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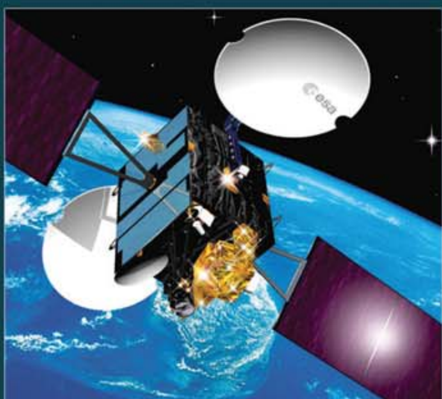

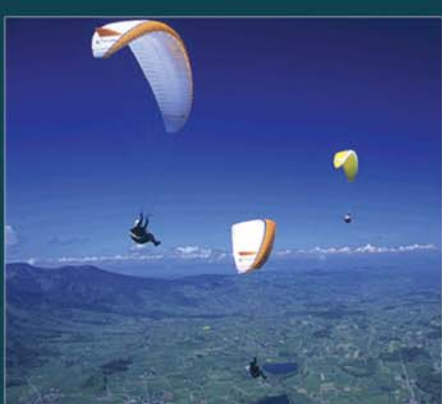

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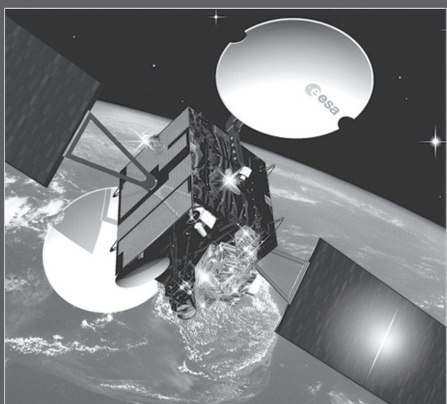

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SAWTEE
SOUTH ASIA WATCH ON TRADE, ECONOMICS & ENVIRONMENT

Published by : South Asia Watch on Trade, Economics & Environment (SAWTEE)

Citation : Pandey, Posh Raj. 2009. *Services Trade Agreement in South Asia: Contours and Modalities.* VI+50, Kathmandu: South Asia Watch on Trade, Economics & Environment (SAWTEE).

First Published : 2009

ISBN :

Price :

Design : Bipendra Ghimire
Effect, Kathmandu, Nepal. Tel: 01-4433703

Cover Photos : Main photo: asisbiz.com. Other photos (from top): esamultimedia.esa.int, chennaiplus.net, www.paragliding.org

Printed at : City Press, Lalitpur

Available from : South Asia Watch on Trade, Economics & Environment (SAWTEE)
PO Box: 19366, 254 Lamtangeen Marg
Baluwatar, Kathmandu, Nepal
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Acknowledgements

This Discussion Paper is a publication under SAWTEE's Regional Programme on Research, Capacity Building and Advocacy on Trade (ReCAT). ReCAT is supported by Oxfam (Novib), The Netherlands.

SAWTEE would like to thank Dr. Posh Raj Pandey for writing this paper. Dr. Pandey is Executive Chairman, SAWTEE.

Acronyms and abbreviations

ADB	Asian Development Bank
ASEAN	Association of Southeast Asian Nations
CARICOM	Caribbean Community
CoE	Committee of Experts
EEA	European Economic Area
EFTA	European Free Trade Area
EIA	Economic Integration Agreements
ESM	Emergency Safeguard Measures
EU	European Union
FDI	Foreign Direct Investment
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
IT	Information Technology
LDC	Least-Developed Country
MERCOSUR	Southern Common Market
MFN	Most-Favoured-Nation
NAFTA	North American Free Trade Agreement
PTA	Preferential Trading Arrangements
RCA	Revealed Comparative Advantage
RTA	Regional Trading Agreements
SAARC	South Asian Association for Regional Cooperation
SAFAS	SAARC Framework Agreement on Trade in Services
SAFTA	South Asian Free Trade Area
SAPTA	SAARC Preferential Trading Arrangement
UK	United Kingdom
UNCTAD	United nations Conference on Trade and Development
WTO	World Trade Organization

Contents

Chapter 1

Introduction

Regional trade liberalization in the South Asian Association for Regional Cooperation (SAARC)—comprising Afghanistan[1], Bangladesh, Bhutan, India, the Maldives, Nepal, Pakistan and Sri Lanka—has been relatively slow, notwithstanding the signing of the SAARC Preferential Trading Arrangement (SAPTA) in 1993 and the Agreement on South Asian Free Trade Area (SAFTA) in 2004. The SAARC Heads of State or Government, at the Thirteenth SAARC Summit (Dhaka, 12–13 November 2005), first recognized the potential of cooperation on trade in services for deeper regional trade liberalization.

The Declaration of the Fourteenth SAARC Summit (New Delhi, 3–4 April 2007) specifically stated the need to integrate services into the SAFTA Agreement and called for a collective vision of South Asia with a free flow of goods, services and ideas. The Declaration also called upon member countries to work towards an early conclusion of the SAARC Framework Agreement on Trade in Services (SAFAS). In March 2008, the SAFTA Ministerial Council directed the senior officials of member countries to draft the SAFAS. The Fifteenth SAARC Summit (Colombo, 2–3 August 2008) endorsed the decision of the Ministerial Council. Thereafter, the Committee of Experts (CoE) held various rounds of meetings to finalize the SAFAS.

Available literature on regional trade integration in South Asia points to a variety of economic and non-economic factors that have slowed the integration process. The major non-economic factors include the strained political relations between India and Pakistan, security concerns of member countries, bureaucratic hassles and high hidden transaction costs, and lack of political will. Similarly, available infrastructures, including transport and energy, in the region are poor, and some of the countries lack supply capacity.

The birth defects in the architecture of SAFTA, such as the narrow range of products covered for liberalization and trade-related issues, the limited trade interest and potential of member countries in the products that are covered, and the modalities of trade liberalization, have also impeded intra-regional trade expansion. The economic factors consist of, among others, limited market size, lack of scale economies, lack of complementarities among the economies and competing trade structures. Thus, most studies tend to be pessimistic about the prospects for integration in SAARC, concluding that the economic rationale for a regional bloc is weak (Chanda 2009, ADB and UNCTAD 2008, Pitgala 2005, Krueger et al. 2004, Baysan and Panagriya 2006).

The birth defects in the architecture of SAFTA have impeded intra-regional trade expansion.

Against the conclusions of these studies on the prospects of regional trade integration in South Asia, it is but natural to question the economic rationale for the inclusion of services in the agenda of regional trade liberalization. However, we argue that if the dynamism of South Asian economies in the services sector, the sector's role in the national economies, and the differential com-

Table 1.1 Services' contribution to GDP

Country	1990	1995	2000	2008
Afghanistan				
Agriculture	…	…	…	40.0
Industry	47.4	21.0	40.4	26.5
Services	40.6	23.8	19.8	33.5
Bangladesh				
Agriculture	31.5	26.4	25.5	19.1
Industry	21.4	24.6	25.3	28.6
Services	47.2	49.1	49.2	52.3
Bhutan				
Agriculture	39.0	34.1	28.4	21.9
Industry	27.6	28.0	26.4	28.6
Services	42.4	45.2	50.4	52.4
India				
Agriculture	30.0	26.8	23.2	19.0
Industry	27.6	28.0	26.4	28.6
Services	42.4	45.2	50.4	52.4
Maldives				
Agriculture	14.6	11.0	8.4	6.0
Industry	12.4	13.0	14.5	17.5
Services	73.0	76.0	77.1	76.6
Nepal				
Agriculture	47.2	37.8	36.6	32.9
Industry	12.3	17.7	17.3	16.4
Services	40.5	44.5	46.1	50.7
Pakistan				
Agriculture	24.9	24.7	24.1	20.4
Industry	25.9	24.2	24.0	26.7
Services	49.2	51.1	51.9	52.9
Sri Lanka				
Agriculture	25.3	20.5	17.6	13.2
Industry	29.8	30.1	29.9	32.2
Services	44.9	49.4	52.5	54.6

Source: UNCTAD 2009.

