movement of service providers (Mode 4). The analysis of development and comparative advantage has to cover all modes, and we generally do so even if the data availability for Mode 2 and in particular Mode 4 is limited. For this purpose the analysis relies on a number of data sources: We mainly use data from the IMF Balance of Payments (BOP) statistics (for services trade, covering Modes 1 and 2); UN statistics on services trade (for bilateral trade flows); UNCTAD statistics on FDI (Mode 3); supplemented with the World Development Indicators (variables on country characteristics). For Mode 4 we do not have appropriate data but some indirect evidence can be obtained from international migration data, and various databases for international migration are therefore used in Chapter 6. For the study of Norway's services trade, we also supplement with national statistics on services trade and FDI.
6. In the analysis of trade flows and FDI, we split the world into five country groups: EU, other high-income (HIGH), upper middle income (UM), other low and lower middle income (LLM) and LDC. While our main focus is on the LDC group, we also consider whether SDT should discriminate between LDC and LLM. LDC contains 800 million people (12% of the world population in 2008) and LLM 3.8 billion (57%). In terms of population, LLM is five times larger than LDC, and in terms of economics it is nominally about 20 times larger (with variation across variables to be considered).
7. SDT is for developing countries and even if special forms are granted to LDC only, one has to consider the questions of efficiency and equity: the LDC income average is well below LLM, but the latter group also contains many poor countries as well as a large proportion of the world's poor. Based on poverty data available in the World Development Indicators for 2005 or later, we

find that there were 202 million poor (below 1.25\$ a day) in LDC but 766 million in LLM (456 of these are in India). In many sectors, LDCs are weak suppliers and preferences could have greater trade-promoting impact if they were given to countries one step up the ladder. For such reasons, Norway has recently extended her GSP for goods to low-income countries beyond the LDCs. Given that the dividing line is not sharp and its location to some extent arbitrary, an issue is whether provisions for LDCs, at least in the longer run, should be extended to LLM or parts of it. Alternatively, one could think of such measures as special treatment for the very poorest that are eliminated as they become richer.

8. The LDC group experienced significant economic growth since the mid-1990s, with its share of world GDP increasing from 0.64 to 0.82% (nominally) or from 1.07 to 1.39% (PPP-adjusted). Exports of goods (mainly resource- and labour-intensive) grew faster than GDP from 1998 onwards, while exports of services lagged somewhat behind. The LDCs have a particularly high share of world imports of services (see Chapter 4); probably driven by aid money. For example, the LDC share of world imports of construction services grew to a high 6% in 2007 (see fact sheets in Appendix C).
9. The fast recent growth of LLM including China and India is well known and continued the last decade after a slight downturn due the Asian crisis. Also for LLM, goods exports were the “leader” but services exports also expanded. LLM services exports were hit more heavily by the Asian crisis and the LLM share of the world total for services exports is currently somewhat lower than for GDP or goods exports. The statistics used here do not include the recent financial crisis and its adverse impact on trade, especially in 2009.
10. For aggregate services exports (Modes 1 and 2), developing countries are net importers, and developed countries are net exporters. The trade deficit in services is relatively small for LLM and relatively large for LDC. Contrary to this, developing countries now have a surplus for trade in goods. In order to exploit comparative advantage in the DDA, developed countries should also liberalise goods, and developing countries should also liberalise services.
11. A large share of world services exports is in Mode 3 and this trade is not shown in the services trade statistics. For example, almost all trade in distribution services (trade) is via FDI and this significant part of services exports is not shown in trade data. Financial services (including insurance) and distribution have traditionally been sectors where FDI is of major importance, and in recent years

the role of FDI has increased also for other sectors such as other business services, transports and communication. About 2/3 of the world FDI stock in 2007 was in services, and Mode 3 is a major form of services trade. Estimates vary somewhat but suggest that around half of world services trade is in Mode 3. According to UNCTAD (2004), estimates based on foreign affiliate sales indicate that approximately 2/3 of world services trade was FDI-driven by the turn of the century. FDI is even more dominated by rich countries than services trade; with net outflows to developing countries but also large two-way flows between rich countries. The LDC share of outward FDI is extremely low; confirming a low share for LDC in FDI- or affiliate-driven services sales. For inward FDI, however, the LDC share is considerably higher.

12. Analysis of comparative advantage at the sector level reveals that developing countries generally have a low share of exports of skill-based services such as financial services; insurance; computer and information services; personal, cultural and recreational services (including audiovisual services); and other business services. At the other end of the scale we find travel and passenger transports, for which developing countries including the LDC group have stronger export performance. For many LDCs, tourism has been a successful activity and a major foreign exchange earner. A particular feature of tourism in some LDCs is that it is not a narrow and sharply delineated sector, but has linkages to a number of other services sectors such as transportation, hotels and restaurants etc. For tourism, a lot of foreign trade is in Mode 2 but FDI may also play a core role for related sectors. The quality of roads and infrastructure is also important.
13. Compared to LDCs, the ranking of sector export shares is to a large extent similar for LLM; but with a notable exception: The top ranked sector is computer and information services, with an LLM share at 23% of world exports. This is mostly (or 87%, to be exact) driven by India's success in this sector; where India is the world's largest exporter. Exports of computer services are therefore not generally spread out among the LLMs; it is as yet an exception. The general pattern is more similar to the LDCs but one step higher in terms of world export shares and performance. Travel, communication and transports are also in this case in the top of the ranking, and the bottom sectors are the same as for LDC (finance, insurance, personal services, other business services). LLM had a share of inward FDI larger than its share of world nominal GDP (12 against 10% in 2005), but China absorbed about 2/3 of this so again it did not apply generally to the LLM group. For the group as a whole, performance was weaker in the high-tech or FDI-driven services sectors.

14. The analysis of comparative advantage shows that with some exceptions, LDCs are marginal suppliers in international services trade. Other developing countries are also net importers in most service sectors, but have a stronger supply capacity. If preferential market access for services is extended beyond LDCs, the economic impact could be larger.

### **2.3. Norway's services trade**

15. Norway's services trade is generally in line with the global pattern, but with some modifications. Norway has relatively large services trade (Modes 1- 2) due to shipping exports and imports of various business services from Europe. Due to the proximity to and integration with Europe, however, the share of developing countries in Norway's services trade is lower than in world trade. This pattern is repeated for FDI, where inward FDI is mainly from the OECD and Offshore Financial Centres. 15% of outward FDI is in developing countries.
16. According to the available services trade and FDI data, Norway's registered imports of services from LDCs are at zero. This limits the potential impact of preferential market access and suggests that SDT in services has to include other approaches as well. There may however be imports of tourism from LDCs that are not captured by current statistics.

### **2.4. Services trade: Modes of trade, and regulation**

17. The analysis above has already shown that poor countries have a particular profile with respect to modes of services trade: They had lower shares for FDI-driven services trade (Mode 3), high shares for some sectors dominated by consumption abroad (Mode 2, travel and partly passenger transports), and a mixed pattern for cross-border trade (Mode 1). Mode 4 (temporary migration) constitutes a very small fraction of world services trade (1-2% according to some estimates). Modes of trade are however affected by technological developments as well as barriers to trade, and one argument related to Mode 4 is that it is small precisely because it is generally not allowed. Trade is also affected by technological change: The outsourcing of computer and business services to India is made possible by better information and communication technologies. The ICT revolution generally reduces the need for physical proximity in production and consumption processes, as illustrated by electronic trading and exchange of information.
18. For a number of services sectors, explicit "prohibitions" or barriers to trade are not the main barriers but international trade can be se-

verely limited by differences in regulation. Financial services, insurance and professional business services are examples of sectors where licensing, qualification requirements and other regulations play a major role and where international liberalisation is technically demanding. Two countries may for legitimate reasons have different regulations, and this difference may reduce trade even if there was no explicit intention to do so. The experience from the European internal market shows that the process of reconciling different services regulations is difficult, even among the like-minded. For the WTO, it is generally unrealistic to pursue harmonisation on its own, but in some cases the matter can be facilitated if strong international standardisation organisations exist in the particular area in question. In that case, the WTO can agree to adhere to the international standards. This principle has also been successfully implemented for trade in goods, where e.g. Codex Alimentarius standards for food are *de facto* implemented in some cases. In the GATS, work on regulation is important in several sectors. An example is accounting services. If regulatory differences constitute the main trade barrier, it goes without saying that preferential market access may be difficult to implement: should accountants from LDCs be allowed to have less education?

19. Due to the complexity of regulation in some types of services, poor countries are sometimes at a disadvantage due to the weakness of their institutional capacity. It is difficult to measure the average complexity, restrictiveness or quality of a country's regulatory regime. The World Bank's "ease of doing business" index has recently become available for many countries. This indicator is strongly correlated with income, so doing business is inherently more difficult in the poorer countries. This is an indication that the regulatory environment in poor countries limits trade in services sectors that rely more on regulation. This may contribute to explaining why finance and business services are on average weak performers in LDC as well as in LLM countries.

## 2.5. Temporary movement of services providers

20. Mode 4 liberalisation is currently limited in GATS and one of the difficult issues of the current negotiations. Mode 4 commitments in GATS have mainly been related to FDI and to skilled labour; by allowing business visitors, professionals and intra-company transferees. Developing countries have suggested that Mode 4 commitments are de-linked from FDI and extended to less skilled labour categories. Given the political controversies about migration, developed countries have so far been reluctant. According to some observers, progress on the issue is critical for the overall balance of the DDA negotiations (see e.g. Gootiiz and Mattoo 2009).



21. Mode 4 trade constitutes a very small share of international migration, but evidence on international migration nevertheless sheds useful light also on some aspects of Mode 4. International migration, especially South-to-North migration of skilled labour has increased rapidly in recent decades and migrants now constitute 9% of the population in the OECD. In spite of this, almost half of international migration is still South-South. Also for Mode 4 movements, it is likely that local migration between developing countries will remain an important element. All trade has a “gravity factor” with a strong role for geographical proximity, and for a construction firm in Bangladesh, work in Kolkata is in most cases likely to be more relevant than missions to Norway.
22. While South-North migration is driven by income gaps, the emigration rates are not highest when the income gap is largest but at intermediate levels: The poorest countries have lower emigration rates than the second poorest and for the LDCs, a large share of outward migration is to low-income countries. So even for Mode 4 trade, the implication may again be that the supply capacity of LDCs is more limited than for countries one step up the ladder.
23. Emigration of skilled labour contributes to a “brain drain” but in some cases, the prospect of emigration can lead to more investment in education and the net result may be a “brain gain”. This is more likely for large countries such as India, but for poor countries with limited skills the brain drain can be a real problem. The state-of-the-art conclusion is that brain drain is a problem for small and poor countries if the emigration rate for skilled labour is too high. This is relevant in the Mode 4 context even if temporariness partly eliminates the risk. For this reason, it might sometimes be useful to consider Mode 4 movement as an element in the human capital development of poor countries rather than as an end in itself. Some LDCs consider skilled emigration as a future prospect and are not worried about the brain drain. For temporary migration, concerns for brain drain are less serious.

## **2.6. Discrimination in services: experience from regional trade agreements**

24. In the literature on services, a general argument has been that liberalisation has only to a limited extent been discriminatory. There are various reasons for this: A major reason which is frequently forgotten is that the OECD contributed to services liberalisation among rich countries from the 1980s<sup>6</sup> and by 1995, this liberalisa-

<sup>6</sup> Through the OECD Code of Liberalisation of Current Invisible Operations, see [http://www.oecd.org/document/63/0,3343,en\\_2649\\_34887\\_1826559\\_1\\_1\\_1\\_1,00.html](http://www.oecd.org/document/63/0,3343,en_2649_34887_1826559_1_1_1_1,00.html).

tion had advanced quite far. Preferential trade agreements (PTAs) between rich countries have, even when services were included, not proceeded too far beyond the OECD regime. A reason is that further liberalisation is difficult since regulatory issues may be difficult to handle. An example is the financial liberalisation in the EU internal market, which is still far from complete in spite of serious efforts to this effect over two decades.

25. During the last decade, regional trade integration has however expanded strongly beyond OECD countries, and this creates a greater scope for discrimination in services trade. A number of new RTAs covering services have been negotiated, and an examination of these shows that they go far beyond GATS, by including more sectors and new liberalisation commitments (see e.g. Marchetti and Roy 2008). Some countries even liberalised “sensitive” sectors such as education or audiovisual services, for which liberalisation in the GATS is difficult to achieve. Hence one experience from PTAs is that they make it possible to agree also in difficult areas which are notoriously challenging in the WTO context with its 153 members.
26. According to the literature, another reason why services liberalisation is not strongly discriminatory has been liberal rules of origin (RO). Rules of origin define the country of origin for goods or services and thereby determine whether they are entitled to lower tariffs or other trade preferences. For trade in goods, the ROs define what kind of physical transformation or value increase or change of product classification that is necessary if a product is to be considered as originating from a certain country. In the field of services, other types of rules are needed: since services are non-tangible, the rules have to relate to the service provider rather than the product. The major distinction is then whether the RO is based on (i) location or (ii) ownership or control. If location is sufficient, the RO is liberal and a trade preference may be exploited by establishing an affiliate in the country in question. For example, some PTAs use the criterion of “substantive business operations” and then foreign-owned companies may also benefit from preferences. At the other end we find e.g. the Thailand-Australia PTA, where Thailand only grants preferences to companies that are “owned and controlled by Australian persons” (Fink 2008). The “substantive business operations” rule is actually written into GATS (jointly with the requirement of being a judicial person of the country, in Article V:6 of the GATS) and this may explain why many PTAs have liberal ROs that limit their discriminatory impact. This applies to Modes 1 and 3; for Mode 4 the matter is less complicated since persons are not “multinational” like companies.

For Mode 4, nationality – and in the GATS also permanent residency – is the main RO criterion.

27. On the whole, the recent wave of PTAs covering services adds liberalisation and some more discrimination to the world trade system for services. The extent of discrimination is however still limited due to previous OECD liberalisation as well as liberal ROs in most cases.
28. Chapter 3 in this report illustrates forms of providing services preferences for developing countries. EU liberalisation in the CARIFORUM EPA agreement is mainly for skilled labour, but illustrates that there is a menu of options for gradual liberalisation. Interpreted as a supplement to other measures, such trade preferences can be beneficial even if their economic impact for the very poorest countries turns out to be limited.
29. For Mode 4, discrimination is possible and since liberalisation is very limited in the GATS as well as the OECD, new PTAs could in principle add a new dimension to the issue. Some PTAs include Mode 4 liberalisation beyond the GATS: Examples of agreements such as these are provided by Chanda (2009), who investigates temporary cross-border movement of less-skilled service providers in two specific bilateral agreements (Spain-Ecuador and Canada-Mexico, respectively). These agreements exemplify possible ways of managing temporary migration that ensures temporariness and mutual benefit for both parties. These agreements establish quotas for migrant workers and specify the number of admitted workers; their categories of workers, scope of work and other conditions related to employers and workers. Temporariness is defined in detail, including provisions on possible renewal and extension. The agreements also cover wages and working conditions for the migrants, and give preferences to local workers to ensure local support. Administrative mechanisms for recruitment and entry are established and defined. An important feature of these agreements is flexibility in design and implementation, in the sense that the agreements are adjusted to local labour markets and conditions. The enforcement of the contracts is ensured through incentives (possible for the workers to return if they comply with regulation) and disincentives (not returning withheld wages and other sanctions). Support for the agreements is ensured through a broad-based stakeholder participation in designing the framework. Importantly, enforcing the agreements depends upon good coordination and cooperation between departments, ministries and agencies involved both within and across the countries. Furthermore, regulation and mechanisms protecting the workers' rights and interests are necessary in both host and source country. Finally, the agree-

ments must cohere to national laws on migration, taxation and other regulations. In the case of Norway, the recently adopted immigration act includes a “carve-out” for international treaties and also includes special provisions for temporary or seasonal migration.

## **2.7. SDT in services: A menu of options**

30. How could LDC development be promoted by means of SDT or other measures related to services trade? SDT can be provided in different forms. In the analysis, we distinguish between (i) non-reciprocity in negotiations – whereby LDCs or developing countries are expected to make fewer market access commitments; (ii) aid for trade (AfT) which has been an important part of the DDA agenda; (iii) longer transition periods for implementing liberalisation, which have been used in earlier WTO rounds and may be used again; (iv) preferential market access which is still not allowed for services but proposals are on the table; and (v) preferential coverage, whereby MFN liberalisation is undertaken particularly for services that are exported from LDCs or other developing countries. One might even add (vi) general aid to education, infrastructure or other purposes that are particularly relevant in the context of services. In DDA there is disagreement about (iv) but the other forms of SDT are generally accepted (although (vi) would generally be outside the realm of WTO negotiations).

### **2.7.1. Non-reciprocity and transition periods**

31. Non-reciprocity in negotiations applies to goods as well as services and can be measured by the extent of market access commitments made by rich and poor countries, respectively. Analysis of the Uruguay Round outcome confirms that developing countries made fewer commitments and this is in conformity with the non-reciprocity principle. In a setting where WTO proponents teach the virtues of free trade as a lever for development it is indeed a paradox that favourable treatment is implemented as the right to have less trade. This outcome however corresponds to the mercantilist logic of WTO negotiations: increasing your own openness is bad, but market access abroad is good. Luckily, this thinking is rescued by the new trade theory which generally tells that trade is good but liberalisation should be two-way: in the presence of scale economies and imperfect competition, an element of mercantilism makes sense. This applies to the pure model of trade with scale economies, and the result can be modified if concerns for technology transfer are added: If technology is transferred via trade, the gains from protection are reduced or eliminated. For services, mercantilist thinking is further weakened due to the strong input-

output effects for infrastructure services such as transportation, communication, finance, insurance and trade. Efficiency in these sectors spills over to the rest of the economy since they are inputs in production as well as consumption activities. For example, the expected gains from the EU internal market were particularly strong for services, due to the indirect impact on other sectors. For the LDCs and LLMs, an implication is that GATS liberalisation is relevant not only for the top-ranked sectors where their exports are relatively large, but also for the less competitive sectors at the bottom of the graph, which matter greatly for the overall performance of their economies. If liberalisation through GATS can improve their performance, it has a value beyond the mercantilist calculus.

32. Whereas the arguments above weaken the case for non-reciprocity in services, other aspects work in the opposite direction: Liberalisation is not always appropriate for services and this is linked to development. For example, it is widely acknowledged that financial liberalisation should not be undertaken unless a country has an appropriate regulatory regime in place, and poorer countries have greater difficulties in this respect. Liberalising banks should not be exchanged for exports of T-shirts; financial liberalisation has a systemic impact which is different. Liberalisation is in principle a good thing, but not at all times, and not without preconditions. Non-reciprocity may be used in order to take into account such regulatory concerns, and make sure that poor countries are not pressurised into premature liberalisation. It is legitimate to consider the sequencing and wait if necessary. Non-reciprocity should however not be exaggerated to the extent that too many WTO countries become B-members with blanket exemptions from main policy decisions. In the longer run, this will certainly undermine the WTO.
33. Transition periods were used extensively in the Uruguay Round but a criticism has been that such measures were temporary and had the main purpose of sweetening pills that developing countries were not really prepared to swallow. In order to avoid such a feeling of deceit, it is important that transitional arrangements are given an appropriate motivation in terms of alleviating structural transformation or safeguarding the need for gradual reforms. Transition periods make sense in this light: For example, countries may need to develop regulations and standards parallel to liberalisation and should have time for that (cf. the example of financial services). If liberalisation is expected to lead to substantial job losses in particular sectors, this is also a legitimate reason for transition periods, and such periods could then be supplemented with AfT for relevant purposes.

### 2.7.2. Preferential coverage: Sectors and modes

34. In the GATS, the principle we have called “preferential coverage” has been established as a form of SDT: Even if market access discrimination between suppliers continues to be prohibited, MFN liberalisation could be undertaken especially for sectors and modes of particular importance to developing countries. Is this feasible or an illusion?
35. With respect to sectors of particular interest to poor countries, the experience from goods trade suggests that preferential coverage will not be easy to obtain. For trade in goods, one had de facto the reverse phenomenon: GSP tariff reductions as well as MFN tariff cuts in rich countries were frequently more limited for the so-called “sensitive sectors” – which happened to be sectors of particular interest to developing countries (e.g. textiles, agriculture and fish in the EU). For services, the situation is different since some of the most simple and labour-intensive services can never be traded unless we allow migration: Haircuts cannot be done online. It also seems that some sectors for which the developing countries perform above average, are among the less protected. For example, tourism is considered to have a more liberal trade regime; maybe because consumption abroad is something that few countries aim to restrict. In most services sectors, rich countries currently have a large share of world exports (see fact sheets), and it would not make sense to halt liberalisation in order to maintain preferential coverage. In terms of sector focus, it therefore seems that the principle of preferential coverage is of limited value.
36. The most serious issue in terms of “preferential coverage” is therefore about modes rather than sectors, and about Mode 4 in particular: Liberalisation in Mode 4 is more limited and the developing countries are pushing for liberalisation. Allowing for temporary migration could make it possible for more advanced developing countries to exploit wage differentials for skilled labour, and it would allow all developing countries to undertake low-skill services production in selected areas. In Europe, for example, there is considerable temporary migration for seasonal work in agriculture, and these workers could be replaced by migrants from Sudan or other countries in LDC and LLM, where there are 4.6 billion people to recruit from. In principle, such migration could lead to economic gains to exporting as well as importing countries, and increased remittances. On the other hand, there might be substantial implementation problems related to illegal migration, and for skilled labour the brain drain issue would be present if migration becomes permanent or recurrent. We will revert to these issues in the later analysis.

37. For the other modes, services exports from FDI-driven or skill-based sectors are dominated by rich countries, but developing countries gradually increase their interest in the field. As noted, Mode 2 is considered as fairly liberalised. In Mode 1 there are barriers in activities related to tourism; e.g. air transports are partly exempted from GATS and this limits the development of tourism in some poor countries.

### **2.7.3. Discriminatory market access: A new waiver?**

38. In the GATS, all liberalisation so far had to be non-discriminatory, i.e. on an MFN (Most Favoured Nation) basis. Along with the initial approach for trade in goods, a waiver is now being proposed that will allow explicit discrimination to the favour of LDC countries. The proposal only encompasses the LDCs, and not developing countries in general. It is not clear whether this should be considered as a temporary approach (extension to LLM may be suggested later, and LDC may be the door opener), or a permanent solution. The LDCs themselves would probably suggest the latter but other developing countries might wish to obtain such preferential treatment later.

39. Discriminatory market access is possible for Mode 4: If quotas for temporary migration of less skilled labour from LDC are established, increased trade will be the result. In the WTO it is generally acknowledged that liberalisation in Mode 4 is a politically sensitive issue so the expectation is hardly massive liberalisation but some steps that gradually open this door.

40. Trade policy discrimination is easy in the case of tariffs for goods, where the rate may be set lower for developing countries. For services, this is more complicated and for some sectors and modes, discriminatory market access may be a non-feasible approach. For example: Discriminatory market access in tourism is mainly non-feasible; rich countries cannot limit travel to non-LDC countries. In some cases, regulation constitutes the main barrier and discriminatory regulation generally makes little sense: banks from LDCs should not have lower capital adequacy requirements.

41. The study of comparative advantage in services generally confirms the weak supply capacity of LDCs. Discriminatory market access for Modes 1, 2 and 3 will therefore have limited economic impact. In some cases, it may also be questionable from a perspective of equity or efficiency: Should FDI commitments be granted only to those who cannot exploit them? Some possibilities nevertheless exist and a waiver could be used as an experiment to find possible ways of implementation. SDT should however not rely too much

on discriminatory market access, but be combined with aid, investment and other efforts to promote the development of the services sectors of the LDCs. If preferential market access is granted to LLM countries as well, the argument of limited supply capacity is invalidated and such policies could have a stronger impact.

#### **2.7.4. Mode 4 market access for LDCs: Some further issues**

42. According to current practice, GATS covers foreign individuals and foreign firms delivering services, but not foreigners employed by host country services firms. There is however some ambiguity in the GATS legal text and a future option is to allow the latter category and thereby recruitment of temporary workers by host country firms. If the LDCs are granted new special provisions in the GATS, one option is to extend the scope of GATS in this way only for the LDCs, in addition to providing more or deeper commitments.
43. Temporary migration may easily become permanent and current regimes for temporary migration in the OECD are generally based on strict implementation regimes. As noted above, these are in several cases based on bilateral cooperation where source countries also have responsibility for screening, return and control. Mode 4 liberalisation without appropriate control regimes is likely to be an illusion, and a waiver could therefore extend flexibilities on implementation and allow bilateral arrangements.
44. A major distinction is whether Mode 4 market access should also be given for less skilled labour categories. Mode 4 commitments in GATS may either be horizontal (across sectors), or defined in terms of specific professions and level of skills. The Uruguay Round was meant to cover mainly two categories of natural persons: (i) intra-company transferees, “essential personnel” (management, professionals, skilled staff), and (ii) business visitors with short-term presence, but generally not employed by the host country (see e.g. Karmakar 2008). Extending Mode 4 is one of the main demands of LDCs. In the GATS negotiations, they have focused on four categories: (i) independent professionals, (ii) business visitors, (iii) contractual service suppliers and (iv) others. The most controversial request concerns the fourth category, which includes unskilled labour. The EU responded in 2005 that their offer would not be extended to non-professional (i.e. low-skill) service suppliers, arguing that most low-skilled service providers do not provide services under contract or on a fees basis in the way intended by Mode 4. In this understanding, “lower skilled workers generally provide their services by direct recruitment on the employment market”, to which the GATS does not apply. The EU



was however willing to commit on some of the categories of service suppliers not linked to commercial presence (contractual service suppliers; independent professionals; graduate trainees).

## 2.8. Trade-related aid for services development

45. Alternative to discriminatory trade measures, development of the LDC services sectors could also be promoted by aid. AfT has become more important during the DDA negotiations and an increasing share of AfT (currently above  $\frac{1}{4}$ ) is directed towards the LDCs. Some AfT is provided by the WTO and specialised agencies such as IF (the Integrated Framework), but the major share is given bilaterally or through multilateral institutions. The World Bank has worked to “mainstream” trade policies and AfT into the poverty reduction strategies of poor countries. Some AfT is specifically related to export promotion and trade capacity building; so-called *trade-related technical assistance and capacity building*, whose share of total aid has increased.<sup>7</sup>
46. Such “narrow” forms of AfT may also be provided for services but our view is that in general, the LDC problems with slower growth in services exports are deeply rooted. These are development problems that cannot easily be solved by means of export promotion or other trade-specific remedies. Providing export promotion assistance to LDC banks will not help too much: it may be better to provide aid for education, financial regulation or institution building. The tourism industry in LDCs can be supported with narrow AfT but it depends on infrastructure and development in a much broader sense. Such broader aid is beyond the scope of the WTO but may be of great importance, especially for the poorest countries.
47. It is likely that some of the “consumption abroad” in LDCs as well as their imports of services are driven by aid and this shows that aid probably has a significant influence on the services sectors of LDCs. AfT for tourism may indirectly increase the Mode 2 exports of services from LDCs further, and other options could be considered (such as health stays).

## 2.9. Concluding comments

48. On the whole, the analysis suggests that discriminatory market access for LDCs may play some role, but a limited one due to the weak supply capacity of LDCs. This is particularly clear in the

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<sup>7</sup> For an overview of AfT up to 2006, see Melchior, A., 2007. Aid for Trade and the Post-Washington Confusion, NUPI Working Paper No. 715, available on [www.nupi.no](http://www.nupi.no).

case of Norway, where current registered services imports or inward FDI from LDCs are zero or close to zero. If Mode 4 market access is extended to less skilled labour categories, the scope for trade seems greater. This raises a number of implementation and control issues but methods exist for solving them if the political willingness is present.

49. Due to the limited potential impact of market access discrimination for LDCs, SDT in services should not rely mainly on such policies but include other measures such as trade-related aid.

For other developing countries, trade policy discrimination could have a greater economic impact. The scope for such policies is nevertheless more technically limited than for goods tariffs: for qualification and accountability requirements in services, discrimination across trade partners rarely makes sense.

### 3. The potential role of services trade preferences in fostering export diversification in low income states

Christopher Stevens\*

#### Abstract

Preferences for services trade in the WTO represent a new concept where the practices as well as the consequences are little known. Such practices in regional and bilateral agreements on services may therefore provide useful knowledge about how to shape preferences, and their consequences. This Chapter therefore examines the recently concluded CARIFORUM-EU EPA (Economic Partnership Agreement), which is the only EPA with a fully developed services agreement.

- Due to their extreme export specialisation, many of the Least Developed Countries (LDCs) are particularly vulnerable to fluctuations in international markets and the global financial crisis. This has earlier been well known for LDC commodity exporters, but it has recently become clear that vulnerability also applies to services exporters. Some LDCs rely heavily on tourism, which has been hard hit by the crisis. Services trade preferences for LDCs could promote diversification and thereby reduce their vulnerability.
- Trade preferences for services are only effective where trade is impeded by government regulations rather than business practices. Furthermore, qualification or accountability requirements are often motivated by non-trade concerns and therefore not subject to international negotiations or suitable for discrimination across countries. For such reasons, services trade preferences should be more case-specific than for goods, and focus on cases where it is likely that such government measures will generate more exports
- The services chapters of the CARIFORUM EPA cover 13 non-LDC states. Compared to LDCs, these countries are one step up the ladder and therefore represent a “best case” in terms of services trade potential. The agreement contains specific “positive lists” for each CARIFORUM country with increased market access for specific sectors and modes in services, in addition to some “horizontal” offers that apply across to all countries. Commitments also vary across EU members so the agreement is complex with 13x27 schedules.

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- For GATS Mode 4, the CARIFORUM EPA mainly provides liberalisation for skilled labour, and the EU has opened 29 sub-sectors for temporary visits of “contractual services suppliers”. There are no quotas or ceilings, but individual EU countries may apply economic needs tests.
- While the economic impact of services preferences is somewhat uncertain and difficult to quantify in advance, such preferences may be a useful supplement to other measures. If such preferences also provide help to conclude the Doha Development Agenda, this would have an additional value that should not be underestimated.

### 3.1. Introduction

Trade preferences as a development instrument have a long and controversial history. The combination of two events – the impasse in the Doha Development Agenda (DDA) and the Global Financial Crisis (GFC) – has made a reconsideration timely. The former has exposed painfully the difficulty of agreeing new trade rules in a body with the WTO’s membership and *modus operandi* whilst the latter has had an impact even on countries with a minimal share in world trade and exposed their structural weaknesses. Could innovative new preferences appropriate to the state of global trade policy in 2010 deal with both of these: revitalise the DDA and make LDCs and other poor countries less vulnerable? This is a valid question even for those who consider universality in trade rules to be the ideal and for whom, therefore, differentiation of any kind (including preferences) is a second-best option or worse.

This paper provides three sets of information to contribute to an answer. First, it uses the lens of the GFC to highlight the structural trade weaknesses of many poor countries, and the role that services trade could play in their mitigation. Second, it analyses the potential for North-South preferences on services trade and the features that would be required in any such regime to make it commercially useful. Third, it examines the recently agreed EU-CARIFORUM Economic Partnership Agreement (EPA) to see how far it contains such features. It has been written to complement Melchior and Johnsen (2009).\*\*

#### 3.1.1. The lens of the GFC

Trade is a key transmission mechanism of the global financial crisis (GFC) for least developed countries (LDCs), as it links them to markets that are heavily affected by the financial crisis via changed terms of trade and export demand. This is more the case for LDCs than for other developing countries as they are relatively more dependent on

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\*\* This refers to a preliminary version of Chapter 2 in this report.

trade and on external flows (remittances, foreign direct investment) in general. Moreover their exports tend to be more concentrated than those of other developing countries. This combination of factors makes LDCs more exposed to the vagaries of external markets (Cali and Kennan, 2009a).

The full impact of the GFC on LDCs (and on small vulnerable economies (SVEs)) has not yet been felt, but Cali and Kennan have forecast GDP cuts of 4% or more for many (2009 a and b). They point out that both groups are characterised by small market size and high transport costs. Their small domestic markets mean that most of the firms are small and medium enterprises with limited opportunities for reaping the benefits of economies of scale and investing in research and development. Furthermore, in the case of LDCs, most lack skilled labour or adequate human capital which limits access to external capital and constrains industrial development. All these factors contribute to high unit production costs which put them at a relative disadvantage in international trade in *goods*.

As a result, these countries tend to have a less diversified production structure, with most exports concentrated in a few sectors, and a large number of products and services acquired from abroad. For most LDCs and SVEs the combined share of the first and second most valuable export products is over 50% of total exports.

So services offer a tempting opportunity to break out from this vicious circle because they are less dependent than goods on transport costs and involve lower levels of scale economies. But the mirror of the Global Financial Crisis (GFC) shows that this goal has not yet been fully achieved. Whilst services exports as a whole appear to have been more resilient to the GFC than have goods, tourism and transport have been more severely affected than the average. And it is on these vulnerable sectors that the services of poor countries are often concentrated. A lack of diversification is even more noticeable in poor countries that have managed to grow their services exports than is the case for goods. The ratio of services exports over GDP in the Commonwealth small island community, for example, is five times larger than in the rest of the world (against a factor of two in goods). It seems that the services actually exported by SVEs have made them just as vulnerable as the goods exporting LDCs and LICs. A Commonwealth Secretariat/World Bank review in 2006 suggested that small states should reposition themselves in the global economy by diversifying into knowledge-based service industries such as tourism, finance, insurance, health, education, and information and communication technology services (Qureshi and te Velde, 2008). Could preferences help to induce this shift?

### 3.2. What would services preferences look like?

Preferences on trade in goods have been controversial because, when effective, they have involved trade diversion as well as creation. Whether or not the diversion can be justified depends on whether there are offsetting development benefits. In practical terms, this means the following: will the preference lead to self-sustaining (and, ideally, diversifying) exports in a country that would not otherwise have achieved this?

