CHAPTER – III

TRADE IN SERVICES: A
GLOBAL PROFILE
CHAPTER III

TRADE IN SERVICES: A GLOBAL PROFILE

In recent years international trade has flourished in a category that had been considered largely nontradable i.e., the services. Services are being exchanged across national boundaries in large volumes, with growth rates exceeding those for trade in merchandise. The range of traded service activities is wide, ranging from software to health to telecommunications to construction and engineering, among others. Trade in services today is an integral part of the total developmental effort and national growth of many economies. Due to the importance of the service sector and the emphasis placed on trade in services during the Uruguay round of trade negotiations, issues related to international trade in services has got lot of attention from the researchers.

3.1 The concept and Nature of Trade in services

A question that arises in any discussion of trade in services is what exactly is being traded. The problem arises because services such as haircuts cannot be produced in one country and sold in another. Such services require that either the producer or the consumer must move at least temporarily, to the other country. We are all familiar with the distinction between goods and services. Goods are tangible and services are intangible. Goods are visible whereas services are invisible. Economists have attempted to arrive at more precise distinction between goods and services. Its origin can be traced to the distinction between productive and unproductive labour in the age of classical political economy. All value added in an economy comes from services i.e. from factor
services. The economists assert that services are 'anything sold in trade that could not be dropped on your foot’. The characteristics of services as immaterial goods is open for criticism, since some services have elements of tangibility (e.g. printed report of a consultant or a computer software programmer on a diskette); visibility (haircuts or theatre plays); storability (automatic telephone answering machine) may not require face to face contact between producers and consumers. The first attempt to study services as a distinct economic activity was made by Colin Clark in his endeavour to analyse the role of service sector in the process of economic growth and structural change.

A service may be defined as a change in the condition of a person or of good belonging to some other economic unit, which is brought about as a result of activity of some other economic unit, with the prior agreement of the former person or economic unit. As Prof. Hill argued, 'the fact that services must be acquired by consumers as they are produced means that they cannot be put into stock by producers. Because the only goods, which cannot be put into stock, are highly perishable goods, the impression has been formed that services must also be perishable, but this analogy is totally false. The inability to stock services has nothing to do whatsoever with their physical characteristics. It is a logical impossibility because a stock of changes is a contradiction in terms (Hill 1977).

Due to the diverse activities in different service sectors as telecommunications, banking, insurance, travel, construction and engineering, shipping, legal and accounting work, while it is clear what service industries produce, it is not so clear how to measure their output, for individual governments and international organizations use different
accounting methods to determine the value of traded services in national accounts. This makes international comparison and analysis of data rather difficult. Moreover the data on trade in services are not very good, for analytical and other purposes and what exists is patently incomplete. The two main reasons sited for this are services by nature have no physical presence; they are difficult to value and for various reasons e.g. tax avoidance they are often under reported. But as far as physical proximity is concerned it has been observed that they are exceptions to these aspects, which is made possible through modern technology. Trade can often be pursued moreover through the use of local, indigenous representatives or brokers. Secondly services are often subsumed in a contract for goods and the value of the services provided is counted as part of the cost of goods.

A principal reason why services splinter from goods is simply a consequence of the way industry-of-origin services is identified. Any intra-firm transactions even when they partake of the nature of services otherwise so defined are automatically classified as part of that firm's output. If the firm is producing goods then such transactions are classified as part of the value added in the goods sector for e.g. if a car factory has a paint job done on the premises using its own labour and capital, i.e. part of car production. If the paint job however is sourced out to another firm, then the paint job is classified as a service. Thus is seen even more dramatically if one considers transport or accounting within and outside firm. Within a firm, producing goods, it would all go into goods production, whereas when purchased from outside the value added from these activities would classify as services. Thus we get the remarkable phenomenon that as specialization
emerges owing to economies of scale and service activities are taken out of the firm and become a part of inter-firm transactions there will be a shift in the relative proportions in the production of goods and services in favour of latter (Bhagwati, 1984).

The service sector has become much more complex and varied with the passage of time. The word 'services' is used to describe a phenomenal range of heterogeneous economic activities, some of which have nothing in common with each other. The service sector includes inter alia infrastructural services such as transport, communication, electricity and water supply, social services such as education and health, financial services such as banking, insurance, accountancy and brokerage, technological services which includes construction, engineering and consultancy, marketing services such as advertising, wholesaling and retailing, commercial services such as chartering, leasing and franchising, professional services such as those provided by lawyers, doctors and architects, government services such as those in public administration and defense, personal services such as hotels, restaurants, hair dressers, beauty parlours and even domestic help (Nayyar, 1995).

In sharp contrast with the literature on economic growth and structural change, it would seem that economists have paid less attention to services in the context of international trade. This neglect has been due to the following reasons. Firstly, there is a presumption that services can be treated in exactly the same manner as goods so that the existing theories of international trade are perfectly adequate. Secondly there is a presumption that services are non-traded and hence do not matter in international trade.
Trade in services may be defined as international transactions in services between the residents of one country and the residents of another country, irrespective of where the transaction takes place (Nayyar, 1995).

International trade in services can be divided into four categories

a. Those in which the producer moves to consumer
b. Those in which consumer moves to producer.
c. Those in which either producer or consumer moves to other.
d. Those in which neither producer nor consumer moves to each other.

In first three categories, physical proximity of the producer and consumer is essential, if the international service transaction has to take place. It is in conformity with the characteristics of the services traded in those categories (Sampson and Snape, 1985).

Services are also often classified according to their economic function and/or their intrinsic value to consumers or providers. Although there are inevitable overlaps among these functional classifications, they are commonly used for policy-oriented analyses. A distinction is usually made, for example, between market (private) services and non-market services. They may be divided into intermediate and final services according to their use. Intermediate services are sometimes further divided into distributive services (wholesale & retail trade, transport, storage and warehousing & communication) and producer services (financial, business & professional services) while final services...
encompass social services (household services, recreational and cultural services, hotels and restaurants) (Mckee, 1993).