Table 1.2 GDP and services sector growth (average annual growth rates in %)

Country	GDP growth rates (2000-07)	Services growth rates		
		1980-90	1990-2000	2000-07
Bangladesh	5.8	5.0	5.1	6.3
Bhutan	8.8	9.4	12.2	11.7
India	7.7	6.3	7.4	8.8
Maldives	7.7	11.7	8.6	7.3
Nepal	3.1	4.2	6.5	2.9
Pakistan	6.4	6.4	4.1	6.5
Sri Lanka	5.3	5.3	5.8	5.6

Source: UNCTAD 2009 and Chanda 2009.

parative advantages and externalities to be generated by cooperation on services are taken into consideration, regional cooperation on services is not only beneficial to SAARC member countries but may also help create complementarities in the economies as well. However, the modalities of liberalization of services trade should be unique and region specific, taking into account the development needs of member countries, the institutional capacity to regulate the sectors and the distributional implications among the members.

The services sector has emerged as an important and leading sector in SAARC countries. With the exception of Afghanistan, over half of the gross domestic product (GDP) of South Asian countries comes from the services sector, ranging from 33.5 percent (Afghanistan) to 76.6 percent (the Maldives). In most of the countries, the declining role of agriculture in the total output has been offset by the increasing role of the services sector (Table 1.1).

The services sector has also emerged as the most dynamic sector in South Asia. In all South Asian economies except the Maldives and Nepal, it grew not only much faster than overall GDP during 2000–2007 but also much rapidly compared to previous decades. However, there is a high variation in the growth rates of services across the countries. While services in India witnessed a growth rate of 8.8 percent during 2000–2007, Nepal could manage to achieve a growth rate of only 2.9 percent. Pakistan, Bhutan and Bangladesh also recorded impressive rates of growth in services during the same period. Another important observation is that while the growth of the services sector in Bangladesh, Bhutan, India and Pakistan accelerated during 2001–2007, compared to the previous decade, the Maldives, Nepal and Sri Lanka recorded decelerated growth rates (Table 1.2).

The rise in the services sector's importance in South Asian economies has been accompanied by the rise in its importance for employment in all the countries. Table 1.3 shows that the services sector in the Maldives contributes about half of total employment (50.2 percent in 2000), while the share in other countries ranges between 34.6 percent (Bangladesh) to 38.7 percent (Sri Lanka). However, the rate of growth of employment in services has been far lower than the rate of growth of services GDP, implying jobless growth in services (Table 1.3). It may be because services growth may in part reflect increased factor productivity as opposed to factor accumulation (Banga and Goldar 2004; Singh 2006). However, since most of the services sectors operate in the informal economy, the available data which cover only the formal sector, generally underestimate the role of services in employment generation.

Table 1.3 Services employment (% in total employment)

Country	1991	1985	2000	2003
Bangladesh	..	25.0	23.5	34.6
India	18.4	20.3	25.1	..
Maldives	..	50.4	50.2	..
Nepal	14.9	21.0	..	..
Pakistan	32.7	34.6	33.5	37.1
Sri Lanka	29.6	33.6	33.4	38.7

Source: SAARC 2009.

Table 1.4 Services GDP distribution in South Asia (%)

Country	1980	1990	2000	2007
Bangladesh	9.0	8.0	6.9	6.0
Bhutan	0.0	0.1	0.1	0.1
India	73.9	74.9	79.8	81.9
Maldives	0.0	0.1	0.1	0.1
Nepal	1.1	1.0	0.9	0.7
Pakistan	14.0	14.3	11.1	9.8
Sri Lanka	1.9	1.7	1.0	1.3

Source: http://data.un.org/

The most striking feature of the services sector in South Asia is the asymmetry in the level of production of services among the countries. India, accounting about 82 percent of the regional services output in 2007, is the largest producer of services in the region and its share has increased over time, whereas all other countries' shares have declined. At the absolute level, India's production of services is about 819 times larger than that of the smallest economy, Bhutan, and 8 times larger than the second largest producer, Pakistan (Table 1.4).

Against the background of the emerging dynamism of the services sector in the SAARC region, the purpose of the paper is to suggest the architecture of services trade liberalization under the SAFAS. The rest of the paper is organized as follows. Chapter 2 briefly reviews the literature on the linkages between economic growth and the services sector, and also the major global initiatives on regionalism in services, including the key features of these initiatives. Chapter 3 evaluates the state of and trends in services trade in SAARC countries. It also discusses the potential of services trade liberalization within the region. Chapter 4 presents the commitments of SAARC countries under the General Agreement on Trade in Services (GATS) of the World Trade Organization (WTO). Chapter 5 reviews the provisions of the draft SAFAS and Chapter 6 concludes the discussion with recommendations.

Chapter 2

Review of literature

2.1 Background

The traditional definition of services, which focuses on the three distinguishing features of no-storability, non-tradability and intangibility, is inappropriate in a dynamic world where transnational corporations and rapid advances in information and communications technology have transformed the way services are produced and traded. Therefore, it would be appropriate to define services broadly to encompass activities that add value, either directly or indirectly, to another economic unit or to a good belonging to another economic unit (Chanda 2002). It means services are a diverse group of economic activities distinct from manufacturing, mining and agriculture.

The GATS has adopted a very comprehensive approach to trade in services, both in terms of coverage and mode of supply. Article 1:2 of the GATS defines trade in services for the purpose of the Agreement as consisting of four types of transaction or modes of supply, namely (a) Mode 1: supply of services from the territory of one member into that of another member, i.e., suppliers and consumers interact across distance (cross-border trade); (b) Mode 2: consumption of services by consumers of one member who have moved into the territory of the supplying Member (consumption abroad); (c) Mode 3: services are provided by foreign suppliers that are commercially established in the territory of another member (commercial presence); and (d) Mode 4: services are supplied by foreign natural persons, either employed or self-employed, who currently stay in the territory of another member (presence of natural persons) (WTO 1999). It means that the GATS covers not only traditional trade flows across borders but also three additional types of transactions where suppliers and consumers directly interact by way of consumers moving abroad or suppliers, either a commercial entity or a natural person, moving into the territory of consumers.

Services currently represent more than two thirds of world GDP. The share of services in GDP and employment tends to rise with income, but even for the poorest countries it is now significant. In 2001, services accounted for 45 percent of GDP in low-income economies; 57 percent in middle-income economies; and almost 71 percent in high-income economies. Services activities in low- and middle-income countries have been expanding faster than GDP for the last two decades, and represent on average 5 to 10 percentage points more of GDP than in the early 1980s.

The GATS has adopted a very comprehensive approach to trade in services, both in terms of coverage and mode of supply.

An implication of this continuous shift toward services is that the overall growth of productivity in the economy will be increasingly determined by what happens in the services sector (Marchetti 2007). The expansion in the service intensity of economies is driven by a number of factors. Standard explanations revolve around both demand- and supply-side factors, including income and demand elasticities for services that exceed one, limited scope for labour productivity improvements in the supply of consumer services, the rise in demand for coordination and intermediation services associated with structural changes, and the expansion of the extent of the market as well as incentives for firms and government bodies to spin off services activities to specialized providers (Hoekman and Mattoo 2008).

Recent trends in the pattern of world trade in services indicate three distinct features. First, services have been the fastest-growing sector of the global economy over the last three decades. After five years of stagnation in the early 1980s, global exports of services[2] grew regularly, reaching US$3,371 billion in 2008, a nine-fold value increase compared to 1980. Exports of services grew on average at around 8.61 percent a year in value terms over the period 1980−2008, faster than goods exports (7.96 percent) and world GDP (6.39 percent). As a result, the share of commercial services exports in total world exports (goods and services) rose from 15.2 percent in 1980 to 18.8 percent in 2008, after reaching an all-time high of 19.7 percent in 2002.

Services perform many functions in relation to overall economic growth.

Second, the share of travel and transport in total commercial services decreased, to the benefit of other commercial services. Indeed, the share of transport in total commercial services declined steadily from 37 percent in 1980 to 23 percent in 2008. On the other hand, the share of other commercial services rose from 35 percent to 51 percent of world services trade between 1980 and 2008. These other commercial services, which include many services prone to global outsourcing, such as business and computer-related services, have proven to be the most dynamic segment of world trade in the last two decades (Marchetti 2009).

Third, developing countries' share in world trade in services has grown significantly in the last two decades. Low labour costs, the availability of a well-educated pool of workers, and the improvement in the quality and price of international telecommunications along with spatial fragmentation of goods and services production due to technological advancement have allowed several developing countries to take the lead in this field (Marchetti 2007).