#### 3.2.1. The features of 'successful' goods preferences

Often goods preferences have been ineffective in that they either offer no significant commercial advantage to the notional beneficiary (as import restrictions on competitors are light) or are for goods that the beneficiary cannot produce sufficiently competitively (at least within the requirements of the origin rules). By definition, in such cases, there is neither a direct cost nor benefit.<sup>8</sup> Yet there have also been some clear cases where preferences have conferred a commercial advantage and, in some of these, also a development benefit. At one extreme is Mauritius which used the economic rent from EU sugar preferences to invest in clothing and the rent from this to develop services. At the other are those Caribbean banana and sugar exporters for which preferences have kept alive (just) traditional trades that will probably cease once wider liberalization erodes the preference. In the middle are cases such as Lesotho's clothing exports made possible by AGOA (USA's African Growth and Opportunity Act) (which *may* survive the eventual removal of all WTO safeguards on Chinese exports) and Kenya's horticulture exports to the EU (where competition is so severe that only preference-receiving countries are able to maintain significant market shares<sup>9</sup>).

Both the development gains and the trade diversion costs tend to be case-specific. One consequence is that it is difficult to make a general conclusion that preferences have been 'good or bad'. Another is to draw attention to the characteristic that to be 'effective' (which is a precondition for their being 'developmentally good') they must respond to the specific production and market features of the target country.

#### 3.2.2. The ways in which services are different

Since there is a *prima facie* case from goods trade that preferences can be useful *in certain cases* it makes sense to consider new preferences

<sup>8</sup> Although there may be indirect costs such as erosion of most favoured nation treatment or the opportunity cost of negotiation.

<sup>9</sup> The term preference-recipient is used to cover all countries that pay lower than MFN tariffs including, for example, Israel under its FTA with the EU.

on services for LDCs but, as pointed out by Melchior and Johnsen (2009), many questions arise. Some of these relate to the LDCs' production structure: many do not have the human resources or infrastructure to produce tradable services. This problem is not unique to services; it is a variant of one that applies to preferences on goods trade. Countries that export, for example, mainly hard commodities rarely benefit from trade preferences since the international barriers that they face are generally low. Indeed, given the frequently observed macroeconomic effects of a large extractive industry one can even say that there is a tendency in such countries for trade that is immune to preferences to drive out trade that could benefit (as, for example, in Zambia).

Other problems, though, do relate to characteristics of services trade that are different from those of goods. Even though there are 'behind-the-border' measures affecting trade in goods (such as standards) there are many more for trade in services, the regulation of which is much opaque, complex – and not necessarily negotiable. A consequence is that services preferences need to be even more context specific than do those on goods if they are to be commercially useful.

For preferences to be technically feasible there must be scope for *governments* to agree to, and effectively implement, liberalization. This is not always the case with services. Professional services provide a good example. If domestic law establishes that no-one can call themselves an accountant or an auditor unless they belong to the appropriate, non-governmental professional body then it is the membership requirements of these bodies that have a major influence on whether trade can occur and in what form. And reform to their autonomously determined requirements may require wide-ranging change to domestic law involving considerations within which trade policy is a minor element.

It may be the case that a foreign 'accountant' is not be permitted to advertise their Mode 1 or 2 services or to practice via Modes 3 and 4 unless they satisfy the requirements of the non-governmental professional body. And a domestically registered company may not be able to import the services of a foreign auditor that has not obtained such recognition. On the other hand, an individual can use any foreign accountant (registered or not) to undertake private, non-statutory work provided that they have the means to make contact, to receive the work and to pay.

In none of these cases is there much scope for international negotiation – for one of two opposite reasons. One is jurisdictional: unless the requirements of the domestic professional body are grossly biased against foreign suppliers, they are unlikely to be required to amend them even as an indirect result of foreign trade negotiations. The other is practical: governments have difficulty restricting the import through Modes 1 and 2 of professional services by private indi-

viduals with a means of foreign exchange payment; and if governments are unable to interfere in trade, there is nothing to negotiate about.

By definition, if governments are unable to restrict trade or unable to remove non-governmental restrictions there is no scope for 'liberalisation' either multilaterally or selectively such as through preferences for poor countries. Attention on the scope for services preferences must be restricted, therefore, to areas of trade in which useful negotiations on liberalization is technically possible. And, as pointed out by Melchior and Johnsen (2009), a high proportion of these concern types of trade in which LDCs cannot participate or where liberalization faces significant domestic political obstacles (as with Mode 4).

This suggests that any identification of commercially-useful services preferences for a given set of countries must be very specific. This view is reinforced because gains from services liberalization will often be less generalized than those for goods. If all tariffs are cut by half, for example, it will affect all sectors and any differences in the proportional effect can be easily calculated by reference to the initial tariff level. Moreover, it is clear what some of the immediate effects will be. There will be a transfer from the importing states' revenue to elements in the supply chain. The distribution of this transfer between the stages in the supply chain are a matter for speculation, but one way or another the net effect is likely to be to increase international trade.

With services trade there are no universal results: a change to horizontal rules of establishment, for example, though notionally of general impact may be of central importance to one (sub) sector but only of tangential relevance to another. Nor is the scale of the potential effect easily calculable. Take the example of national treatment (NT). If a foreign service provider is treated in exactly the same way as a national firm, this might appear to remove all discrimination against it. However, the main reason why a foreign services provider may be able to offer services more competitively than the domestic supplier is that it can draw upon resources (technical, financial or personnel) from its home base abroad. But NT does not, by itself, necessarily give the firm the right to draw freely upon its resources abroad. Prudential requirements concerning reserves may require a firm to hold deposits in the host country rather than using its reserves in its home base. Immigration and work permit restrictions (outside the scope of Mode 4) may frustrate its attempt to utilise its foreign holdings of technical and human resources. In other words, whereas NT in goods trade allows a firm to take advantage of all the support available to its domestic competitors yet also benefit from lower cost production in its home base, in the case of services NT means exactly what it says: foreign firms are treated no worse – but no better – than their



domestic competitors. Given the nature of services trade, this may remove, in whole or in part, their competitive advantage.

### 3.2.3. A checklist for commercially useful services preferences

To be commercially useful, therefore, any services preferences would need to meet the following tests.

1. Do they remove a barrier that significantly limits either the volume or the value of exports from the target beneficiaries?
2. Do the target's competitors face the same barriers, and will these remain in place for their exports?
3. Are there other barriers, not subject to preferences, that will prevent any increase in imports from the target countries?
4. Do the target countries currently export the services covered by the preference?
5. If not, could they reasonably be expected to develop a capacity with appropriate investment (of plausible levels) and, if so, how does the payback period of the investment relate to the likely duration of the preferences (which may be limited either by a finite application period or by the probability of more generalized liberalization?)

It is not necessary for any preference regime to be limited exclusively to the measures and products that offer positive answers to these questions. But unless there is at least a *prima facie* case that some elements in a broad package do produce positive answers the exercise may result simply in the addition of a further layer of complexity to international rules without any offsetting gain.

## 3.3. Services provisions in the EU-CARIFORUM EPA

How far do the provisions of the only EPA so far to include a services chapter tick these boxes? This question is asked not to critique the EU-CARIFORUM EPA but to use it as a case study on the likelihood of conventional trade negotiations resulting in commercially useful services preferences. None of the 13 CARIFORUM states participating in the services EPA are LDCs,<sup>10</sup> though many are SVEs, so the results present a 'best case': compared to LDCs, there is a wide range of services that these countries are able to produce competitively. But this is in itself useful: it shows the potential of a preference agreement to assist countries with relatively sophisticated services sectors; ad-

<sup>10</sup> The services chapter does not cover the Bahamas (which is not a WTO member) or Haiti (which is classified as LDC at WTO); since neither has submitted a GATS-compatible service offer they are excluded from EU preferences.

justments can then be made to take account of the more limited LDC supply capacity.

The parties have expressed their concessions through a positive list approach covering all four modes and various sectors but with limitations.<sup>11</sup> One feature that has an obvious implication for the modalities of any generalized services preference scheme is that there are not two schedules but 40 – different ones for each of the 13 CARIFORUM and 27 EU states. Although this is a function of shared competences in the EU and of the absence of a common CARIFORUM services policy, it indicates that detailed preferences are likely to be country-specific. As with the GSP, the specific details of what is on offer vary markedly between preference-giving states. A ‘services DFQF’ for LDCs is very far into the future.<sup>12</sup>

In relation to the issue noted in Melchior and Johnsen (2009) on the origination of services supplies, the EPA provides that originating status requires a juridical person not only to have its registered office in a territory but also to engage in ‘substantive business operations’ there.

In some respects, the EU’s offer is extensive but there are also important limitations. The sectors in which it has made commitments include business services, communication, construction, distribution, environmental services, financial service and recreational services (with entertainment services of particular interest to CARIFORUM). It has also made broad horizontal commitments.

The EU’s horizontal offer on commercial presence applies to almost all economic activities although audio-visual services, national maritime cabotage and most air transport services are among the exclusions and there are general reservations on the acquisition of land and public utilities. It includes a range of business services of particular interest for the Caribbean.<sup>13</sup> Although some EU countries (mainly the new EU member states) have restricted the share of foreign investment for professional services and have limited access to health and social services (e.g. by economic needs tests), this does not appear to be too burdensome. The provisions on tourism and travel-related services offer broad access to hotels, restaurants and catering, travel agencies and tour operators, tourist guides and entertainment services (including live band, circus and discotheque services).

Treatment for modes 1 and 2 covers many sectors (again with the exclusion of audio-visual services, national maritime cabotage,

<sup>11</sup> As a reciprocal agreement both parties made ‘concessions’ but this paper focuses on those of the EU as a guide to what might be possible in an autonomous preference offer. Details of the CARIFORUM offers can be obtained in Stevens, Meyn and Kennan (2009) on which this section is based.

<sup>12</sup> DFQF = duty-free, quota-free.

<sup>13</sup> Such as legal services, accounting and bookkeeping, auditing, taxation advisory, architecture, research and development (R&D), computer, real estate, several medical services, rental/leasing services without operators, environmental services, financial services and other business services (e.g. advertising, management, security, translation, educational services, maintenance, and telecommunication and postal services).

most air transport services as well as government services) and is generally wide ranging though there are important limitations for telecommunication services, which are virtually excluded.<sup>14</sup> Given the increasing importance of services provided via telecommunication this appears to be a serious limitation for Caribbean service providers. Another limitation applies to health and social services where almost all EU states have excluded mode 1 services for hotels, restaurants/ catering and cultural services.

Given the relative importance of Mode 4 for LDCs, the provisions in the EPA are of particular interest. The temporary presence of natural persons is limited to key personnel (senior employees and specialists working in the commercial presence); graduate trainees, business services representatives, contractual service suppliers (employed by the commercial presence in either state), and independent self-employed professionals. Commitments are linked to the sectors in which commercial presence has been offered and is limited to three years for intra-corporate transfers, one year for graduate trainees and 90 days in any 12-month period for business visitors and business service sellers.

The EC has opened 29 sub-sectors for contractual service suppliers which is limited to 6 months annually.<sup>15</sup> It applies only to those with at least three years professional experience for contractual service providers or six years for independent professionals, with a university degree or an equivalent qualification and professional qualification required in all cases except fashion models, *chefs de cuisine* and entertainment services.

Although there are no quotas or economic ceilings, several EU countries have imposed nationality requirements or an economic needs test in some sectors. Moreover a very broad language is used when establishing general reservations in all sectors, providing a peg on which EU member states could hang restrictions to the presence of Caribbean key personnel, graduate trainees, contractual service suppliers and independent professional – even if no such restrictions are detailed in the relevant annexes.

An innovation that has attracted some attention is that annexed to the EPA is a Protocol on Cultural Cooperation. This aims to facilitate the temporary stay of artists and cultural professionals not covered in the services chapter following the 2005 United Nations Educational, Scientific and Cultural Organization's Convention on the Pro-

<sup>14</sup> The EU offer excludes any economic activity consisting of the provision of content that requires telecommunications services for its transport. Satellite broadcast transmission services 'may be subject to obligations to safeguard general interest objectives.'

<sup>15</sup> Including accounting and bookkeeping, taxation, engineering, medical service (dental, midwives, nurses, physiotherapists), computer and related services, R&D, management consulting, technical testing, fashion models, *chefs de cuisine*, travel agencies, tourist guides and entertainment services. Independent professionals have access to 11 high-qualified sub-sectors such as architecture and urban planning, engineering, computer, R&D, management service and translation.

tection and Promotion of the Diversity of Cultural Expressions. But no reference is made to the Protocol either in the text or in the annexes specifying parties' service commitments. And the language of the Protocol is lax and does not include any enforceable provisions.

### 3.4. Conclusions

Only time will tell whether the EPA supports increased (or more remunerative) services exports, but as the analysis of services trade regulation suggests it is likely to be only a part of the process of removing barriers. Given the lengthy negotiations (in which the CARIFORUM negotiators were extremely committed, believing the services provisions to offer the potential for a major improvement to the *status quo*) it is likely that identifying commercially useful preferences for LDCs will be time-consuming and will require country-focussed analysis. As Melchior and Johnsen (2009) point out, restricting such preferences to LDCs (a group with a particularly low services supply capacity) makes the task much harder than would be the case if the net were widened somewhat.

One implication is that services preferences are not sufficiently attractive to make them an acceptable alternative to other trade measures in support of LDCs. Full, widespread and enforceable DFQF for LDCs' goods exports is likely to have a much more substantial initial impact as it would open markets for agricultural as well as manufactures exports. Special quotas for LDCs on temporary migration could also be useful. As Melchior and Johnsen (2009) point out these would need to go beyond the visits covered by Mode 4 to respond to the current supply capacity of most LDCs.

If seen as an 'addition' rather than as an 'alternative' to such measures, though, services preferences could play a useful role. In those cases where goods preferences have been trade creating it has often been because the liberalising state has calculated that it has a political mandate to open up towards less competitive, smaller producers but not towards the most competitive. As generalised liberalisation spreads among OECD states the occasions where such a calculation needs to be made for goods has dwindled. But in the area of services there are many potential cases, where cautious opening towards a country likely not to supply large volumes of highly competitive exports is politically feasible whereas a GATS commitment is not. The provision of enabling architecture within the WTO allowing such restricted liberalisation to occur for specific groups of countries might allow future experimentation. And if, together with DFQF and special temporary migration quotas, it were to provide a fillip to get Doha moving again, that would be a bonus!

## 4. Development and comparative advantage in services

Arne Melchior

### Abstract

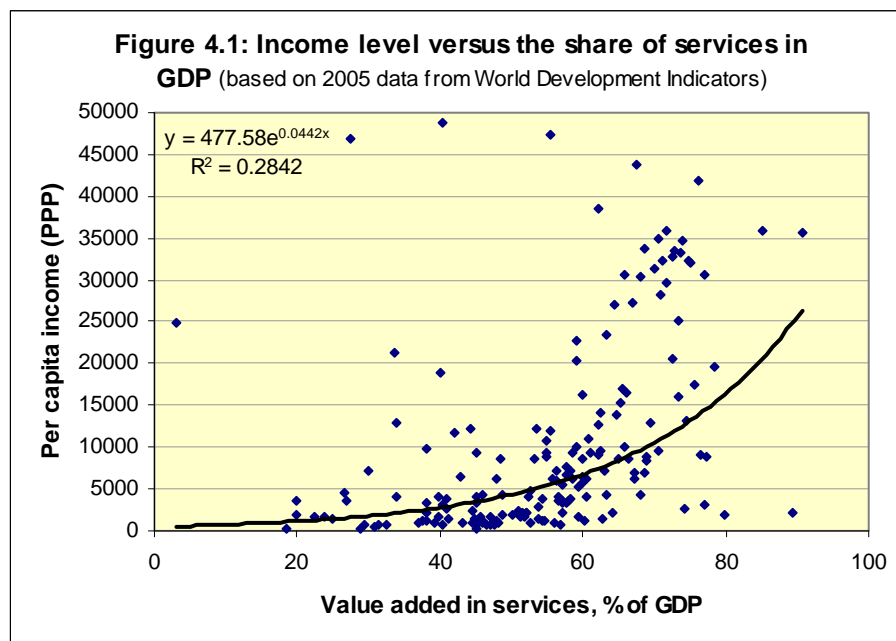
Since the purpose of services trade preferences is to promote development and reduce poverty, it is important to know how services trade is related to development. Trade in services takes place according to the four supply modes defined by the WTO, and the analysis must therefore address FDI and temporary migration as well as ordinary services trade.

- According to WTO data, international trade in goods and services have grown at the same pace during 1990-2008. International FDI has grown almost twice as fast during the same period. Cross-border trade (Mode 1 of the GATS) and commercial presence (Mode 3, including FDI) are the most important modes of supply.
- Rich countries have larger services sectors and are on average net exporters of services as well as net suppliers of FDI. While developing countries have developed a significant trade surplus for trade in goods, they are on average net importers of services as well as FDI. For migration, net flows go in the opposite direction: from poor to rich countries. For services, there is a lot of two-way trade between rich countries.
- During 1990-2007, lower middle income countries had continuous growth in their income levels and their share of world trade, and trade in goods grew faster than trade in services. The Least Developed countries experienced growth during 2000-2007, and their goods trade and services imports increased considerably. While their exports of goods grew fast, their services exports lagged behind. Probably due to aid, LDCs have relatively high services imports.
- At the more disaggregated level, there are considerable differences across services sectors: Rich countries tend to be net exporters of skill-based services; developing countries do better for passenger travel and tourism; and construction and freight are intermediate cases. The ranking across sectors is mostly similar for LDCs and other developing countries. The notable exception is computer and related services, where India's export success has boosted developing country performance. This is however still the exception rather than the rule. For LDCs, tourism is the most important services activity.

- Developed nations have 80% of outward and 2/3 of inward FDI. LDCs have a significant share of inward FDI but almost no outward FDI. About 2/3 of world FDI is in services, with financial services and business services as the leading sectors.
- Temporary movement (Mode 4 trade) has also increased but current data availability is very limited. Such trade is estimated to represent 1-2% of total services trade but the figure is uncertain. Mode 4 trade is much more restricted than Modes 1-3 and with a more liberal regime, such trade could increase.

#### 4.1. Introduction: Rich countries produce more services

It is well known that the proportion of services production in GDP increases with income: Poor countries may have shares at 50% or even lower, while the share for the richest countries is typically about 70% or even higher. Figure 4.1 plots value added in services as a percentage of GDP on the horizontal axis, and the income level (GDP per capita, PPP) on the vertical axis. We use 2005 in order to obtain the highest possible data coverage.



In spite of some non-typical observations and heterogeneity across countries there is a statistically significant positive relationship: richer countries have on average larger services sectors. The exponential curve captures 28% of the variation and the graph shows that for developing countries, there is huge variation in the services share of GDP. For higher income levels, the majority of countries have a high services

share of GDP, with a cluster between 70 and 80%. There are various reasons why rich countries produce more services, for example:

- Richer countries generally have a larger public sector.
- In rich countries, wages and therefore also price levels for services are higher and this boosts the GDP share for services.
- Rich countries have higher skill levels and therefore larger production of skill-intensive services.
- The transfer of labour-intensive manufacturing away from the richest countries may have contributed to their higher services share in GDP.

#### 4.2. The GATS supply modes and the growth in world trade

Since services can be delivered in different ways, as reflected in the four modes of the GATS, there is no easily available single figure for services trade. Mode 1 (cross-border trade) and mode 2 (consumption abroad) are in principle covered by the services trade statistics published by statistical agencies. Mode 3 (commercial presence) is mainly covered by FDI (foreign direct investment) statistics. Mode 4 could partly be included in migration statistics, but temporary migration to deliver services is generally difficult to trace in migration data so in practice statistics for Mode 4 trade are rather limited.

Various attempts have been made to quantify the relative importance of the various modes. A difficulty is that trade flows in Modes 1 and 2 are not comparable to FDI stocks in Mode 3 or the number of temporary migrants in Mode 4; and it is not easy obtain accurate statistics on the service sales flows corresponding to Modes 3 and 4. Current figures should therefore be considered as approximations only. According to Francois et al. (2009), the composition was as follows in 2004:

	USD Billion	% of total
Mode 1 Cross-border trade	2034	48.2
Mode 2 Consumption abroad	620	14.7
Mode 3 Commercial presence	1500	35.5
Mode 4 Producer movement	70	1.7
Total Modes 1-4	4225	100

Source: Francois et al. (2009), Table 1 page 11.

Hence according to this, cross-border trade and commercial presence are the most important modes. UNCTAD(2004, 98) present estimates

based on affiliate sales and according to that, Mode 3 is currently more than half of world services trade. For some countries, the ratio between services exports and foreign affiliates' sales was up to 2.5 in 2001 (ibid.). Hence estimates vary somewhat, and we are not able to draw a final verdict about the exact shares.

The relative importance of each mode depends on technology as well as barriers. For example, market access in Mode 4 is restricted due to the sensitive nature of migration issues, and more liberal trading conditions might result in larger trade (Winters 2003). The expansion of India's exports of information technology services in recent years illustrates the role of technology: trades that were impossible a few years ago may now be undertaken due to better communication and data flows.

There is some uncertainty with respect to the growth rates of world goods trade versus world services trade. Data from the WTO database ([www.wto.org](http://www.wto.org)) suggest that world services trade during 1990-2008 grew at approximately the same speed as goods trade: The share of services in world goods+services trade fluctuated between 18.2 and 19.9% with no clear trend. These statistics capture Mode 1 and – depending on data availability – Mode 2. Contrary to this, Francois et al. (2009) conclude that during 1996-2004, world Mode 1 services trade grew much faster than world goods trade. Hoekman and Mattoo (2008) report a slight increase in the worldwide ratio of services imports to GDP, from 11 to 12%. This was mainly due to import growth in developed and upper middle income countries; there was actually a decline in this ratio for lower middle income and low income countries. Facing the uncertainty in reported trends, which may partly be due to the limits of available data, we choose to believe in the WTO data: world services trade (Modes 1 and 2) has grown at par with merchandise trade and constitute slightly less than 1/5 of world trade in goods + services trade (Modes 1 and 2).

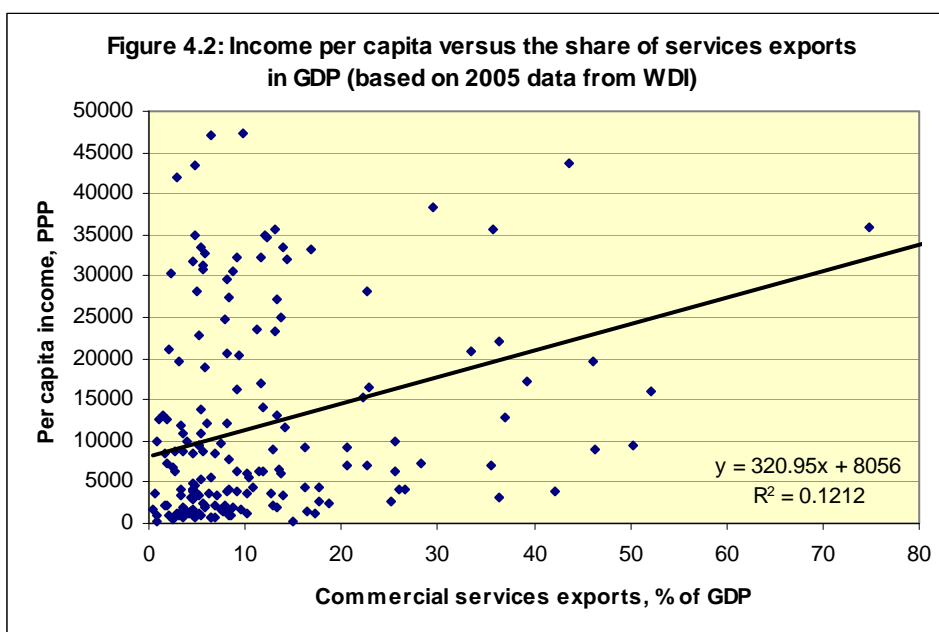
Comparing UNCTAD data on world FDI with WTO data on trade, there is however no doubt that FDI grew much faster than trade in goods and services. The ratio of FDI stocks as well as flows to world merchandise trade almost doubled from 1990 to 2008. Given that more than half of world FDI is in services and this share has grown over time (see analysis below), the most dynamic element seems to be Mode 3 services trade.

### **4.3. Comparative advantage in services: The aggregate pattern**

On the background of section 4.1 we might expect that rich countries should also have a comparative advantage in services and be net exporters. This is indeed true, but it is not the whole truth: Some middle-income countries have significant exports in particular services sec-



tors. For example, some poor countries have extensive tourism, and some offshore financial centres have relatively low income per capita. Due to these “exceptions”, the positive relationship between income levels and services exports is weakened. In Figure 4.2, we show the ratio of services exports to GDP on the horizontal axis, and par capita income on the vertical axis.



There is a positive and significant relationship but it is relatively weak.<sup>16</sup>

Figure 4.2 is based on services trade data that mainly capture cross-border trade (GATS Mode 1) and to some extent Mode 2 (consumption abroad). The picture is therefore incomplete since it does not include services trade in Mode 3 (commercial presence) or Mode 4 (temporary movement of service providers). Mode 3 is reasonably well captured by FDI statistics, but data on Mode 4 are very scarce. As a very crude proxy for elements of Mode 4 we will therefore sometimes use data on migration and remittances; however with a strong note of caution since Mode 4 trade only represents a tiny part of migration.

In the further analysis, it is convenient for analytical purposes as well as presentation to distinguish between five country groups: These are LDC (the 49 Least Developed Countries), LLM (other Low and Lower Middle Income, 51 countries), and three higher-income groups (EU-27, upper middle and high-income, see Appendix C for

<sup>16</sup> The trend line has  $R^2=0.12$  but if a couple of extreme observations are dropped (one is not shown in the diagram), the explained variation drops to 3%. A similar graph using net services exports/GDP obtains  $R^2=0.08$  so there is a positive relationship but not very strong.

details. We will generally use the term “developing countries” for UM+LLM+LDC.

In the following analysis as well as the more detailed examination of individual sectors in Appendix C, we sometimes use simple specialisation indexes or “Balassa indexes” of the form  $(x-m)/(x+m)$ , where  $x$  is export and  $m$  import. If all trade is exports the index is 1, if all is imports it is -1, and if trade is balanced it is zero. This index is a simple measure of comparative advantage.

In Figure 4.3 we show the Balassa indexes for goods trade, services trade, FDI and migrants’ transfers for the five country groups.<sup>17</sup> We use the year 2005 in order to obtain the most extensive data coverage. Observe that the aggregate results for goods, services etc. hide that there are differences across sectors. We will revert to some of these sector differences later.

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<sup>17</sup> Data are from IMF: Balance of Payments (BOP) online statistics, except the FDI figure for LDC which is based on data from the UNCTAD online FDI database. The reason for the latter is limited LDC coverage for outward FDI in the BOP data.

**Figure 4.3: Net specialisation indexes for goods trade, services trade, FDI and migrants' transfers, for five country groups in 2005**



- For trade in goods, developing countries have a comparative advantage (are net exporters) but the more advanced developing countries (UM, LLM) perform better. The LDC group is barely above zero; indicating their limited supply capacity in spite of low labour cost.
- For services trade, the pattern in 4.3(b) corresponds to Figure 4.2; net exports are higher, the richer you are. But the deficit for LLM is very small, confirming some ambiguity also for this relationship.
- For FDI, the pattern is overwhelmingly clear; net outflows are from rich to developing countries and the poorest countries have virtually no outward FDI.

- For migrants' transfers, the pattern is mixed but tends to be opposite to FDI, with net outward transfers from the richer countries and net inflows in developing countries. Observe that there is no net inflow into LDCs (see Chapter 6 for more analysis).

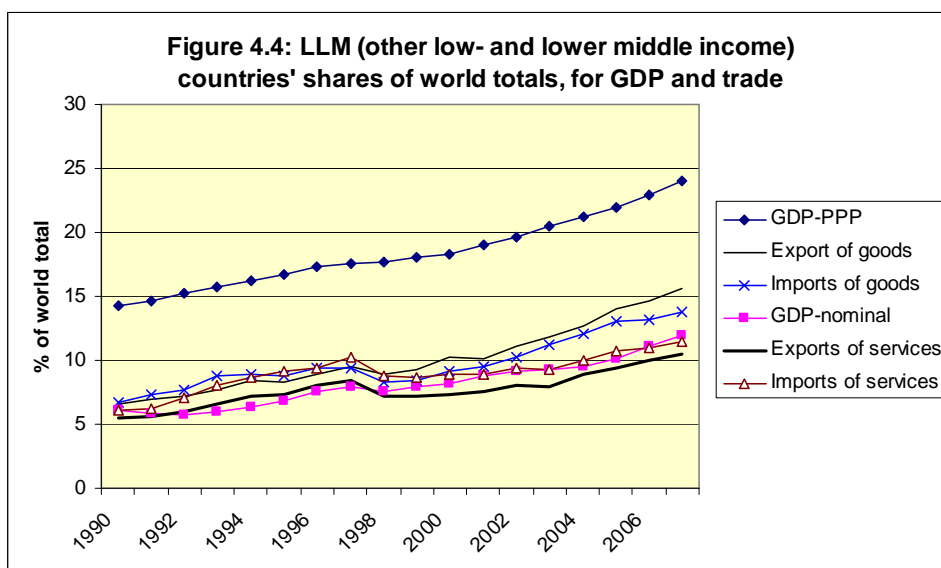
For the WTO, this aggregate pattern has important implications: Liberalisation of trade in goods is particularly important in order allow poor countries to exploit their comparative advantage, and liberalisation of trade in services is particularly important in order to exploit the comparative advantage of the richer countries. If such specialisation is allowed, rich countries will benefit from better goods, and developing countries from better services. That is a simple logic that tends to be forgotten sometimes in the "mercantilist" atmosphere of trade negotiations. This is however only the aggregate picture; in addition there will be sub-sectors within each aggregate where the pattern of comparative advantage varies, which we revert to below.

For factor movement, it is evident that rich countries can offer more capital, and developing countries more labour. While the overlap between Mode 4 trade and migration in general is limited, there is such a link and it is indeed no surprise that developing countries hope for freer movement of labour also for the delivery of services.

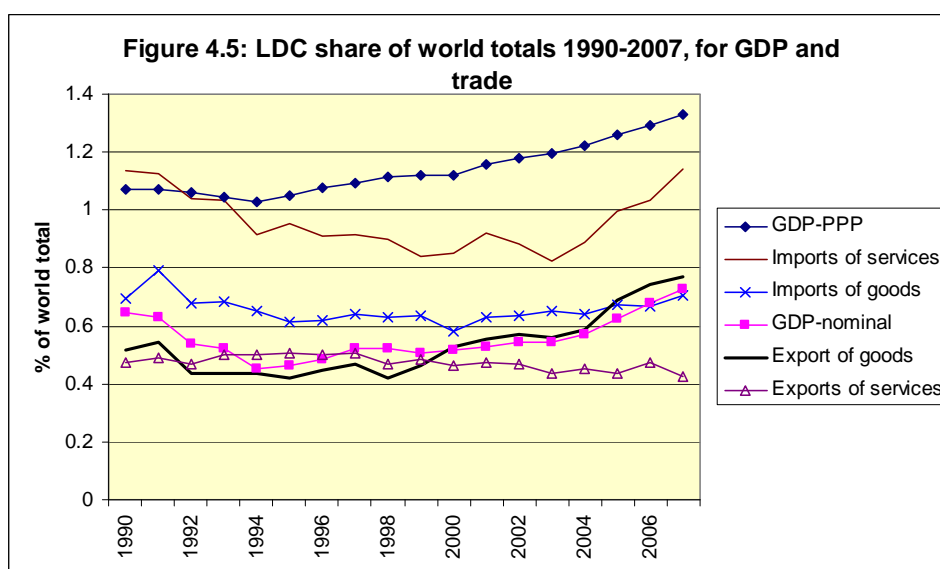
The results here are based on a snapshot for 2005 and it is evident that the pattern changes over time. In figures 4.4 and 4.5, we show trends over time for LDC and LLM, respectively, indicating how their shares of the world total have changed over time for various items.<sup>18</sup> When interpreting the figures, it should be recalled that FDI grew faster than trade in goods and services so the shares do not tell the whole story (cf. analysis above). For the developing countries, share of world economic aggregates are generally lower than their share of the world population. As a background it may therefore be recalled that in 2008, LDC represented about 800 million people or 12% of the world population, while LLM included 3.8 billion or 58%. Their shares of economic aggregates are generally much lower, precisely since they are developing countries with lower income levels.

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<sup>18</sup> Data are from World Development Indicators, online version. For GDP and population, we used samples with a constant number of countries during 1990-2008. The number of observations is 161 for nominal GDP, 159 for GDP-PPP (Purchasing Power Parity) and 199 for population. For goods and services trade, we allowed some variation in country coverage over time so the number of observations is varying in the range 141-162 over the period (30-40 for LDC).



For the LLM group including China and India, all curves generally increase except for a modest stagnation phase in 1998-2000 that is linked to the Asian crisis. Measured in shares, goods trade is more dynamic and the share for exports grew faster than imports. Hence LLM increased their net export ratio or Balassa index from zero in 1990 to 0.06 in 2007. For services, trade grew more at par with nominal GDP and the Balassa index did not change much over time.



For LDCs, the pattern is more mixed and for many of the time series there was a reversal of the trend, with falling shares and marginalisation at the beginning and increases towards the end of the period for most series. Towards the end, there were fast increases for GDP, manufacturing exports and services imports. Some LDCs have signifi-

cant commodity exports and before the onset of the financial crisis, these exports grew and contributed to growth.

For services, Figure 5.5 shows that LDC is a particularly large importer of services relative to its economic size. A possible explanation for the large LDC services imports is that is driven by aid. This is confirmed by regression analysis (not reported in detail); aid is a significant determinant of services imports. For services exports, however, there was no increase and LDC exports grew slightly lower than the world aggregate. For the LDCs, the export/GDP ratio for services even fell during the last decade, contrary to the other variables. Recent LDC growth (before the financial crisis) was particularly driven by manufacturing exports; see e.g. UNCTAD (2008).<sup>19</sup> As examined by UNCTAD (2006), LDC goods exports focus on (resource-intensive) processing of spices, fish and fishery products, as well as labour-intensive manufacturing (especially the garment exports of Bangladesh).