M.A. Katouzian has classified services as new services (e.g. entertainment, education and health services) complimentary services (e.g. banking, finance, transportation, wholesale and retail trade) and old services (e.g. domestic or households services). According to this approach, new services are those activities that are particularly sensitive to growth in per capita income and leisure time. They are characterized as new because their mass consumption is a relatively new historical phenomenon. The complimentary services group includes activities closely linked to industrialization and urbanization. Finally the old service group refers to activities that have been losing economic importance because of substitution effect (Mckee, 1993).

The US office of technology assessment has classified services as knowledge based services (e.g. insurance, professional and technical services, certain banking services, information technology services, advertising, motion pictures, health care, education and some government services) and tertiary services (e.g. leasing, shipping, distribution, franchising, retail trade, travel, some social services, most entertainment and personal services). The first group services are classified by high human capital content and later are characterized by lower human capital requirement and more standardized production methods.
Service transactions identified in the current account can be divided between factor and non-factor services. Factor services refer to income earned through the cross border movement of factor of production. Investment income, royalties & fees and labor income are usually in this category. Non-factor services encompass shipment, other transportation like travel, official services and other private services.

The WTO secretariat has divided all services into following 12 sectors. They are business services (including professional and computer services), communication services, construction and engineering services, distribution services (e.g. commission agents, wholesale & retail trade and franchising), education service, environment services, finance (including insurance & banking) services, health services, tourism & travel services, recreation, cultural & sporting services, transportation services, other services not included elsewhere (WTO Negotiations on Trade in Services, 2002).

3.2 Growing Importance of Services

It is hard to imagine how trade could be conducted without service industries. Trade must be financed, cargo insured and goods transported, distributed and marketed. Such services however can also be traded i.e. provided to a resident of a foreign country without a link to goods. For example i) Banks and huge companies transact huge volumes of business every day, ii) Managing financial resources and providing insurance coverage, without reference to physical products, iii) Planes, ships and railways transport
people as well as merchandise. These activities are part of growing segment of world trade, which is quaintly described as 'invisible trade' (Schott 1983).

GATT was created to bring some order to international trade in goods. It focused mainly on tariffs imposed on goods at national borders and did not envisage a world economy i.e. more and more driven by flows of information. The shift from jobs related to physical production of goods to jobs involving the creation, processing and distribution of data has been dramatic. Information is more involved in support of production of goods now than in past. The developing countries trail further behind, but some of more advanced among them e.g. Singapore are rapidly developing information based jobs. Many of new information based white collar jobs are in service industries. The international communication system serves as the central transport network of world information economy. Investment in communication networks in US keeps climbing, but increase in volume and investments are even larger on a percentage basis in developing countries, which are only constructing integrated communication system. The potential trade in this area could be very large, provided that procurement practices by communication monopolies can be liberalized (Feketekuty & Aronson, 1984).

Trade and development are seen as two sides of same coin, which means trade begins development and development in turn promotes or boost trade. Given the growing awareness of the role, services play in development, there is a new interest in trade in services. Until 80's, it was common to view the service sector as a collection of mainly non-tradable activities with low productivity growth potential. This conventional view of
services is fast changing; the development of certain services is coming to be regarded not as a consequence of economic growth but as one of its preconditions. Trade in commercial services has grown faster than trade in merchandise over the past decade.

Commercial services encompass transport, travel, insurance and financial services among others. According to World Bank, the internationalization of services is likely to lead the next stage of economic globalisation. Thus closely related to interest in services and development is an interest in liberalization of trade in services. Liberalization of trade in services opens important new opportunities and brings new challenges for developing countries.

There is growing evidence that outward-oriented trade policies, in which exports are encouraged or at least not discriminated against, promote more rapid economic growth. Liberalization of trade, removal of restriction on import as and reduction of discrimination against exports, is believed to benefit world at large. Thus, if trade is liberalized it will support increased growth in the world economy, reduce payment imbalances, allow countries to address debt repayment difficulties through increased exports and provide an environment which makes long term adjustment easier (Wahba & Mohieldin, 1998).

Many service industries also have become more international in scope as the economic advantages of specialization and greater economies of scale have become apparent at an international level. Trade in services provides the same mutual economic gains made
possible by trade in goods. It permits international specialization on the basis of comparative advantage. It increases efficiency of domestic industries through increased competition and it enriches consumer choice by widening the range of available services (Brock, 1982).

International trade in services is critical to economic growth. It creates significant new job opportunities, stimulates gains in productivity and provides consumer benefits. It is essential to and inseparable from international trade in goods. International trade in traditional services like shipping, aviation, communications, banking and insurance have always been important to trade in goods and in fact trade in goods could not take place without these services. Where the flow of services is hampered trade in goods is hampered too and where restrictions increase the cost of providing these services, trade in goods is reduced. Trade in services is becoming a vital factor in the world economy and there is an increasing, even an urgent need for public policies to take this development into account.

Services such as data processing, computer programming, scientific research, engineering and consulting are an important and rapidly growing element in international trade. The application of new technologies in communications, data processing and transport has made it increasingly feasible to perform a wide variety of services at a distant geographical location and this has opened up new trade opportunities. Today an analyst in London or Tokyo can have instantaneous access to data banks maintained in Cleveland
or Hamilton and a computer programmer in India can work on software commission by a computer company in Silicon Valley.

These represent an important development in world economy. International transactions in services are broadening the scope for employment for educated youth, thus reducing pressure on them to emigrate and trade in services also permits any country, whatever its location to make use of best available technology, talent or information available anywhere in the world.