2.2 Services and economic growth

Economic theory postulates that aggregate growth is a function of increases in the quantity and productivity of capital and labour inputs, with long-run (steady state) growth being driven by technological progress. Growth theory accords no special role to services activities, with the exception of financial services. The literature identifies five major functions of the financial system in reducing transaction costs and improving the allocation of real resources: facilitating the trading risk; allocating capital to productive uses; monitoring managers; mobilizing savings through the use of innovative financial instruments; and easing the exchange of goods and services (Cesar and Liu 2003). Other services such as telecommunications, transport and business services such as accounting, engineering, consulting and legal, distribution, education and health also will have a powerful influence on increasing productivity and growth.

Services perform many functions in relation to overall economic growth: they are inputs into production through facilitating transactions through space (transport, telecommunications) or time (financial services) (Melvin 1989). Services are frequently direct inputs into economic activities, and thus determinants of the productivity of the "fundamental" factors of production—labor and capital—that generate knowledge, goods and other services (Hoekman and Mattoo 2008).

The broad conclusion of the theoretical studies on the role of services in the production process and international trade is that the positive welfare effects of liberalizing trade in goods also extends to services as well. Thus, an appropriately timed and sequenced liberalization of the services sector ought to provide the conventional Harberger Triangle welfare gains by reducing, if not entirely eliminating, the wedge between domestic and foreign prices, as well as permitting the "rationalization of service activities along the lines of comparative advantage" (Deardorff 2001). In addition, there are certain dynamic gains from trade consequent upon additional competition (Grossman and Helpman 1991). Further, welfare gains could accrue to consumers from the availability of broader product variety of specialized producer services as well as enhanced product quality.

Services liberalization provides three main sources of gains: it removes the bottlenecks in infrastructural services, lowers the prices of liberalized services, and improves the range and quality of services provided. There are many potential sources of real income gain from exposing a country's services sector to foreign competition: dynamic gains arising from the increased pressure to innovate, gains from lower prices for services through reduced price markups, gains from lower unit costs and a wide range of product choice due to scale economies, and the traditional gains from greater specialization along the lines of comparative advantages (Deardorff 1985, Hindley and Smith 1984).

Empirical studies not only show that the gains from services liberalization may be greater than the gains from goods liberalization but also that adjustment costs associated with services sector reforms may be lower because, with the possible exception of agriculture, access to many services markets has remained more heavily restricted than access to goods markets, most of the restrictions applied are more economically dubious, often consisting of non-revenue generating quotas, than tariff-based protection in merchandise trade and, given the role of many services as generally used inputs, barriers to access and use may stifle efficiency and growth throughout the economic system (Word Bank 2002a).[3]

Mattoo et al. (2001), empirically analyzing the impact of services on growth, found that openness in services influences long-term growth performances. Their estimates suggest that countries with fully open telecom and financial services sectors grow up to 1.5 percentage points faster than other countries. Rajan & Bird (2002) suggested that the greatest gains come from "complete liberalization" and the largest single benefit comes from reducing impediments to market access, particularly, in the context of "establishment" rather than "operations".

Robinson et al. (1999) suggested that the welfare gain for the world as a whole from a 50 percent cut of protection in the services sectors is five times larger than that from non-services sector trade liberalization. Stern (2005) calculated that free trade in services could result in a global welfare gain of US$1.7 trillion. As the highest barriers to trade in services are found in Mode 4 (movement of natural persons), Hoekman (2006) concluded that if advanced countries were to grant an annual immigration quota for both skilled and unskilled temporary workers equivalent to just 3 percent of their labour force, the resulting global gains would be about US$150 billion annually.

Empirical studies show that the gains from services liberalization may be greater than the gains from goods liberalization.

In recognition of the role of services in international trade as well as in economic growth and the need for further liberalization, services were included in the multilateral trade architecture of the WTO in the form of the GATS. Services are prominently featured in recently concluded regional trading arrangements too.

2.3 Regionalism in services trade

Preferential trading arrangements (PTAs) containing discipline on trade in services are proliferating. While only five service PTAs were notified to the WTO at the time of its establishment, 73 economic integration agreements (EIAs) have been notified to the WTO under Article V of the GATS as of 1 September 2009. This figure includes all type of EIAs and membership of developed and developing countries, including the successive European Union (EU) enlargements, the European Economic Area (EEA), the European Free Trade Area (EFTA), the North Amercian Free Trade Agreement (NAFTA), the Southern Common Market (MERCOSUR), the Association of Southeast Asian Nations (ASEAN) and most recent bilateral or regional trade agreement covering services.

Marchetti (2009) and Marchetti and Roy (2008) identify a key feature of the new wave of regionalism: traditional demandeurs in services negotiations, such as the United States (US), the European Commission (EC) and Japan have, for the first time, entered into services PTAs beyond their most immediate neighbors. The EU has asked a number of countries to negotiate services trade liberalization as part of the economic partnership agreements (EPAs) (Marchetti and Roy 2008). Another apparent feature of the recent wave of services agreement is that they often bring together developing and developed countries. EIAs between developing countries have also become more common in recent years. The US-Australia PTA is the only EIA between developed countries since 2000.

The manner in which privileged access can be granted in services markets depends on the instrument of protection in use.

Trade policy implications for trade in services are different from those for trade in goods because of the nature of services themselves. Border measures, particularly tariffs, are almost impossible to apply to trade in services, and other price-based measures, such as taxes, may be applied to services (including foreign services) although they will not be typically levied at the border but, rather, within a country's borders. Additionally, if services trade requires the movement of suppliers and/or consumers, then the ability of governments to impede international transactions in services will depend on regulations affecting the entry, establishment and operations of services suppliers (be they firms or persons) or the movement of consumers. Barriers to trade in services may, therefore, take the form of outright prohibitions, quantitative limitations on services or the number of services suppliers (both natural and juridical persons), local content requirements, foreign equity limitations, discriminatory taxation and subsidization, and discriminatory access to distribution networks, to name just a few (Hoekman and Primo Braga 1997).

Therefore, the manner in which privileged access can be granted in services markets depends on the instrument of protection in use. Since services trade often requires proximity between the supplier and the consumer, it is not enough to extend preferences to cross-border trade, but also to foreign direct investment (FDI) and foreign individual services providers. Moreover, preferential treatment in services is granted not through tariffs but through discriminatory restrictions on the movement of labour and capital (e.g., in terms of the quantity or share of foreign ownership) and through a variety of domestic regulations, such as technical standards, licensing and qualification requirements (Mattoo and Sauve 2008). It means that unlike with regard to trade in goods, protectionist measures in services either increase the variable cost of production without generating rents for government or affect the fixed cost of supply through quantitative restrictions on the number of services suppliers (Fink and Mattoo 2004).

2.4 Key disciplines and features of regional services agreements

Market access commitments are key elements in PTAs, which generally go further than the GATS in this area. In addition, reviewing the provisions of various PTAs, Marchetti and Roy (2008) noted three broad features of services PTAs. First, services obligations are usually included in the comprehensive PTAs covering not only trade in goods, but also investment, intellectual property rights, competition, and a number of provisions to facilitate cooperation in a variety of non-trade areas. Second, PTAs have not introduced critical innovation to the framework of the rules governing trade in services. That is, they do not generally go beyond the GATS, for example, in disciplining subsidies, emergency safeguard measures, domestic regulations and government procurements.

Third, PTAs have produced some innovation with regard to scheduling modalities and approach. They have adopted either the GATS approach of undertaking commitments on the basis of positive lists, or replicated the North American Free Trade Agreement (NAFTA) approach of undertaking commitments on the basis of negative lists, or used a hybrid modality combining elements of the GATS and NAFTA models by using negative-list modalities and including market access obligations modelled on GATS provisions.

Under the "positive list" or "bottom up" approach, only the sectors that parties have expressly identified are subject to market opening undertakings. Countries are free to maintain or impose trade restrictive measures in non-scheduled sectors, although those measures may still be subject to an agreement's general disciplines. Commitments in each listed sector are made with respect to four different modes of supply: cross-border trade (Mode 1), consumption abroad (Mode 2), commercial presence (Mode 3) and movement of natural persons (Mode 4).

Members may inscribe most-favoured-nation (MFN) reservation in relation to both services activities and trade restrictive measures. GATS-style scheduling does not require signatories to make bindings at the level of actual openings. Members of MERCOSUR, EFTA-Singapore FTA, Japan-Singapore FTA, ASEAN Framework Agreement on Services and US-Jordan FTA, for example, adopted one version of the positive-list approach with a view to liberalizing services trade (Table 2.2)

Trade is unrestricted across all covered services unless scheduled limitations indicate otherwise if commitments are scheduled under the negative list approach. Reservations are typically for existing non-conforming measures and future measures. Existing non-conforming measures include all current laws and regulations that a country seeks to maintain, but which would be inconsistent with one or more of the obligations enshrined by the agreement. By definition, limitations scheduled in this category reflect status quo policies (Fink and Molineuevo 2008).