Figures 4.4. and 4.5 also reveal the huge difference in economic size between LLM and LDC. While LLM is five time larger than LDC in terms of population, the group is 10-24 times larger for economic variables – around 20 times larger for most economic variables.

#### **4.4. Comparative advantage in services trade: Differences across sectors**

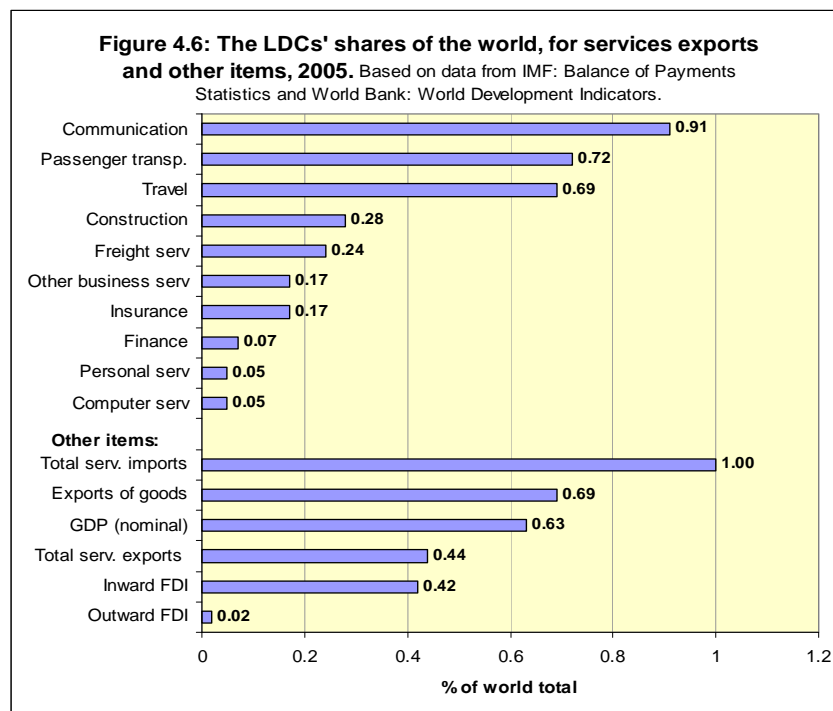
The patterns shown for aggregate goods and services trade hide considerable differences across sectors. For trade in goods, it is well known that poor countries have a particular edge in low-skill labour-intensive sectors, while the rich countries perform better in skill-intensive differentiated goods. Similar differences also exist for services. The following analysis is based on Appendix C, where we present a number of fact sheets for world services trade. The fact sheets cover 14 sub-sectors reported in IMF's BOP (balance-of-payments) statistics, including information about net trade patterns for major country groups. Given the focus of the analysis on development in general and the LDCs in particular, we focus particularly on LLM and LDC when reporting the results.

Even if the average LDC export performance in services was weak, it can be seen from Appendix C that the performance varied across sub-sectors. In some sectors there was an increase, in spite of

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<sup>19</sup> See e.g. UNCTAD's Least Developed Countries Report 2009, page 144: "...this Report focuses on industrialization via manufacturing, which does not deny the importance of services, which also registered high rates of growth in some LDCs, especially in island LDCs. However, given that the growth has been registered largely in the petty trade, low productivity services in most LDCs in the informal sector (for which no reliable data are available), and given the heterogeneity of services, it is beyond the scope of this chapter to include the services sector in the analysis."

the overall weak performance of LDCs in services exports. In Figure 4.6, we show the LDC share of world exports in 2005, for selected sub-sectors. As a benchmark for comparison, we also show LDC shares for some of the aggregates discussed above.



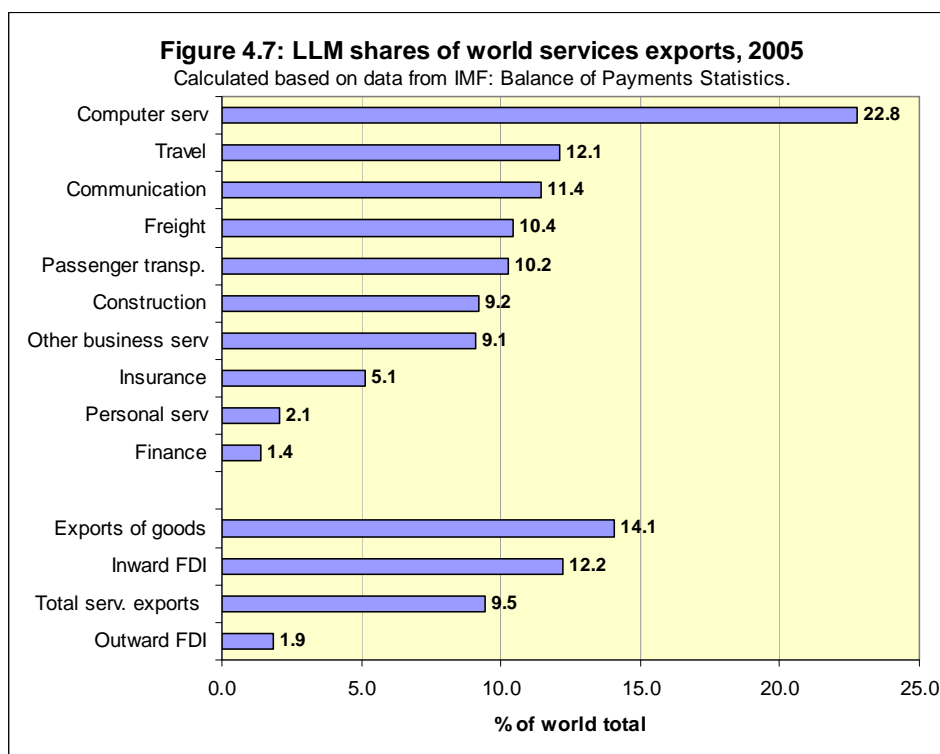
The importance of tourism for development is well known and discussed in e.g. Grosso et al. (2007), Honeck (2008). Measuring tourism is difficult since the sector has strong linkages to other services sectors such as hotels and restaurants, transports etc. Contrary to the situation for services trade in general, we find some sectors where the LDCs have positive Balassa indexes and are net exporters. This is reflected in Figure 4.6 by larger shares of the world total for passenger transports, travel services and communication services. While the role of tourism in some LDCs is well documented and may explain the high shares for travel and passenger transports, we do not have an immediate explanation of the high share for communication services. This is surprising and may be driven by tourism as well as aid-related activity.

At the other end of the scale, we find more technologically advanced sectors: insurance, financial services, computer and information services.<sup>20</sup> The sector “Personal, cultural and recreational services” also contains audiovisual services, which is more high-tech and

<sup>20</sup> Observe from Appendix C that for financial services, LDCs are some years’ net exporters. This is partly due Vanuatu, which is listed by the Financial Stability Board as an offshore financial centre. But also Bangladesh, Ethiopia and Uganda had export surpluses some years. We have not examined the explanation of this in more detail.

this may explain why it is at the lower end of the LDC range of specialisation. For many of the skill-intensive sectors, commercial presence is a core model of supply, and the low LDC share of outward FDI is a related fact that we examine below.

The LLM group is one step up the ladder. Given the prominence of emerging markets such as China and the success of India's services exports, we might expect the sector pattern to be different for LLM, compared to LDC. In order to examine this, Figure 4.7 shows the similar graph for the LLM countries.



The main change compared to LDC, apart from the generally higher levels, is the spectacular performance of computer and information services. This is driven by India: 87% of LLM export of computer and information services in 2007 was from India (37.5 billion USD), and India was the world's largest exporter in the sector. Hence the top performance of this sector is not a general feature of the LLM group; China had most the remaining 13% of LLM export in 2007. An issue is whether the ICT success of India could be replicated in other poor countries, or whether it is possible only in India due to the country's large pool of skilled labour, combined with the familiarity with the English language. For a discussion of India's ICT revolution, see Karmakar (2008).

Apart from the ICT sector, however, the ranking of sectors is largely similar to the LDC pattern. Also here we find finance, insur-



ance and personal services at the bottom, construction in the middle, and travel and communication at the top.

Low shares in services exports for LDC and LLM must correspond with high shares for others. In Appendix C, it is easily confirmed that for the high-income countries and EU, the rankings are reversed and finance is on top. What should be observed is that the combined share for EU+high income in world exports has decreased over time for some sectors such as transport, construction, travel. In these cases, it is mainly LLM and upper middle income countries that have expanded; except for travel where even LDC has taken a measurable share of the total.

Our analysis of the sector composition of developing country exports confirms the picture emerging from the macro-analysis: Developing countries have, on average, a slight comparative disadvantage in services; although there is considerable variation across sectors. Over time, developing countries have increased their market shares in some important sectors. Income convergence, especially between LLM and the rich countries, could also lead to convergence between rich and poor countries over time in terms of their services export performance.

#### **4.5. FDI and services trade**

For several types of services, commercial presence is the only feasible form of delivery, and in other cases there may be a combination of commercial presence and other modes. For example, telecommunication services are traded across borders (Mode 1) but in addition, cross-border FDI (Mode 3) plays an important role. As shown above, Mode 3 constitutes a major services supply mode.

In general, a considerable share of international FDI is North-North, but some is North-South with more outflows going from rich to developing countries. South-South FDI has recently increased but still has a modest share of total FDI. As a platform for analysing Norway's FDI patterns, we present some recent evidence on global FDI flows. Table 4.2 shows the global distribution of inward and outward FDI by country groups, based on the most recent UNCTAD data:

<b>Table 4.2: Inward and outward FDI in 2008: Percentages of the world total</b>				
	Inward		Outward	
	Stock	Flow	Stock	Flow
World	100	100	100	100
Developed economies	68.50	56.69	84.07	81.09
EU	43.14	29.66	49.90	45.06
USA	15.29	18.62	19.51	16.78
Developing economies	28.68	36.57	14.54	15.76
Africa	3.42	5.16	0.60	0.50
Latin America and the Caribbean	7.93	8.51	3.46	3.40
Dev. Asia and Oceania	17.33	22.90	10.47	11.85
South East Europe and the CIS	2.82	6.74	1.39	3.15
Developing and transition economies	31.50	43.31	15.93	18.91
Least Developed Countries	0.91	1.95	0.06	0.21

Source: Calculated on the basis of UNCTAD (2009), Annex Tables B.1 and B2.

Hence developed nations have more than 80% of outward FDI and about 2/3 of inward FDI. Corresponding to this, developing countries have a considerable net inflow. The Least Developed Countries have a significant share of inward FDI but a very small share of outward investment. Figure 4.2(c) above also confirms this strong North-South pattern.

Investment in the services sectors constitutes a large share of world FDI. This share has increased during the last decades and now approaches 2/3. Figures for 2007 are shown in Table 4.3.

**Table 4.3: Distribution across sectors and country groups for inward FDI stocks in 2007.**

<b>(A) Distribution by sector for each country group and the world total</b>				
	Developed	Developing	SEE&CIS	World
Total	100	100	100	100
Primary	7.46	6.31	22.88	7.47
Manufacturing	28.07	24.02	26.05	27.05
Services	63.03	67.77	44.98	63.84
– Trade	11.89	6.87	7.21	10.58
– Transport, storage and comm.	5.71	6.45	4.45	5.86
– Finance	21.22	14.28	13.32	19.38
– Business activities	13.27	35.15	16.05	18.64
<b>(B) Distribution by country group for each sector and the world total</b>				
	Developed	Developing	SEE&CIS	World
Total	73.79	24.31	1.89	100
Primary	73.66	20.54	5.80	100
Manufacturing	76.58	21.59	1.82	100
Services	72.86	25.81	1.33	100
– Trade	82.92	15.79	1.29	100
– Transport, storage and comm.	71.81	26.75	1.44	100
– Finance	80.79	17.91	1.30	100
– Business activities	52.52	45.85	1.63	100

Note: SEE&CIS = South East Europe and the CIS.  
Data source: Calculated from UNCTAD (2009); Annex A, Table A.I.4.

Hence in 2007, 64% of world inward FDI stocks were in services. 74% of these stocks were in developed countries, with particularly high shares for trade and financial services. Developing countries had a particularly high share of inward FDI for business services. Eastern Europe and the CIS had large inward FDI in agriculture.

Also for LLM, the share of outward FDI (shown in Figure 4.7, here included in “developing”) is lower than the group’s relative size, in spite of all the talk about China’s outward FDI. Given the important role of FDI in total services trade, it is another piece of evidence confirming that in spite of India’s ICT success, services exports is on average the least dynamic element of LLM trade. As for the LDCs, the share of inward FDI is much higher than for outward FDI; for the LLMs approximately at the same level as the group’s share in world nominal GDP. China and India are different from LDCs due to their large markets and recent high growth; and especially China has attracted large amount of inward FDI even if the country still scores low on various indicators of the “ease of doing business”. A closed look at the data shows that during 1994-2007, China absorbed 63% of inward FDI to the LLM group and represented 54% of its outward FDI. India

absorbed 6% of LLM inward FDI and had 19% of the group's outward FDI (with a higher share towards the end of the period).<sup>21</sup>

For outward FDI, LDC is at the low end of the scale, as also shown in Figure 4.6. The extremely low share of world outward FDI for the LDCs is a signal that trade preferences in GATS Mode 3 may not be easy for them to exploit.

The LDCs have a much higher share for inward FDI and this may contribute to the development of some of their services sectors. According to UNCTAD (2004), finance and business services are sectors where inward FDI is particularly important in developing countries. Ramasamy and Yeung (2007) find that inward FDI in services is driven mainly by the same determinants as FDI in manufacturing: FDI is positively related to market size and economic growth; factor costs (for labour and capital) also matter; openness is positive; and the quality of infrastructure and the ease of doing business is important. The LDCs have a low score on many of these factors and this may explain why their share of inward FDI is considerably lower than their share of world GDP. Attracting more investment in tourism-related sectors could be particularly important for the LDCs, given the strong linkages of tourism to other sectors.

#### 4.6. Mode 4 global trade

Appropriate data on Mode 4 delivery of services generally do not exist, and this also applies to Norway. There are several reasons for this:

- Some of the Mode 4 activity, such as business visits of limited duration, is not registered in the migration statistics.
- In migration statistics, temporary and long-term migration are not separated. Since there is no WTO definition of the duration of temporariness, this would also be difficult.
- To the extent that temporary migration is reported, it is difficult to distinguish services from non-services, and commercial from non-commercial.

Hence if reliable data on Mode 4 trade is to be obtained, a major effort has to be made. For discussions, see e.g. Mattoo and Carzaniga (2003, various chapters) and Magdeleine and Maurer (2008).

As shown in Table 4.1, current estimates indicate that Mode 4 constitutes a modest 1-2% of total world services trade. In the WTO, Mode 4 has until now been linked to commercial presence; i.e. by facilitating commercial visits, intra-company transfer etc. Hence FDI statistics provide some indirect information also on Mode 4: FDI has increased considerably, much of it is North-North, but with a substan-

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<sup>21</sup> For India, data is missing for 2007 so we use the 1994-2006 period.

tial North-South component. For the FDI-related Mode 4 trade, trends should be similar.

Mode 4 trade is clearly limited by the modest number of commitments in GATS. If more liberalisation took place, temporary movement to deliver services could clearly expand considerably. This however touches upon national migration policies which politically represent a highly sensitive area. Figure 4.5(d) above is a first indication to the effect that while poor countries do not have abundance of skills and capital, they have large populations that are ready to move. Hence for semi- and low-skilled labour, the pattern of comparative advantage is reversed and poor countries have an interest in greater market access.

In the DDA, developing countries have requested that Mode 4 should be de-linked from Mode 3 and that temporary movement of less skilled labour should also be allowed. Contrary to services trade and FDI, there is little doubt about the “capacity to move” for less skilled labour categories. Even if the largest component of world migration flows is South-South (see Chapter 6), the second largest component is South-North and there is clearly a net outflow from poor to rich countries. Also the poorest countries have substantial outward migration. While the LDCs perform below average on services exports and FDI, their share of migration is high. The LDC share of the world population is about 12%, but their share of world outward migration in 2000 was 14%. The LDCs do not have much capital and skilled labour, but a lot of labour with lower skills. Even if Mode 4 trade and migration are two different things, they are related and Mode 4 liberalisation raises issues where the literature and evidence on migration provides useful and relevant knowledge. In Chapter 6, we therefore provide an overview of issues related to migration.

## 5. Norway's services trade and the potential impact of trade preferences

Arne Melchior

### Abstract

If the scope for trade preferences for services is increased, current trade patterns may indicate where such preferences may be successfully applied if they are to be effective. The analysis below shows that Norway's trade pattern partly conforms to the global patterns shown in Chapter 4. But due to the proximity and integration with Europe, Norway's services trade with developing countries is more limited than for the world at large.

- Norway has traditionally had large services trade, with shipping exports as a driving force. In spite of the rising importance of the oil and gas sector, services trade is still important, with a share of GDP that is higher than for the Euro area.
- Norway is currently a large net exporter of maritime services and other transport and communication services, and a significant net importer of travel services. The USA is a significant market for shipping and 29% of services exports go to North America. For services imports, 80% comes from Europe.
- Norway's imports of services from developing countries is very limited, and large countries such as China, India and Brazil have much lower shares in Norway's imports of services than for goods. According to the data available, Norway recently did not import services from LDCs. Some imports of tourism may however be unregistered.
- At 50%, the share of services in FDI is somewhat lower for Norway than for the world, due to FDI related to oil and gas. Almost all inward FDI was from OECD or Offshore Financial Centres, while 15% of outward FDI was directed to developing countries. There was virtually no inward FDI from LDCs, and the outward FDI to LDCs was mainly related to oil.
- We have no data on Mode 4 services trade, but since current Mode 4 trade is linked to FDI, the FDI evidence indirectly shed light on Mode 4 as well. In addition, we use migration data to illustrate the geographical distribution of migrants. A large share of immigration into Norway is from developing countries, and 14% of the inward migrant stock was from the LDCs.
- Since Norway's registered services imports from LDCs are close to or equal to zero according to the analysis, the short-term material impact of preferential market access for LDCs in Norway is

likely to be limited. For Mode 4, there may be scope for an increase if market access is improved for less skilled workers. This is however a politically controversial issue and the impact will depend on the measures taken. In order to help the LDCs develop their services sectors, the analysis suggests that aid and investment will be more important than market access discrimination. Hence a wider perspective on SDT (Special and Differential Treatment) is needed.

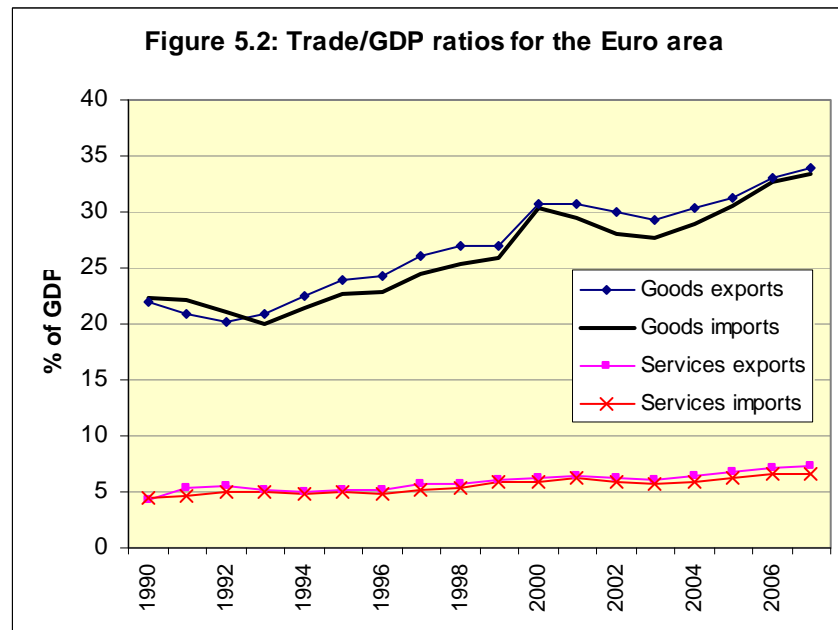
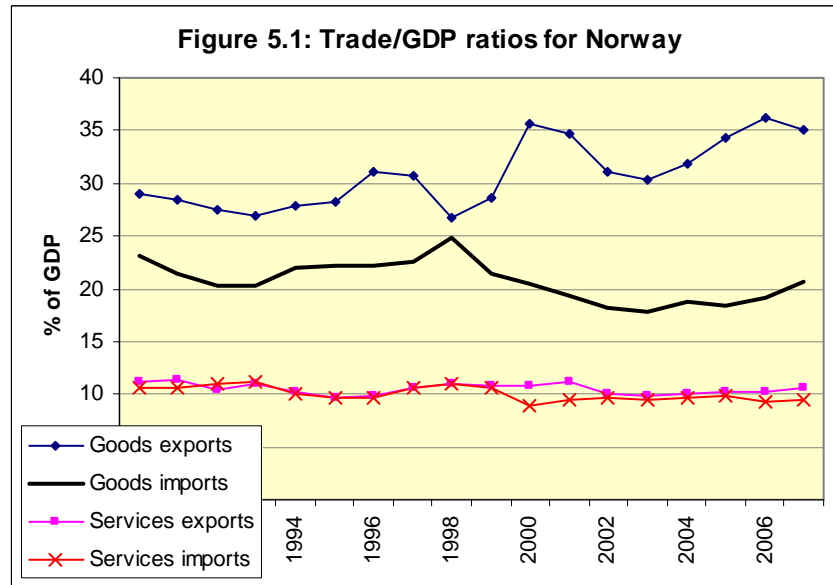
## 5.1. Introduction

Norway is a small and rich country. The relationship between income level and services trade was examined in Chapter 4. Norway's trade pattern in services partly corresponds to the global patterns shown there. In addition, there are other particular features which strongly affect Norway's services trade:

- Through the European Economic Area (EEA) Agreement, Norway is fully integrated in the EU internal market. This includes far-reaching liberalisation for services trade, FDI and even labour movements.
- Norway is abundant in some natural resources (oil and gas, hydroelectric power, fish) and especially the oil sector has strong influence on the economy in general and the trade pattern.
- Norway *smallness* implies that it is sometimes a marginal market: when an LDC starts outward FDI, Norway is not likely to be the first destination.

## 5. 2. Norway's cross-border services trade

Norway has traditionally relied more on services exports than other OECD countries; especially due to exports of maritime services (shipping). This is still the case, in spite of the fact that oil and gas exports have shifted the balance towards a growing export surplus for trade in goods. Figures 5.1 and 5.2 show exports and imports as % of GDP, for of goods and services and for Norway and the Euro area, respectively (data source: World Development Indicators).



The trade/GDP ratio for services is substantially higher for Norway than for the Euro area. This gap however decreased over time, due to a rising ratio in the Euro area and a slight fall in this ratio for Norway. Both export and imports of services was in 2004 around 10% of GDP in Norway, with a modest export surplus. Services trade also grew considerably, but growth was smaller than for Norwegian GDP (hence the falling shares) as well as services trade in the Euro area.

Table 5.1 provides an overview of the composition of Norway's services trade in 2004, in terms of trade partners and services sectors. In the table, all values for exports (imports) are expressed in % of total services exports (imports). Hence the top rows in each sec-



tion of the table gives the allocation across geographical areas for total services exports and imports, respectively, and the column to the right (Sum) gives the allocation across sectors. In the lowest part, we show simple specialisation indexes ranging from -100 (only imports) to 100 (only exports).<sup>22</sup>

<b>Table 5.1: Norway's services trade in 2004: Distribution across sectors and geographical areas</b>							
	<b>Area</b>						
	<b>EU/EEA</b>	<b>Other Europe</b>	<b>North America</b>	<b>Central &amp; South America</b>	<b>Africa</b>	<b>Asia &amp; Oceania</b>	<b>Sum</b>
<b>Services exports (% of total)</b>							
<b>Services, total</b>	<b>57.44</b>	<b>3.45</b>	<b>28.74</b>	<b>2.68</b>	<b>0.51</b>	<b>7.18</b>	<b>100</b>
Maritime services	20.26	1.95	17.89	0.97	0.16	4.97	<b>46.21</b>
Other transp./comm.	8.97	0.25	1.73	0.62	0.13	0.31	<b>12.01</b>
Travel services	9.22	0.54	1.28	0.01	0.02	0.19	<b>11.27</b>
Financial services	2.87	0.13	0.75	0.08	0.00	0.10	<b>3.93</b>
Business services	14.75	0.50	6.74	1.00	0.14	1.47	<b>24.60</b>
Other services	1.36	0.09	0.35	0.00	0.06	0.12	<b>1.98</b>
<b>Services imports (% of total)</b>							
<b>Services, total</b>	<b>73.96</b>	<b>5.11</b>	<b>10.82</b>	<b>1.09</b>	<b>0.70</b>	<b>8.31</b>	<b>100</b>
Maritime services	17.98	1.77	2.64	0.68	0.48	6.88	<b>30.44</b>
Other transp./comm.	4.87	0.46	0.96	0.02	0.01	0.26	<b>6.57</b>
Travel services	30.99	1.39	2.24	0.05	0.04	0.13	<b>34.83</b>
Financial services	2.52	0.09	0.81	0.25	0.00	0.06	<b>3.73</b>
Business services	16.19	1.30	3.69	0.08	0.10	0.78	<b>22.14</b>
Other services	1.42	0.11	0.47	0.02	0.07	0.19	<b>2.29</b>
<b>Specialisation index (between -100 and +100)</b>							
<b>Services, total</b>	<b>-9</b>	<b>-16</b>	<b>48</b>	<b>45</b>	<b>-12</b>	<b>-3</b>	<b>4</b>
Maritime services	10	9	76	21	-48	-12	<b>24</b>
Other transp./comm.	33	-26	32	94	89	13	<b>33</b>
Travel services	-51	-41	-24	-57	-21	22	<b>-48</b>
Financial services	10	20	0	-48	-23	29	<b>6</b>
Business services	-1	-42	33	87	21	34	<b>9</b>
Other services	2	-8	-12	-100	-5	-18	<b>-3</b>
<b>Memo item: Area distribution for Norway's trade in goods (2004)</b>							
Goods exports	76.73	3.81	12.3 7	1.20	0.45	5.44	100
Goods imports	66.46	9.42	7.20	2.54	1.09	13.29	100
Data source: Calculated on the basis of Statistics Norway: External account by country, Table 3 on <a href="http://www.ssb.no/urland/">http://www.ssb.no/urland/</a> . More detail on classification is available there.							

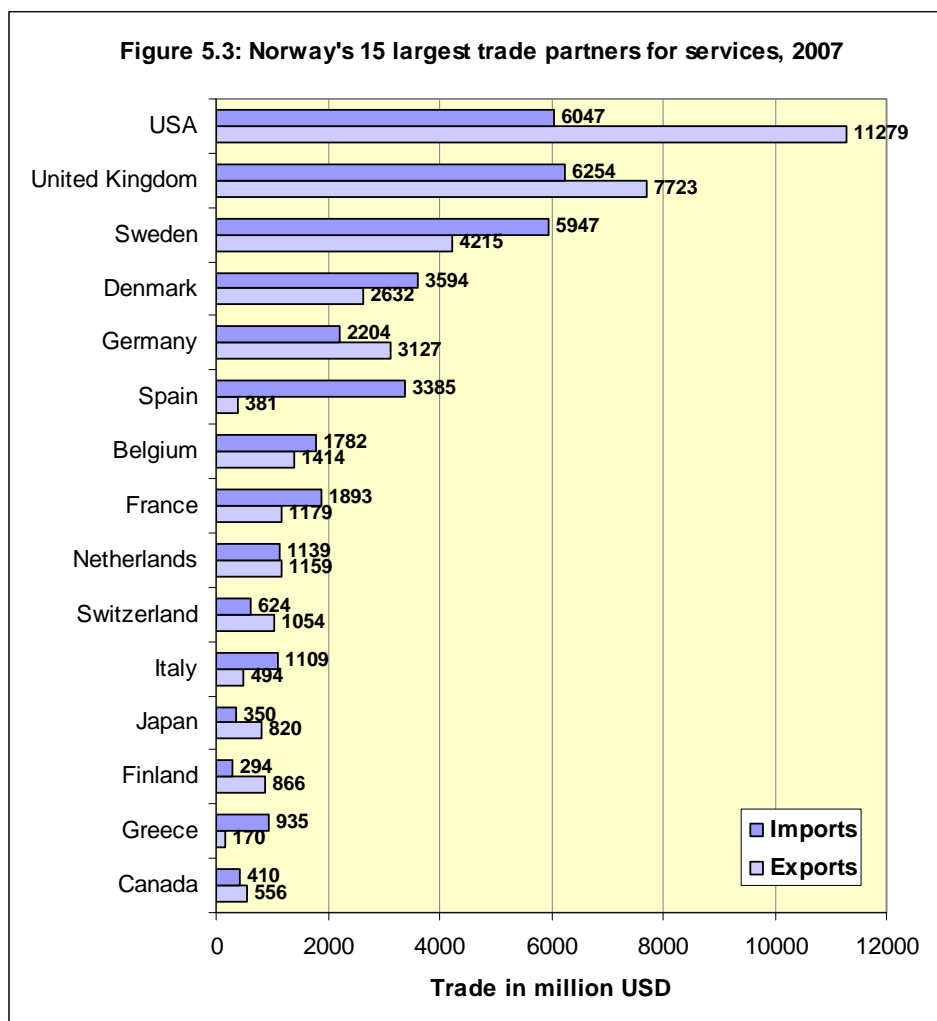
The bottom rows also show, as a benchmark for comparison, the geographical distribution for goods trade. Here the share for the

<sup>22</sup> These are calculated as  $100 \cdot (x-m)/(x+m)$ , where  $x$ =exports and  $m$ =imports.

EU/European Economic Area is particularly high for exports, since exports of oil and gas are mainly destined for the EU. But even for goods imports, the EU/EEA share is a high 2/3.

Along with trade in goods, Norway's services imports are strongly concentrated on the EU/EEA, with a 74% share. Services exports are more dispersed, especially due to the high share of shipping exports to the USA. As shown by the specialisation index, Norway has a considerable trade surplus for maritime services in general and particularly to North America, and these exports represent 18% of total services exports. Norway also has a significant trade surplus for other transport/ communication services, but a substantial deficit for travel services. Observe that for maritime services, there are also large imports which are partly reflecting the substantial costs related to the shipping activity. Hence shipping leads to two-way trade in services, with freight charges one way and payment for local services (port fees, catering, repair, supply etc.) in the opposite direction.

On the bilateral pattern of trade, data availability is limited but improving. Services trade data should include consumption abroad (e.g. tourism) but it goes without saying that this is not easy to measure. It is therefore uncertain to what extent Mode 2 services trade is appropriately covered by the current data. Figure 5.3 shows Norway's largest trade partners for services in 2007, based on the United Nations Service Trade Statistics Database (<http://unstats.un.org/unsd/servicetrade/default.aspx>).

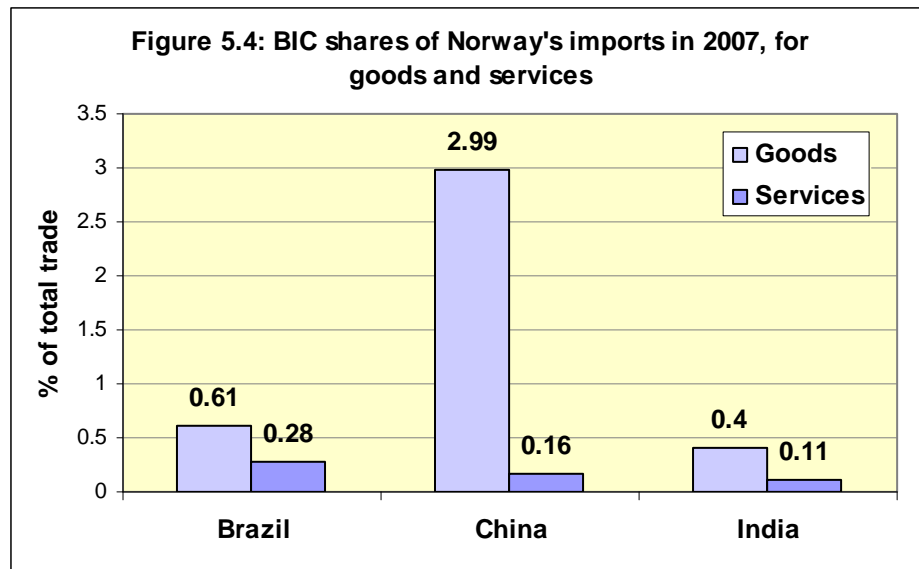


All the 15 largest trade partners in 2007 were OECD countries. Further down the list we find some developing countries, but not too many. This is shown in greater detail in Appendix Table A1, where we show all the countries included in the UNSTAT data on bilateral total services trade for Norway. Here we find a few developing countries, including Brazil (0.28% of Norway's services trade in 2007), China (0.16%) and India (0.11%). The small number of developing countries on the list may partly be due to data limitations, but nevertheless suggests that *services trade is disproportionately concentrated on high-income countries and European trade partners*. According to these data, *Norway has no services trade with the LDCs*.<sup>23</sup> There may however be trade, e.g. related to tourism, that is not captured by the currently available data.

While China is already a giant in international merchandise trade, and India is by now famous for its accelerating services exports,

<sup>23</sup> In Appendix Table A1 we have included an aggregate figure for Central and Southern Africa, where some exports are observed, but imports from this group are zero.