International trade in services is also essential for the functioning of international business of multinational enterprises, which are important agencies of development in world economy. Many of economic linkages between a parent firm and its subsidiaries abroad like email transfers of service activities, ranging from managerial, accounting, insurance and legal advise to financing, marketing, advertising, research, engineering and data processing. The unhampered international movement of services is thus critical to the operation of multinational enterprises (Brock 1982).

The growth of trade in services is expected to lead to following benefits

1. Economic performance: presence of an efficient service infrastructure is a precondition for economic success. Services such as telecommunication, banking, insurance and transport, supply strategically important inputs for all sectors, both in goods and services.
2. Development: access to world class services help exporters and producers in developing countries to capitalize on their competitive strength, whatever goods and services they are selling.

3. Employment opportunities: growth in trade in services promotes employment within the country and to a larger extent, growth in opportunities for professional overseas.

4. Consumer choice: there is a strong evidence in many services e.g. telecom that liberalization leads to lower prices, better quality and wider choice for consumers.

5. Technology transfer: services liberalization encourages, FDI. Such FDI generally brings with it new skills and technologies that spillover into the wider economy in various ways (WTO Negotiations on Trade in Services, 2002).

3.3 Emergence of General Agreement on Trade in Services

The magnitude of world trade in services and its rapid growth have been widely given as a major reason why there was a need for a stable institutional environment, for a framework of principles and rules to foster further development of the service sector. While there did exist an international legal framework for trade in goods, there was very little done for trade in services except for certain specific industries. This was of special concern especially because services made up for a greater percentage of Gross National Product of major industrialized countries than the production of goods and they also comprised a significant percentage of world trade.
Industrial countries like US have been emphasizing that international trade in services should constitute an integral part of proposed new round of multilateral trade negotiations and the ultimate objective was to create a legal framework of rules and international regime of discipline that would make trade in services as open as possible through a progressive dismantling of barriers to such trade. US believed that such legal framework should provide for national treatment, market access, transparency and open regulatory procedures and dispute settlement. It was believed by US that overall legal framework would inhibit the adoption of new restrictive measures on trade in services whereas sectoral negotiations would bring about a progressive reduction and elimination of existing barriers to trade in services (Nayyar, 1995).

In September 1986 at Punta del Este, the member countries of the GATT agreed to launch a new round of multilateral trade negotiations, the Uruguay round. The agenda covered familiar topics such as trade in manufactured and agricultural products, unfinished businesses from the Tokyo round negotiations and new topics such as trade in services, intellectual property rights and trade related investment measures. This round offered another chance to reach an effective agreement regarding the imposition of emergency protection (Hoekman, 1988).

Incorporating trade in services into GATT was not easy, as they often do not involve tangible property and it was somehow difficult or impossible to identify when a service crosses a border, the national or international regulations of service activities were very difficult. The notion that GATT should have been simply amended, so that it could be
applied not only to goods but also to services, was not feasible for number of reasons. Amending the GATT was very difficult for it required the consent of two third of contracting parties or in some cases unanimity.

The need to develop an international institutional and rule-oriented framework for discipline on national government measures relating to trade in services was very clear. The time was up, and need was urgent. Delay could have been very damaging because temptation were growing for national government to cater to domestic service providers at the expense of opportunities for international trade in providing services. The subject was however complex. Consequently an approach that stresses the establishment of legal institutional framework which needed to facilitate a pragmatic step-by-step evolution of specific rules for various service industries seemed best at that time (Jackson, 1988).

Considering all the above issues, for the first time in history of GATT, international trade in services and its attendant problems featured prominently on the agenda of multilateral trade negotiations and entered into force on 1st Jan. 1995, with the establishment of WTO. The multilateral legal instrument resulting from Uruguay round was treated as a single undertaking. India also signed all the WTO agreements under the single undertaking rule and GATS is a part of this whole package. Prior to Uruguay round, services were considered to offer less potential for trade expansion than goods, due to existence of technical, institutional and regulatory barriers. However, the development of new transmission technologies facilitating the supply of services, the opening up of monopolies in many countries and gradual liberalization of regulated sectors like
transport, banking and insurance combined with changes in consumer preference, enhanced the tradability of services. These developments were supposed to increase international service flows and create a similar need for multilateral discipline as in area of goods.

3.3.1 General Agreement on Trade in Services and its Principles

The preamble to GATS states that the general goal of participants was to establish a multilateral framework of principles and rules for trade in services with a view to expanding such trade under conditions of transparency and progressive liberalization. This would promote economic growth of all the trading partners and the development of developing countries. Thus, the main purpose for the creation of GATS was to create a credible and reliable system of international trade rules, which ensured fair and equitable treatment of all countries on the principles of non-discrimination. It aimed at stimulating trade and development by seeking to create a predictable policy environment wherein the member countries voluntarily undertake to bind their policy regimes relating to trade in services. The agreement also expressed the desire to facilitate the increasing participation of developing countries in trade in services and expansion of their service exports including inter alia through the strengthening of their domestic service capacity and its efficiency and competitiveness. The agreement also takes a serious note of difficulty of LDC's in view of their special economic situation and their development, trade and financial needs.
Efficient services are crucial to economy's global competitiveness. Thus, GATS article IV seeks increasing participation of developing countries in world trade in services through negotiated specific commitments for access to technology on a commercial basis, improved access to distribution channels and information networks and liberalization of market access in sectors of export interest to developing countries.

The GATS covers all internationally traded services with two exceptions viz services provided to the public in the exercise of governmental authority, and in the air transport sector, traffic rights and all sectors directly related to the exercise of traffic rights (Chadha R., 2000)

The four modes of service supply under GATS are as follows

Mode 1: cross border supply refers to a situation where the service flows from the territory of one member country in to the territory of another member country. It crosses the sovereign national barriers much like that of international trade in goods. E.g. an architect can send his architectural plan through electronic means, doctor sitting in India can advise a patient in some African countries through electronic means. In all these cases trade in services takes place and this is equivalent to cross border movement of goods.