Apart from liberalization provisions, it goes beyond the GATS by subjecting Mode 3 to service-wide disciplines such as domestic regulation and by subjecting investment in services (including Mode 3) to extensive investment provisions, such as on expropriation, minimum standard of treatment, and investor-state dispute settlement procedures. (Roy et al. 2006). This approach has been adopted by most of the services agreements in the Western hemisphere. Since NAFTA took effect in January 1994, Mexico has played a pivotal role in extending this liberalization approach and similar types of disciplines on services to other subregional agreements it has signed with other countries in South and Central Americas (Table 2.2).

PTAs have produced some innovation with regard to scheduling modalities and approach.

While various PTAs still follow either the NAFTA or GATS structure, there are a few PTAs which have adopted a combination of the two approaches. The aim is to achieve greater coherence between services and investment disciplines so as to avoid discrepancies in the treatment of investment in goods and services or in the treatment of trade in services under different modes of supply.

The combined approach seeks to ensure that services trade under all modes of supply is subject to the same disciplines and Mode 3 is covered by generic investment disciplines.

While regional trading agreements (RTAs) covering services come in many different shapes and sizes, they tend to feature a common set of key disciplines governing trade and investment in services that are also found in the GATS, although with different burden of obligations. There seems convergence in rule-making between the multilateral and regional levels in the areas of scope and coverage of agreement, disciplines on transparency, national treatment, MFN treatment, disciplines on payment and transfers, monopolies and exclusive services providers, general exceptions and state-to-state dispute settlement. Lesser convergence or more limited regional progress can be observed in areas of rule-making that have posed recurring difficulties in the GATS setting. This includes issues such as non-discriminatory quantitative restrictions (or market access in GATS terminology), domestic regulation, emergency safeguards and subsidies.

Under the GATS, national treatment is not a general obligation but the result of specific commitments by each WTO member

MFN and national treatments

National treatment and MFN treatment are two of the most essential building blocks for any agreement on services. However, these principles are incorporated in the agreement in a different manner than in an agreement in goods.

Under the GATS, national treatment is not a general obligation but is, rather, the result of specific commitments by each WTO member, and MFN, although a general obligation, can be qualified through time-bound exemptions. As with the GATS, very few RTAs set out such principles in unqualified form, regardless of whether they are framed as general obligations (which is the case for MFN in virtually all agreements and for national treatment in agreements pursuing a negative list approach to liberalization) or as obligations that apply solely to sectors where liberalization commitments are positively undertaken (Mattoo and Sauve 2008). However, MERCOSUR and the Andean Community set out the two principles in an unqualified form, which means that there can be no deviation from the application of MFN treatment or national treatment principles for members (Stephenson and Prieto 2002), whereas the Caribbean Community (CARICOM) and the Central American Economic Integration have not specified any MFN obligations (Table 2.1).

Market access

Market access is a central obligation in PTAs (Table 2.1), but as in the GATS, is not a general and unconditional obligation. In other words, these agreements do not contain any obligation to grant access to foreign services and services suppliers. Rather, under these agreements, the freedom to access the market through any mode of supply is subject to negotiations, and the resulting commitments are entered into national schedules.

In GATS-type agreements, six types of market access limitations are contemplated: a) limitations on the total number of suppliers; b) limitations on the total number of transactions or assets; c) limitations on the total value of operations or output; d) limitations on the total number of employees; e) restrictions on the type of legal entity required to supply services; and f) restrictions on foreign equity participation. NAFTA-type agreements do not have a specific provision on "market access", but contain a somewhat similar discipline addressing "quantitative restrictions", which are defined as non-discriminatory measures that impose quota-type limitations on a) the number of services providers, or (b) the operations of any services provider (Marchetti 2009).

NAFTA-type agreements are, however, weaker than the GATS, allowing members to list non-conforming measures in the annexes even in scheduled sectors whereas under GATS-type agreements, members undertake policy binding in

Table 2.1 Key disciplines in GATS and RTAs covering services

Agreements	MFN Treatment	National Treatment	Market Access+	Domestic Regulations	Emergency Safeguards	Subsidies Discipline	Government Procurement	Rules of Origin
GATS	Yes	Yes	Yes	Yes	Future negotiation	Future negotiation	Future negotiation	Yes
NAFTA	Yes	Yes	Yes	Yes*	No	No	Separate chapter	Yes
Canada-Chile	Yes	Yes	Yes	Yes*	No	No	No	Yes
Chile-Mexico	Yes	Yes	Yes	Yes*	No	No	No	Yes
Bolivia-Mexico	Yes	Yes	Yes	Yes*	Future negotiation	No	Separate chapter	Yes
Costa Rica-Mexico	Yes	Yes	Yes	Yes*	Future negotiation	No	Separate chapter	Yes
Mexico-Nicaragua	Yes	Yes	Yes	Yes*	No	No	Future negotiation	Yes
Mexico-Northern Triangle	Yes	Yes	Yes	Yes*	Future negotiation	No	No	Yes
Central America-Dominican Republic	Yes	Yes	Yes	Yes*	Future negotiation	Future negotiation	Separate chapter	Yes
Central America -Chile	Yes	Yes	Yes	Yes*	No	No	Separate chapter	Yes
Group of Three	Yes	Yes	Yes	Yes*	No	No	Separate chapter	Yes
MERCOSUR	Yes	Yes	Yes	Yes*	No	Future negotiation	Future negotiation	Yes
Andean Community	Yes	Yes	Yes	Yes*	No	No	No	Yes
CARICOM	Not specified	Yes	Not	Yes*	Yes	No	No	Yes
CARICOM-Dominican Republic	Yes	Yes	Yes	Yes*	Future negotiation	No	Separate chapter	Yes
Central American Economic Integration	Not specified	No general article	No	No	No	No	No	Not specified
EU	Yes	Yes	Yes	Yes	No	Yes	Yes	Yes

Cntd...

Table 2.1 Cntd...

Agreements	MFN Treatment	National Treatment	Market Access+	Domestic Regulations	Emergency Safeguards	Subsidies Discipline	Government Procurement	Rules of Origin
Europe Agreements	Yes	Yes	Yes	Yes	No	Yes	Yes	Beneficiaries specified through definition of 'undertakings'
EU-Mexico	Yes	Yes	Yes	No	No	No	Separate chapter	Yes
EFTA-Mexico	Yes	Yes	Yes	Yes	No	No	No	Not specified
EFTA-Singapore	Yes	Yes	Yes	Yes	No	Request for consultation	Separate chapter	Yes
Japan-Singapore	No	Yes	Yes	Yes	No	No	Separate chapter	Yes
ASEAN Framework Agreement on Services	Yes	Yes	Yes	Not specified	Yes	No	No	Yes
Australia-New Zealand Closer Economic Relation Trade Agreement	MFN for excluded sectors	Yes	Yes	Yes	No	No export subsidies prohibited other subsidies excluded	No	Yes
US-Jordan	No	Yes	Yes	Yes	No	Future negotiation	Yes	Yes
US-Singapore	Yes	Yes	Yes	Yes*	No	No	Separate chapter	Yes
US-Chile	Yes	Yes	Yes	Yes*	No	No	Separate chapter	Yes

*Note: + Non discriminatory quantitative restrictions; * Rules on domestic regulations are set out more narrowly (in most cases they apply only to the licensing and certification of professional services suppliers)*
Source: Mattoo and Sauve 2008.

sectors and modes of supply against which market access commitments are scheduled (Mattoo and Sauve 2008).

Domestic regulation

Protectionist measures in services usually take the form of regulations. Regulations are very heterogeneous, and while some may have been designed as protectionist devices, others may be necessary to achieve legitimate economic or social objectives (Marchetti and Mavroidis 2004). Therefore, in a services agreement, it is necessary to distinguish between trade restrictions and "domestic regulations". The disciplines on market access and national treatment are meant to capture the most outrageous or explicit forms of protection of national services industries, i.e., discriminatory measures or specifically identified limitations on market access; while the disciplines on "domestic regulation" deal with more implicit forms of barriers to trade in services stemming from licensing and qualification requirements and procedures, and technical standards.