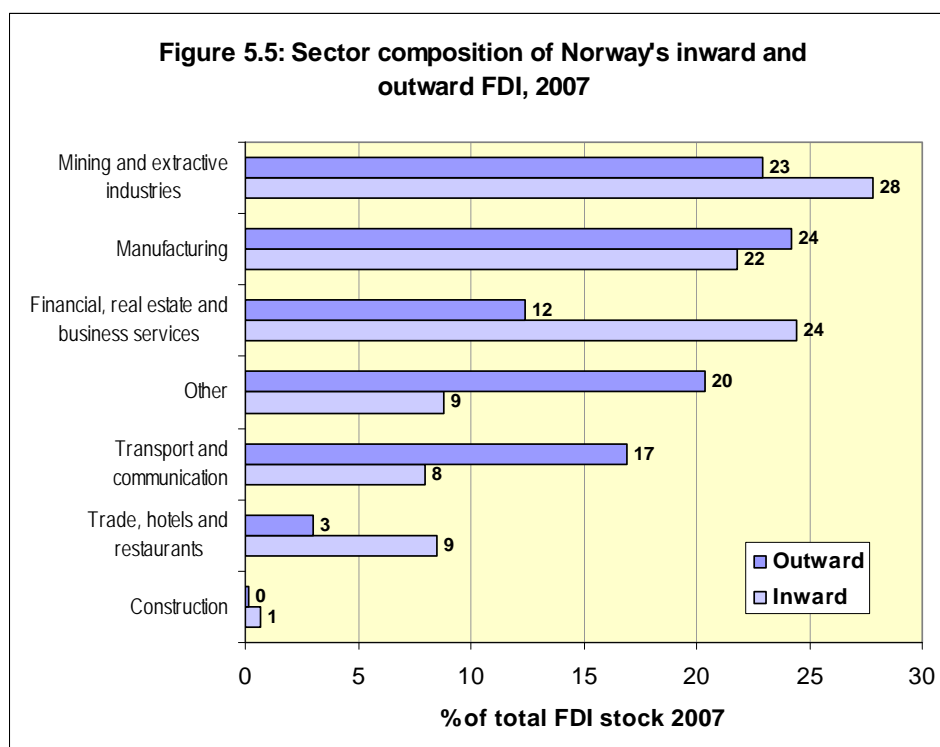
their shares in Norway's service trade are minimal. This is shown in Figure 5.4, covering three of the "BRIC" countries (therefore named BIC). The diagram shows the shares of these countries in Norway's imports of goods and services.



This illustrates that Norway's trade pattern in services mirrors what we also see in global services trade statistics: Exports are heavily dominated by high-income countries. This is particularly the case for skill-based services (see Chapter 4). Figure 5.4 may suggest that *due to the smallness of the Norwegian market as well as proximity and integration with European countries, imports from developing countries are particularly limited.*

### 5.3. FDI and Norway's services trade

Norway's FDI pattern broadly corresponds to the global pattern: There is a net outflow, and developing countries have a low share of inward but higher share of outward FDI. Services however have a slightly lower share of Norwegian FDI than for the world average. This is mainly due to the important role of FDI related to oil and gas, as shown in Figure 5.5.



The share for mining/extractive industries + manufacturing has remained around 50% for inward as well as outward FDI during the last years. Hence the share for services is lower for Norway than for the world total. Tables A2 and A3 in the Appendix show more detail. To a large extent, the pattern for FDI reflects the pattern for services trade: Financial and business services have a large share for inward FDI whereas transport services including shipping are important in outward FDI. For maritime services, there is also significant inward FDI.

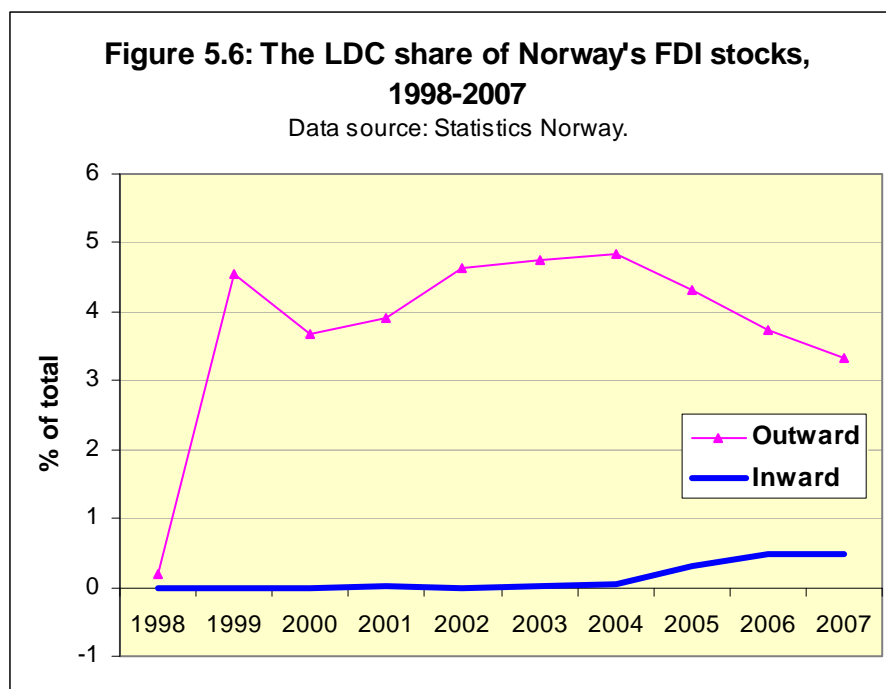
We do not have FDI data for Norway that are disaggregated by sectors and countries simultaneously, so we have to examine the country distribution only for aggregate FDI.<sup>24</sup> With respect to countries, Norway's FDI is even more strongly concentrated on the OECD than the world total. This is shown in Table 5.2.

<sup>24</sup> Such data have not been published but could be constructed by Statistics Norway at some cost. For the purpose of this project, however, it was considered that such data would not be required.

<b>Table 5.2: Norway's FDI by main country groups</b>								
Data source: Statistics Norway, online data bank <a href="http://www.ssb.no/di">www.ssb.no/di</a> .								
<b>(A) Figures in million NOK.</b>								
	Inward				Outward			
	2004	2005	2006	2007	2004	2005	2006	2007
OECD	277977	294531	329862	347940	314327	390904	456379	525190
Offshore Fin. Centres	6095	6914	11615	18558	33593	42737	68411	74436
Others	-2083	-1783	4587	1542	63955	73233	105174	96412
World	281989	299662	346064	368040	411875	506874	629964	696038
<b>(B) Shares of total (%)</b>								
	Inward				Outward			
	2004	2005	2006	2007	2004	2005	2006	2007
OECD	98.6	98.3	95.3	94.5	76.3	77.1	72.4	75.5
Offshore Fin. Centres	2.2	2.3	3.4	5.0	8.2	8.4	10.9	10.7
Others	-0.7	-0.6	1.3	0.4	15.5	14.4	16.7	13.9
World	100	100	100	100	100	100	100	100

Almost all inward FDI is from the OECD, with a slight additional contribution from Offshore Financial Centres. For outward FDI, countries except OECD and Offshore Centres represented around 15%. Hence some outward FDI is directed towards developing countries, but this is lower than the share of 24% for developing countries in world inward FDI (see Chapter 4).

For outward FDI, we even find a role for the Least Developed Countries (LDCs). This is shown in Figure 5.6.

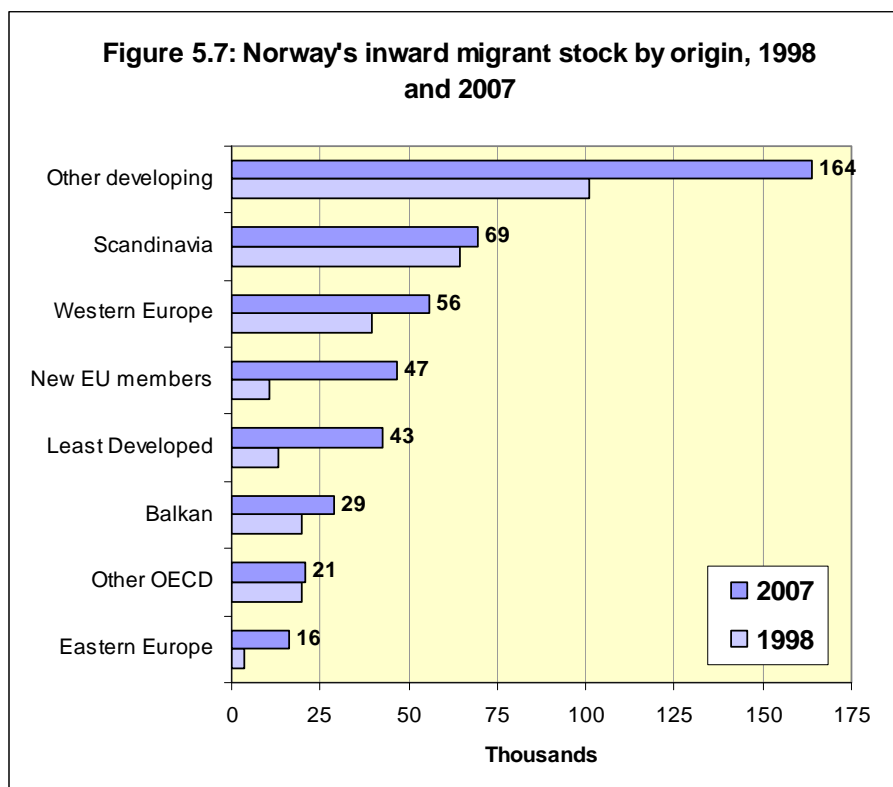


From 1999 onwards, there have been substantial oil-related investments in Angola, which accounts for about 2/3 of the outward FDI stock in LDCs. The rest is mainly captured by Liberia, and this is presumably related to the shipping register of Liberia. This was also the reason why the inward FDI stock from LDCs increased somewhat in 2005-2007 (the lower curve). Hence *beyond the shipping activity in Liberia, there is little evidence of Norwegian services-related FDI in the LDCs.*

#### **5.4. Temporary migration in services?**

Corresponding to Norway's pattern of FDI, much of the Mode 4 trade of this type would be related to OECD countries, but with some outward movement to developing countries related to investment in oil and gas, manufacturing and shipping. Given that inward FDI from developing countries to Norway is zero if we exclude the offshore centres, there will be little Mode 4 exports of this type from developing countries to Norway. There is certainly substantial movement of persons related to trade, but not related to FDI. Given that Mode 4 exports from developing countries to Norway are limited, and probably close to zero for the LDCs, we have not attempted to provide more detailed statistical evidence on FDI-related temporary movements.

While the LDCs are mostly absent in Norway's inward services trade and FDI, they are strongly represented in the inward migrant stock. As noted, migration is very different from Mode 4 trade but nevertheless may illuminate some aspects that are relevant for Mode 4. Figure 5.7 shows the share of various country groups in the Norwegian inward migrant stock (data source: OECD 2009).



Liberalising Mode 4 trade by allowing semi- and low-skilled workers, or allowing more seasonal work under the GATS for non-EEA countries, could potentially increase Mode 4 trade. This is however likely to be a controversial issue: In Norway, as elsewhere, immigration is strictly regulated and there are sharp political debates about current migration policies and trends.

In Norway, migration is currently regulated by the new immigration act adopted in 2009 and the accompanying regulation containing more specific rules (Ministry of Justice and the Police 2008, 2009). The law as well as the regulation entered into force 1.1.2010. It is interesting that the law includes a “carve-out” with respect to international treaties in §23 (on workers hired by Norwegian firms) as well as §24 (individual service suppliers and staff of foreign services firms). While the normal precondition is a needs assessment; i.e. that it is impossible to obtain suitable workers from Norway or the EEA, this can be dispensed with if this follows from international treaties that Norway is part of. The individual needs assessment for non-EEA workers can also be dropped for particular categories of skilled labour delivering services (§24). For services delivery, the law also includes a parity condition for wage and working conditions; these should not be inferior to applicable wage agreements or what is normal for the relevant place and profession (§24). The law also allows quotas and group permissions for seasonal work (§23). Particular rules apply to



EEA citizens that have privileged access for services delivery and the labour market.

Due to the carve-out provisions of the immigration act, the impression is that the law is not an obstacle to improved Mode 4 market access. This would however be a political issue.

### **5.5. On the potential impact of trade preferences for LDCs**

The analysis in this chapter has shown that Norway's imports of services from LDCs are close to or equal to zero, according to available services trade data as well as FDI statistics. There is some inward FDI related to Liberia and shipping, but this could hardly be a main target for new trade preferences. It could be the case that available trade statistics is underreporting, for example for tourism. For tourism, it is however not likely that import restrictions in Norway are the main impediments to more trade, so the scope for preferences is limited. As shown by Grosso et al. (2007), investment in tourism-linked sectors in LDCs would be important for developing tourism further, but this would hardly be influenced by preferences related to Norway's GATS commitments.

When trade is zero, it cannot be scaled up or down in any trade model and this suggests that the short-term impact of services trade preferences for LDCs is likely to be limited. For Mode 4, it is less certain what the impact might be. During recent years, temporary migration from the EEA has increased considerably, for example for seasonal labour in agriculture. In principle (see Chapter 6), Mode 4 could be implemented more widely to cover such seasonal labour and this could allow more Mode 4 trade.

The limited short-term impact of market access preferences suggests that other forms of SDT (Special and Differential Treatment) are more important than GSP-type discrimination, at least for Norway and in the shorter run. Aid to infrastructure, human capital formation, regulation and standardisation and other purpose could be used to promote the development of the services sectors in LDCs, and our analysis suggests that such measures could be more important than trade discrimination.

## 6. International Migration, the Least Developed Countries and the WTO

Arne Melchior

### Abstract

This chapter provides a survey with some new evidence on aspects of international migration. While Mode 4 trade constitutes a very small share of international migration, this broader evidence sheds light on some aspects that are also relevant in the GATS context.

- International migration, especially South-to-North migration of skilled labour has increased rapidly in recent decades and migrants now constitute 9% of the population in the OECD. 44% of international migration is South-South. The poorest countries have lower emigration rates and for the LDCs, 61% of outward migration is to low-income countries. International migration and Mode 4 in the GATS are therefore not North-South issues but global issues.
- Emigration of skilled labour contributes to a “brain drain” but in some cases, the prospect of emigration can lead to more investment in education and the net result may be a “brain gain”. This is more likely for large countries such as India, but for poor countries with limited skills the brain drain can be a real problem. In spite of this, some LDCs consider skilled emigration as a future prospect. For temporary migration, concerns for brain drain are less relevant.
- According to current practice, GATS covers foreign individuals and foreign firms delivering services, but not foreigners employed by host country services firms. There is however some ambiguity in the GATS legal text and a future option is to allow the latter category and thereby recruitment of temporary workers by host country firms. If the LDCs are granted new special provisions in the GATS, one option is to extend the scope of GATS in this way only for the LDCs, in addition to providing more or deeper commitments.
- Temporary migration may easily become permanent and current regimes for temporary migration in the OECD are generally based on strict implementation regimes. These are in several cases based on bilateral cooperation where source countries also have responsibility for screening, return and control. Mode 4 liberalisation without appropriate control regimes is likely to be an illusion, and a waiver should therefore extend flexibilities on implementation and allow bilateral arrangements.

## 6.1. Introduction

In recent years, major international institutions have argued that large global welfare gains could be obtained by relaxing barriers to international migration. The World Bank (2006, p. 34ff.) argued that increased migration from developing to developed countries can lead to global welfare gains in the order of 350 billion USD or 0.6% of world GDP. About one half of the gains accrue to the 15 million new migrants from poor to rich countries, who triple their income. Walmsley and Winters (2003) obtained comparable estimates, and argued that these could be obtained also by means of temporary migration.

The gains from migration are in line with what is to be expected from a neoclassical trade model with capital and labour: Countries can trade and obtain gains from specialisation, with labour-abundant countries exporting the labour-intensive goods (such as clothing etc.) in exchange for imports of capital-intensive goods. But if countries are too different in terms of factor composition, they will specialise in different goods and no more reallocation of factor use can happen through trade. Beyond some point, there is nothing more to gain from trade specialisation. Through migration, however, further gains can be obtained.

In spite of the optimistic estimates, the political enthusiasm in rich countries is limited. Immigration is in most rich countries a contentious political issue, involving a host of issues such as cultural identity, fiscal burdens, illegal immigration and workers' rights. In this situation, some have argued that *temporary* migration is a solution: the gains from migration may be obtained without the burdens. According to Winters (2003, 60): "Unlike the concerns associated with the mass migration of less skilled workers, fears for cultural identity, problems of assimilation, and the drain on the public purse are hardly relevant for the temporary movement of natural persons. The biggest concern it raises is its competitive challenge to local less skilled workers. But this challenge is no more imposing than that presented to such workers by imports of labour-intensive goods from developing countries, which has been overcome by the weight of gains that such trade can deliver and by policies to easy adjustment ...". Furthermore, temporary migration avoids the brain drain problem, which could otherwise represent a problem, especially for small developing countries.

Supported by such arguments, developing countries in the WTO have intensified their demand that there should be liberalisation also for Mode 4 movement of labour beyond experts and intra-company transferees related to FDI. Liberalisation of "the temporary movement of natural persons" (TMNP) for developing countries in general is however politically unrealistic even in the DDA, and from the proposals tabled so far it seems that a rather limited liberalisation

for skilled labour is what may be expected (see e.g. Adlung 2008). If a “waiver” is accepted that allows preferential treatment for LDCs (Least Developed Countries) in the field of services trade, an issue is whether such a waiver should be used to provide mode liberal access in Mode 4 exclusively for LDCs. This is indeed what the LDCs hope for; see documents in Appendix B.

As demonstrated in Chapters 4 and 5, LDCs have limited supply capacity for many services sectors; especially those with higher skill requirements (financial services, telecom, business services etc.). Hence in these sectors, preferential market access for LDCs in rich countries may have modest impact. Tourism-related services constitute an exception where LDCs are significant suppliers, but the future development of the services industries of the LDCs is not primarily hampered by import barriers in rich countries (see e.g. Honeck 2008, Grosso et al. 2006). While some such barriers exist, the main obstacle seems to be development of infrastructure and linked industries in the LDCs themselves, which can be promoted by better access to investment (Mode 3) in their own markets, and Aid-for-Trade related to infrastructure and tourism. Some scope surely exists for GSP-like market access preferences for LDCs in rich countries, but the overall impact, at least in Norway, will hardly be massive.

Given the limited potential impact of rich country preferences for LDCs in Modes 1-3 (cross-border trade, consumption abroad and commercial presence/ investment), the attention has turned to Mode 4. LDCs may supply unskilled labour to the rich countries. When asked about the potential impact of LDC preferences in services, the unambiguous answer from LDCs themselves is: Mode 4.

Increased temporary movement from LDCs to developed countries raises a number of issues that are also relevant in the context of migration. For example, it is argued that the brain drain is primarily a problem for permanent migration, and with Mode 4 trade one may obtain the gains while avoiding the brain drain problem. An examination of the brain drain issue, based on the migration literature and related evidence, is therefore relevant as a background for discussing measures in GATS. Similarly, potential Mode 4 liberalisation raises a number of control problems, for example that temporary migrants may try to become permanent. Such problems are familiar in the migration context and a review is therefore useful also for the GATS context.

## **6.2. Migration: Not only a North-South issue**

In the WTO context, migration is a North-South issue where developing countries are the “demandeurs”: Rich countries should allow temporary migration from poor countries. In the context of an LDC waiver, the implicit expectation is that rich countries are the ones that

should grant better market access. Our first message is: Migration is not mainly a North-South issue. This is only 1/3 of the truth, and especially for the poorest countries, it may be grossly misleading.

Using the bilateral data matrix of migrant stocks in 226 countries at the Development Research Centre on Migration, Globalisation and Poverty (Migration DRC, 2007) we aggregate migrant stocks by the income groups of the origin and destination countries. Income group classification is missing for some countries, and with these countries deleted we have a data matrix for 208 countries, covering 167 million migrants in 2000. Table 6.1 shows the origin and destination income groups of these migrants, with absolute figures in millions and % of the world total. In the lower part of the table, we also show the allocation across destination income groups for the LDCs, the Small Island Developing States (SIDS, with two different definitions), and the group of landlocked developing countries.

<b>Table 6.1: The world migrant stock 2000, according to the income levels of origin and destination countries</b>						
Source: Calculations based on Migration DRC (2007)						
(A) The number of migrants in millions						
		Income level of destination country				All countries
		High	Upper middle	Lower middle	Low	
Income level of sending country	High	26	2	3	1	31
	Upper middle	16	1	2	1	19
	Lower middle	32	8	24	4	68
	Low	14	5	8	21	48
All countries		87	16	36	27	167
(B) In % of the total world migrant stock						
		Income level of destination country				All countries
		High	Upper middle	Lower middle	Low	
Income level of sending country	High	15.3	1.1	1.6	0.7	18.8
	Upper middle	9.5	0.8	1.0	0.4	11.7
	Lower middle	19.2	5.0	14.2	2.5	40.9
	Low	8.2	2.7	4.9	12.9	28.6
All countries		52.2	9.7	21.7	16.5	100.0

While the projected migrant stock in 2010 is 214 mill. persons (UNDP 2009, 146), the countries used for calculations here cover 167 million in 2000, when the stock was 195 million. A migrant is a person living in a country and born abroad. Our data generally cover legal migration and in addition there is illegal migration, which varies strongly across countries and may represent between 10 and 60% of the reported stocks (World Bank 2006, 62).

The table shows that slightly more than half of the world migrant stock goes into high income countries. Observe that this is not only the OECD, but some Middle East and Asian high income countries are significant migration destinations. If we count Upper+Lower middle and Low income countries as developing countries and sum the figures in 6.1(B), we obtain Table 6.1(C).

		Destination	
		High income	Other
Origin	High income	15.3	3.5
	Other	36.9	44.3

For trade and investment, a large share of the world total is between rich countries, but for migration the figure is much lower: Only 15% of world migrant stocks in 2000 were between high income countries. Only 37% of world migration in 2000 was from South to North, and the largest part (44%) was between developing countries.

In spite of representing less than half of the total, South-North migration has recently been the most dynamic component (Lowell 2007). People in rich countries do not often migrate to live in poorer places, so the share of migration from “High” to “Other” above is low. This is further illustrated in Table 6.2, which shows the allocation of migration across rows and columns in Table 6.1 above.

(A) Share of destinations by income groups						
		Income level of destination country				All countries
		High	Upper middle	Lower middle	Low	
Income level of sending country	High	81.4	6.1	8.7	3.8	100
	Upper middle	81.7	7.0	8.3	3.1	100
	Lower middle	46.9	12.2	34.8	6.2	100
	Low	28.7	9.5	17.0	44.9	100
All countries		52.2	9.7	21.7	16.5	100
(B) Share of origin countries by income groups						
		Income level of destination country				All countries
		High	Upper middle	Lower middle	Low	
Income level of sending country	High	29.3	11.9	7.6	4.4	18.8
	Upper middle	18.2	8.5	4.4	2.2	11.7
	Lower middle	36.7	51.6	65.6	15.4	40.9
	Low	15.7	28.0	22.4	78.1	28.6
All countries		100	100	100	100	100

For upper middle and high income countries, more than 80% go to high income, but this share is lower for the poorer countries. Especially for low-income countries 45% go to other low-income countries. Hence for developing countries, a considerable part of migration goes to other developing countries. This also applies to LDCs. Table 6.3 shows figures as in Table 6.2(A) for LDCs and some other groups of interest.

Country group	Income level of destination country				All countries
	High	Upper middle	Lower middle	Low	
Least Developed Countries (LDCs)	18.2	6.7	14.5	60.6	100
Small Island Dev. States (SIDS, def. 1)	84.8	4.4	5.2	5.7	100
Small Island Dev. States (SIDS, def. 2)	84.9	3.6	5.0	6.6	100
Landlocked developing countries	12.2	4.7	49.7	33.4	100

Hence for the LDCs, 61% of outward migration is to low-income countries. Migration is not only economically motivated but also driven by wars, natural disasters etc. The cost of migration and the lack of skills may also be a reason why they more often migrate to other poor countries in the neighbourhood.

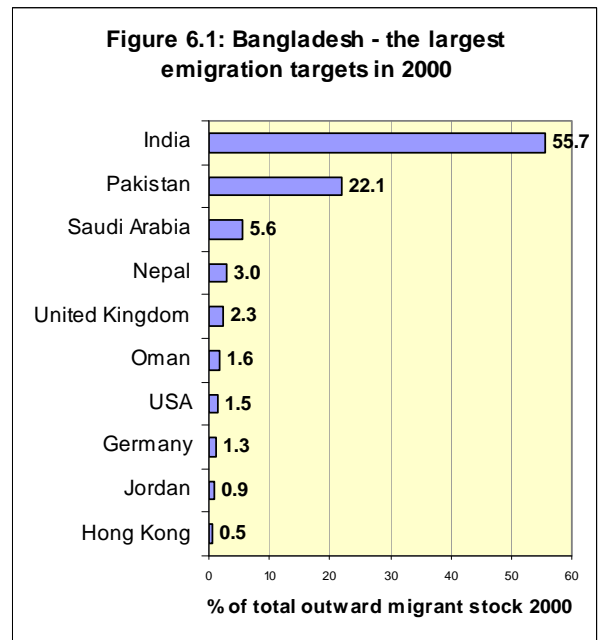
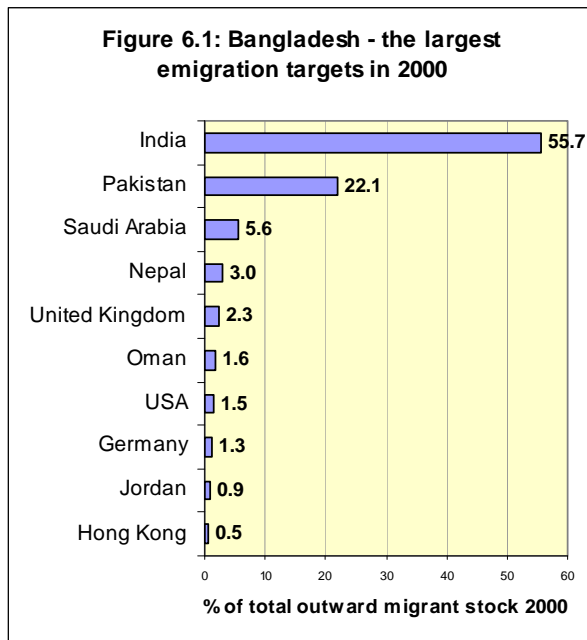
Observe also the strikingly different results for Small Island Developing States (SIDS), which also includes many LDCs.<sup>25</sup> These results show that for the SIDS, a very high share of migration is for high-income countries. For a number of Pacific Islands, the USA or Australia is the main migration target.

Worldwide migration is highly restricted and one might argue that if regimes had been more liberal, a higher share of poor country migration would go to rich countries. This contains some truth, but immigration restrictions also exist in poor countries. Hence the pattern observed in Tables 6.1-6.3 is not only a matter of restrictions, but it also reflects other aspects. In particular, geographical distance plays an important role, as shown by several studies (see e.g. Letouzé et al. 2009). Migration declines strongly with distance between the origin and destination. This may have various explanations: The most obvious is that transaction costs are larger for migrating over larger distances. Transaction costs may also be lower due to language or cultural and institutional similarity; it is easier to adapt in your neighbour country than in a remote country with a different language and culture.

<sup>25</sup> For SIDS, no unambiguous definition exists so we have used two alternative definitions, with similar results in both cases. For more about SIDS definition, see <http://www.unctad.org/Templates/Page.asp?intItemID=3620&lang=1>, or <http://www.unohrrls.org/>.

Finally, there may also be a “clustering” phenomenon since rich countries are more often than not located close to other rich countries, and the same applies to the poor. Hence geographical distance may also reflect economic similarity, for example that sector composition and skill requirements are more similar.

An illustration of this proximity factor in migration is Bangladesh. Due to being formerly a part of India, but also due to geographical proximity, the bulk of the Bangladesh outward migrant stock is in India. This is frequently not even included in analyses of international migration for Bangladesh (see e.g. Siddiqui 2003). According to our data set, the outward migration stock of Bangladesh in 2000 was 6.8 millions. The ten largest destinations, accounting for 94% of the total, are shown in Figure 6.1.



Hence almost 80% of Bangladesh’s outward stock was in India and Pakistan, the neighbour country Nepal is also high on the list. Rich countries (UK, USA, Germany) as well as Middle East countries (Saudi Arabia, Oman, Jordan) were important destinations, although much smaller than India and Pakistan. Although not seen from the diagram, countries in South East Asia (e.g. Malaysia, Philippines, Singapore) are also developing as destinations. The situation for Bangladesh is somewhat special since it was in the larger India jointly with Pakistan after independence. But also for other LDCs, we can find a prominence of neighbour countries among the target destinations. As shown in Diagram 6.2, for Rwanda, 75% of migration stock



in 2000 was in Uganda, Tanzania and Kenya. In Africa, there was significant long-distance migration only from a limited number of countries; in terms of absolute numbers the largest are South Africa, Somalia and Senegal (mainly to Europe); Ethiopia (mainly to the USA); and Nigeria and Ghana (split between the two) (Black 2004, see also Black et al. 2004a,b). While the average share of remote emigration for poor countries is low, we have already seen that exceptions are found among island states. There are also other cases, for example due to history and colonial ties. For example, 77% of Cambodia's migrant stock was in USA, France, Australia and Canada.

This "static" picture of migration stocks clearly demonstrates that for the poor countries, and especially the LDCs, a large share of migration is to other developing countries. A policy implication is that preferential market access for LDCs is not an issue only for rich, but also for developing countries. It does not weaken the case for better market access in rich countries, but it shows that many of the concerns related to migration in poor countries are of a South-South nature. For example, UNDP (2009) draws attention to the need for improvement in the living and working conditions of migrants.

### **6.3. Characteristics of South-North migration: The migration "hump"**

For policy purposes, an important issue whether trade preferences for the poorest are economically efficient and stimulate trade, or whether the supply capacity of poor countries is too limited. In Chapters 4 and 5, we have seen that for cross-border trade and FDI, the supply capacity of LDCs is limited, at least for many services sectors. Some evidence suggests that a similar phenomenon is present for migration: The very poorest do not have the resources to migrate, so it is the second poorest that actually do so. Hence also for migration, there may be a threshold that limits the impact of better access to migration for the poor.

As a first illustration of this phenomenon, Table 6.4 expresses outward and inward migrant stocks in % of the total population of the four income groups. For LDCs, SIDs and landlocked developing countries we have calculated the shares only for the outbound stock.

Country group	Outward	Inward
Income group	High	9.0
	Upper middle	4.9
	Lower middle	1.4
	Low	1.2
World	2.7	2.7
Least Developed Countries (LDCs)	3.6	Not calculated
Small Island Dev. States (SIDS, def. 1)	12.3	
Small Island Dev. States (SIDS, def. 2)	16.0	
Landlocked developing countries	6.0	

There is net inward migration in rich countries, and net outward migration for developing countries. The share of inward migration clearly increases by income level; supporting the expectation that migration is at least partly driven by economic motives.

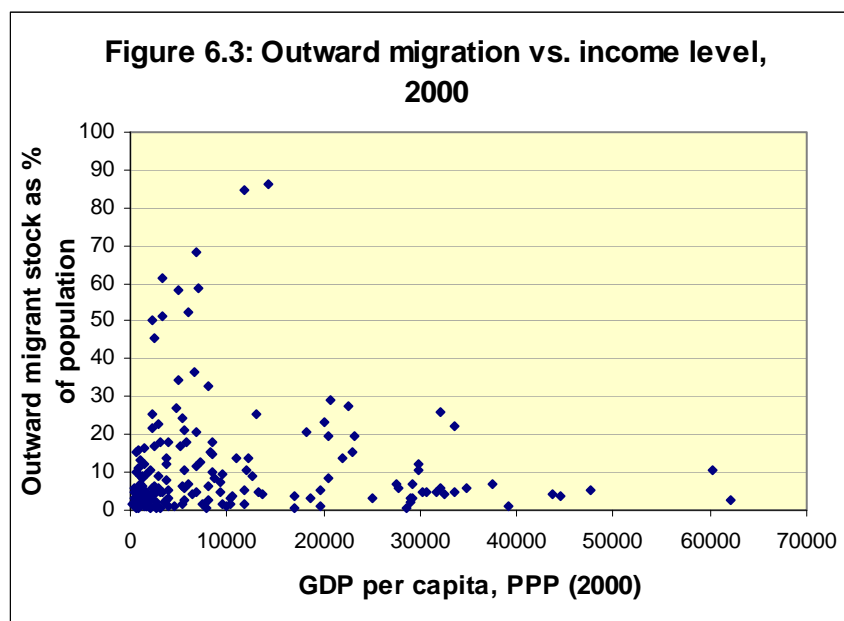
For the outward shares, however, the share is highest in the upper middle income countries and not the low-income. Hence the migration rate is not highest where the income gap is largest, but in the intermediate range. This is a first illustration of what has been called the “migration hump” in the research literature: The emigration rate seems to increase up to some income level and then fall. For example, Letouzé et al. (2009) find a threshold income around 13-14000 USD per capita beyond which the emigration rate tends to fall.

The falling part of this curve is easy to explain: When the income gap is reduced, the incentive to emigrate is lowered, so as countries get richer, their population become more satisfied and stops emigrating. But why does the migration curve increase at low income levels? The standard explanation offered is that the transaction cost of migration is so high that the really poor people cannot afford to migrate. According to de Haas (2007, 832) “The poorest tend to migrate less than those who are slightly better off. This seems particularly true for the relatively costly and risky international migration .... in order to migrate, people need the human, financial and social resources as well as the aspiration to do so.”

A pitfall in the analysis of the “migration hump” is that we should control also for characteristics of receiving countries. In particular, migration is high from middle-income countries that are located close to rich destination countries. For example, North African middle-income countries have more migration to Europe than poor African countries further south, and this may be due to proximity to Europe rather than their higher income level. As noted by Hanson (2008, 7): “Countries with the highest emigration rates tend to be small, poor countries close to the US.” When controlling for distance

and destination country characteristics in their regression analysis, Letouzé et al. (2009) found that the “hump” result became gradually weaker.