Mode 2: Consumption abroad refers to a situation where consumer of a service moves in to the territory of another member country to obtain the service. This will involve tourist or a student joining any educational institution abroad.
Mode 3: Commercial presence implies that service suppliers of a member country establish a territorial presence in another member country with a view to providing their services. In this case, the service supplier establishes a legal presence in the form of a joint venture/subsidiary/representative/branch office in the host country and starts supplying services. It includes services such as banking, legal advice, insurance etc.

Mode 4: Movement of Natural Persons refers to temporary movement of natural persons. Where a foreigner moves temporarily into a country to supply a service. E.g. software developers from India moving to US to provide software services, a professor giving series of lectures in some other nation. However, GATS covers only temporary movement and not citizenship, residence or employment on a permanent basis in the foreign country. The national government has power to regulate this mode of service supply by granting or refusing visas to the prospective service providers (Goyal A. 2000).

3.4 Different Types of Trade in Services

There are many types of services which are traded internationally, ranging from travel, tourism and motion pictures to expertise provided by lawyers, accountants and other professionals. In general, the trade in services is classified into the following types.
3.4.1 Financial Services

Financial services include two broad categories of services viz insurance and insurance related services and banking and other financial services. These two categories are further subdivided into following:

Insurance and insurance-related services covers, life and non-life insurance, reinsurance, insurance intermediation such as, brokerage and agency services and services auxiliary to insurance such as consultancy and actuarial services.

Banking and other financial services includes services provided by banks such as acceptance of deposits, lending of all types and payment and money transmission services. Other financial services include trading in foreign exchange, derivatives and all kinds of securities, securities underwriting, money broking, asset management, settlement and clearing services, provision and transfer of financial information and advisory and other auxiliary financial services (Goyal A., 2000).

3.4.2 Telecommunication & Data flows

There is a service, which provides a medium for the trade of other goods and services namely data flows. High-speed telecommunication have shrunk a world to a size i.e. more accessible and understandable to a vast number of people. As such it has dramatically narrowed one of most important impediments to international trade and investment, the knowledge gap which in the past made it much more costly to engage in overseas business.
The rapid development of new technologies for the transmission and utilization of data has led to the creation of a widespread range of new products and services and has made it easier and cheaper for many more people and industries to take advantage of data banks and advanced communication services. As with financial services most of financial problems arise out of restrictive government regulations. Telecommunications and information services have been subjected to a significant degree of government regulations. The regulation limits the right of access to data banks, information system and communication networks in many cases exclusively to domestic companies. When permitted, foreign participation in the market is usually controlled through restrictive licensing policies and high taxes (Schott, 1983).

3.4.3 Transport, Travel and Tourism

Another area where rapid changes in technology have revolutionized the provision of services is in the transport, travel and tourism industries. The development of containerized cargoes has transferred the transport industry, allowing the use of lighter and more efficient fuel vessels and facilitating the loading, off-loading and storage of cargo. Such changes have also, however undercut market position and competitiveness of certain shopping lines and bulk cargo carriers and have led to increased calls for protection.

This is not very surprising. Government has regulated the transport industry for years inorder to provide incentives for the development and maintenance of national flag carriers. Because transport services require large capital investment, there is a need to
have fairly good estimate of the future revenue from the service before a decision can be made to sink funds into new ships or aircraft. Government has attempted to afford a kind of guarantee of probability for their transport industry through domestic regulations and negotiations of international agreements, which restrict price competition and fix market shares for national flag carriers (Schott, 1983).

In today’s world, tourism and travel-related services assume great significance for both developed and developing countries, given the industry’s capacity for employment creation, income generation and also as a source of foreign exchange earnings. The sub sectors of tourism and travel related services are hotel and restaurants, food serving services, beverages serving services, travel agency and tour operators, tourist guide services, hotel and resort development services, others including holiday camps, auxiliary tourism enterprises, car rentals for tourist transport operation, computer reservation system and other services.

Tourist services are relatively easy to export, as the dominant mode of delivery is consumption abroad, where the consumers come to the country of the providers for purchasing such service. This is the reason most of the countries compete with each other to attract tourist from all over the world and increase their foreign exchange earnings.
3.4.4. Information Technology

The creation, processing and distribution of information have become a major growth business in the world economy. New jobs are being created in computer programming, in the development of computerized databases for every type of user, including doctors, politicians, bankers and households in professionals service such as law, accounting, engineering & management consulting and in the development of educational & training materials, videotapes & videogames.

Large investments are being made in expansion and improvement of communication facilities. Air France for e.g. invested billions of dollars in its communication and computer facilities, which was more than the investment done in aircrafts. Long standing restriction on international trade in communication equipment and accumulation of new restriction on international trade in information services limited the growth throughout (Feketekuty & Aronson, 1984).

As far as software services and its trade is concerned it constitutes the fastest growing segment of the IT market. With the world sale exceeding every year, hardware suppliers and specialized software firms alike target the software sector. Though largely dominated by enterprises from the developed countries software is still regarded as an opportunity in developing countries. Even though an opportunity exists in this field for developing countries their share in current world software production and trade is extremely low. The reason for this poor performance is the gap between the technical possibility of developing software and commercial viability of selling it successfully.
Domestic markets in large countries such as Brazil and India are relatively small and are unable to provide a platform for development of products above a certain level of complexity and costs.

3.4.5. Other services

There are number of other kinds of services that are traded internationally and face restriction which are similar to those hindering the provision of all major services. These category of services includes for e.g. 1. Construction, engineering and consultancy services. 2. Professional services such as those performed by lawyers and accountants. 3. Motion pictures and other forms of entertainment.