Most of the RTAs, barring a few (notably, EU-Mexico FTA and Australia-New Zealand Closer Economic Relations Trade Agreement), provide that national measures relating to qualification requirements and procedures, technical standards, and licensing requirements must be based on objective and transparent criteria and must not be more trade restrictive than is necessary to ensure the quality of the service (among other requirements) (Table 2.1). They also encourage, but do not mandate, the recognition of the education, licenses, or certifications of providers of professional services (subject to exceptions). This stands in contrast to the GATS, which is neutral toward recognition (that is, the GATS authorizes recognition but does not encourage or mandate it).

In addition, transparency disciplines, that is, obligation to publish relevant measures and to notify new (or changes to existing) measures affecting trade in services and to establish national enquiry points to provide information on measures affecting trade in services upon request are common. Some of the RTAs in the Western hemisphere, e.g., US-Chile FTA and US-Singapore FTA, provide opportunity to the members for prior comment on proposed changes to services regulations (Mattoo and Sauve 2008).

Emergency safeguard measures

Within the GATS, negotiations on disciplines on emergency safeguard measures (ESM) have not been moving because of conceptual challenges, data limitations, and political sensitivities. RTAs also have not made any headway in devising rules on ESM. Only a few members of CARICOM have adopted such an instrument, and questions remain as to the operational feasibility of an ESM in services trade (Table 2.1). However, NAFTA has provided for such measures in financial services framed essentially in the context of transitional (or phase-in) liberalization measures which feature safeguard-type characteristics (Sauve 2002).

Subsidies

Like ESM, "subsidies" is another unfinished rule-making agenda under the GATS. Few RTAs have provisions on rules on subsidies. The EU disciplines subsidies through competition regulations and the Australia-New Zealand Closer Economic Relations Trade Agreement include rules on export subsidies (Table 2.1). Many RTAs have provisions, as in the GATS, to develop future disciplines on subsidies in services trade but most of the NAFTA-type agreements exclude subsidies from their coverage. The EFTA-Singapore FTA requires that sympathetic consideration be given to the request by a party for consultation where subsidies are deemed to have injurious effects on trade in services. The Japan-Singapore New Partnership Agreement also features provisions on subsidies but are generic in nature and applicable to both goods and services (Mattoo and Sauve 2008).

Emergency safeguard measures and subsidies are unfinished rule-making agendas under the GATS.

Government procurement

Because of the large number of contracts tendered, government procurement is an important component of market access in services. NAFTA broke new ground by including government procurement of services within the scope of the chapter on government procurement, requiring all federal agencies and several state enterprises to open public contracts to services providers in the three NAFTA member countries (under a positive-list approach for entity coverage and a negative-list approach for services coverage). Similar provisions are included in some bilateral FTAs such as Bolivia-Mexico, Costa Rica-Mexico, the Group of Three,

Table 2.2 Key features of GATS and RTAs

Agreements	Sectoral coverage	Negotiating modalities	Treatment of investment in services	Right of non-establishment	Ratchet mechanism
GATS	Universal*	Positive list approach	Covered as commercial presence (mode 3)	No	No
NAFTA	Universal*	Negative list approach	Separate chapter	Yes	Yes
Canada-Chile	Universal*	Negative list approach	Separate chapter	Yes	Yes
Chile-Mexico	Universal*	Negative list approach	Separate chapter	Yes	Yes
Bolivia-Mexico	Universal*	Negative list approach	Separate chapter	Yes	Yes
Costa Rica-Mexico	Universal*	Negative list approach	Separate chapter	Yes	Yes
Mexico-Nicaragua	Universal*	Negative list approach	Separate chapter	Yes	Yes
Mexico-Northern Triangle	Universal*	Negative list approach	Separate chapter	Yes	Yes
Central America-Dominican Republic	Universal*	Negative list approach	Separate chapter	Yes	Yes
Central America -Chile	Universal*	Negative list approach	Separate chapter	Yes	Yes
Group of Three	Universal*	Negative list approach	Separate chapter	Yes	Yes
MERCOSUR	Universal*	Positive list approach	Separate protocols	No	No
Andean Community	Universal*	Negative list approach	Covered as commercial presence (mode 3)	No	No
CARICOM	Universal*	Negative list approach	Covered as commercial presence (mode 3) and in separate chapters	No	No
CARICOM-Dominican Republic	Universal*	Negative list approach	Separate chapter	Yes	No
Central American Economic Integration	Construction service	Positive list approach	Not specified	No	No
EU	Universal*	Negative list approach	Treated as freedom to establish	Yes	No
Europe Agreements	Universal*	Negative list approach	Separate chapter	Yes	No

EU-Mexico	Universal* (audio-visual service explicitly excluded)	Standstill (+ future negotiation a la GATS commitments)	Covered as commercial presence (mode 3) and in separate chapters on investment	No	No
EFTA-Mexico	Universal*	Positive list approach	Covered as commercial presence (mode 3) and in separate chapters on investment	No	No
EFTA-Singapore	Universal*	Positive list approach	Covered as commercial presence (mode 3) and in separate chapters on investment	No	No
Japan-Singapore	Universal*	Positive list approach	Covered as commercial presence (mode 3) and in separate chapters on investment	No	No
ASEAN Framework Agreement on Services		Positive list approach	Covered as commercial presence (mode 3) and in separate chapters on investment	No	No
Australia-New Zealand Closer Economic Relation Trade Agreement	Universal*	Negative list approach	Covered as commercial presence (mode 3) but no common disciplines on investment	Yes	No
US-Jordan	Universal*	Positive list approach	Covered as commercial presence (mode 3)	No	No
US-Singapore	Universal*	Negative list approach	Separate chapter	Yes*	Yes
US-Chile	Universal*	Negative list approach	Separate chapter	Yes*	Yes

*Notes: * Air transport and in certain cases cabotage in maritime services excluded*
Source: Mattoo and Sauve 2008.

EU-Mexico, Japan-Singapore and US-Singapore. The approach taken in the RTAs is for the most part very similar to that adopted in the WTO, i.e., non-discrimination among members within the scope of scheduled commitments and procedures to enhance transparency and due process (Mattoo and Sauve 2008).

Denial of benefits

The GATS allows a member to deny the benefits of the agreement to the supply of a service and to a services supplier from or in the territory of a non-member of the WTO. Under the WTO, a services supplier that is a juridical person is defined as any legal entity subject to majority ownership, effective control, and affiliation with another person (WTO 1999). The objective of such a provision is to prevent non-member investors from taking advantages of market access opportunities. Almost all RTAs have adopted the provision on "rules of origin" (via a provision on denial of benefits) (Table 2.1). However, it goes further than the GATS, defining a services supplier not only as a legal entity under majority ownership or effective control but also as one that must conduct substantial business activities or operations in the territory of any of the member countries in order to benefit from a given agreement.

Labour mobility

Depending on the degree of geographical proximity of the members and the extent of similarities in their level of development as well as other cultural and historical ties, RTAs have taken a range of approaches to labour mobility, from high degree of mobility to continuation of existing national practices. With regard to coverage, it ranges from essentially only intra-corporate transferees and business visitors to free movement of labour. EEA, Europe Agreements and CARICOM provide a relatively high degree of freedom of labour movement with few special procedures. NAFTA, US-Chile FTA, US-Singapore FTA and Canada-Chile FTA provide for some regulated mobility and involve relatively detailed special procedures implemented among a few partners. Others are aimed more at facilitating existing mobility, involving some special procedures, but with maximum flexibility for continuing existing national practices.

RTAs featuring generic investment disciplines typically provide for a right of non-establishment as a means for encouraging greater volumes of cross-border trade in services.

Investment

WTO does not provide a comprehensive body of investment discipline; however, the GATS incorporates investment in services via commercial presence, but is silent on many issues of investment such as investment protection and pre-establishment rights. Following NAFTA, some of the RTAs concluded in recent years have sought to complement disciplines on cross-border trade in services (Modes 1 and 2 of the GATS) with a more comprehensive set of parallel disciplines on investment and temporary movement of business people (Table 2.2, OECD 2002a, OECD 2002).