The statistical analysis of “hump” issue is also complicated by the presence of many “outliers” or “untypical observations”. This is seen from Figure 6.3 where we plot the outward migrant stock as % of population (vertical axis) against income per capita.<sup>26</sup>



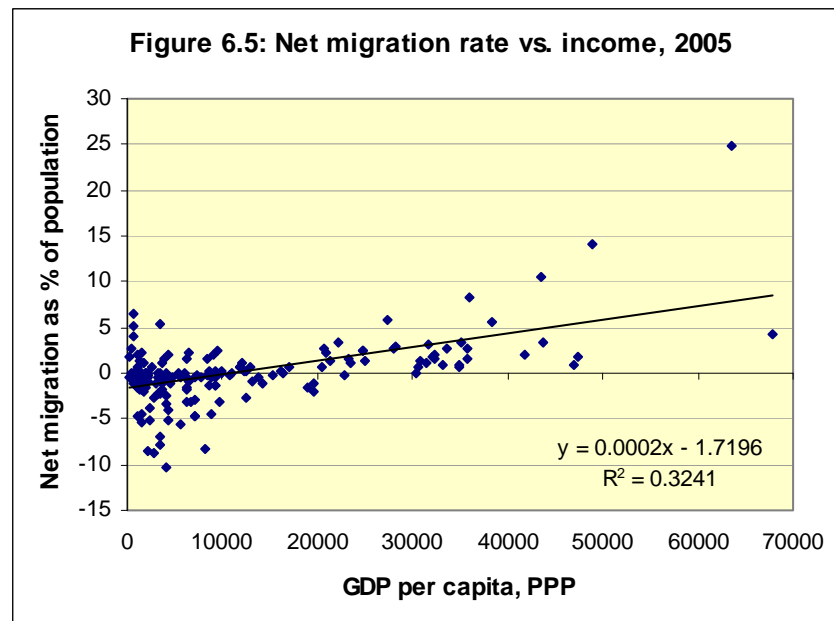
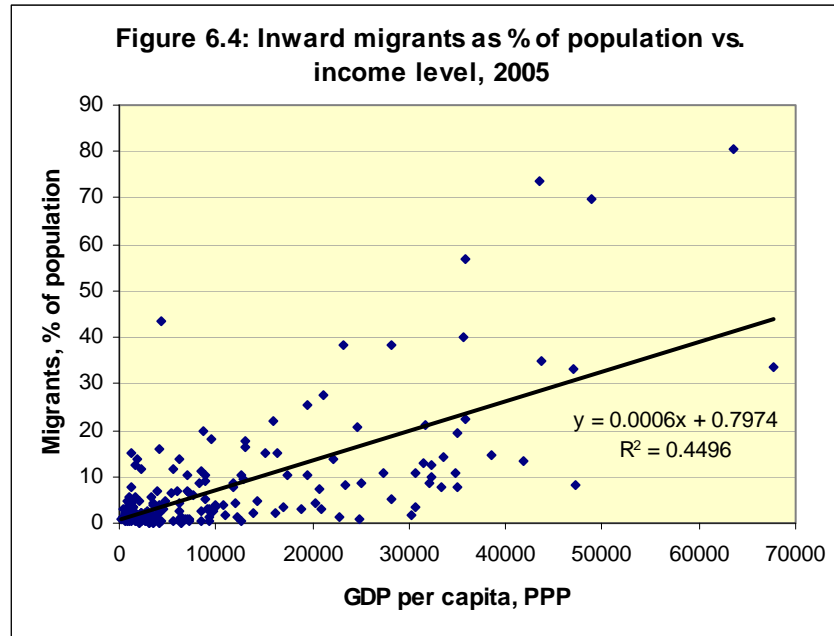
With the outliers included, there is apparently a maximum level at 12-14,000\$, but if we drop the outliers the maximum would be lower. The figure nevertheless supports the idea that for the very poorest countries, the emigration rate is low.

While there is some uncertainty about the robustness and the implications of the “hump” phenomenon, it seems clear that the explanation of de Haas is supported at the micro level: Even for unskilled migration, it is not the poorest that migrate, but intermediate workers. Hanson (2008) presents evidence on the “positive sorting” in international migration; it is generally not the least educated that leave. For example, Mexican emigrants tend to come from the middle of the skill distribution (ibid., 21).

While there is an inverse hump for countries of origin, a similar phenomenon is not evident for destination countries. In Figure 6.4 we plot the *inward* migrant stock as % of population (vertical axis) against income per capita. The graph covers 178 countries in 2005, based on data from the World Development Indicators. In figure 6.5

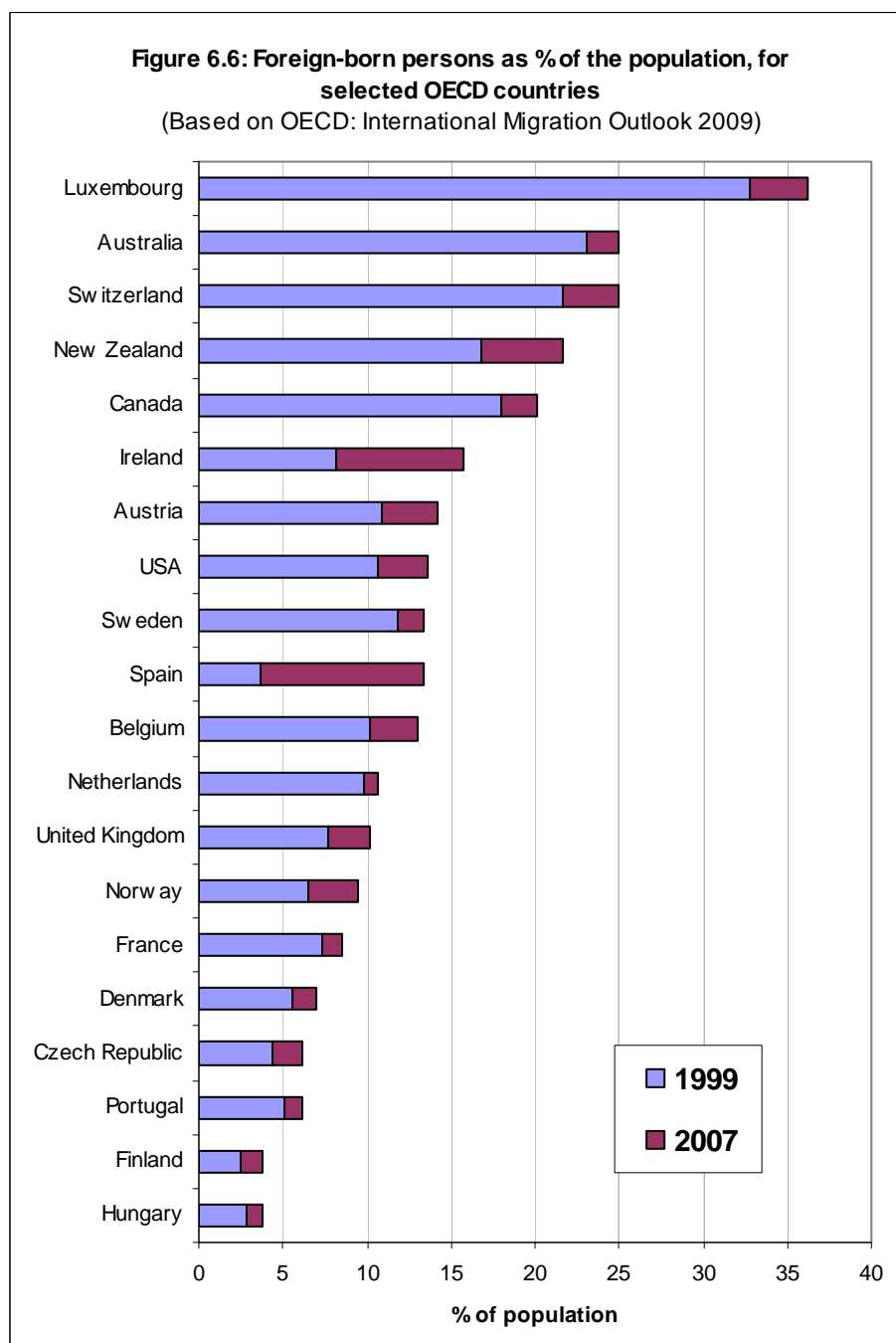
<sup>26</sup> Migration data is also here from Migration DRC (2007), and income and population data are from the World Bank’s World Development Indicators.

we show a similar relationship using net migration rates (net migrant stock as % of the population).



Hence for inward migration there is a more or less monotonous and significant positive relationship: the richer you are, the higher is immigration. The regression line explains 45% of the variation in the data in Figure 6.4, and 32% in 6.5. The remaining 55% or 68% may be explained by immigration policies, geographical location, history and other features. Hence there is considerable room for other influencing factors, but income gaps constitute a main driving force.

Outcomes also vary depending on immigration policy as well as history and geography. A further illustration of this is Figure 6.6 which, based on OECD data, shows migrant stocks as % of the population for selected OECD countries in 1999 and 2007. The selection is based on data availability.



Among these 20 OECD countries, the migrant share varied from 4 to 36%. In all cases there was an increase from 1999 to 2007. Hence

globalisation has not only led to more trade and investment, but also a significant increase in migration. For Europe, the international migrant stock increased from 16 to 64 millions from 1975 to 2005, with the strongest increase during the period 1985-1995 when the inward migrant stock trebled (Lowell 2007). Norway was in 2007 close to the OECD average, with a migrant share at 9.5%. In Chapter 5, the composition of Norway's inward migrant stock is also described.

#### **6.4. Skilled migration and the brain drain**

A general worry about South-North migration is that only skilled labour migrate and that they "drain" the developing countries of valuable skills. It may be argued that this problem does not apply to Mode 4 since it is temporary. This is however not fully convincing since Mode 4 may support "circular" or repeated migration that has more in common with permanent migration. Furthermore, there may be a control problem so that temporary workers try to become permanent. Temporary migration can also increase knowledge about the destination country and thereby also facilitate attempts to migrate permanently. The evidence on brain drain is therefore indirectly relevant.

Skilled migration has recently been the most dynamic element of international migration. From 1990 to 2000, skilled inward migration in the OECD increased by 64% whereas unskilled migration increased by only 14% (Docquier and Marfouk 2006, Docquier and Rapoport 2008, Beine et al. 2008). This has been influenced by several factors, including globalisation and multinational companies; a larger supply of skilled labour in some developing countries such as India; and deliberate policies in various countries to attract skilled labour.

There is considerable variation in the rate of skilled to unskilled migrants across origin as well as destination countries. Some destination countries have immigration policies that make it easier for the skilled to enter. For example, the USA has facilitated the entry of skilled labour through the so-called H1B visas, and only in 2001 more than 160 000 Indian specialists were allowed to immigrate (Nielson and Cattaneo 2003). Table 6.5 shows the share with tertiary education in the inward migrant stock of the OECD in 1990 and 2000, based on Lowell (2007):

**Table 6.5: The share of inward migrants with tertiary education, for OECD countries (including intra-OECD migration)**

	1990	2000
Total	30	35
Europe	26	32
North America	47	58
Latin America and Caribbean	27	26
Asia	40	47
Oceania	40	45
Africa	22	31

The share with tertiary education in the world migrant stock increased from 30% in 1990 to 35% in 2000. For the outward migration from Africa, it increased from 22 to 31%. The emigration rate was higher for skilled labour; for example Lowell (2007) shows that for LDCs the emigration rate in 2000 was around 1% for the whole population and above 10% for the skilled.<sup>27</sup>

According to the state-of-the-art conclusion in the current research literature, brain drain is a problem in some cases, but not all. Countries such as India have a large pool of educated labour and can send some hundred thousands abroad without the country collapsing. Furthermore, the option of migration may increase the incentive for higher education so the net result may be a “brain gain” rather than a brain drain (see e.g. Mountford 1997). Beine et al. (2008, 2009) confirm that skilled emigration prospects promote human capital formation in the origin countries, and thereby provide some support for the brain gain hypothesis. The outcome is however mixed and depends on country characteristics. The authors conclude “We find that most countries combining low levels of human capital and low migration rates for skilled workers end up with a positive net effect. In contrast, the brain drain appears to have negative effects where the migration rate of the highly educated is above 20% and/or the proportion of people with higher education is above 5%. There appears to be more losers than winners and, in addition the former incur *relatively* high losses. However, the gain of the latter dominates in *absolute* terms, resulting in an overall gain for developing countries” (Beine et al. 2008, 632). Docquier and Rapoport (2004, 2008) conclude that the optimal emigration rate for developing countries is positive, but according to an inverse U-shaped curve so the poorest countries should have a lower emigration rate. Also for the brain drain, we have a “hump” that has important policy implications: Unfettered skilled emigration from small and poor countries may not be good for development.

<sup>27</sup> The result was based on Defoort (2006).

Hence while India may gain due to its large pool of skilled labour, other developing countries may not be so lucky and their loss of skills can be costly and damaging. Frequently mentioned examples are related to the emigration of health personnel from developing countries, and several examples are mentioned in Chanda (2001) (according to her analysis, also Indian doctors constituted a problem). For India, 63% of the total migrant stock in six large OECD countries had tertiary education.<sup>28</sup>

Hence on South-North skilled migration, brain drain is selectively a problem but cases of brain gain also exist. Many LDCs have high rates of skilled emigration (Docquier and Marfouk 2006, Varma 2009) and according to this they would be in the problem area with respect to brain drain. Evidence also exists on detrimental brain drain in some African LDCs (Varma 2009). When interviewing LDC representatives, however, a surprising impression was that temporary migration of skilled labour was also considered as a positive prospect. It is hard to say whether this is also affected by political realism, since immigration policies in the OECD are more restrictive for unskilled labour. But even today, some LDCs had a significant share of skilled labour in their outward migrant stock. For example, in 2000 Bangladesh had a share of 37.5% among their emigrants to six OECD countries. In Asia, several countries openly encourage emigration of skilled labour (World Bank 2006, 68). Among LDCs in Africa, there are different attitudes to emigration and Rwanda is an example of a country that aims at becoming a migration hub in the region (Varma 2009). But the evidence on the home country impact of skilled migration is nevertheless mixed, and e.g. the World Bank (2006, 68) concluded that an aggregate, reliable estimate of the impact of such migration is impossible to give. As noted by Varma (2009), skilled emigration could be implemented as part of programs for human capital formation in LDCs and not as an end in itself.

## 6.5. Remittances

For some developing countries, brain drain is a minus on the scorecard of emigration. On the positive side, there are remittances which are, taken together, more than twice the size of international aid flows (World Bank 2006). Remittances are the largest gain from migration to the origin countries. Table 6.6 shows remittances paid and received for the world and major income groups in 2008, in billion current USD and % of aggregate GDP.<sup>29</sup>

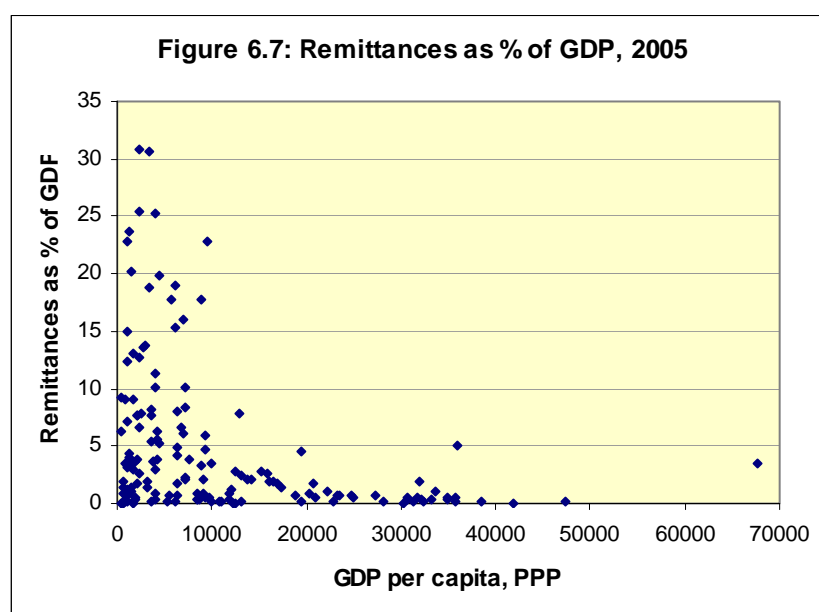
<sup>28</sup> Calculated from the data set World Bank (2009). This is also the source for the Bangladesh figure below.

<sup>29</sup> Data source: World Development Indicators online. The variable definition is "Workers' remittances and compensation of employees, current US\$".



	In billion current USD			In % of GDP for group		
	Paid	Received	Net	Paid	Received	Net
High income	211	105	-106	0.49	0.24	-0.24
Middle income	63	297	234	0.37	1.76	1.39
Low income	2	31	28	0.41	5.41	5.00
LDCs	3	21	19	0.48	3.85	3.37
Sub-Saharan Africa	4	20	16	0.38	2.01	1.62
World	276	433	157	0.46	0.71	0.26

There is a net outflow from high income countries, and a net inflow into developing countries. According to World Bank (2006, ix), South-South remittances make up 30-45% of inward flows in developing countries. For the LDCs, net inflows amounted to 3.4% of GDP which is a significant share. For individual countries, this may sometimes be even higher. This is evident from Figure 6.7, which shows inward remittances as a share of GDP plotted against income levels, for 158 countries in 2005.<sup>30</sup>



For a number of poor countries, remittances constitute a significant share of GDP.

This concludes our overview of migration. The evidence presented does not cover the whole range of issues related to migration. Remittances are but one element in the overall calculation that determines whether migration is beneficial or not for a country as a whole. What is evident from the literature is that the largest gains from migration accrue to the migrants themselves and their families. Statements

<sup>30</sup> Data source: World Development Indicators, online data.

on other effects, for example on labour markets, fiscal balances, brain drain, culture and other aspects, are often exaggerated due to the political sensitivity of the migration issue. The evidence on these additional issues is however often mixed and unambiguous conclusions are hard to make. For a discussion, see Gordon (2008).

## **6.6. Migration and the GATS: The definition of Mode 4**

Mode 4 of GATS only covers a small fraction of global migration; temporary migration related to services. Given the political controversies about migration, temporary migration has been suggested as a remedy that gives the gains without the costs. For example, there would be no brain drain since workers will return back, and the labour market impact as well as the fiscal impact would likely be more limited. On the other hand there could also be some down sides; for example that the transaction cost of moving could be larger relative to the pay, and that learning and adaptation would be more limited. Both these aspects – the cost calculation and the adaptation problem – also limit the scope for temporary migration: The net gain for long-distance migrants may be small if the work period is short, and employers would not hire people who need time to learn how to do the job. For such reasons, temporary migration is different from migration in general. Examples of temporary migration are:

- Temporary movement of staff within multinational companies; which has become much more common due to globalisation and the increased role for multinationals.
- Temporary services jobs abroad, e.g. in business services (accounting, consulting, installation, repair etc.).
- Seasonal work, for example in agriculture.
- Temporary stays to undertake particular business tasks; e.g. related to sales.

The observed increase in temporary migration is partly due to politics: countries do not want permanent immigration and instead opt for the “light version” of temporary visas. According to the World Bank (2006, 72), skilled temporary migration has been stimulated by unilateral visa programs such as the H1B visas in the USA, while unskilled temporary migration has more often been allowed in bilateral or regional agreements. In the GATS, actual Mode 4 commitments have often been linked to Mode 3 (commercial presence), in order to facilitate the cross-border movement of staff involved in the foreign affiliate. For evidence on temporary migration; see e.g. Nielson and Cattaneo (2003).

The definition of GATS' coverage is important and to some extent disputed (for a discussion, see Carzaniga 2008):

- 1) First, it relates to “natural persons who are service suppliers of a Member, and natural persons of a Member who are employed by a service supplier of a Member”.
- 2) Second, GATS does not apply to “measures affecting natural persons seeking access to the employment market of a Member, nor shall it apply to measures regarding citizenship, residence or employment on a permanent basis.”<sup>31</sup>

A natural or “physical” person distinguishes the service supplier from a judicial person; hence GATS only covers the cases where the person moves abroad. In order to illustrate the definition, we use the examples of various service suppliers shown in Table 6.7, in all cases assuming that the natural person is from country A, that service is delivered in country B, and that the stay for this purpose is temporary:

<b>Table 6.7: Cases to illustrate the coverage of GATS</b>			
Note: The natural person is living in country A, and the service is delivered in country B.			
Case No.	Service	Employment status of the natural person	Covered by GATS
1	Auditing of an account	Individual	Yes
2	Auditing of an account	In firm from A	Yes
3	Auditing of an account	In firm from B	No (?)

Cases 1 and 2, where the product as such (accounting) is undeniably a service, and the supplier is an individual or an employee in a firm from A, are clearly covered by GATS. Case 3, where the natural person is employed by a firm in the host country, is less clear. Bullet point 1) above does not sort out the matter since the last term is “a Member” and not e.g. “that member” which would exclude the host country firm. However, we might resort to para 2 and define employment in the host country as a matter of “seeking access to the employment market”. Then case 3 in the table would also be excluded. This issue is however debated: For example, Self and Zutshi (2003, 34) consider the history of GATS negotiations and state that “The issue of employment of foreigners by local firms apparently did not come up for detailed examination, because it was understood that access to the labour market was outside the scope of the coverage under the GATS. The negotiating history of this issue is less clear, and the descriptive language that emerged for mode 4 is ambiguous ... a sound case could be made in favour of multilateralization of such re-

<sup>31</sup> The quotes are from the GATS “Annex on movement of natural persons supplying services to the Agreement”, see [www.wto.org](http://www.wto.org).

cruitment from foreign sources. Participants in the current negotiations should explore this avenue for further liberalization under Mode 4.” It should be added that in practice, the current WTO practice is not fully consequent. For example, the USA has bound in GATS its H1B scheme but this seems to involve migration of type 3 above.

In Table 6.7, the product delivered is clearly a service. An issue is whether the interpretation is the same if the product is a labour service to producing a good. For example, firms in origin countries could deliver “fruit-picking services” to agriculture, or part of any production process for physical goods. In principle, this is still services delivery and in principle it could be considered as cases 1-3 above. The definition of “Other business services” in the current GATS classification lists (WTO 1991) is quite wide and seems to allow these types of services. Since commitments are made on a sector/mode basis, it is nevertheless up to WTO members to decide how wide the definition should be.

According to current practice, it seems justified to interpret “access to the employment market” as excluding case 3 (see also Carzaniga 2008). On the other hand, some ambiguity exists and if WTO members agree, it would be possible to allow case 3. This would be meeting the recently expressed wishes of the UNDP: While the Human Development Report 2009 (UNDP 2009) does not advocate “wholesale liberalisation” for migration (p. 17), it suggests selective steps such as expanding schemes for seasonal work in e.g. agriculture and tourism, and better access for low-skilled migration (ibid., p. 4 and p. 96ff.). Allowing foreign recruitment to domestic firms, as in case 3, and allowing a wide definition of what services are included, would facilitate temporary migration.

### **6.7. A waiver for the LDCs in GATS: More Mode 4 access?**

If a waiver is granted that allows discriminatory treatment in favour of LDCs, it may also be used to facilitate Mode 4 movements. This could be done in various forms:

- Access for LDCs could be provided for additional categories of skilled workers, as an extension of current GATS practice. There is a risk that such measures would have limited impact, given the limited supply of skill-based services. Some LDCs nevertheless see skilled emigration as a future prospect so this approach could be excluded.
- If access is given for less skilled labour categories, the potential would partly depend on how such measures are implemented. A radical approach would be to allow migration as in case 3 above. This would allow systematic recruitment of temporary migrants,

and increase the potential for such migration. If access is provided for

- A waiver could be used to differentiate with respect to duration and possible re-entry of migrants. In the GATS, temporariness is not precisely defined but in practice, business visitors are often allowed 3 months of stay whereas intra-firm transfers are allowed for longer periods – up to 5 years in some cases. This is also a dimension where an extended preference is technically feasible.

For any commitment under Mode 4, a number of implementation and legal issues would have to be considered. On implementation, an issue is how to make sure that migration is temporary and not permanent. Various solutions have been considered in bilateral arrangements, such as deferring the payment to workers until they return, or requiring a bond for employing firms that is forfeited if workers do not return. Some examples of temporary guest worker regimes are discussed in Chanda (2009, on Spain-Ecuador and Canada-Mexico) and Schiff (2008, reviews several others). Such regimes are often highly detailed, they often involve bilateral cooperation, and arrangements on working conditions, possibly extension provisions, and rules for entry and exit. There are also cases where incentives are used to promote temporariness; e.g. that later extension or new visas are more likely for those who return on time. Schiff (2008) includes a theoretical analysis of various arrangements, and concludes that arrangements with foreign firms rather than individuals are better since they provide incentives to keep the defection rate low.

Given that implementation of temporary migration is often supported by bilateral cooperation, an issue is whether a waiver for LDCs would require that any arrangement would be made for all the LDCs jointly, or whether special arrangements are allowed for individual countries. Given that LDCs count about 800 million inhabitants, Mode 4 access without appropriate controls will not be politically accepted. Concerning Mode 4 access granted in the DDA, various authors have argued for implementation arrangements that involve bilateral cooperation and source country responsibilities (see e.g. Chaudhuri et al. 2004, Mattoo 2005). For example, countries that are to benefit of improved market access may have to accept, screening and to combat illegal migration (Mattoo 2005). Such bilateral implementation arrangements could also be allowed under a waiver, in order to make Mode 4 access politically feasible. GATS Article V(bis) allows bilateral labour market integration agreements but it is uncertain whether this would provide a basis for bilateral implementation arrangements. For this reason, it might be considered to include language on this in a waiver as well.

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**Appendix Table A1: Norway's bilateral trade in services in 2007.**

Country	Services trade in million USD			In % of total with the world		
	Exports	Imports	Trade	Exports	Imports	Trade
USA	11279	6047	17326	27.84	15.25	21.61
United Kingdom	7723	6254	13977	19.06	15.77	17.43
Sweden	4215	5947	10162	10.40	15.00	12.68
Denmark	2632	3594	6226	6.50	9.06	7.77
Germany	3127	2204	5330	7.72	5.56	6.65
Spain	381	3385	3766	0.94	8.54	4.70
Belgium	1414	1782	3196	3.49	4.49	3.99
France	1179	1893	3071	2.91	4.77	3.83
Netherlands	1159	1139	2299	2.86	2.87	2.87
Switzerland	1054	624	1678	2.60	1.57	2.09
Italy	494	1109	1603	1.22	2.80	2.00
Japan	820	350	1170	2.02	0.88	1.46
Finland	866	294	1160	2.14	0.74	1.45
Greece	170	935	1105	0.42	2.36	1.38
Canada	556	410	967	1.37	1.03	1.21
Australia	403	315	717	0.99	0.79	0.89
Hong Kong	195	201	396	0.48	0.51	0.49
Ireland	154	239	392	0.38	0.60	0.49
Turkey	4	261	265	0.01	0.66	0.33
Portugal	89	170	259	0.22	0.43	0.32
Austria	181	72	253	0.45	0.18	0.32
Poland	64	168	232	0.16	0.42	0.29
Brazil	141	83	224	0.35	0.21	0.28
Central and Southern Africa	179	0	179	0.44	0.00	0.22
Luxembourg	138	37	175	0.34	0.09	0.22
China	41	88	129	0.10	0.22	0.16
Iceland	58	49	106	0.14	0.12	0.13
Slovenia	8	95	103	0.02	0.24	0.13
India	36	51	87	0.09	0.13	0.11
Cyprus	40	43	83	0.10	0.11	0.10
Russian Fed.	17	52	70	0.04	0.13	0.09
New Zealand	37	24	61	0.09	0.06	0.08
Hungary	17	23	41	0.04	0.06	0.05
Latvia	16	24	40	0.04	0.06	0.05
Estonia	19	19	38	0.05	0.05	0.05
Liechtenstein	30	4	34	0.07	0.01	0.04
Czech Republic	19	14	33	0.05	0.03	0.04
Lithuania	13	14	27	0.03	0.03	0.03
Slovakia	19	6	25	0.05	0.02	0.03
Malta	19	2	20	0.05	0.00	0.03
<b>World</b>	<b>40514</b>	<b>39654</b>	<b>80167</b>	<b>100</b>	<b>100</b>	<b>100</b>

Data source: United Nations Service Trade Statistics Database.

<b>Appendix Table A2: Norway's FDI in 2004-2007 by sector</b>								
Date source: Statistics Norway, <a href="http://www.ssb.no/di">www.ssb.no/di</a> Tables 1 and 2.								
<b>(A) Figures in million NOK.</b>								
	<b>Inward FDI</b>				<b>Outward FDI</b>			
	2004	2005	2006	2007	2004	2005	2006	2007
Mining and extractive industries	110987	135442	149122	182827	106201	170602	221474	177549
Manufacturing	130261	137911	145875	143620	143979	191660	162253	187225
Construction	4280	4177	4788	4611	789	1352	2206	1436
Trade, hotels and restaurants	60648	61413	63165	56094	20506	16814	19704	23141
Transport and communication	49244	47219	55787	52330	68210	79345	132561	130955
Financial, real estate and business services	90855	95047	131794	160736	52166	56805	71472	95996
Other	33272	35491	48477	57722	96976	112511	144400	157604
Sum	479547	516700	599008	657940	488827	629089	754070	773906
<b>(B) Shares in % of total</b>								
	<b>Inward</b>				<b>Outward</b>			
	2004	2005	2006	2007	2004	2005	2006	2007
Mining and extractive industries	23.14	26.21	24.89	27.79	21.73	27.12	29.37	22.94
Manufacturing	27.16	26.69	24.35	21.83	29.45	30.47	21.52	24.19
Construction	0.89	0.81	0.80	0.70	0.16	0.21	0.29	0.19
Trade, hotels and restaurants	12.65	11.89	10.54	8.53	4.19	2.67	2.61	2.99
Transport and communication	10.27	9.14	9.31	7.95	13.95	12.61	17.58	16.92
Financial, real estate and business services	18.95	18.40	22.00	24.43	10.67	9.03	9.48	12.40
Other	6.94	6.87	8.09	8.77	19.84	17.88	19.15	20.36
Sum	100	100	100	100	100	100	100	100
Of which: Mining + extractive + manufacturing	50.31	52.90	49.25	49.62	51.18	57.59	50.89	47.13

**Appendix Table A3: Norway's inward and outward FDI 2004-2007, with an alternative sector division.**

Data source: Statistics Norway, online data.

<b>Inward FDI</b>	<b>Million NOK</b>				<b>Shares of total sectors 45-93</b>			
	2004	2005	2006	2007	2004	2005	2006	2007
45 Construction	2982	3205	3705	3767	2.14	2.28	2.20	2.03
50 Trade and repair of motor vehicles, trade in fuels for motor vehicles	34211	34943	34307	32471	24.56	24.83	20.34	17.54
55 Hotels and restaurants	843	651	1527	1831	0.61	0.46	0.91	0.99
61 Maritime transport	15593	14240	22785	20689	11.19	10.12	13.51	11.17
62 Air transport	13092	14325	15021	16444	9.40	10.18	8.91	8.88
65 Financial services excluding insurance and pension funds	44185	47627	54667	62667	31.72	33.84	32.41	33.84
70 Trade and management of real estate	27029	23864	35038	44658	19.40	16.95	20.77	24.12
85 Health and social services	153	161	223	285	0.11	0.11	0.13	0.15
92 Leisure activity, cultural services and sports	828	864	586	187	0.59	0.61	0.35	0.10
93 Other personal services	394	872	814	2177	0.28	0.62	0.48	1.18
94 Private purchase/sale of holiday houses and apartments	25526	26342	32349	40988				
Sum 45-93	139310	140752	168673	185176	100	100	100	100
<b>Outward FDI</b>	<b>Million NOK</b>				<b>Shares of total sectors 45-93</b>			
	2004	2005	2006	2007	2004	2005	2006	2007
45 Construction	337	730	1963	1213	0.29	0.63	1.07	0.58
50 Trade and repair of motor vehicles, trade in fuels for motor vehicles	8108	9072	10302	12644	7.07	7.78	5.59	6.00
55 Hotels and restaurants	368	521	164	297	0.32	0.45	0.09	0.14
61 Maritime transport	23583	36589	48155	51414	20.57	31.39	26.14	24.38
62 Air transport	39459	34107	77101	79023	34.41	29.26	41.85	37.48
65 Financial services excluding insurance and pension funds	6315	8369	9963	23874	5.51	7.18	5.41	11.32
70 Trade and management of real estate	32859	26932	36124	41981	28.66	23.11	19.61	19.91
85 Health and social services	4	0	0	0	0.00	0.00	0.00	0.00
92 Leisure activity, cultural services and sports	283	273	503	353	0.25	0.23	0.27	0.17
93 Other personal services	3350	-47	-49	62	2.92	-0.04	-0.03	0.03
94 Private purchase/sale of holiday houses and apartments	71816	87830	116614	135144				
Sum 45-93	114666	116546	184226	210861	100	100	100	100

**Table A4: All destinations for Norwegian outward FDI (stocks, 2007).**

Figures in million NOK.