The ability to perform professional services abroad is also sometime hampered by restriction or administrative difficulties in gaining accreditation to practice in foreign country and/or membership of foreign professional association. In addition visa are often denied to foreign professionals in order to force companies to retain local experts. Restriction on the impact of motion pictures and other forms of entertainment are imposed of reasons of cultural sovereignty and to protect the market for local industries and performers (Schott, 1983).

3.5 Emerging Trend and Growth of Trade in Services

In recent years there has been an apparent increase in the possibilities of international trade in services, without any change in degree of restriction on such trade, which is
attributable to technological change on one hand and near revolution in transport on the other. Taken together, these developments have had the following consequences.

1. Non-traded services have become tradable

2. Some altogether new services have entered in to the relation of international transaction

3. The possibilities of trade in services since then have become much larger.

The technological revolution in transport and communication has made till now non-traded services tradable either by a dramatic reduction in the cost of transport, which increases the mobility of the products and the consumer of a service or by developing a means of communication. Such as satellite links or video transmission, which eliminate the need for proximity between the producer and consumer of a service.

The phenomenal pace of technological change in the sphere of telecommunication and informatics and the consequent merger of these two sectors in telematics has created altogether new spaces of traded service in the form of transborder data flows. There are commercial transborder data flows in which the data themselves are the object of international trade and there are corporate transborder data flows in which the data are used within the firm to support their economic activities across national boundaries. Transnational Corporation are among the major users of international information flows for the management of their production, marketing, and trade on global scale.
Such technological change has subsequently enhanced the possibilities of trade in what has always been traded services, for example, financial services such as banking and insurance, which can be disembodied from the producer and transported to the consumer, have entered into this category. In these cases, the impact of technical change is such that the physical proximity of the producer and consumer, which was not necessary so far is now eagerly sought for, because it enlarges the size of market and of the profitability for producer of services (Nayyar, 1995).

Developing countries covered fewer services in their commitments than did industrial countries. Tourism and travel related services were the only activities in which a substantial number of developing countries made commitments. By late 1994, 78 developing countries had offered commitments in services, indicating their support for multilateral discipline for services. The number of commitments in services activities offered by the middle-east countries was the lowest (106) compared to other countries, while, as a percent of maximum possible service commitments (16.5%) was the third lowest (Wahba & Mohieldin, 1998).

A number of studies suggested that the data pertaining to figures of service exports significantly understate the true value of exports. E.g. of one source estimated that American exports of services were in excess of $ 60 billion in 1980 as compared with $ 35 billion recorded in official data. The reason for this is that services are not as easily measured as goods as they cross international borders and few government have developed comprehensive data collection systems require to obtain more accurate figures.
The figures for trade in services in the world during the time period 1985 to 2003, shows that as a percentage of world trade in goods, the world trade in services has increased over the years. Table 3.1, shows that in the year 1985, world trade in services was 19.82% of world trade in goods, this percentage increased to almost 23% in 1990 and to 24% in 2003. Thus the data in the table exhibits that trade in services has been increasing over the years.

Table 3.1 Share of world’s trade in services in world’s trade in goods

<table>
<thead>
<tr>
<th>Year</th>
<th>Service Trade (US$ millions)</th>
<th>Goods Trade (US$ millions)</th>
<th>Percentage share</th>
</tr>
</thead>
<tbody>
<tr>
<td>1985</td>
<td>784485</td>
<td>3958000</td>
<td>19.82</td>
</tr>
<tr>
<td>1986</td>
<td>904386</td>
<td>4338000</td>
<td>20.85</td>
</tr>
<tr>
<td>1987</td>
<td>1074387</td>
<td>5083000</td>
<td>21.14</td>
</tr>
<tr>
<td>1988</td>
<td>1222388</td>
<td>5802000</td>
<td>21.07</td>
</tr>
<tr>
<td>1989</td>
<td>1341389</td>
<td>6271000</td>
<td>21.39</td>
</tr>
<tr>
<td>1990</td>
<td>1622190</td>
<td>6974000</td>
<td>23.26</td>
</tr>
<tr>
<td>1991</td>
<td>1692691</td>
<td>7125000</td>
<td>23.76</td>
</tr>
<tr>
<td>1992</td>
<td>1865292</td>
<td>7648000</td>
<td>24.39</td>
</tr>
<tr>
<td>1993</td>
<td>1896893</td>
<td>7651000</td>
<td>24.79</td>
</tr>
<tr>
<td>1994</td>
<td>2076794</td>
<td>8752000</td>
<td>23.73</td>
</tr>
<tr>
<td>1995</td>
<td>2381795</td>
<td>10439000</td>
<td>22.82</td>
</tr>
<tr>
<td>1996</td>
<td>2538396</td>
<td>10926000</td>
<td>23.23</td>
</tr>
<tr>
<td>1997</td>
<td>2631297</td>
<td>11302000</td>
<td>23.28</td>
</tr>
<tr>
<td>1998</td>
<td>2669298</td>
<td>11160000</td>
<td>23.92</td>
</tr>
<tr>
<td>1999</td>
<td>2769899</td>
<td>11609000</td>
<td>23.86</td>
</tr>
<tr>
<td>2000</td>
<td>2938600</td>
<td>13142000</td>
<td>22.36</td>
</tr>
<tr>
<td>2001</td>
<td>2949701</td>
<td>12643000</td>
<td>23.33</td>
</tr>
<tr>
<td>2002</td>
<td>3117602</td>
<td>13148000</td>
<td>23.71</td>
</tr>
<tr>
<td>2003</td>
<td>3700814</td>
<td>15058280</td>
<td>24.58</td>
</tr>
</tbody>
</table>

Source: WTO Annual Reports

Table 3.2 shows that if the service exports as a percentage of total service trade are considered then the statistics reveal that the world service exports during 1985 was
almost 49% of its total trade in services, 50% each in 1995 and 2003. Thus, service exports comprises half of the total service trade in the world over the years.