NAFTA and NAFTA-type RTAs (e.g., Canada-Chile, Chile-Mexico, Bolivia-Mexico, Europe Agreements, US-Singapore, US-Chile) provide investment rules and disciplines covering both matters of investment protection and liberalization combined with investor-state dispute and state-to-state dispute settlement provisions for both goods and services in a separate chapter. A GATS-like approach has been followed in a number of RTAs, notably MERCOSUR, ASEAN Framework Agreement on Services, US-Jordon FTA EU-Chile FTA and EU-Mexico FTA. A number of RTAs, such as Japan-Singapore FTA, CARICOM, EFTA-Mexico FTA and EFTA-Singapore FTA address investment in services under the commercial presence mode of supply (in their services chapter) as well as in a separate chapter dealing with investment, the right of establishment or the movement of capital. RTAs featuring generic investment disciplines typically provide for a right of non-establishment (i.e., local presence requirements as a precondition to supply a service, subject to the right to reserve and list existing non-conforming measures) as a means for encouraging greater volumes of cross-border trade in services (Mattoo and Sauve 2008).

Chapter 3

Services trade in South Asia

3.1 Trends in services trade

The structural transformation, though slow, of South Asian economies in favour of the services sector has been reflected in the services trade of the region. Available data[4] show that the participation of South Asia in global services trade has increased much faster than in goods trade. The share of SAARC in world services export has increased from less than 1 percent in 1990 to about 3 percent in 2008.

One observes similar increasing trends in the services imports, but the incremental rate of participation is higher for exports. As a result, deficits in services trade narrowed down over the period, and the region started recording a surplus in trade in services (Table 3.1). The growth of services export is higher than the growth of the services sector in the economy. Service exports have been consistently increasing during the last two decades and the rate of growth is higher than that of imports. It is not only that the growth in services exports exceeds the growth of other sectors. The average annual rates of growth for South Asia's exports and imports of services have exceeded those for the world economy in all the periods during 1991–1995, 1996–2000, 2001–2005 and 2006–2008 (Table 3.2). This suggests that the growth of the services sector in the South Asian economy is trade oriented.

South Asia's services exports showed a steady upward growth trend in the 1990s and the growth rate accelerated from 2001. While there has been a spurt in the growth of services trade worldwide, reflecting the dynamism in the services sector due to technological, regulatory and structural factors, the growth in the SAARC region is noteworthy as it has registered the highest growth in services exports. The expanding services exports have resulted in a structural change in the composition of exports of South Asia. Services exports constitute around one fourth of all trade flows (goods and services), which is comparable to the contribution of services to overall trade in a developed region such as the EU. The competitiveness of services

Table 3.1 Exports and imports of services in SAARC and their shares in world trade

Year	Exports (Million US$)	Imports (Million US$)	Share in world exports (%)	Share in world imports (%)
1990	7219	9735	0.87	1.11
1995	11076	16352	0.89	1.30
2000	20691	25017	1.35	1.65
2005	63063	60501	2.46	2.47
2008	112886	107102	2.92	2.97

Source: UNCTAD 2009.

Table 3.2 Annual average growth rates of exports and imports of services

Periods	SAARC		World	
	Exports growth (%)	Imports growth (%)	Exports growth (%)	Imports growth (%)
1991–1995	9.08	11.30	8.54	7.65
1996–2000	13.41	8.93	4.31	3.80
2001–2005	26.02	20.32	11.13	10.25
2006–2009	21.61	21.07	14.70	13.75

Source: UNCTAD 2009.

Table 3.3 Share of SAARC countries in the region's services exports and imports

Country	1995		2000		2007	
	Share in exports (%)	Share in imports (%)	Share in exports (%)	Share in imports (%)	Share in exports (%)	Share in imports (%)
Bangladesh	6.30	9.99	3.93	6.73	1.93	3.64
Bhutan	0.13	0.17	0.09	0.11	0.09	0.10
India	61.16	66.99	80.62	79.79	90.07	80.22
Maldives	2.10	0.50	1.68	0.45	0.75	0.33
Nepal	6.13	2.04	2.44	0.83	0.61	0.91
Pakistan	16.76	19.16	6.66	9.36	4.49	11.06
Sri Lanka	7.39	1.12	4.53	2.69	2.04	3.71

Source: UNCTAD 2009.

Table 3.4 Average annual growth rates of exports and imports of services in SAARC countries

Country	1990–1999		2000–2007	
	Exports (%)	Imports (%)	Exports (%)	Imports (%)
Bangladesh	9.16	15.33	9.93	11.32
Bhutan	0.40	0.07	22.21	22.48
India	13.74	11.83	26.75	21.32
Maldives	15.33	14.34	11.32	12.71
Nepal	54.48	4.65	-4.20	17.71
Pakistan	2.09	3.35	15.47	21.31
Sri Lanka	11.25	4.02	8.30	40.14

Source: UNCTAD 2009.

measured by the revealed comparative advantage (RCA) index has increased for South Asia between 1995 and 2007 and the growth of RCA in services is higher than the growth of RCA in merchandise trade (Chanda 2009).

The growing opportunities of trade in services are not equally distributed among South Asian countries

Despite the growing opportunities for South Asia to trade in services, as indicated by the level of participation in world market, growth in exports and imports and competitiveness, the opportunities are not equally distributed among the countries of South Asia. The asymmetry is indicated by the dominant share of India in both exports and imports of services. For example, India's service exports in 2007 were more than 750 times higher than the smallest services-exporting country, Bhutan, and about 8 times higher than the second largest services-exporting country, Pakistan. India's share in the region's services exports and imports has increased significantly whereas the share of other countries has declined, except for Pakistan in services imports (Table 3.3). Moreover, India and the Maldives are the only country having a surplus in services trade. Even India's surplus is of a very recent origin, dating from 2004 (UNCTAD 2009).

The growth rates of services exports and imports also exhibit asymmetry among South Asian countries. Although all the South Asian countries, barring Nepal, recorded positive growth in services exports, the growth rate of India's exports is remarkably high and the average annual growth rate is almost double during 2000–2007 compared to the decade of the 1990s. Bangladesh, Bhutan and Pakistan also recorded higher growth rates during 2000–2007 compared to the 1990–1999 period. With regard to services imports, all the countries recorded positive growth and the average annual growth rate of services imports is higher for all the countries except Bangladesh and the Maldives. India is the only country in the SAARC region whose services export growth surpassed services import growth during 2000–2007 (Table 3.4).

The above analysis shows that the rise in services trade in South Asia, in terms of growing penetration in world markets and increased competitiveness, is driven by India. Thus, given the existing level of asymmetry in services production and trade, any efforts for regional integration in services may raise the question of whether there would be a convergence of interest and opportunities among the South Asian countries. Does it mean that pursuing intra-regional integration in services in South Asia is only beneficial for India? To answer this question, the following section examines the complementarities in the composition of services trade and individual competitiveness at the sectoral level.

3.2 Composition of services trade

The share of exports and imports in the total services trade of South Asia shows that imports of services were higher than exports of services till 2004, but thereafter, exports have exceeded imports (UNCTAD 2009). However, this important change in the composition of trade in services for the region has been mainly led by India, particularly in computer and information services. Exports are highest in computer and information services from India, followed by Sri Lanka and Pakistan.

In terms of imports, India is the only country that has substantial imports of computer and information services. Travel services are found to be an important service in terms of exports, as almost all South Asian countries have positive net exports in this sector, barring Bangladesh and Pakistan. For countries like Nepal and the Maldives, travel services have a major share in their total exports of services. With respect to transport services, all the South Asian countries are net importers, with India being the biggest importer followed by Pakistan. India and Pakistan are also net importers of insurance, financial and other business services. Almost all South Asian countries are net exporters of communication services (UNCTAD 2009).

If one examines the composition of services trade, no clear pattern emerges for most of the countries. Only in the case of India has there been a strong and consistent structural shift in services exports, away from traditional areas like travel and transport services and towards other services, mainly business services such as computer and information, and business professional services.

India drives the change in the composition of trade in services in the region.