Rank	Country	Mill. NOK	Rank	Country	Mill. NOK
1	Sweden	103433	39	Estonia	932
2	Spain	66019	40	China	927
3	Singapore	57837	41	Libya	918
4	Belgium	56142	42	Serbia and Montenegro	833
5	Netherlands	54012	43	Czech Rep.	818
6	U S A	44560	44	Peru	760
7	Denmark	44117	45	Lithuania	745
8	UK	41460	46	Italy	646
9	Germany	33280	47	Malaysia	501
10	France	26679	48	Cayman Islands	438
11	Canada	19253	49	Hong Kong	376
12	Angola	16199	50	Vietnam	358
13	Russia	12650	51	Portugal	290
14	Algeria	10232	52	Luxembourg	288
15	Turkey	8758	53	Colombia	257
16	Bermuda	8329	54	United Arab Emirates	248
17	Azerbaijan	8053	55	Mexico	241
18	Pakistan	7647	56	Tanzania	233
19	Liberia	6544	57	Malta	218
20	Venezuela	6410	58	India	209
21	Ukraine	6226	59	Nepal	157
22	Brazil	6111	60	Argentina	153
23	Thailand	5830	61	Færøyene	111
24	Hungary	5147	62	Marocco	106
25	Finland	4750	63	Saudi Arabia	103
26	Cyprus	4133	64	Mauritius	87
27	Australia	2751	65	Panama	80
28	Austria	2624	66	Egypt	74
29	South Africa	2423	67	New Zealand	68
30	Chile	2118	68	Oman	66
31	Ireland	2093	69	Indonesia	54
32	South Korea	2093	70	Japan	54
33	Poland	1717	71	Sri Lanka	44
34	Latvia	1676	72	Bulgaria	37
35	Switzerland	1596	73	Philippines	28
36	Iran	1458	74	Croatia	26
37	Slovakia	1152	75	Taiwan	9
38	Iceland	1144	76	Greece	5

Data source: Statistics Norway, online data on [www.ssb.no/di](http://www.ssb.no/di)

## **Appendix B: A selection of relevant WTO documents on SDT in services**

- B1 Modalities for the Special Treatment for Least-Developed Country Members in the negotiations on trade in services, WTO document TN/S/13, 5 September 2003.
- B2 Relevant parts of Annex C of the WTO Hong Kong declaration of December 2004 (WTO document WT/MIN(05)/DEC)
- B3 Communication from the Republic of Zambia on behalf of the LDC group, WTO document TN/S/W/59, 28 March 2006.
- B4 WTO Chairman's summary 2008, Elements required for the completion of the services negotiations, WTO document TN/S/34, 28 July 2008.

## **B1: Common WTO text from 2003 on services and the LDCs**

# **WORLD TRADE ORGANIZATION**

**TN/S/13**  
5 September 2003

(03-4637)

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**Council for Trade in Services  
Special Session**

### **MODALITIES FOR THE SPECIAL TREATMENT FOR LEAST-DEVELOPED COUNTRY MEMBERS IN THE NEGOTIATIONS ON TRADE IN SERVICES**

Adopted by the Special Session of the Council for Trade in Services on 3 September 2003

#### **I. OBJECTIVES AND PRINCIPLES**

1. In pursuance of the objectives of the GATS and as required by Article XIX:3 of the GATS special treatment for least-developed country Members (LDCs) shall be granted by providing special priority to LDCs in the implementation of paragraphs 1 and 2 of Article IV of the GATS. Particular account shall be taken of the serious difficulty of LDCs in undertaking negotiated specific commitments in view of their special economic situation and their development, trade and financial needs.

2. The importance of trade in services for LDCs goes beyond pure economic significance due to the major role services play for achieving social and development objectives and as a means of addressing poverty, upgrading welfare, improving universal availability and access to basic services, and in ensuring sustainable development, including its social dimension. LDCs are facing serious difficulty in addressing a number of complex issues simultaneously, and lack institutional and human capacities to analyse and respond to offers and requests. This should be factored into the negotiating process in general and regarding the individual requests made to LDCs.

3. Together with the Guidelines and Procedures for the Negotiations on Trade in Services (S/L/93), the Modalities for the Special Treatment for Least-Developed Country Members in the Negotiations on Trade in Services shall ensure maximum flexibility for LDCs and shall form the basis for the negotiations.

#### **II. SCOPE**

4. Members shall take into account the serious difficulty of LDCs in undertaking negotiated specific commitments in view of their special economic situation, and therefore shall exercise restraint in seeking commitments from LDCs. In particular, they shall generally not seek the removal of conditions which LDCs may attach when making access to their markets available to foreign service suppliers to the extent that those conditions are aimed at achieving the objectives of Article IV of the GATS.



5. There shall be flexibility for LDCs for opening fewer sectors, liberalizing fewer types of transactions, and progressively extending market access in line with their development situation. 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 which may go beyond their institutional, regulatory, and administrative capacities. In response to requests, LDCs may make commitments compatible with their development, trade and financial needs and which are limited in terms of sectors, modes of supply and scope.

6. Members shall, as provided for in Articles IV and XIX of the GATS, give special priority to providing effective market access in sectors and modes of supply of export interest to LDCs, through negotiated specific commitments pursuant to Parts III and IV of the GATS. LDCs should indicate those sectors and modes of supply that represent priority in their development policies, so that Members take these priorities into account in the negotiations.

7. Members shall work to develop appropriate mechanisms with a view to achieving full implementation of Article IV:3 of the GATS and facilitating effective access of LDCs' services and service suppliers to foreign markets.

8. Members shall take measures, in accordance with their individual capacities, aimed at increasing the participation of LDCs in trade in services. Such measures could include:

- strengthening programmes to promote investment in LDCs, with a view to building their domestic services capacity and enhancing their efficiency and export competitiveness;
- reinforcing export/import promotion programmes;
- promoting the development of LDCs' infrastructure and services exports through training, technology transfer, enterprise level actions and schemes, intergovernmental cooperation programmes, and where feasible, financial resources; and
- improving the access of LDCs' services and service suppliers to distribution channels and information networks, especially in sectors and modes of supply of interest to LDCs.

9. It is recognized that the temporary movement of natural persons supplying services (Mode 4) provides potential benefits to the sending and recipient Members. LDCs have indicated that this is one of the most important means of supplying services internationally. 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 categories of natural persons identified by LDCs in their requests.

10. LDCs shall be granted appropriate credit for their autonomous trade liberalization. In addition, Members shall refrain from requesting credits from LDCs.

11. In developing any multilateral rules and disciplines, including under GATS Articles VI:4 (Domestic regulation), X (Emergency safeguard measures), XIII (Government procurement) and XV (Subsidies), Members shall take into account the specific interests and difficulties of LDCs.

### **III. PRINCIPLES FOR THE PROVISION OF TECHNICAL ASSISTANCE WITH REGARD TO TRADE IN SERVICES**

12. Targeted and coordinated technical assistance and capacity building programmes shall continue to be provided to LDCs in order to strengthen their domestic services capacity, build institutional and human capacity, and enable them to undertake appropriate regulatory reforms. In pursuance of Paragraph 14 of the Guidelines and Procedures for the Negotiations on Trade in Services

(S/L/93), technical assistance shall also be provided to LDCs to carry out national assessments of trade in services in overall terms and on a sectoral basis with reference to the objectives of the GATS and Article IV in particular.

#### **IV. MECHANISMS AND PROCEDURES**

13. The Special Session of the Council for Trade in Services shall review, as necessary, the implementation of these modalities under the standing item on "Review of Progress in the Negotiations".

14. In his report to the Trade Negotiations Committee, the Chairman of the Special Session of the Council for Trade in Services will include the issues raised by Members with regard to these modalities.

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## **B2. Relevant part of Annex C of the WTO Hong Kong declaration of December 2004**

... achieve a progressively higher level of liberalization of trade in services, with appropriate flexibility for individual developing country Members,

Page C-2

3. Members shall pursue full and effective implementation of the Modalities for the Special Treatment for Least-Developed Country Members in the Negotiations on Trade in Services (LDC Modalities) adopted by the Special Session of the Council for Trade in Services on 3 September 2003, with a view to the beneficial and meaningful integration of LDCs into the multilateral trading system.

Page C-3

9. Members, in the course of negotiations, shall develop methods for the full and effective implementation of the LDC Modalities, including expeditiously:
  - (a) Developing appropriate mechanisms for according special priority including to sectors and modes of supply of interest to LDCs in accordance with Article IV:3 of the GATS and paragraph 7 of the LDC Modalities.
  - (b) Undertaking commitments, to the extent possible, in such sectors and modes of supply identified, or to be identified, by LDCs that represent priority in their development policies in accordance with paragraphs 6 and 9 of the LDC Modalities.
  - (c) Assisting LDCs to enable them to identify sectors and modes of supply that represent development priorities.
  - (d) Providing targeted and effective technical assistance and capacity building for LDCs in accordance with the LDC Modalities, particularly paragraphs 8 and 12.
  - (e) Developing a reporting mechanism to facilitate the review requirement in paragraph 13 of the LDC Modalities.

10. Targeted technical assistance should be provided through, *inter alia*, the WTO Secretariat, with a view to enabling developing and least-developed countries to participate effectively in the negotiations. In particular and in accordance with paragraph 51 on Technical Cooperation of this Declaration, targeted technical assistance should be given to all developing countries allowing them to fully engage in the negotiation. In addition, such assistance should be provided on, *inter*

*alia*, compiling and analyzing statistical data on trade in services, assessing interests in and gains from services trade, building regulatory capacity, particularly on those services sectors where liberalization is being undertaken by developing countries.

**WORLD TRADE  
ORGANIZATION**

RESTRICTED

**TN/S/W/59**  
28 March 2006

(06-1426)

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**Council for Trade in Services  
Special Session**

Original: English

**COMMUNICATION FROM THE REPUBLIC OF ZAMBIA  
ON BEHALF OF THE LDC GROUP**

A Mechanism to Operationalize Article IV: 3 of the GATS

The following communication, dated 27 March 2006, was received from the delegation of the Republic of Zambia on behalf of the LDC group, with the request that it be circulated to Members of the Council for Trade in Services.

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**I. BACKGROUND**

1. Article IV:3 of the GATS provides the mandate for granting special priority to LDCs by stating that "special priority shall be given to the least-developed country Members..." in the liberalization of market access in sectors and modes of supply of export interest to them, among other things. However, there is no mechanism through which this 'special priority' can be accorded to LDCs,<sup>1</sup> which means that currently, any special treatment accorded to LDCs would have to be extended on an MFN basis in order to comply with the MFN obligation. This would nullify the "special priority" clause, a consequence that is not contemplated in the GATS.<sup>2</sup>

2. WTO Members are aware of this gap and they have expressly recognized this in paragraph 7 of the LDC Modalities<sup>3</sup> which provides that:

"Members shall work to *develop appropriate mechanisms* with a view to achieving full implementation of Article IV:3 of the GATS

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<sup>1</sup> The GATT, on the other hand, has several preferential treatment mechanisms, for example: the Decision on Differential and More Favourable Treatment, Reciprocity, and Fuller Participation of Developing Countries - Decision of 28 November 1979 (L/4903) (the Enabling Clause), which replaced the GSP Waiver - Decision of 25 June 1971 (BISD 18S/24); and the Preferential Tariff Treatment for Least Developed Countries (Waiver adopted on 15 June 1999) (WT/L/304).

<sup>2</sup> "One of the corollaries of the "general rule of interpretation" in the Vienna Convention on the Law of Treaties (1969) is that interpretation must give meaning and effect to all the terms of the treaty. An interpreter is not free to adopt a reading that would result in reducing whole clauses or paragraphs of a treaty to redundancy or inutility": *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/AB at p.23. This principle has been applied in many subsequent WTO cases: See Appellate Body Repertory of Reports and Awards 1994 – 2004 at [www.wto.org](http://www.wto.org).

<sup>3</sup> Modalities for the Special Treatment for Least-Developed Country Members in the Negotiations on Trade in Services (TN/S/13) – adopted by the Special Session of the Council for Trade in Services on 3 September 2003.

and facilitating effective access of LDCs' services and service suppliers to foreign markets "(Emphasis added).

3. Recently, paragraph 9 of Annex C of the Hong Kong Ministerial Declaration affirmed this provision by reiterating that Members shall expeditiously develop appropriate mechanisms for according special priority to sectors and modes of supply of interest to LDCs. This is in line with paragraph 3 of Annex C of the Hong Kong Ministerial Declaration which says Members shall pursue full and effective implementation of the LDC Modalities with a view to the beneficial and meaningful integration of LDCs into the multilateral trading system.

4. The mechanism for operationalising Article IV:3, that is, providing special priority to LDCs, has to be developed by Members. The LDC Modalities have made this clear, as has Annex C of the Hong Kong Ministerial Declaration. In addition, Annex C says that Members shall develop the mechanism within the course of the negotiations. This implies that the mechanism should be adopted in the present negotiations, as part of the single undertaking, and within the stated deadlines. Paragraph 11(e) of Annex C substantiates this view because it states that Members shall strive to develop the mechanism by 31 July 2006.

5. In light of the above, LDCs could propose the following mechanism for negotiation among and adoption by the Members:

## **II. THE PROPOSED DRAFT TEXT OF THE MECHANISM**

### Understanding on Article IV:3 of the GATS

*Members,*

*Recognizing* the low level of participation in world trade in services by the least developed countries, and the need to ensure their effective participation in the world trading system by taking further measures to improve their trading opportunities;

*Reaffirming* the need for positive efforts to ensure that developing countries, especially the least developed among them, secure a share in the growth of world trade commensurate with the needs of their economic development;

*Recognizing* that enhanced market access has an important role to play in ensuring that least-developed countries secure a share in the growth of world trade commensurate with the needs of their development;

*Noting* that Article IV:3 of the GATS provides that special priority shall be given to least-developed countries;

*Recognizing* that currently there is no operational mechanism for effectively implementing the provisions of Article IV:3;

*Considering* that Paragraph 3 of Annex C of the Hong Kong Ministerial Declaration requires full and effective implementation of the LDCs Modalities as an objective of the negotiations; and that Paragraph 47 of the Hong Kong Ministerial Declaration calls on Members to implement the Modalities for the Special Treatment for Least Developed Country Members in the Negotiations on Trade in Services and to give special priority to sectors and modes of supply of interest to least developed countries;

*Considering* also that Paragraphs 6 and 7 of the LDCs Modalities and Paragraph 9 of Annex C of the Hong Kong Ministerial Declaration require Members to develop appropriate mechanisms with a view to achieving full implementation of GATS Article IV:3;

*Desiring* to provide a mechanism to make Article IV:3 operational, consistent with the abovementioned LDCs Modalities and the Hong Kong Ministerial Declaration;

Hereby *agree* as follows:

1. Notwithstanding any provision of the GATS, non-reciprocal special priority shall be accorded only to least developed countries in sectors and modes of supply of interest to them.
  2. Developed country Members shall, and developing country Members declaring themselves in a position to do so should, accord non-reciprocal special priority to least developed countries.
  3. Any special priority provided under this Understanding:
    - shall be designed to facilitate and promote the exports of least developed countries;
    - shall be designed, and if necessary, modified, to respond positively to the development, financial and trade needs of least developed countries as identified by the least developed countries concerned;
    - shall be provided on a permanent basis and in a manner that ensures security, stability and predictability.
  4. Members providing special priority under this Understanding to least developed countries shall notify the Council for Trade in Services of the special priority that they are providing. Based on such notifications and Members' Schedules of commitments, the Council for Trade in Services shall annually review the special priority that Members are providing to least developed countries with a view to ensuring that positive commitments are made in favor of LDCs.
  5. All least developed countries shall be treated as affected Members for the purposes of Article XXI when a Member modifies the special priority provided pursuant to this Understanding. Compensatory adjustments will be made only in favour of least developed countries.
  6. The dispute settlement provisions of the GATS and the Dispute Settlement Understanding may be invoked with respect to any matter arising from this Understanding.
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## **B4: WTO Council for Trade in Services, Chairman summary 28 July 2008**

ELEMENTS REQUIRED FOR THE COMPLETION OF THE SERVICES NEGOTIATIONS, WTO document TN/S/34, 28 July 2008 (extract).

Members reaffirm their commitment to fulfil the requirements set out in paragraph 9(a) of Annex C of the Hong Kong Ministerial Declaration regarding the development of appropriate mechanisms for according special priority including to sectors and modes of supply of interest to LDCs. Members welcome the Note by the Secretariat "Options to Implement the LDC Modalities" (JOB(08)/8). Of the options identified in this paper, Members are of the view that a waiver, available to all Members, from the obligations of Article II, paragraph 1 of the GATS in respect of preferential treatment benefiting all LDC Members offers the most satisfactory outcome of this negotiation. Members shall strive to complete negotiations on the specific principles and characteristics of such a waiver before the revised offers are submitted, in accordance with the sequence of the timelines set out in paragraph 11 (e) of Annex C of the Hong Kong Ministerial Declaration.

10. Members shall continue to give due consideration to proposals on trade-related concerns of small economies. In recognizing their special situation, further liberalization shall be in accordance with their development needs.
11. Members shall complete the consideration of proposals on special and differential treatment, referred to the Special Session of the Council for Trade in Services by the Special Session of the Committee for Trade and Development, with a view to making clear recommendations for a decision by the General Council prior to the conclusion of the DDA negotiations.
12. Members recognize the special situation of recently-acceded Members who have undertaken extensive market access commitments at the time of accession. This situation will be taken into account in the DDA negotiations.
13. Members recall and reaffirm that targeted technical assistance as agreed in paragraph 10 of Annex C of the Hong Kong Ministerial Declaration is intended to enable developing countries and LDCs to participate effectively in the negotiations. In this regard, Members request the WTO Secretariat to prepare, prior to the submission of revised offers, a comprehensive report of technical assistance activities it has carried out in services since the Hong Kong Ministerial



Conference, to enable Members to identify further required activities, on the basis of which the Secretariat, in consultation with Members, could provide a roadmap for future efforts before the end of the negotiations.

# Appendix C: Fact sheets for trade in services

## Explanatory notes

**Data source:** IMF Balance of Payment Statistics (as of September 2009)

**Data coverage:** The number of countries covered varies across variables and over time, and the number for the total and for LDCs are indicated on each fact sheet. For each country, 1990-2007 includes 18 observations. Calculations for the country subgroups were first undertaken (i) with all observations included; (ii) only for countries with full time series coverage; and (iii) for countries with maximum 5 years missing in the time series. Then it was considered which results had the best trade-off between consistency (constant sample over time); country coverage (number of countries included, in particular LDCs); and time-series coverage. In some cases alternative (iii) was used; and in some cases alternative (i); and in general some years were deleted from the fact sheet graphs when coverage was too limited or variation over time too large. We nevertheless allow some variations in the sample size over time in order to increase coverage, and the graphs should be interpreted with some caution due to this. Hence some fluctuations over time may be caused by countries being added or dropped from the sample. This is the price we pay for better data coverage; using option (ii) above as a criterion would reduce the coverage of LDCs severely since data are often missing for individual years.

**Classification of sectors:** See attached descriptions on the last pages. Observe that the IMF classification is not identical to the classification of services in CPC (see <http://unstats.un.org/unsd/cr/registry/regcst.asp?Cl=25>). The following sectors are covered:

- Services, total
- Transport services
  - o Passenger transports
  - o Freight transports
- Travel services
- Communication services
- Construction services
- Insurance
- Financial services
- Computer services
- Royalties, license fees etc.
- Other business services

- Other business services, miscellaneous business, professional, technical services
- Personal, cultural, recreational services
- Government services not elsewhere included

Other items:

- Trade in goods
- Migrants' transfers
- FDI

## Country groups

The country classification used in the analysis builds on the World Bank's income classification as of 2009 (see

<http://go.worldbank.org/D7SN0B8YU0>). The LDCs and the EU27 are grouped separately so the classification looks as follows:

- Least Developed Countries (LDC): After Cape Verde graduated in 2007 there are 49 countries classified by the UN (ECOSOC) as LDCs. The LDCs belong to different income groups: 35 are low-income, 12 are lower middle income (Angola, Bhutan, Djibouti Kiribati, Lesotho, Maldives, Sudan, Solomon Islands, São Tomé and Príncipe, Timor-Leste, Vanuatu, Samoa) and one is high-income (Equatorial Guinea). Tuvalu is not on the World Bank income classification list but can probably be considered as lower middle income.
- EU: The 27 EU countries are classified in different World Bank categories (High-income OECD, High-income non-OECD and Upper middle income) but we prefer to show the EU as a distinct group.
- Other low and lower middle income (LLM): There are eight low-income countries that are not LDC (Ghana, Kenya, Kyrgyz Republic, Korea, Dem. Rep., Tajikistan, Uzbekistan, Vietnam and Zimbabwe) and 43 lower middle income countries (including large countries such as China, India and Indonesia).
- Upper middle income (UM): There are 46 countries in the World Bank's upper middle income category but five are EU members and included in EU-27 in our classification. Hence 41 countries remain in this group, including countries such as Russia, South Africa and Turkey.
- Other high-income (High): This group includes 43 countries, e.g. the USA, Japan, Korea, non-EU countries in Western Europe.

In order to see which individual countries are in each group, the World Bank link above may be consulted.

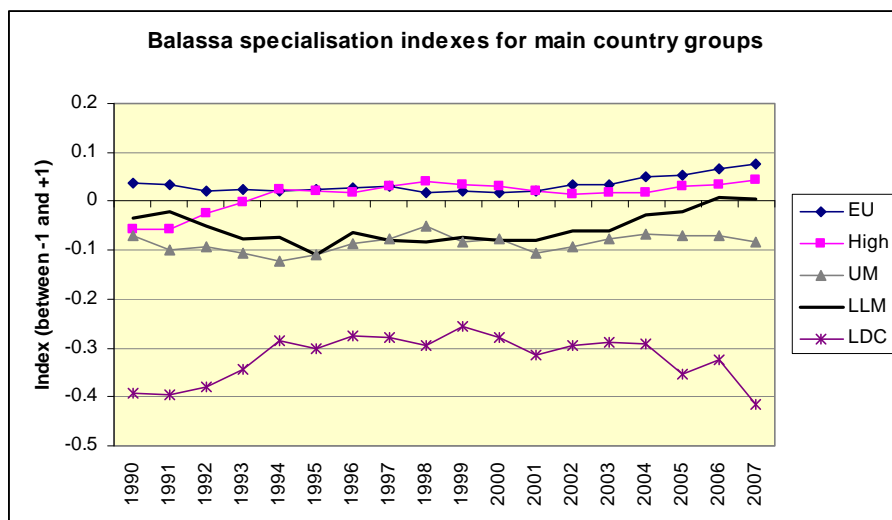
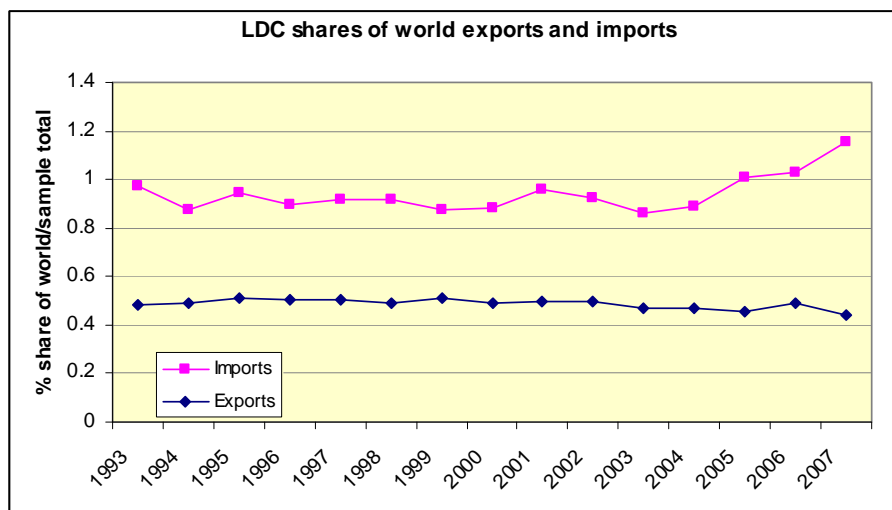
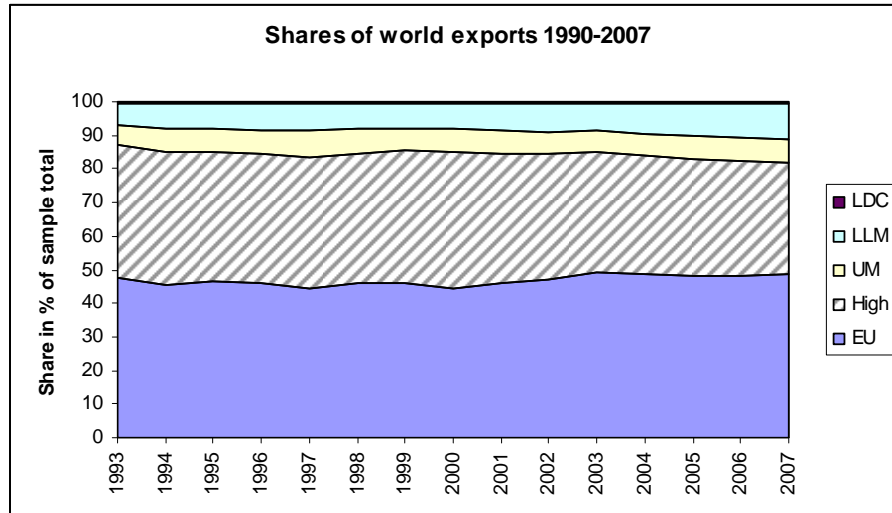
## Balassa indexes

These are simple indexes of the form

Where  $x$ =exports and  $m$ =imports. This varies between -1 (only imports) and +1 (only exports).

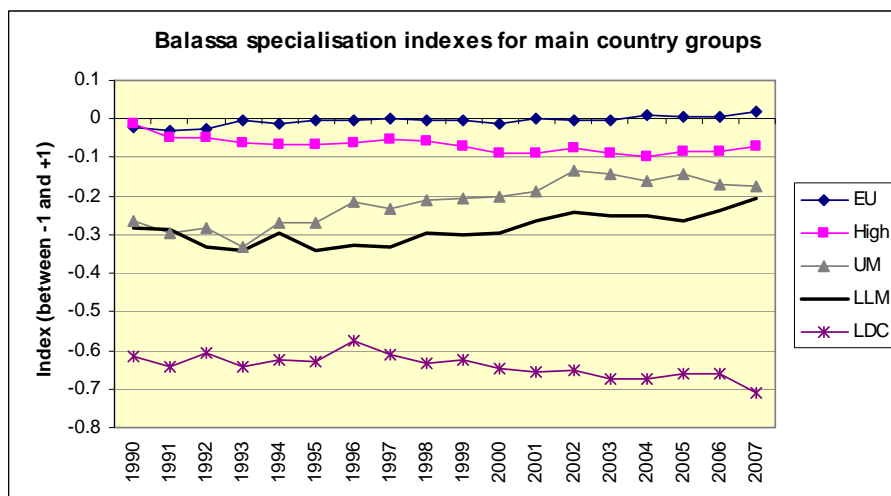
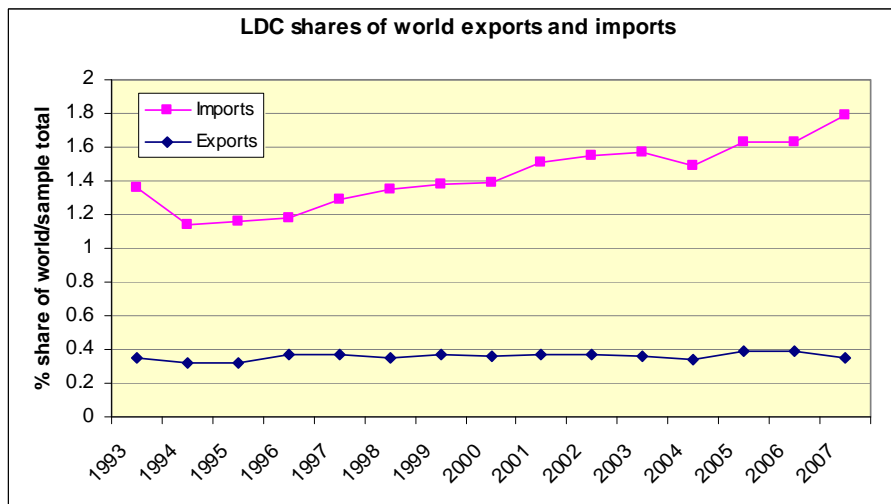
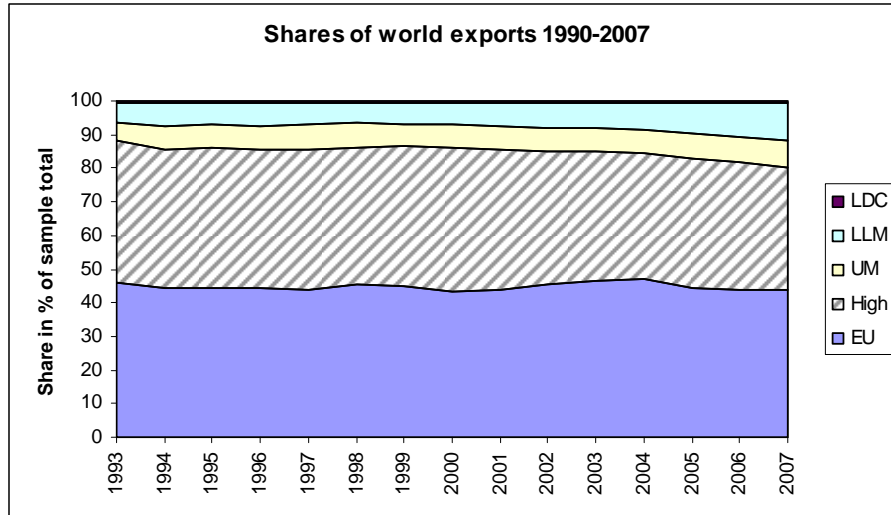
## Sector: Services total

Number of countries (LDCs) covered by data: 137-147 (28-31)



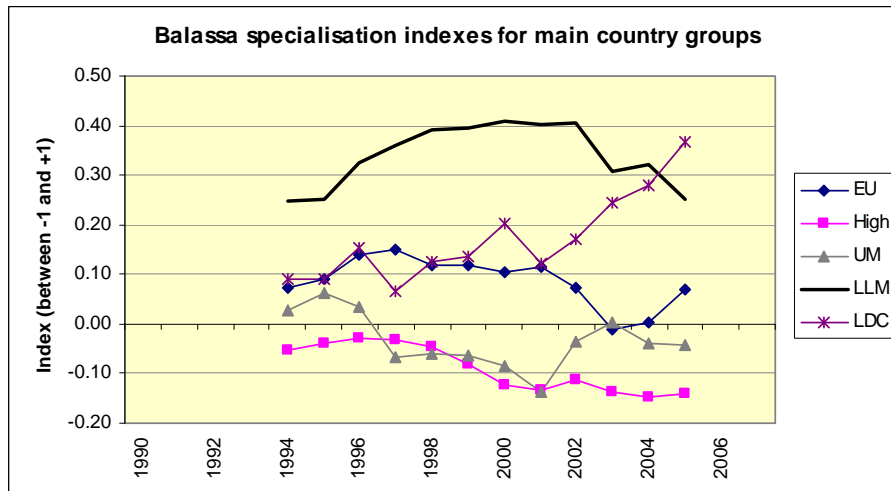
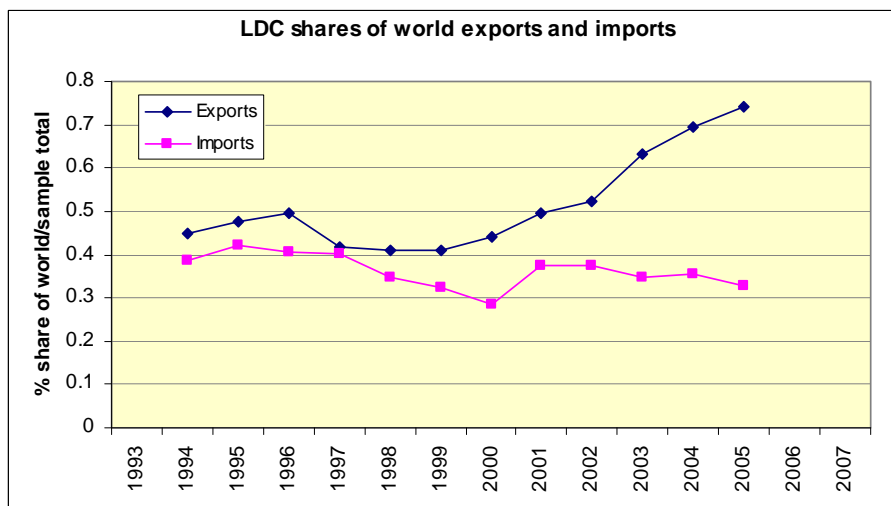
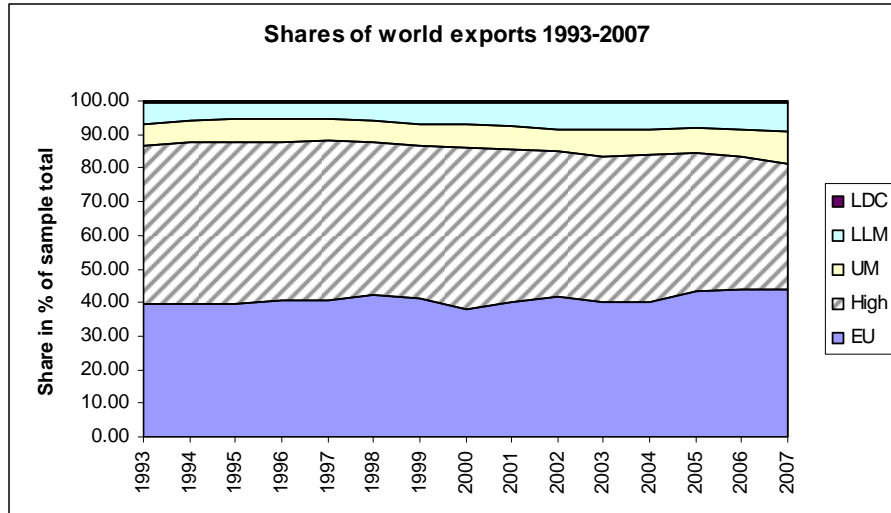
## Sector: Transport services

Number of countries (LDCs) covered by data: 137-147 (28-31)



