The post-Bali trade strategy

By Erik van der Marel - Today, 03:35 CET

The EU should focus on strengthening its competitiveness in the service sector.

FOCUS ON TRADE The EU should concentrate on trade in services and not just goods as part of the Bali Package.

The recent summit of the World Trade Organization (WTO) concluded with the ‘Bali package', a mini pre-Christmas deal from the otherwise battered Doha Round that includes trade facilitation and some smaller issues regarding trade in agriculture and development. Yet the deal is far from the initial expectation of the Doha Round – and it excludes the reform that would give greatest welfare gains for both developed and developing countries, namely the opening up of trade services. The European Union now needs to turn its attention to how it can liberalise the service sector – at home and in trade talks with other countries.

The Bali deal includes an agreement on trade facilitation that will simplify customs procedures, reduce costs and improve the speed and efficiency of delivering goods of all kinds across borders. The arrangement on agriculture addresses tariff quota administrations in case these remain unfilled, a political commitment to ensure that export subsidies stay low, plus a statement committing the WTO's members to improve market access for cotton products from least-developed countries (LDCs). Finally, the package also deals with development issues such as duty and quota-free access and simplified preferential rules of origin for LDCs to rich countries' markets.

All these trade issues are undoubtedly extremely important and, above all, they are consistent with the initial Doha pledge to deliver on development. Yet, even though the Bali package is only a selection of a broader set of topics as part of the Doha Round of negotiations, one pressing issue has unfortunately not been dealt with, namely unlocking trade in services. True, the deal includes a ‘services waiver' for LDCs, giving them preferential access to developed-country markets. But a lot more could be negotiated on services if policymakers truly want to create significant welfare gains from trade.

Why are services so important? Traditionally trade has been thought of as a final good travelling from one country to another. In today's world this is no longer the case: a good crosses the border as an input many times before it becomes a final good. Hence, value is added by processing these inputs, which are then sent abroad for further production. It therefore becomes important to know what the ‘net' added value is each time an input is exported. And this net export measure is actually much higher for services than for goods, which in turn brings higher economic gains for everyone. Second, services are often used as inputs for the further production of goods. A well-functioning domestic and external-services market renders goods production much more competitive. This effect is particularly true for business services, such as consulting and accounting services, but it also

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applies to telecoms and financial services. Third, the services sector is a massive creator of employment. Services production absorbs a large amount of labour, both skilled and lower-skilled.

However, there is a myriad of policies that inhibit a smooth exchange of services between countries. These are so-called regulatory restrictions, instead of tariffs, which are otherwise applied on a good. The average services restriction in the world for entering another market is around 28%. And in the EU it is around 20%. These numbers are high. And they are only the start: once a service has entered the foreign market it still needs to deal with regulatory customs hurdles, such as administrative procedures or inefficient laws, before it can be consumed by a customer. These are all issues that have a negative impact on welfare.

What can the EU do to spur trade in services? Services represent more than 70% of the EU's economy. For the EU, this is the principal area where prospective jobs and prosperity will come from. Although the EU is also one of the strongest services exporters in the world, the annual average growth rate for the most dynamic part of the services sector – business services – is lower than in the United States. Meanwhile, international competitiveness indicators show that the EU is lagging behind the US. One way for the EU to retain a high level of competitiveness would be to strengthen its own internal market for services, by further removing and de-regulating burdensome services policies. Since the services directive in 2004, already weak and diluted on its arrival, new reforms to re-invigorate the internal services market have lacked ambition.

An alternative prompt to restructuring could come from outside. The EU could commit itself to far-reaching international trade deals that would, as a result, put pressure on domestic constituencies to uphold promises made externally. The ‘Bali package' will not have this effect; other ways that could act as an external vehicle for domestic reform should now be considered. There is an obvious candidate: the recently initiated Trade in Services Agreement (TISA) between the EU and 22 countries. The EU should not miss this opportunity. It should use its weight to go ahead with an agreement.

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