The share of "other services" in India's services exports rose from 67 percent in 2000 to 78 percent in 2007, with computer and information and other business services accounting for more than 69 percent of total services exports. The share of travel and transport services declined over this period. In contrast, in other countries of the region, the composition of services exports has shown little change. In 2007, the Maldives's services exports consisted mainly of travel services, Nepal's consisted

Table 3.5 Composition of services exports in SAARC countries, 2000

Services	Bangladesh	India	Maldives	Nepal	Pakistan	Sri Lanka
Transport	11.21	11.86	5.80	12.13	60.87	42.59
Travel	6.19	20.74	92.04	31.19	5.87	26.40
Other services	82.60	67.40	2.16	56.68	33.26	31.01
Communications	2.64	3.59	..	..	13.77	4.83
Construction	0.02	3.01	..	..	..	..
Insurance	0.43	1.54	0.22	..	0.36	4.32
Financial services	1.60	1.65	..	..	0.72	..
Computer and information	0.40	28.34	..	..	1.59	..
Royalties and licence fees	0.01	0.49	1.06	..	..	..
Other business services	12.18	24.86	..	37.71	9.86	19.35
Personal, cultural and recreational services	0.07	..	..	..	..	..
Government services n.i.e.	65.26	3.92	0.88	18.97	6.96	2.51
Total commercial services	34.74	96.08	99.12	81.03	93.04	97.49

Source: UNCTAD 2009.

mainly of travel and government services, Pakistan's was dominated by transport and government services, Sri Lanka's was dominated by transport and travel services, and Bangladesh's was dominated by government services and to a lesser extent by other business services. It means the orientation of India's export services has been directed towards computer and information and business services whereas other countries are focusing on traditional areas of transport and travel.

Mapping out the compositional changes in services exports and imports of South Asian countries, one can infer potential complementarities.

Services imports have exhibited similar structural change across the countries, with the greatest shift occurring in the case of India, again away from travel and transport services and towards other business services. Pakistan and Sri Lanka also observed significant increases in the imports of travel services, whereas Bangladesh in the imports of transport services. Tables 3.5 to 3.8 provide the shares of services exports and imports disaggregated by the categories for the years 2000 and 2007.

The structural changes in the services trade in the region are further reinforced by the growth rates of exports and imports in specific sectors. In Bangladesh, exports of communication, computer and other professional services recorded significant growth rates whereas the growth rates of imports of travel and business services are high compared to transport services. In India, new and dynamic services sectors such as communication, construction, finance, computer and information and other professional services have higher growth rates than the average growth of the services sector. The growth of imports in these sectors is also prominent.

In the Maldives and Nepal, services export growth rates have declined during 2000–2007 compared to 1990–1999 and are reflected in individual sectors. Nonetheless, travel in the Maldives and recreational services in Nepal have maintained respectable rates of export growth. However, growth rates in the imports of transport and business services are high in these countries. Pakistan also made significant progress in the exports of financial services and professional services whereas Sri Lanka recorded impressive growth in the exports of insurance services (Table 3.9 and 3.10).

Mapping out the compositional changes in services exports and imports of the countries of the region, one can infer potential complementarities, particularly

Table 3.6 Composition of services exports in SAARC countries, 2007

Services	Bangladesh	India	Maldives	Nepal	Pakistan	Sri Lanka
Transport	4.95	10.12	4.55	7.24	28.50	49.05
Travel	4.73	11.86	93.41	39.09	7.34	22.51
Other services	90.33	78.02	2.04	53.66	64.16	28.44
Communications	4.73	2.91	..	7.46	3.41	4.21
Construction	1.85	0.53	..	..	1.76	1.92
Insurance	0.66	1.48	0.13	0.61	0.96	3.23
Financial services	1.28	2.75	..	..	1.78	..
Computer and information	0.99	38.73	..	..	3.35	6.43
Royalties and licence fees	0.00	0.15	1.04	..	0.98	..
Other business services	23.14	30.78	..	11.98	10.99	11.48
Personal, cultural and recreational services	0.08	0.29	..	..	0.03	..
Government services n.i.e.	57.61	0.39	0.88	33.60	40.90	1.19
Total commercial services	42.39	99.61	99.12	66.40	59.10	98.81

Source: UNCTAD 2009.

Table 3.7 Composition of services imports in SAARC countries, 2000

Services	Bangladesh	India	Maldives	Nepal	Pakistan	Sri Lanka
Transport	62.51	45.36	48.84	32.39	67.36	85.75
Travel	17.89	14.02	42.11	36.66	11.10	8.55
Other services	19.60	40.61	9.06	30.94	21.54	5.70
Communications	0.46	0.55	..	..	0.67	2.24
Construction	0.13	0.66	..	..	..	..
Insurance	5.62	4.24	3.61	..	1.51	0.02
Financial services	1.90	6.66	..	..	2.00	0.02
Computer and information	0.09	3.01	..	..	..	0.08
Royalties and licence fees	0.27	1.47	..	..	1.24	0.02
Other business services	5.14	22.52	3.83	27.59	9.77	0.93
Personal, cultural and recreational services	0.01	..	..	..	..	..
Government services n.i.e.	5.98	1.51	1.62	3.36	6.35	2.41
Total commercial services	94.02	98.49	98.38	96.64	93.65	97.59

Source: UNCTAD 2009.

between India and other countries in the region. For example, given the importance of travel and transport services in exports, tourism is clearly one area where all countries have a common interest and there is scope for greater intra-regional trade and related cooperation in this area. Likewise, business services constitute an important export segment for India and an increasingly important segment for some of the other countries, indicating the prospects for exports of business and professional services from India to other countries in the region. Related to these categories is the scope for greater cooperation in air and land transport services, and facilitation of business and leisure travel (Chanda 2009).

3.3 Revealed comparative advantage in services

In order to analyze the pattern of services trade specialization and relative competitiveness of the services, RCA[5] indices of various services sectors are used. The summary table of RCA analysis prepared by SAARC (2008) based on RCA indices of South Asian countries for the period 2000−2006 is presented in Table 3.11. It shows that all the South Asian countries have comparative advantage in one or many tradable services sectors. Bangladesh and the Maldives have comparative advantage in one sector each: Bangladesh in communication services and the Maldives in travel services. Other countries have comparative advantage in more than one sector.

While India has been gaining comparative advantage in skill- and technology-based services such as communication and computer and information services due to its relatively rich IT sector and vibrant service sector, other South Asian countries in general are showing relative advantage in labour-intensive services exports. It means there are two distinct groups of countries in South Asia—one that has comparative advantage in skill-based and technology-intensive services trade (such as India), and the other that offers labour-intensive services trade (virtually all South Asian countries except India). This indicates high potential in intra-regional services trade in South Asia, provided countries have adequate capacity to export such services and match the trade demand correctly, and the barriers to their trade are addressed.

While India has been gaining comparative advantage in skill- and technology-based services, other South Asian countries in general are showing comparative advantage in labour-intensive services.

The analysis of intra-regional service trade has been greatly handicapped by limited data availability on bilateral trade in services. SAARC (2008) reports that none of the SAARC countries, except Bangladesh and Pakistan, have in place a system of collecting data on trade in services at the bilateral and regional levels.

However, there are evidences of intra-regional trade in education, health, tourism and financial services. SAARC (2008) noted that both Bangladesh and Pakistan have deficits in services trade with respect to their global trade, but have a surplus in their trade with South Asia as a group and more specifically with India. Unlike in trade in goods, where most of the South Asian countries have trade deficits with India, intra-regional trade in services is more balanced in the SAARC region.

South Asia is a major source of migrant workers for developed and developing countries at various skill levels

Despite the data limitations, some studies have indentified potential services sectors for intra-regional trade expansion based on comparative advantages, complementarities in services across the countries as well as policy reforms at the national level. The identified services are tourism; transport; IT, IT-enabled services, and telecommunications; energy; education; health; financial services; business services; audio-visual and sports and environmental services (ADB and UNCTAD 2008, SAARC 2008, Chanda 2009.)

3.4 Labour mobility

One of the modes of supply for services is the temporary movement of natural persons in the country of the services consumer. International Migration Reports show that South Asian countries such as Bangladesh, India, Nepal, Pakistan and Sri Lanka are major source countries for migrant workers for developed and developing countries at various skill levels. Available information does not differentiate between permanent and temporary movement of labour but will help to analyse the broad trends and patterns of South Asian migrants.