Table 3.2 Share of world’s service exports in world’s service trade

<table>
<thead>
<tr>
<th>Year</th>
<th>Service exports (US$ millions)</th>
<th>Service Trade (US$ millions)</th>
<th>Percentage share</th>
</tr>
</thead>
<tbody>
<tr>
<td>1985</td>
<td>380900</td>
<td>784485</td>
<td>48.55</td>
</tr>
<tr>
<td>1986</td>
<td>447500</td>
<td>904386</td>
<td>49.48</td>
</tr>
<tr>
<td>1987</td>
<td>531400</td>
<td>1074387</td>
<td>49.46</td>
</tr>
<tr>
<td>1988</td>
<td>599700</td>
<td>1222388</td>
<td>49.06</td>
</tr>
<tr>
<td>1989</td>
<td>658000</td>
<td>1341389</td>
<td>49.05</td>
</tr>
<tr>
<td>1990</td>
<td>793100</td>
<td>1622190</td>
<td>48.89</td>
</tr>
<tr>
<td>1991</td>
<td>838200</td>
<td>1692691</td>
<td>49.52</td>
</tr>
<tr>
<td>1992</td>
<td>924200</td>
<td>1865292</td>
<td>49.55</td>
</tr>
<tr>
<td>1993</td>
<td>941800</td>
<td>1896893</td>
<td>49.65</td>
</tr>
<tr>
<td>1994</td>
<td>1037800</td>
<td>2076794</td>
<td>49.97</td>
</tr>
<tr>
<td>1995</td>
<td>1188900</td>
<td>2381795</td>
<td>49.92</td>
</tr>
<tr>
<td>1996</td>
<td>1274700</td>
<td>2538396</td>
<td>50.22</td>
</tr>
<tr>
<td>1997</td>
<td>1326700</td>
<td>2631297</td>
<td>50.42</td>
</tr>
<tr>
<td>1998</td>
<td>1340500</td>
<td>2669298</td>
<td>50.22</td>
</tr>
<tr>
<td>1999</td>
<td>1391100</td>
<td>2769899</td>
<td>50.22</td>
</tr>
<tr>
<td>2000</td>
<td>1475700</td>
<td>2938600</td>
<td>50.22</td>
</tr>
<tr>
<td>2001</td>
<td>1478100</td>
<td>2949701</td>
<td>50.11</td>
</tr>
<tr>
<td>2002</td>
<td>1570100</td>
<td>3117602</td>
<td>50.36</td>
</tr>
<tr>
<td>2003</td>
<td>1860351</td>
<td>3700814</td>
<td>50.27</td>
</tr>
</tbody>
</table>

Source: WTO Annual Reports

3.6 Trade In Services And Countries Across The World

During the decade of 1990 and 2000, growth of world services output was 2.9% double that of agriculture which was only 1.4%. As a result, the contribution of service sector to world GDP was 64% in year 2000, compared to 57% in 1990. The share of service sector is approximately 50% in the countries belonging to Europe & central Asia, Latin America & Caribbean, Middle East & North Africa, South Asia & Sub-Saharan Africa. During
the same period, the growth of export of commercial services for developing countries (9%) exceeded that for developed countries (5.5%). The 49 least developed countries also experienced particularly strong export growth of commercial services (6.3%). Twenty-five developing countries depend on export of commercial services for more than half of their total export revenues (WDI, 2001).

If we happen to observe the trend in service trade and service exports, among the few industrialised and developing economies, the data suggest that in US, during the year 1990 the percentage of service exports to total service trade was 62%, which increased to 68% in 1995 but the percentage came down to 59% in 2003. In absolute terms there has been increase in service exports over the years. In England the service exports during the three years were 57%, 63% and 58% respectively. As far as Japan was concerned, the service exports increased from 32% in 1990, to 35% in 1995 and 43% in 2003. When developing countries like India and Brazil are considered, the service exports in India as a percentage of total services traded were 45% in 1990, 40% in 1995 and 50% in 2003, while for Brazil it was 36% in 1990, 32% in 1995 and 43% in 2003.

When statistics of the above five countries was considered, to know the total services traded as a percentage of total trade in goods, it was observed that in US the percentage was 26% in 1990, 24% in 1995 and 25% in 2003. In England it was 24%, 25% and 38% for the three years mentioned, while in Japan it was 25%, 24% and 21% for the above-mentioned three years. The situation in India was that percentage of trade in services was
25% in 1990, 26% in 1995 and 37% in 2003 and in Brazil it was 19% each in 1990 and 1995 and 20% in 2003 (WTO Annual Reports).

Liberalization lifts economic growth by eliminating inefficiency through increased international competition. Services are available not only at lower prices but also in greater varieties through an increase in number of firms that would operate in country. More efficient financial, communication and transportation sectors are likely to attract foreign firms to other industries in the country. Liberalization of services in developing countries could provide as much as $6 trillion in additional income in the developing world by 2015, four times the gains that would come from trade in goods liberalization. Bank estimate suggest that countries that have fully liberalized trade and investment in finance and telecommunication grew on average 1.5% fast than other countries over the past decade. Gains from a cut of 33% in barriers to service trade should raise global economic welfare by $389.6 billion, which exceeds their estimated gains from manufacturers liberalization of $ 210.7 billion (World Bank, 2001).

3.7 Perspective Of Developed And Developing Countries Towards Liberalization Of Service Trade

3.7.1 Developed Countries Perspective

Most of the developed countries in general and US in particular strongly advocated the liberalization of trade in services. This was because during the 1980’s there has been a significant increase in the share of service sector in national income as also in employment, in most of the industrialized countries. There was a perception in US that
the increase in the share of services sector's output and employment reflects a shift in its comparative advantage out of manufacturing activities and into service sector. This process was believed, as attributable to the comparative advantage of developing countries in the manufactured goods, which had through increased imports in to US, displaced resources and persons from manufacturing activities that have been redeployed in the services sector. Such reasoning had led to conclusion that it is not possible for US to provide the rest of the world in particular the developing countries, access to its large market for manufactured goods unless the rest of the world in particular the developing countries, provide the US with access to their market for services.