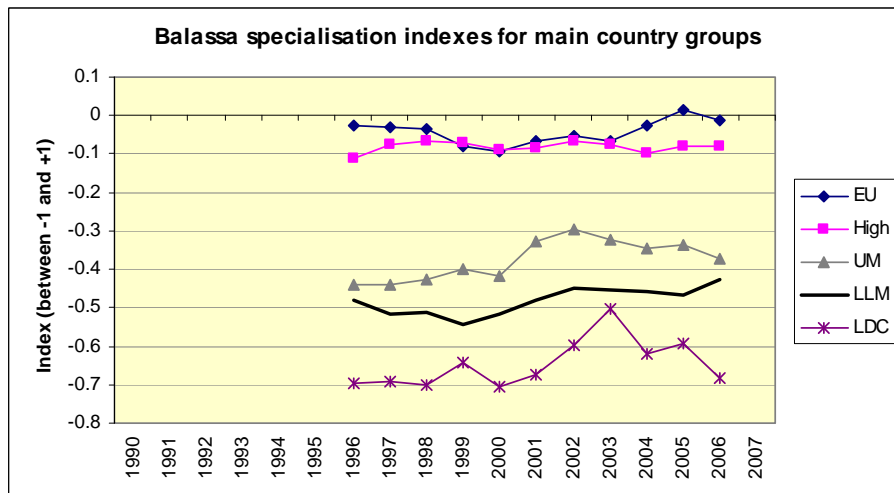
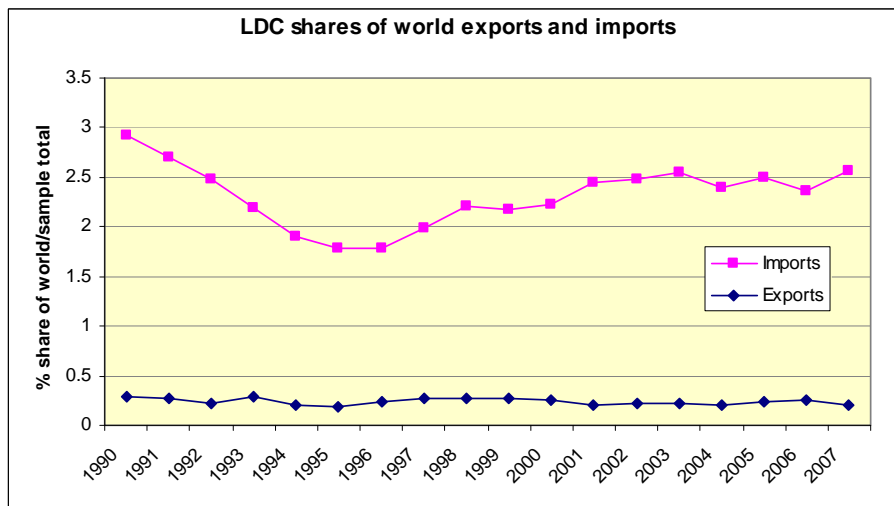
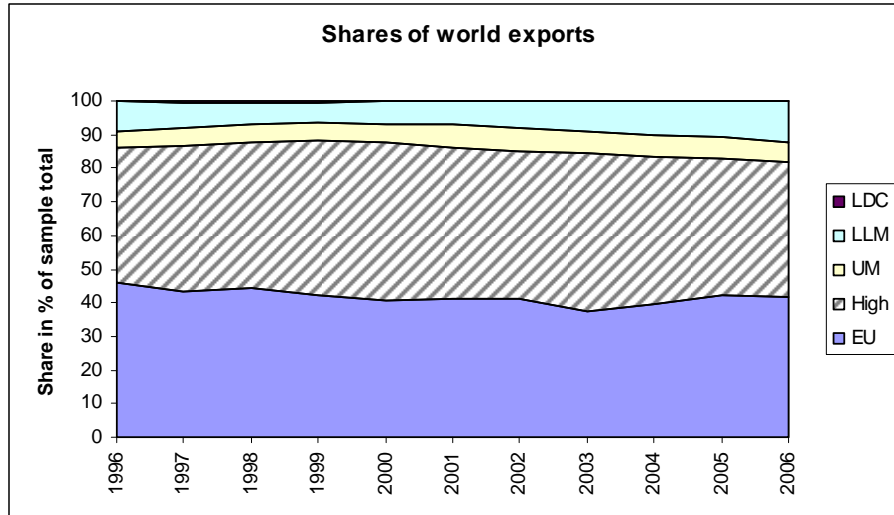
## Sector: Passenger transport services

Number of countries (LDCs) covered by data: 88-91 (10-12)



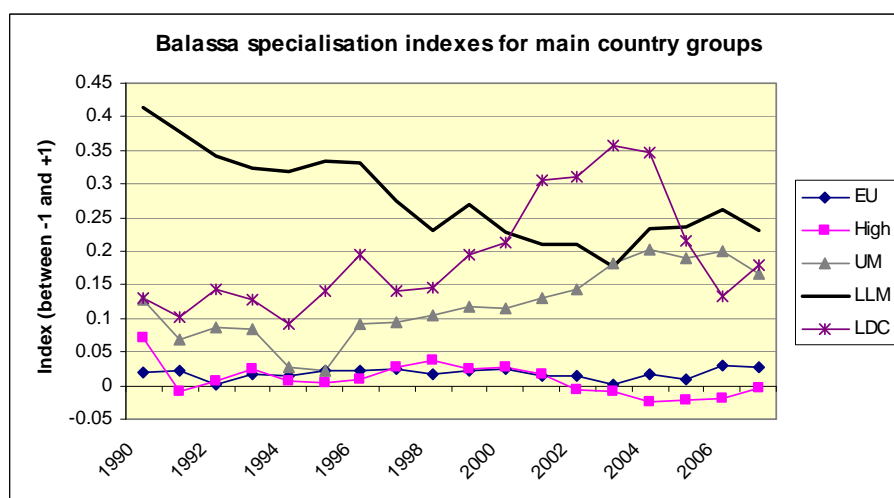
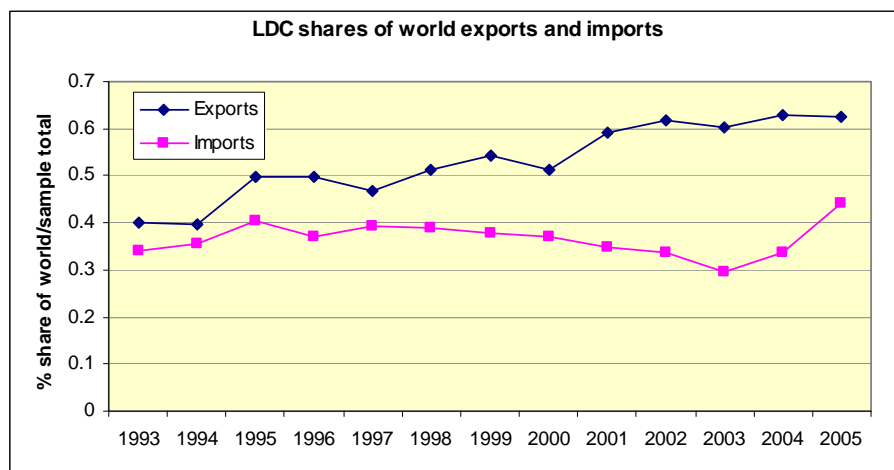
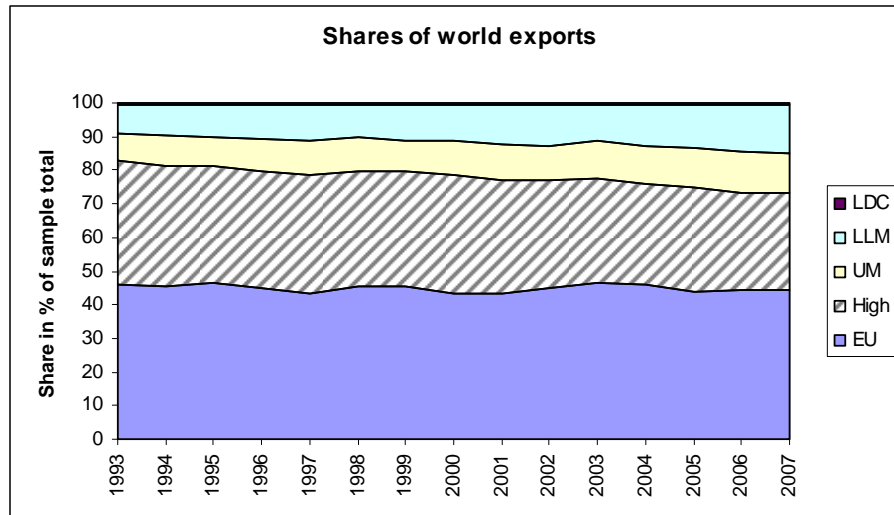
## Sector: Transport freight services

Number of countries (LDCs) covered by data: 118-126 (20-24)



## Sector: Travel services

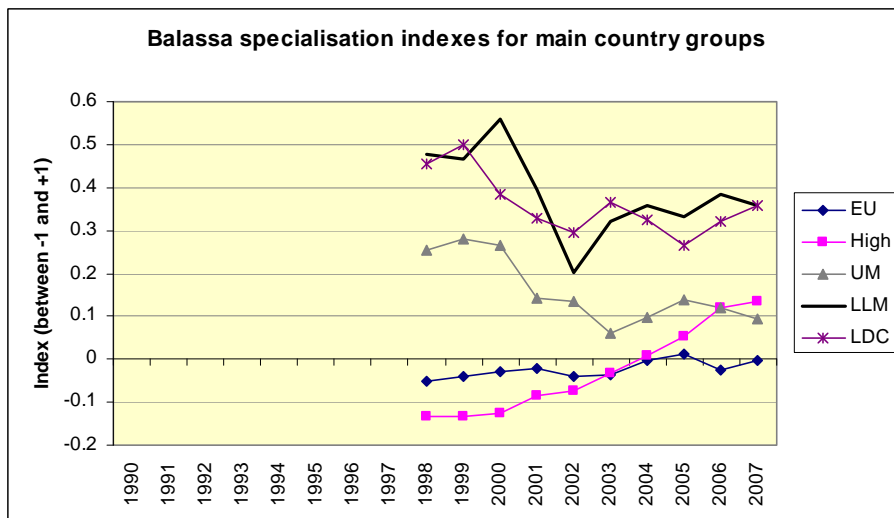
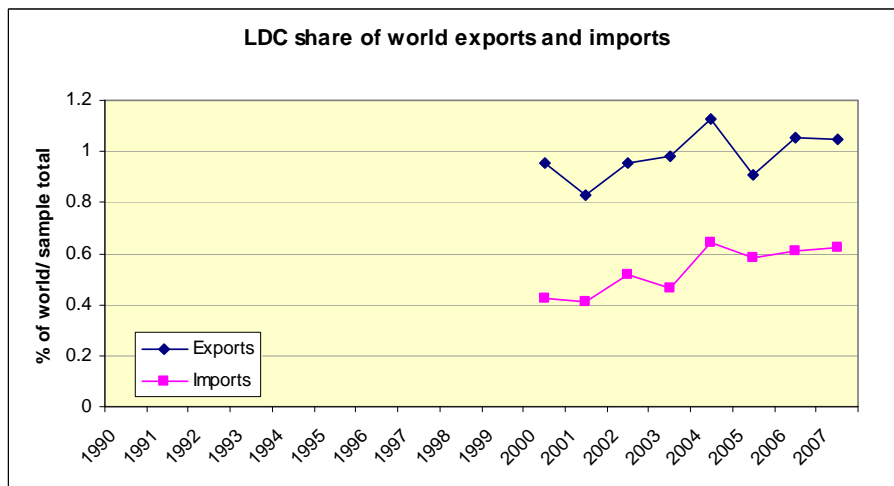
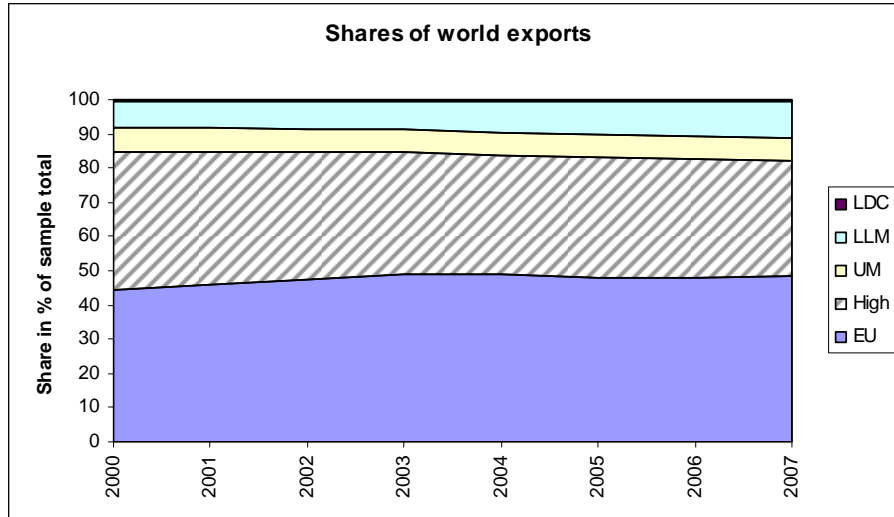
Number of countries (LDCs) covered by data: 133-142 (24-28)





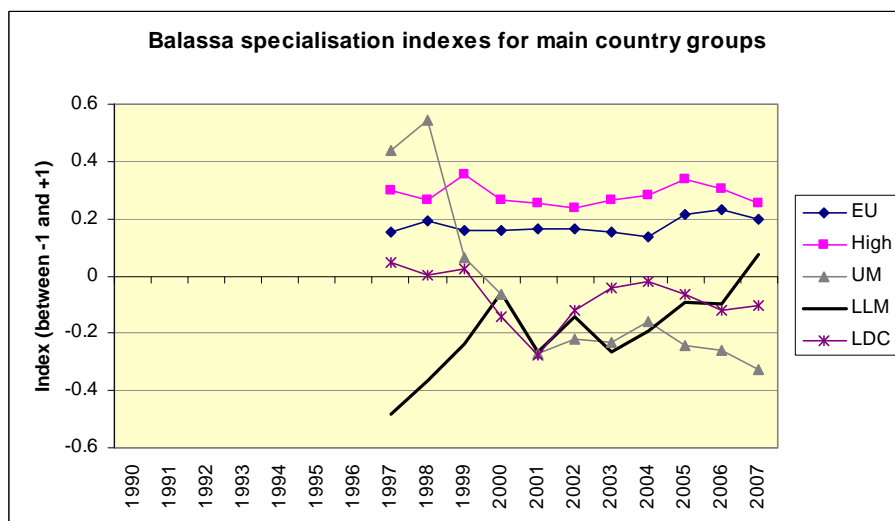
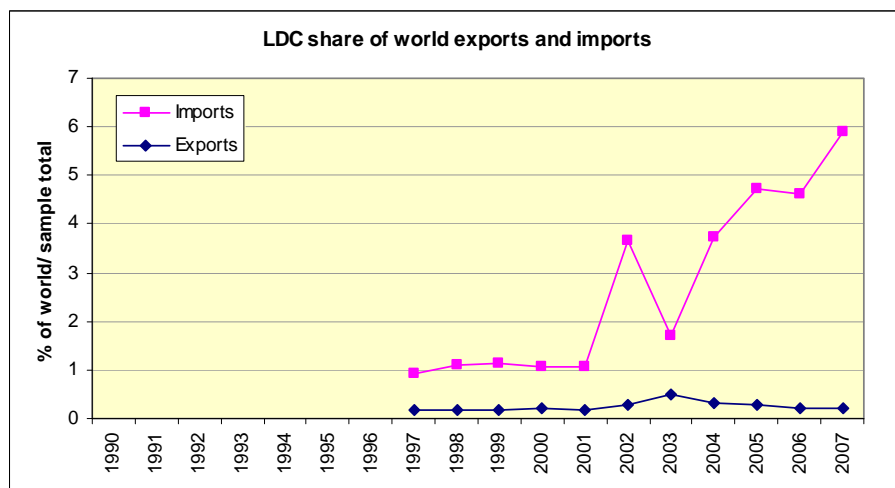
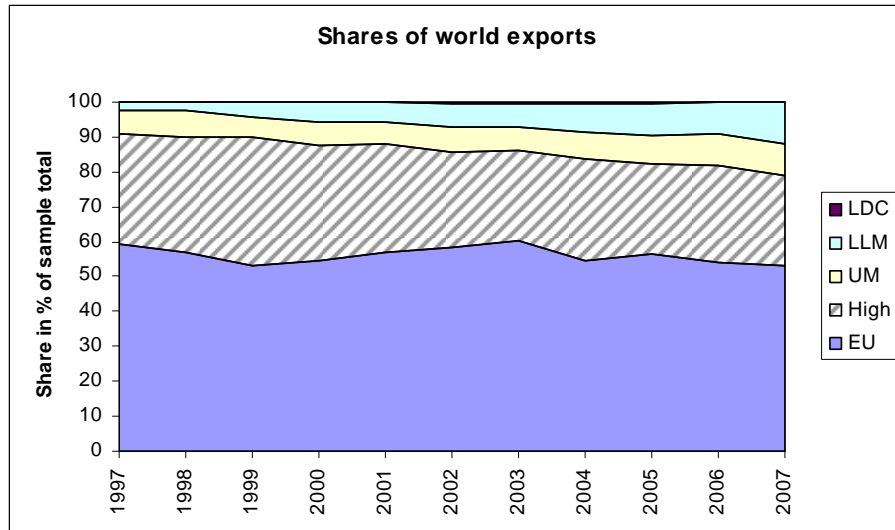
## Sector: Communication services

Number of countries (LDCs) covered by data: 129-140 (22-26)



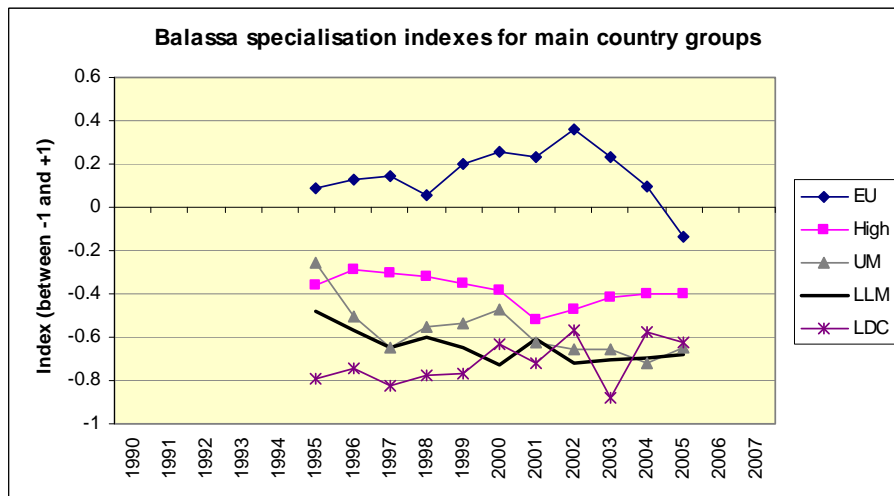
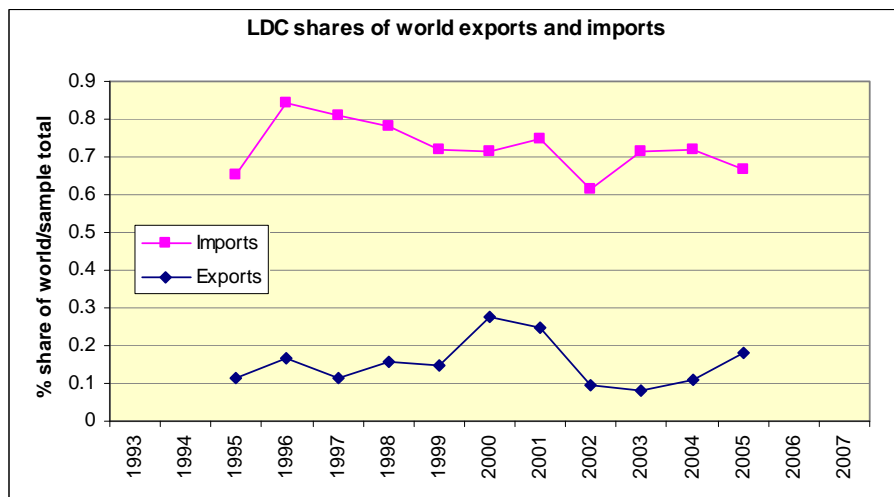
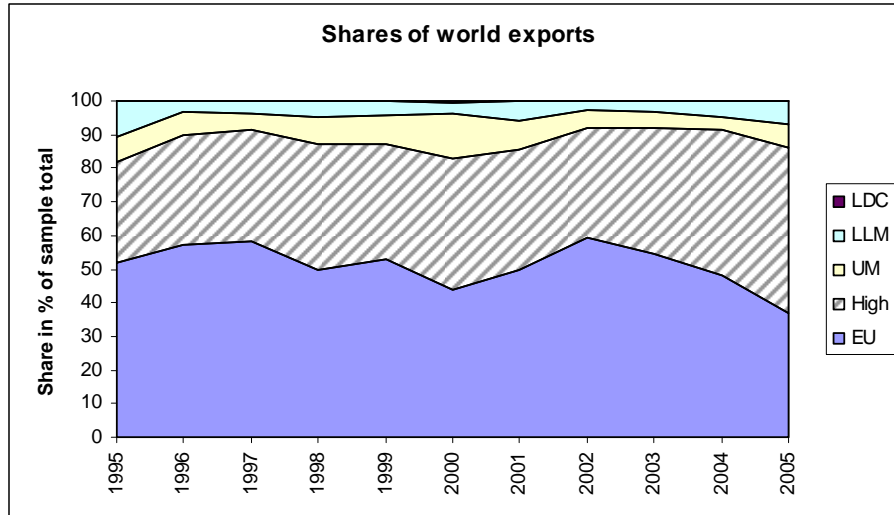
## Sector: Construction services

Number of countries (LDCs) covered by data: 66-88 (9-13)



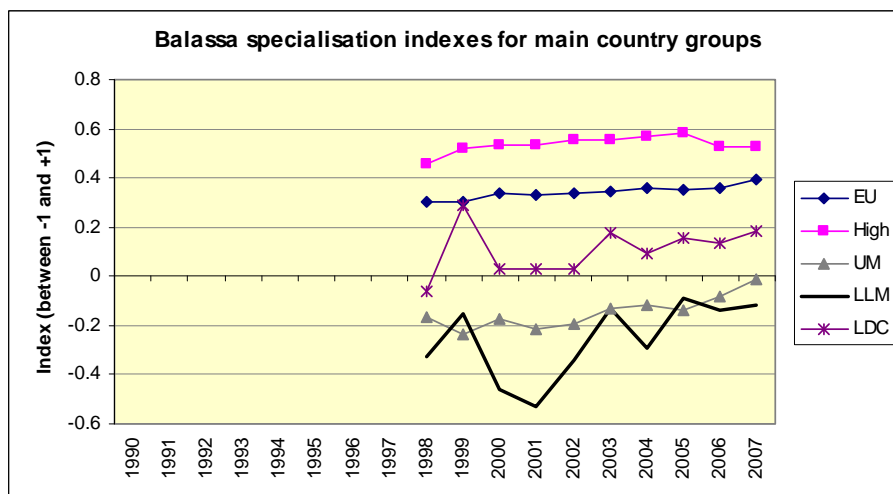
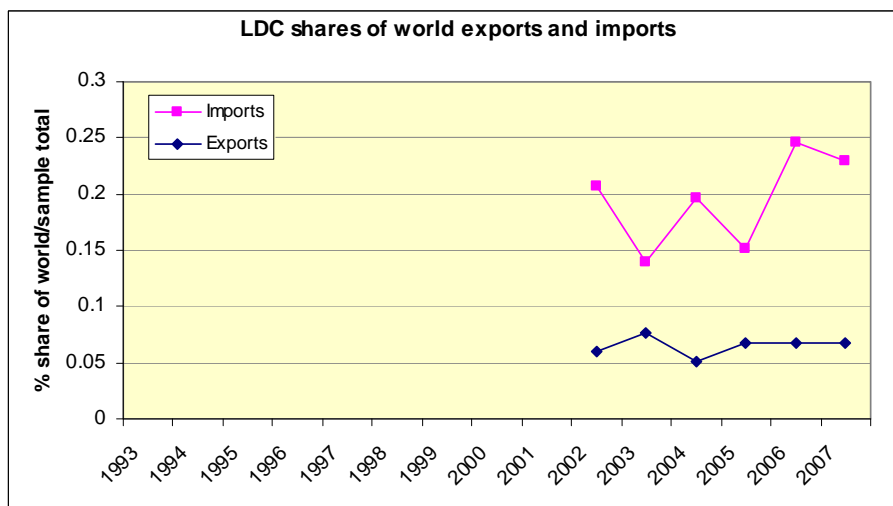
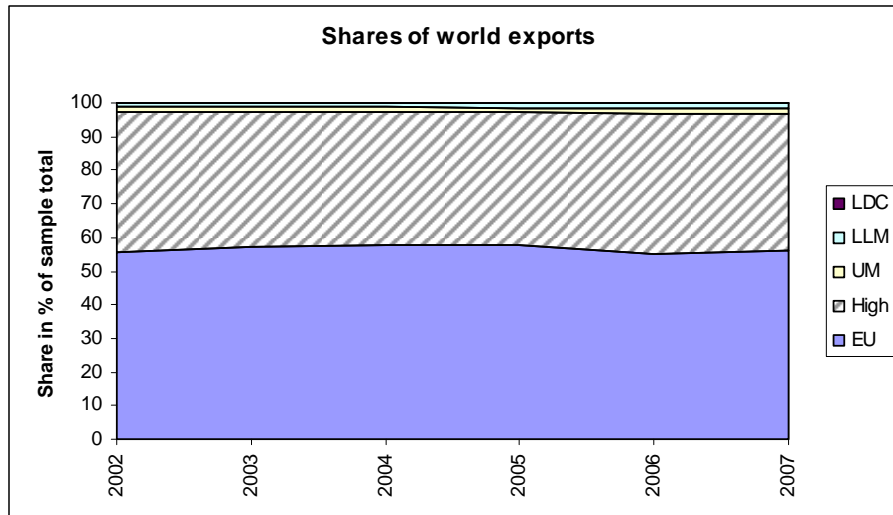
## Sector: Insurance

Number of countries (LDCs) covered by data: 100-103 (12-16)



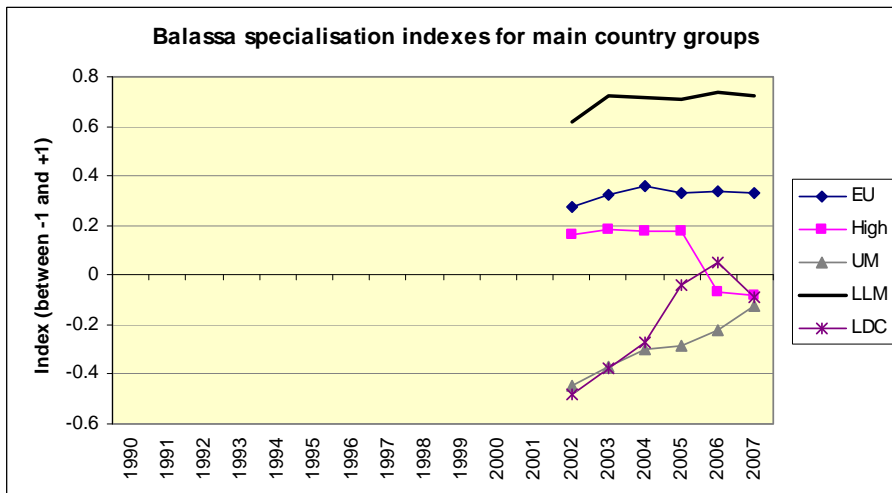
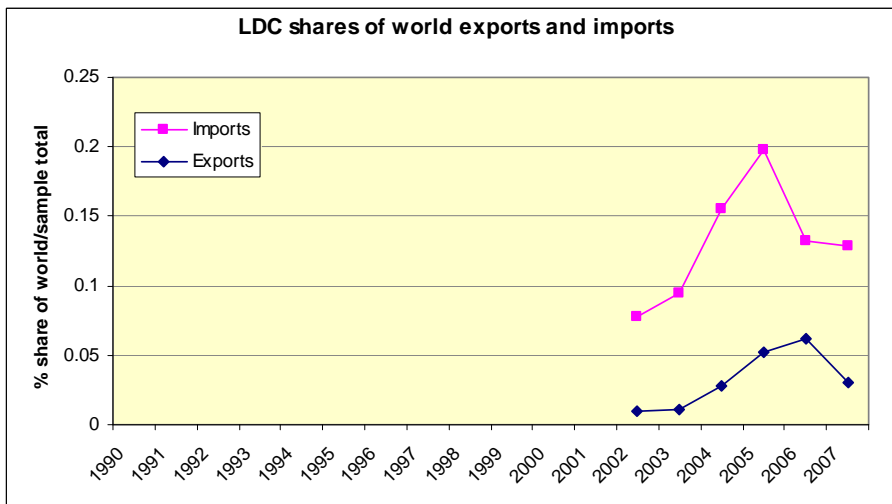
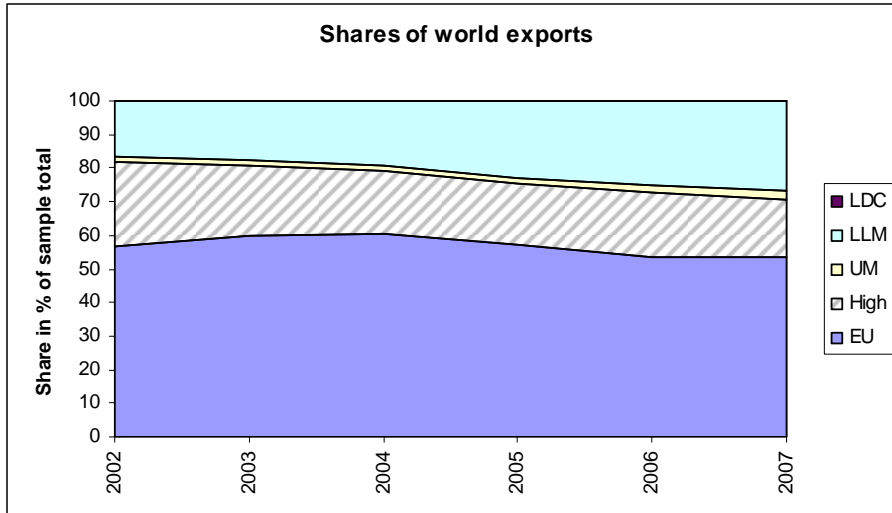
## Sector: Financial services

Number of countries (LDCs) covered by data: 105-112 (16-18)



## Sector: Computer services

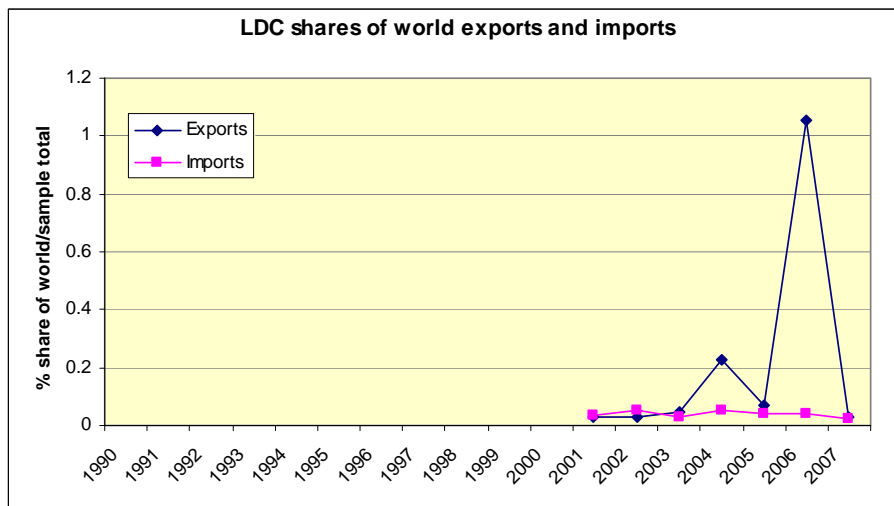
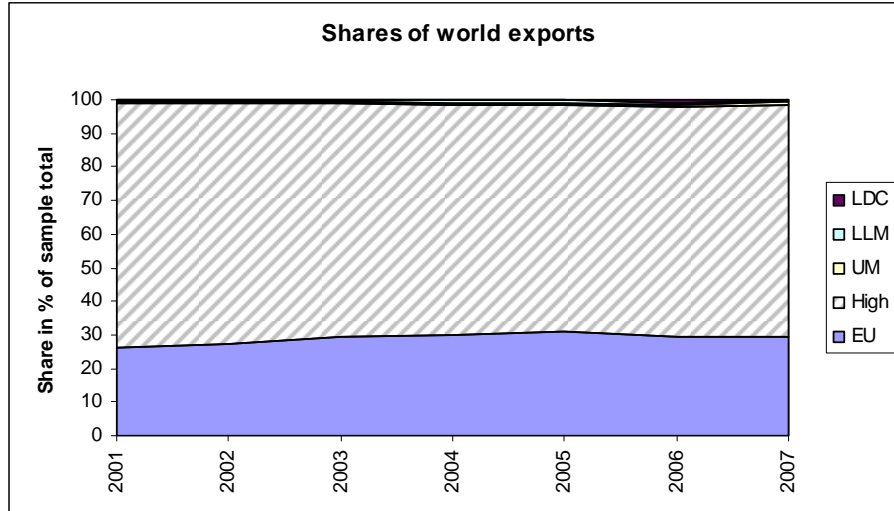
Number of countries (LDCs) covered by data: 96-104 (10-14)



## Sector: Royalties, license fees etc.

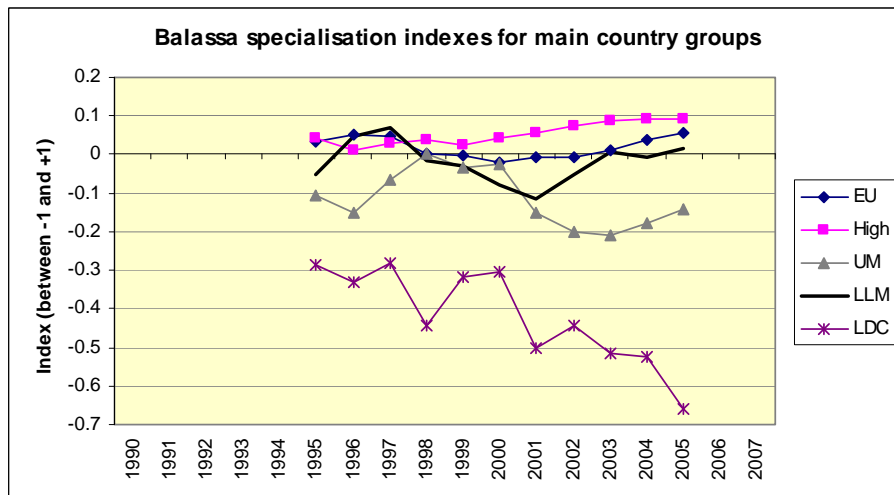
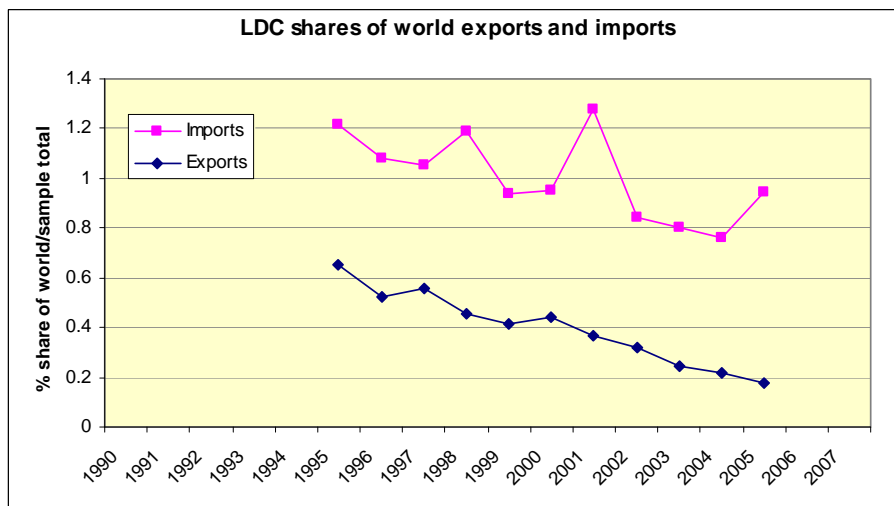
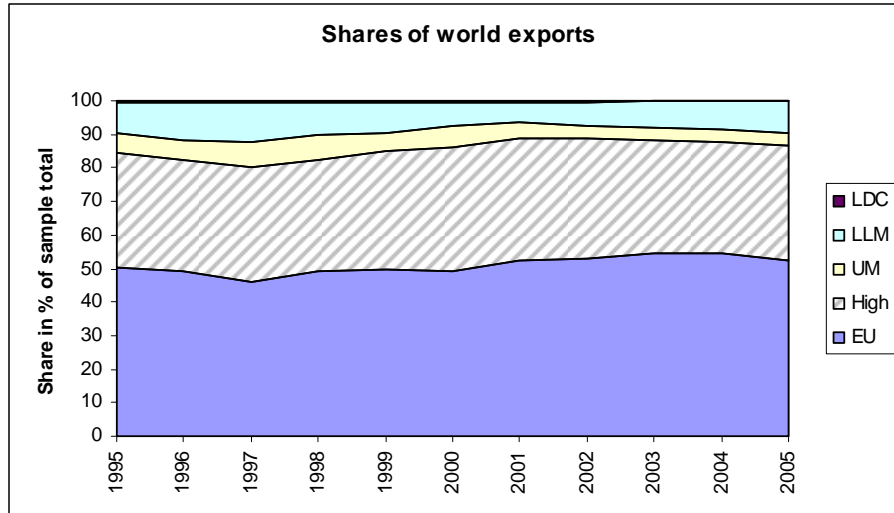
Note: Exports = received.