At one level the US was convinced that, given the technological leads and lags, the economies of scale and already accumulated benefits of learning by it has given it enormous competitive strengths in the service sector, the potential of which remains unrealized largely because of barriers to trade in services. The areas of special interest to developed countries have been services included in Mode 3, which comprises particularly of financial services, but to the dismay of developed countries, it is one of the sub-sector in services which is highly protected by developing countries sighting the national and economic reasons of their interest (Nayyar, 1995).

America has been always focusing and stressing on the need of having a multilateral framework for developing the international trade in services, but this move has always been opposed by developing countries, the reason being most of the restriction maintained by them are integrally linked to their policies for economic development.
Trade is traditionally seen as an activity involving the transfer of goods. But a quarter of world trade flows representing more than $600 billion annually are now accounted for by services such as banking, insurance and telecommunications. These exports have become increasingly significant to the rich economies, where service sectors now accounted on an average for half of national income (70%) in US. In other words, the export advantage in many services as revealed by existing patterns of trade in services seems to lie substantially with the developed countries (Wahba & Mohieldin, 1998).

It is often assumed that a liberal international economic order for information services would work to the detriment of developing countries. But this is almost false as developed countries argue that they will keep their markets open for basic manufacturers produced by developing countries only if they are able to generate more jobs in other information-related industries. This is a matter of politics not economies. Secondly, developing countries such as S. Korea, Singapore, Hong Kong, India and Pakistan have already become major exporters of key information services including computer programming, engineering and keypunching. These types of service industries provide areas in which developing countries are already competitive and can establish export industries without investing large amounts of scarce capital. Thus, developed countries want to put forth the point that liberalization of trade is going to benefit even the developing countries and not alone the developed nations (Feketekuty & Aronson, 1984).

As far as information related services are concerned the establishment of a liberal international economic order for information services is in every country’s interest. Any
country that closes itself off from global sources of information condemns itself not only
to less information but also too less timely information. In a world where information is
of central economic importance such a course can only assure that the country will fall
further and further behind (Correa, 1996).

The nation, which has gained substantially from trade in services, is no doubt America.
Its perspective on trade in services shows that restriction on trade in services breakdown
in to two categories; they are 1) those implemented by familiar non-tariff trade measure
such as import quotas, subsidies and discriminatory procurement, licensing and technical
standard practices. 2) Those implemented by capital controls and discriminatory tax
policies. But many industries particularly those dealing in financial services suffer from
both capital and trade restraints. The only purpose underlying the trade restrictions is to
make it more difficult for foreign firms to compete in markets in question, the former by
undercutting the profitability of firms engaged in service trade and later by affecting the
ability to perform the service (Schott, 1983).

The main message for the developing countries from the developed nation is that they
stand to gain through the liberalization of trade in services. The liberalization of trade in
services is at a stage similar to where the liberalization of trade in goods sectors began
more than 50 years ago. There should be no doubt that reduced barriers on trade in
services in the future would bring benefits to both the developed as well as developing
countries, depending upon their respective degrees of comparative advantage in different
service sectors in a liberalized world economy (Chaddha R, 2000).
3.7.2 Developing Countries Perspective

The section below deals with the arguments and reasons as to why developing countries oppose the liberalization of trade in services every time the issue is discussed in WTO summits.

Saphir argued that freeing trade in services can be beneficial to developing countries since many modern services embodies technology. The acquisition of these services embodies technological transfer. Import of certain services, therefore implies the accumulation of capital by developing countries which will have a wholly beneficial effect in their development and future pattern of trade (Saphir, 1985).

But, in perception of developing countries, the industrialized countries might wish to exchange concession on trade in services for concession on trade in goods, which is an unequal, if not unjust propositions in sectors where developing countries have revealed comparative advantage and GATT rules on trade are already violated, it is possible that the maintenance of present level of access to markets of industrialized countries may become contingent on a corresponding access provided by developing countries to their market for services.

The service sectors, which have been in the proposed agenda for negotiations were those in which a few industrialized countries had an overwhelming comparative advantage. Hence, it was felt that a very large proportion of gains from a liberalization of trade in service would accrue to these industrialized countries. It was not as if the basic gains
from trade proportion cease to be valid, in so far as consumer in the importing countries would also derive some benefit if imports are cheaper than domestic production in terms of domestic resources used. But this argument had serious limitation in the context of services, which are characterized by highly uneven level of development across countries. The distributions of gains from such trade were likely to be unequal between the developed and developing countries. Secondly a liberalization of trade in services at this stage was likely to freeze comparative advantage where it is at this point of time, and such potential comparative advantage that exist in the service sector for developing countries will never be realized (Nayyar, 1995).

The argument of infant industry for protection in the service of developing countries is of particular importance to developing countries. Industries such as telecommunication and informatics, which are infants in terms of their age, whereas services such as banking, shipping and insurance, which are not infant in terms of their age but are infants in the level of their technological developments as compared to their counterparts in the industrialized words. It is plausible to argue that developing countries possess a potential comparative advantage in many of these sectors, which cannot be realized if there is an immediate liberalization of trade in services that does not allow them the time to learn and become competitive in world markets. Most such industries in the service sector are characterized by lumpy investment, long gestation periods and low rates of return, which give rise to externalities in process of development. These industries are also characterized by economies of scale and learning by doing, which are a function of
cumulative production experience not only in terms of output but also in terms of time. Therefore infant industry argument is of special relevance in service sector.

Sectors such as banking, insurance, shipping, transport and telecommunications, which were the proposed focus of the negotiations on services, constitute the core of the infrastructure i.e. strategic in the process of development. Most developing countries wish to retain control over their banking and insurance sectors which mobilize resources to finance the process of development, the allocation of these scarce resources and its effectiveness of financial policies are both, in a sense are a function of such control. Similarly the shipping, the transport and communications sectors are not mere producers of services. These are areas of economic activity where strategic considerations of national sovereignty, national security and national development are of vital importance. A liberalization of trade in services and hence a reliance on foreign firms for these essential services in a world characterized by unpredictable political tensions may well constitute a factor that erodes national sovereignty in political terms. Any legal multilateral discipline, which goes beyond the rule of bilateral reciprocity in the service sector, is likely to limit the freedom of developing countries in the pursuit of national socio-economic objectives they have set for themselves. This is particularly in the sphere of telematics and transport data flows where regulatory institutional frameworks are on an imperative (Nayyar, 1995).

The negotiations in trade in services ought to include sectors in which the developing countries have revealed comparative advantage especially labour services, which require
the movement of the producer across national boundaries to the consumer in order to execute the international transaction. It does not mean permanent migration but a temporary migration from developing to industrialized countries (Nayyar, 1995).

Services account for nearly 20% of total exports of goods and services from industrialized countries to the developing countries, but only 7% of total trade flows in opposite direction. Because developing countries are net importers of services, they had not offered whole-hearted support to GATS negotiated through the Uruguay round. Developing countries feared that many of their own service industries are insufficiently developed to withstand foreign competition.

Service industries are heavily protected by investment regulations. Such regulations are especially extensive in south where government regards the development of indigenous financial service industries as vital for both social and economic reasons. Countries have several devices for protecting domestic suppliers of services from foreign competition. These include visa requirement, investment regulations and restrictions on the ability to repatriate earnings among others (Wahba & Mohieldin, 1998).

Also the firms in developing countries are small and lack financial resources and support. Despite the availability of qualified personnel, firms in developing countries are not accustomed to applying stringent quality standards. This means that internationalization of products developed for domestic market is not necessarily simple or automatic. United States’s firm control the largest part of world market and have preserved an uncontested
leadership in operating system and packages software. Though India has gained considerable recognition as a technically reliable software producer, most firms in the developing countries find it extremely difficult to reach directly the potential end users.

The reasons why developing countries had opposed the liberalization process and a multilateral framework for trade in services was because 1) they fear it would lead to less interest of developed countries in traditional issues. 2) They saw no gains for themselves in liberalizing trade in services for comparative advantage in services lies mostly with the developed countries, especially in ‘modern’ services. 3) They were afraid that developed countries wanted to introduce the subject of FDI in GATT in an indirect way, a very sensitive political issue. 4) They saw no reasons to apply GATT rules to trade in services when developed countries often circumvent GATT rules on trade in goods, to the detriment of developing countries. 5) They consider services to be very important to the development process and want to be able to build their own service industries.

Developing countries want economic development to serve not as a basis for derogation from a more general framework but as a central kernel of the framework for services. As a consequence developing countries want infant industry considerations to be enshrined in the framework, so as to give them the opportunity to catch up with the developed countries (koekkoek, 1988)

Even if trade in services could be small in relation to total trade, the significance of it for LDC’s may be qualitative rather than quantitative. And may have important
macroeconomic implication for the process of investment. As we know, the free trade arguments for goods, which is analytically supporting the advocates of liberalization of trade in services stresses the welfare gains from international specialization and exchange occurring from optimum allocation of resources. It is possible to argue that LDC's may possess the potential comparative advantages that could not be realized by an immediate liberalization of trade in services denying them time to learn and become internationally competitive in 'network' and specialized/science based service sector. Moreover, banking, insurance, shipping, transport and telecommunications are the core of the infrastructure that has strategic role in the process of development. The control over banking and insurance sectors allows for the mobilization and allocation of resources to finance development. Similarly, shipping, transport and communication sectors are areas for which national sovereignty; security and development are of prime importance. Moreover, consumer services are not only a way of improving quality of life but also represent a "package" of TV, fashion advertising, music, fast food and so on, which is likely to influence national cultures and the pattern of development. Therefore it is evident that in many cases, liberalization of trade in services may adversely influence economic development.

From the discussion in the above sub-sections 3.7.2 the study can conclude that negotiations over trade in services have been contentious from the beginning, because although developed countries (esp. OECD countries) are by now united in favouring a strong agreement that would liberalise trade in services, they differ on some of elements and mechanism of such an agreement. LDC's remain hostile to liberalization oriented
service agreement. The US has presented the first comprehensive proposal featuring binding obligation for signatories to provide market access and national treatment with allowance for some reservations to such principles, but LDC’s have made it clear that progress in services depends on the willingness of the developed countries to make concession in areas of interest to them.

Proposal for negotiations were eventually confined to capital related services, the production of which is capital intensive and technology intensive. These are the segments in which developed countries hold an overwhelming comparative advantage. Labour related services in which, LDC’s have a potential or revealed comparative advantage were simply not part of agenda for negotiations.

In this context, Nayyar had voiced the claim that negotiations on services should be more balanced, in which it was not enough to include sector of export interest to developed countries that need temporary movement of corporation and capital across national boundaries for rendering services, but it was also necessary to incorporate sectors of export interest to LDC’s, requiring the temporary movement of labour across boundaries to deliver services. Given the international difference in wages such temporary movement of labourers is likely to be from low wage to the high wage countries. This would provide symmetry to the international trade in services, in so far as capital-intensive services such as banking, insurance or telecommunications are likely to move in the opposite direction. This is only way to ensure a balance of benefits for all negotiators. Any legally binding multilateral framework that does not begin with the
recognition of the implication of disparities in the level of development may seriously hinder the capacity of LDC’s to pursue their own socio-economic objectives therefore LDC’s need to have a right to include or exclude sectors according to their development objectives (Nayyar, 1995).