Number of countries (LDCs) covered by data: 91-100 (10-16).



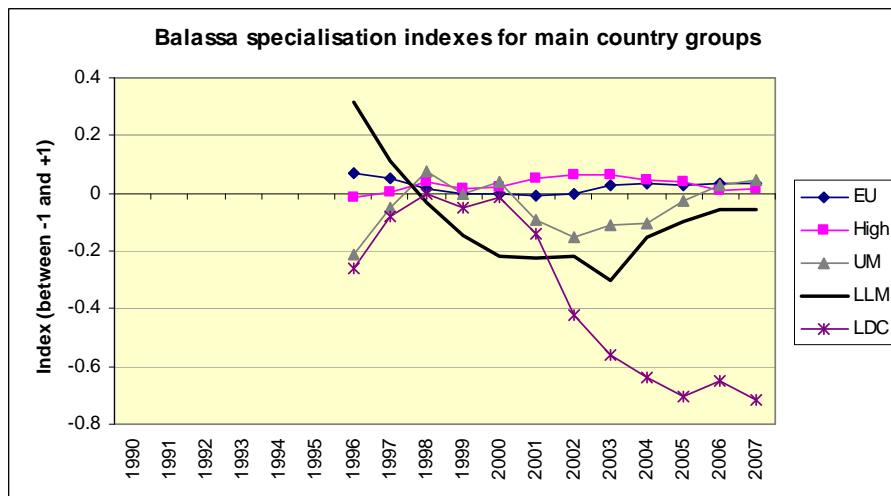
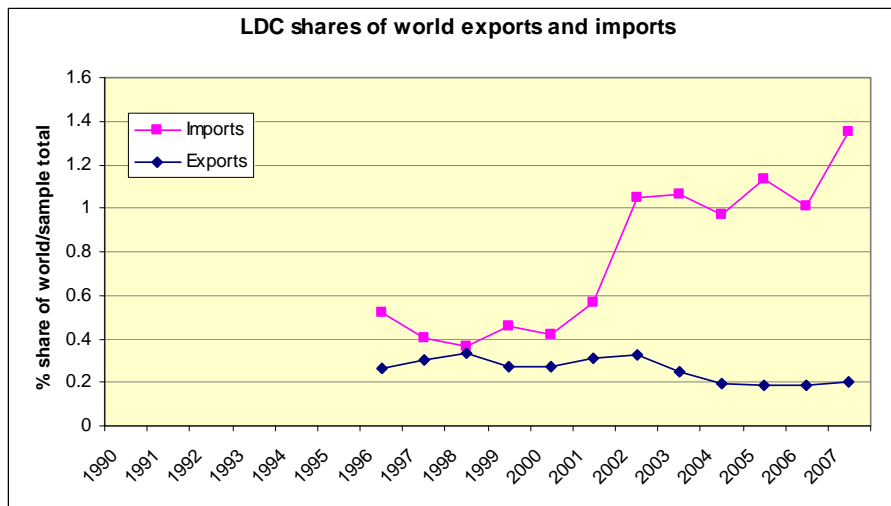
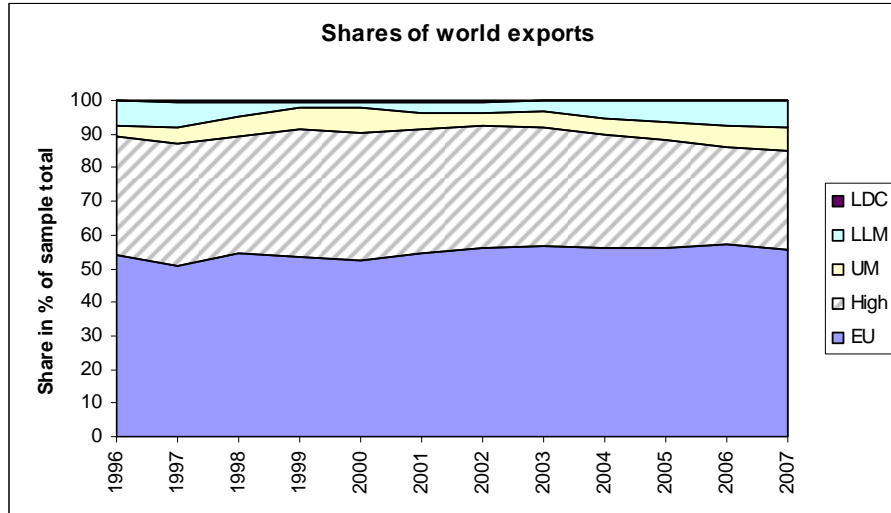
## Sector: Other business services

Number of countries (LDCs) covered by data: 125-130 (21-25)



## Sector: Other miscellaneous business, professional, technical services

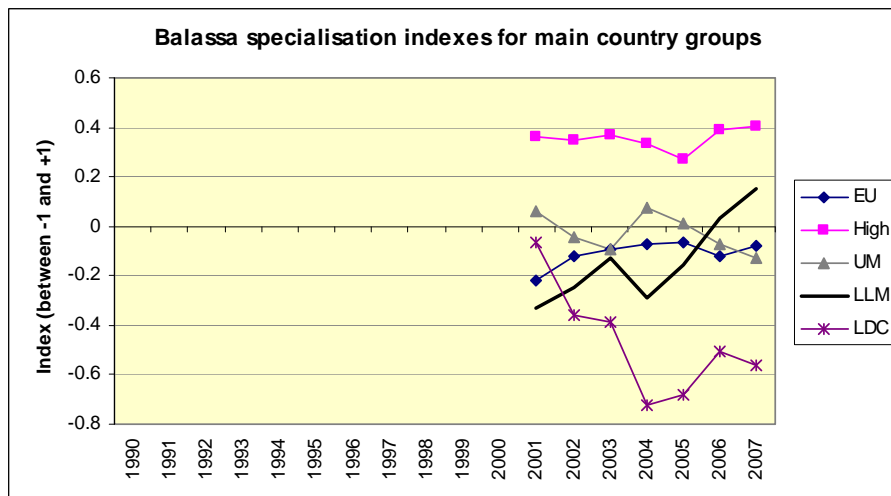
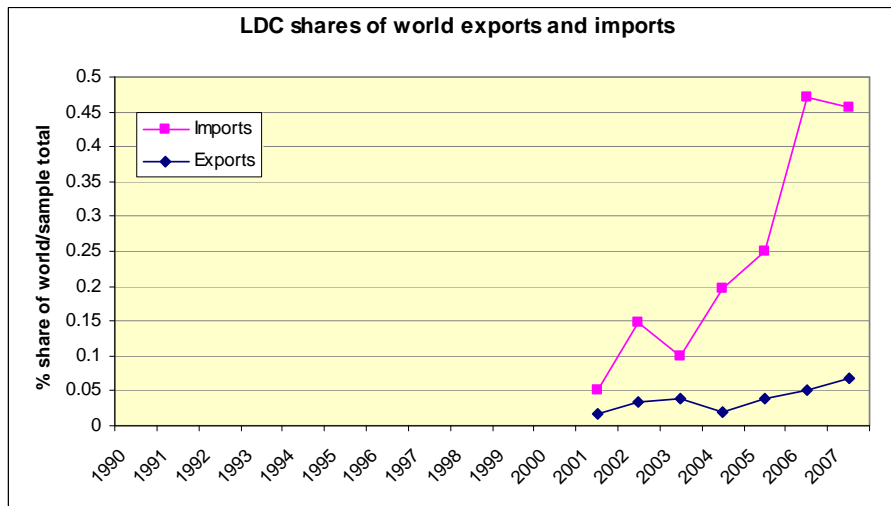
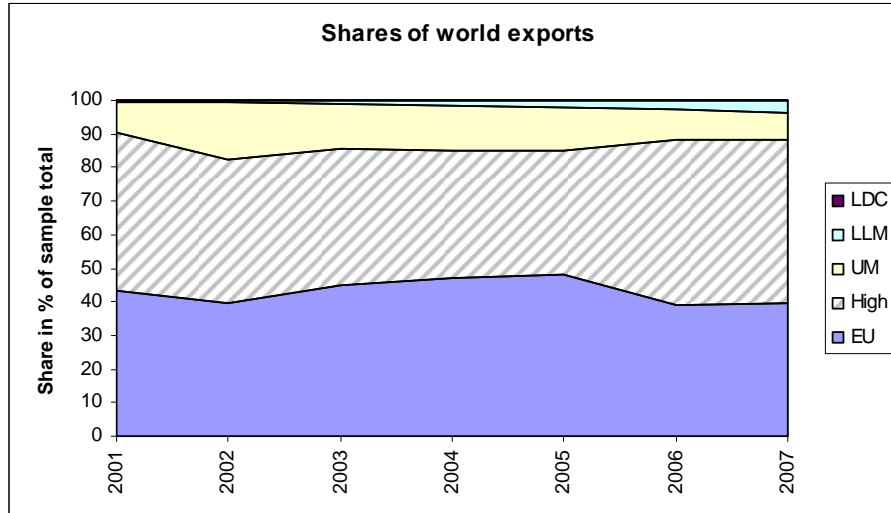
Number of countries (LDCs) covered by data: 98-123 (16-22)





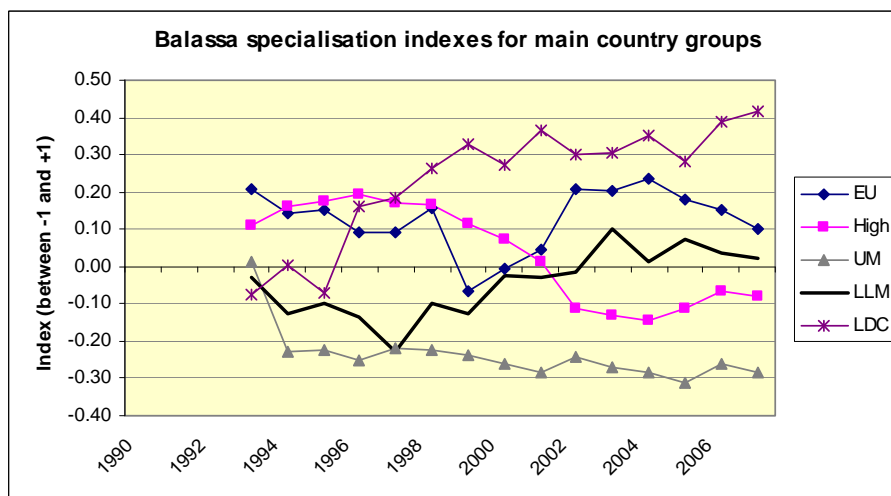
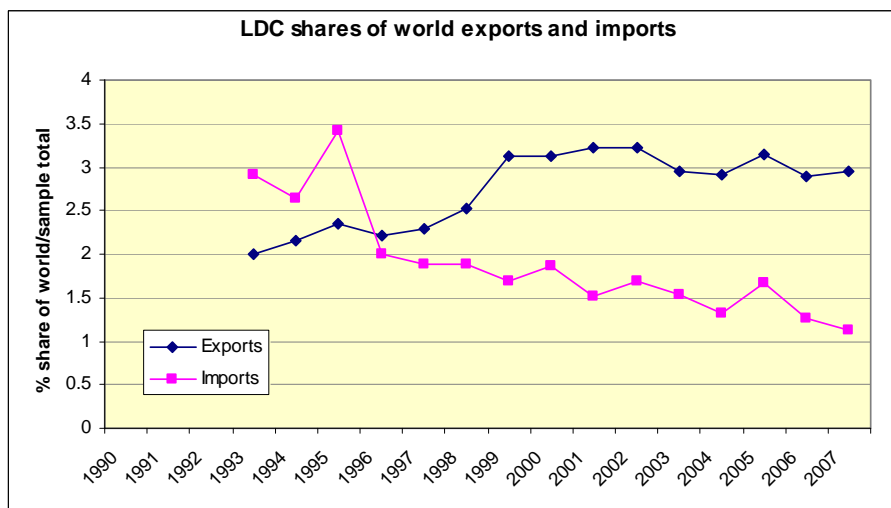
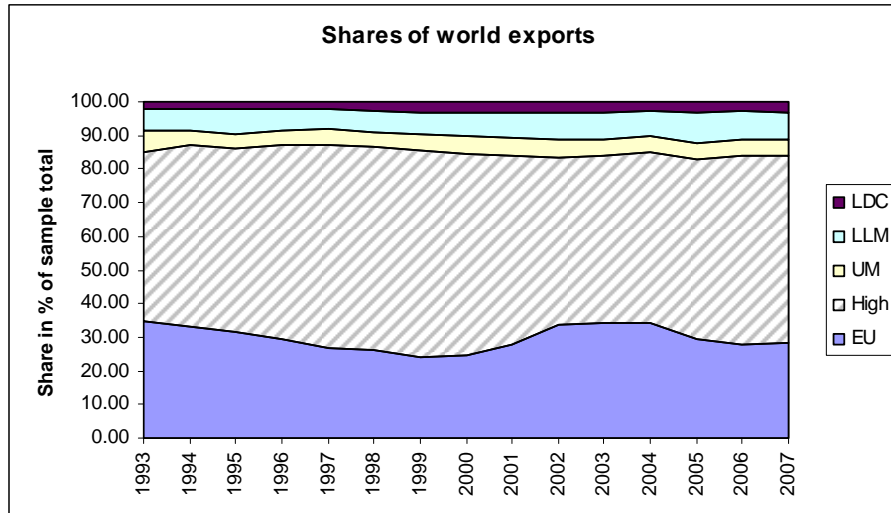
## Sector: Personal, cultural, recreational services etc.

Number of countries (LDCs) covered by data: 83-95 (9-13)



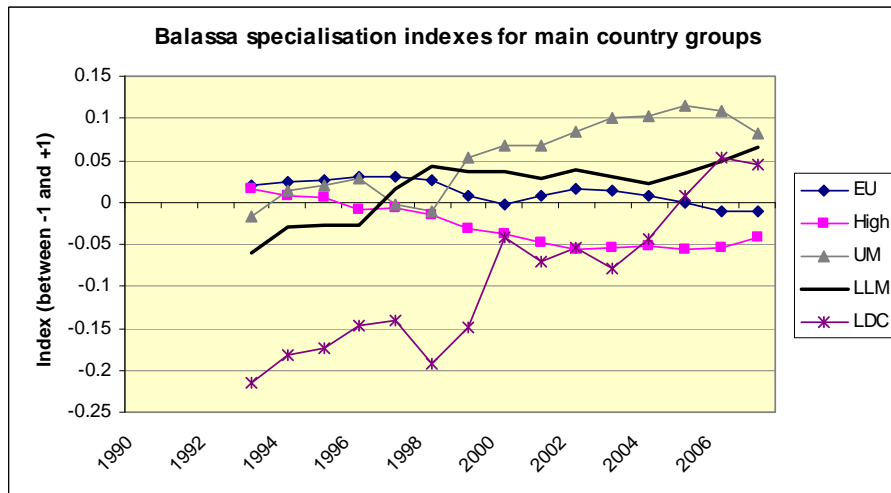
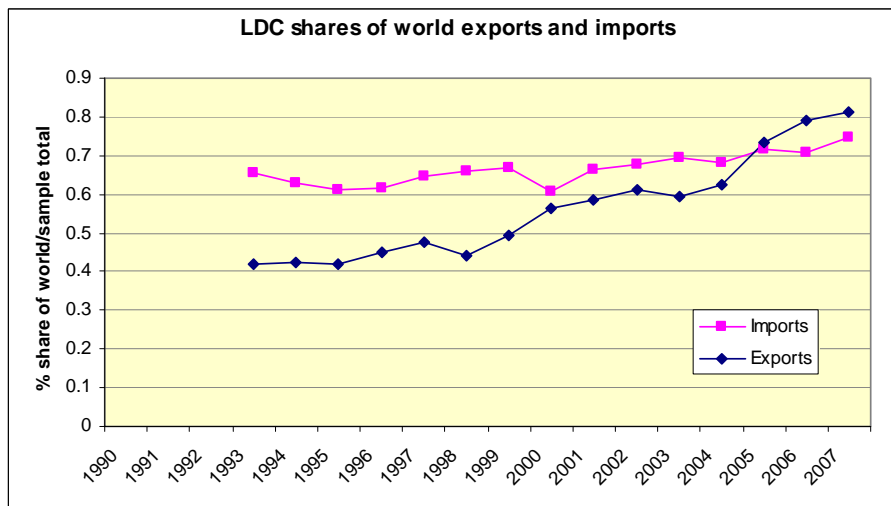
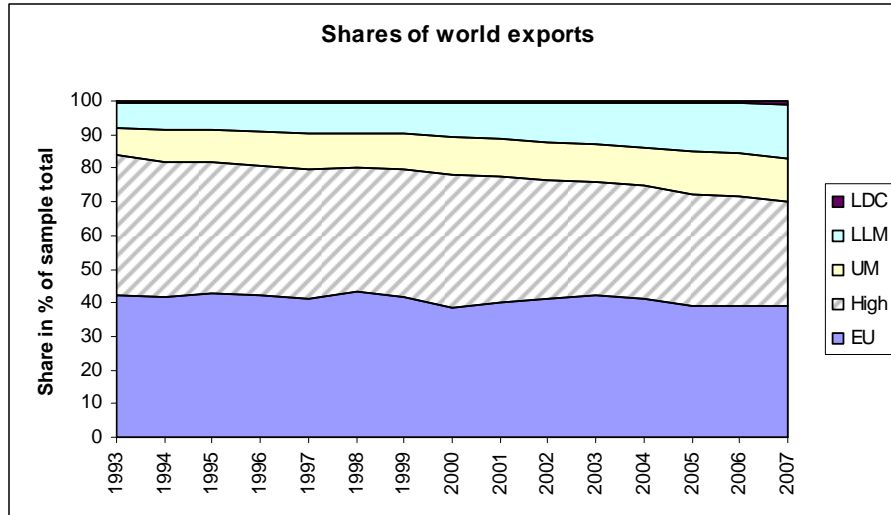
## Sector: Government services n.i.e.

Number of countries (LDCs) covered by data: 117-124 (23-25).



## Sector: Trade in goods

Number of countries (LDCs) covered by data: 137-147 (28-31)

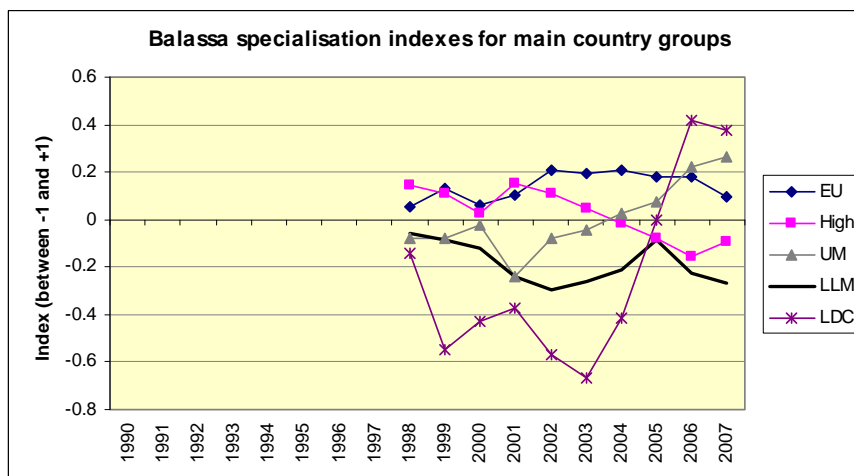
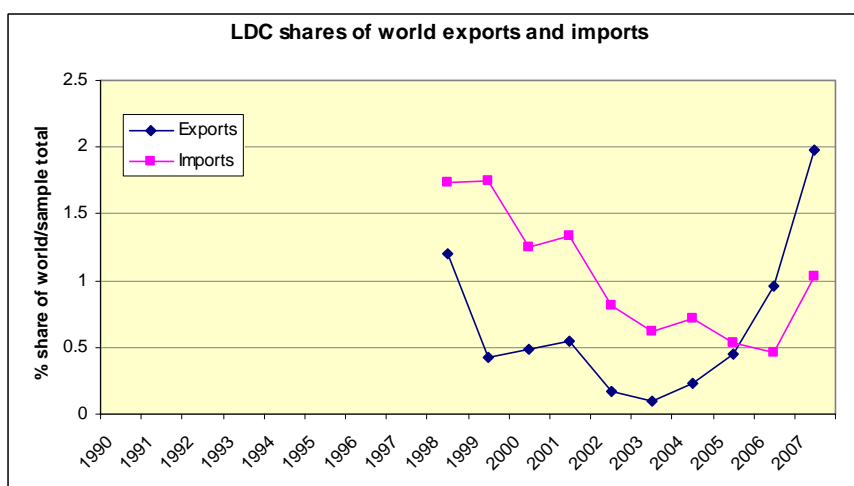
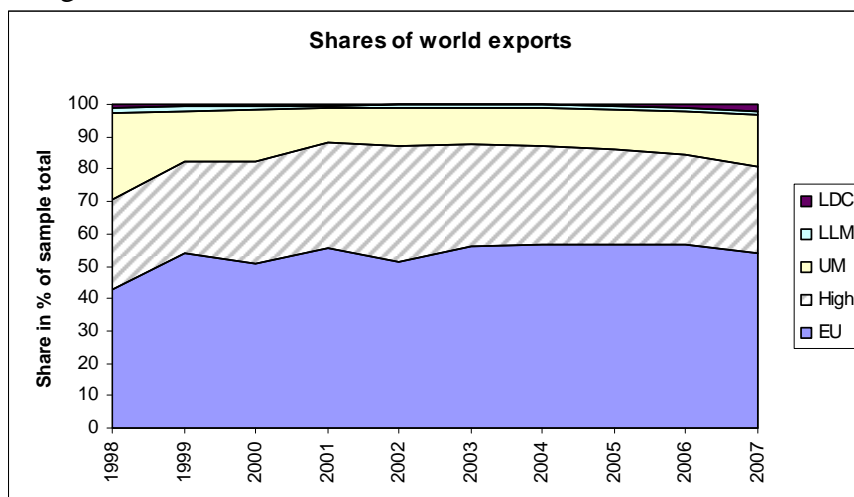


## Item: Migrants' transfers

Number of countries (LDCs) covered by data: 44-54 (2-3)

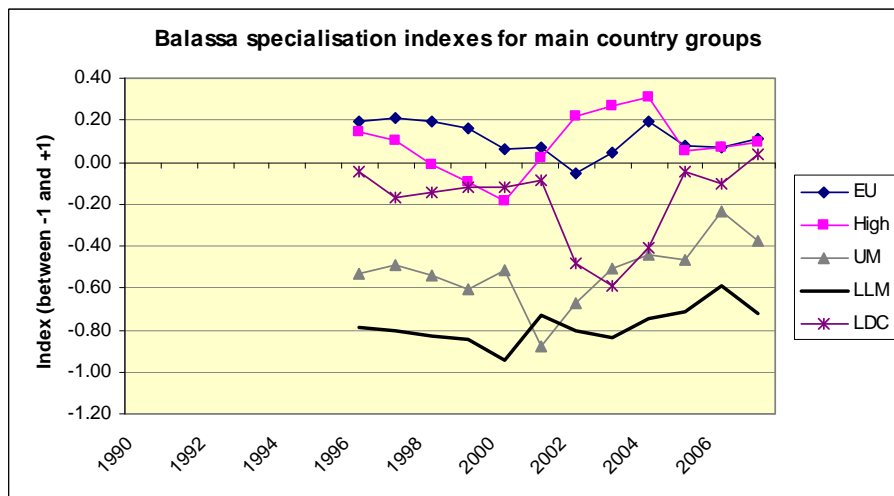
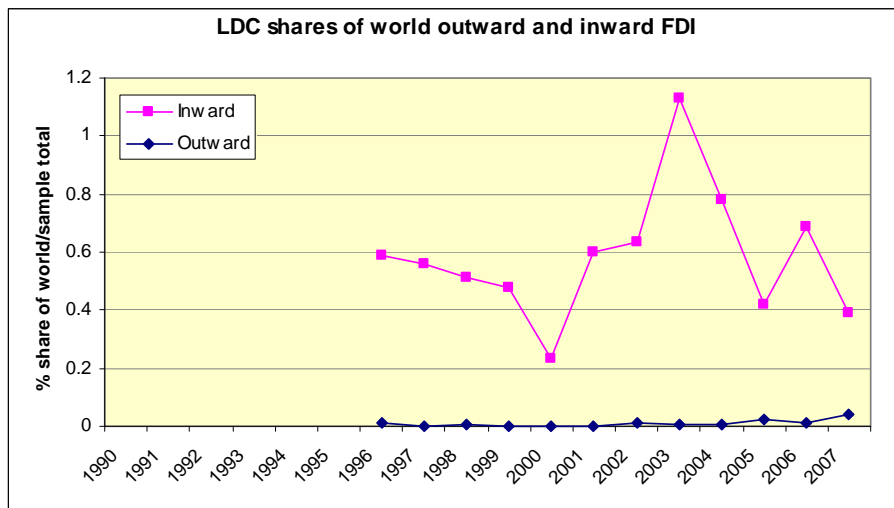
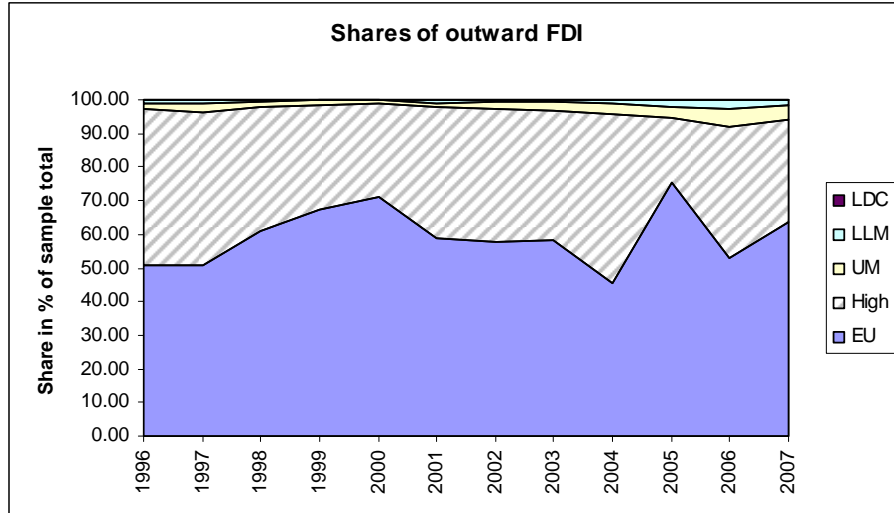
Note: Exports=received.

Note: Limited observations for LDCs: Fluctuations partly due to changes in the number of observations.



## Item: FDI

Number of countries (LDCs) covered by data: 80-90 (5-6)



## Classification of services

The following is downloaded from [www.imf.org](http://www.imf.org) and describes the classification of some relevant sub-items:

**158.** *Transportation* covers most of the services, performed by residents for non-residents and vice versa, that were included in shipment and other transportation in the fourth edition of the *Manual*. However, freight insurance is now included with *insurance services* rather than with *transportation*. *Transportation* includes freight and passenger transportation by all modes of transportation and other distributive and auxiliary services, including rentals of transportation equipment with crew. Certain exceptions are noted in chapters X, XI, and XIII.

**159.** *Travel* covers goods and services—including those related to health and education—acquired from an economy by non-resident travellers (including excursionists) for business purposes and personal use during their visits (of less than one year) in that economy. *Travel* excludes international passenger services, which are included in *transportation*. Students and medical patients are treated as travellers, regardless of their length of stay. Certain others—military and embassy personnel and non-resident workers—are not regarded as travellers. However, expenditures by non-resident workers are included in *travel*, while those of military and embassy personnel are included in *government services, n.i.e.* These cases are noted in chapters XII and XIII.

**160.** *Communications services* cover communications transactions between residents and non-residents. Such services comprise postal, courier, and telecommunications services (transmission of sound, images, and other information by various modes and associated maintenance provided by/for residents by/for non-residents).

**161.** *Construction services* cover construction and installation project work that is, on a temporary basis, performed abroad/in the compiling economy or in extraterritorial enclaves by resident/non-resident enterprises and their personnel. Such work does not include that undertaken by a foreign affiliate of a resident enterprise or by an unincorporated site office that, if it meets certain criteria, is equivalent to a foreign affiliate. Such residency aspects are covered in chapters IV and XIII.

**162.** *Insurance services* cover the provision of insurance to non-residents by resident insurance enterprises and vice versa. This item comprises services provided for freight insurance (on goods exported and imported), services provided for other types of direct insurance (including life and non-life), and services provided for reinsurance. (For the method of calculating the value of insurance services, see paragraphs 256 and 257.)

**163.** *Financial services* (other than those related to insurance enterprises and pension funds) cover financial intermediation services and auxiliary services conducted between residents and non-residents. Included are commissions and fees for letters of credit, lines of credit, financial leasing services, foreign exchange transactions, consumer and business credit services, brokerage services, underwriting services, arrangements for various forms of hedging instruments, etc. Auxiliary services include financial market operational and regulatory services, security custody services, etc.

**164.** *Computer and information services* cover resident/ non-resident transactions related to hardware consultancy, software implementation, information services (data processing, database, news agency), and maintenance and repair of computers and related equipment.

**165.** *Royalties and license fees* cover receipts (exports) and payments (imports) of residents and non-residents for: (i) the authorized use of intangible nonproduced, nonfinancial assets and proprietary rights such as trademarks, copyrights, patents, processes, techniques, designs, manufacturing rights, franchises, etc. and (ii) the use, through licensing agreements, of produced originals or prototypes, such as manuscripts, films, etc.

**166.** *Other business services* provided by residents to non-residents and vice versa cover merchanting and other trade-related services; operational leasing services; and miscellaneous business, professional, and technical services. (See the table on *Selected Supplementary Information* following this chapter and paragraphs 261 through 264 for details.)

**167.** *Personal, cultural, and recreational services* cover (i) audio-visual and related services and (ii) other cultural services provided by residents to non-residents and vice versa. Included under (i) are services associated with the production of motion pictures on films or video tape, radio and television programs, and musical recordings. (Examples of these services are rentals and fees received by actors, producers, etc. for productions and for distribution rights sold to the media.) Included under (ii) are other personal, cultural, and recreational services, such as those associated with libraries, museums, and other cultural and sporting activities.

**168.** *Government services, n.i.e.* cover all services (such as expenditures of embassies and consulates) associated with government sectors or international and regional organizations and not classified under other items."