The World Bank estimates that about 20 million South Asian migrants are working outside their country of birth. India is the major source country in the region, constituting about half of the migrants, followed by Bangladesh, Pakistan and Sri Lanka. The skill profile for South Asian labour flows varies by destination. Unskilled workers are concentrated in oil rich Gulf countries whereas high-skill workers choose developed countries as their destination. Bangladesh, Pakistan and India primarily supply workers to work in infrastructure projects in the Gulf region. Around 90 percent of Pakistani temporary contractual work-

Table 3.8 Composition of services imports in SAARC countries, 2007

Services	Bangladesh	India	Maldives	Nepal	Pakistan	Sri Lanka
Transport	72.89	39.66	51.00	39.77	37.12	44.60
Travel	5.40	11.57	34.14	37.87	18.18	50.25
Other services	21.70	48.77	14.86	22.37	44.71	5.15
Communications	0.82	1.42	..	0.70	1.15	0.75
Construction	0.01	1.43	..	..	0.49	0.10
Insurance	7.00	4.19	4.16	4.25	1.61	0.08
Financial services	0.75	2.07	..	..	1.43	0.18
Computer and information	0.13	3.46	..	..	1.39	0.08
Royalties and licence fees	0.26	1.49	..	..	1.22	..
Other business services	5.40	33.77	9.04	16.53	33.36	1.53
Personal, cultural and recreational services	0.00	0.19	..	..	..	0.18
Government services n.i.e.	7.29	0.76	1.65	0.89	4.05	2.25
Total commercial services	99.12	99.24	98.35	99.11	95.95	97.75

Source: UNCTAD 2009.

Table 3.9 Sectoral growth of services exports in SAARC countries (average annual percent)

Services	Bangladesh		India		Maldives		Nepal		Pakistan		Sri Lanka	
	1991-1999	2000-2007	1990-1999	2000-2007	1990-1999	2000-2007	1990-1999	2000-2007	1990-1999	2000-2007	1990-1999	2000-2007
Transport	11.26	0.43	8.71	22.27	8.63	3.22	6.32	9.16	4.98	4.87	12.47	10.08
Travel	13.94	5.88	7.91	18.93	16.24	12.22	26.42	-2.23	-7.10	18.86	15.90	7.28
Other services	8.93	11.45	21.28	31.09	16.28	11.54	…	…	2.57	30.39	7.86	17.05
Communications	…	41.60	…	…	…	…	…	…	…	-2.92	…	…
Construction	…	…	…	…	…	…	…	…	…	…	…	…
Insurance	60.50	36.93	9.03	27.88	4.95	4.59	…	…	20.29	51.36	16.00	111.67
Financial services	…	13.32	…	…	…	…	…	…	…	38.83	…	…
Computer and information	…	45.95	…	…	…	…	…	…	…	45.32	…	…
Royalties and licence fees	…	62.26	71.98	61.75	41.16	21.32	35.64	-9.78	…	…	…	…
Other business services	-4.49	30.22	21.85	43.50	…	…	…	…	-6.05	17.34	8.05	-1.39
Personal, cultural and recreational services	…	…	…	…	…	…	22.55	4.06	…	…	…	…
Government services n.i.e.	25.57	8.26	96.84	-4.50	42.60	18.16	15.32	0.82	-0.35	79.07	5.58	-2.37
Total commercial services	2.71	13.42	13.47	28.39	15.28	11.51	7.89	8.26	2.97	7.58	11.74	8.54

Source: UNCTAD 2009.

ers to the Gulf countries are engaged in semi- and low-skilled jobs. Sri Lanka and Bangladesh are important source countries for domestic workers to the Middle East countries (Chanda 2009)

The importance of migrant workers (Mode 4) is reflected in the importance of remittance in the economy of South Asian countries in terms of its share in total income and growth in the recent past. Remittances amounted to more than one fifth of the GDP in Nepal in 2008. The remittance-GDP ratio was 11.4 percent for Bangladesh, 7.2 percent for Sri Lanka, and 4.2 per cent each for India and Pakistan. The flows of remittances recorded an impressive double-digit growth for all countries except for Maldives, during the period 2000−2008. The growth rate is the highest for Nepal followed by Pakistan, Bangladesh and India (Table 3.12).

Although the preferred destination for South Asian workers is outside the region, SAARC countries have been the destination for more than one third of the migrant workers. Bangladesh has the largest number of workers working in the region but the role of South Asia as a destination market varies across the countries.

The share of the SAARC region in the destination markets for migrant workers is quite high for Bhutan, Nepal and Bangladesh, standing at 87.2 percent, 78.5 per cent and 70.8 percent, respectively. About one fifth of the migrant workers from India and Sri Lanka, and about half from Pakistan are working in the region. Interestingly, more than two thirds of the migrant workers working in South Asian countries are from the region. India is the largest market for regional migrant workers. For Bangladesh, India, Nepal and Sri Lanka, more than 90 percent of the migrant workers are from within the region, but the inflows of regional migrant workers are negligible in Afghanistan, Bhutan, the Maldives and Pakistan. This shows the importance of intra-regional movement of workers in the SAARC region and future prospects for regional integration in labour-intensive service sectors (Table 3.13).

The available information on regional flows of remittance shows that Bangladesh gets the highest amount of remittance from the region but the South Asia region accounts more than half of the total inflows of remittance in Nepal. Regional share in the remittance is 32.1 percent for the Maldives, 15.0 percent for Pakistan, 7.9 percent for Sri Lanka and 7.4 percent for India.

At the regional level, about 14 percent of the total remittances come from the region which is far below the regional share of migrant workers, implying that the employment of regional workers in low skill and low paid jobs (Table 3.14)

The above analysis shows that in the SAARC region, there has been an increasing trend of workers going abroad for jobs and the inflows of remittances have been playing an important role in the national economies. Intra-regional movement of workers is also considerable. Intra-regional flows are driven by the employment opportunities in some of the larger markets, such as India, and by demand-supply mismatch in selected sectors in selected markets. Intra-regional labour flows also reflect the asymmetries in relative size and labour market depth, as well as dynamics arising from poverty and social and cultural networks within the region (Chanda 2009).

Table 3.10 Sectoral growth of services imports in SAARC countries (average annual %)

Services	Bangladesh		India		Maldives		Nepal		Pakistan		Sri Lanka	
	1991-1999	2000-2007	1990-1999	2000-2007	1990-1999	2000-2007	1990-1999	2000-2007	1990-1999	2000-2007	1990-1999	2000-2007
Transport	8.63	3.22	8.22	21.83	13.28	13.68	10.99	20.46	4.07	11.65	28.25	30.73
Travel	16.24	12.22	18.94	20.82	17.29	9.69	7.79	21.53	2.47	45.31	18.19	73.63
Other services	16.28	11.54	15.74	21.77	15.47	22.57	2.22	12.71	5.63	35.72	-6.24	39.60
Communications	..	…	…	72.68	…	…	…	…	…	…	..	512.43
Construction	…	…	…	63.99	…	…	…	…	…	…	…	…
Insurance	4.95	4.59	6.53	24.26	16.83	14.09	…	…	10.61	19.89	…	…
Financial services	…	…	…	12.62	…	…	…	…	…	18.67	…	…
Computer and information	…	…	…	29.56	…	…	…	…	…	…	…	36.87
Royalties and licence fees	41.16	21.32	14.31	18.62	…	…	…	…	…	31.71	…	…
Other business services	…	…	18.55	23.91	21.41	32.73	3.33	13.01	2.05	61.60	..	…
Personal, cultural and recreational services	…	..	…	…	…	…	…	…	…	…	…	…
Government services n.i.e.	42.60	18.16	10.47	15.23	6.74	18.97	7.20	2.89	6.89	7.99	4.23	49.35
Memo item: Commercial services	15.28	11.51	11.96	21.39	14.52	12.67	4.64	18.30	3.23	22.62	4.80	40.09

Source: UNCTAD 2009.

Table 3.11 South Asian countries with revealed comparative advantage in services sectors

Categories of services	Sectors	Countries with revealed comparative advantage (RCA>1)
Labour and resource intensive	Transport	Sri Lanka, Pakistan
Labour and resource intensive	Travel	Maldives, Nepal
Labour intensive	Construction	Sri Lanka
Skill and technology intensive	Communication	Bangladesh, India, Nepal, Pakistan, Sri Lanka
Skill and technology intensive	Computer and information services	India, Sri Lanka
Skill and technology intensive	Financial and insurance services	Sri Lanka

Source: SAARC 2008.

3.5 Investment flows

Commercial presence in the countries of services consumers is the most important mode for providing services in many sectors. This subsection presents the status of foreign direct investment in SAARC countries. One of the major components of the economic reform agenda adopted by the South Asian countries is the liberalization of overall foreign investment policy or foreign investment in key sectors. The overall regional and country-level trends for FDI shows that there is a growing role for foreign investment in the countries of the region and some of the countries have emerged as potential exporters of FDI.

There has been significant growth in the inward flow of FDI in South Asia during the last two decades. Inward flows have increased from an average of about US$2.5 billion during 1990−2000 to more than US$48 billion in 2008. Outward flows have also registered considerable growth. Country-wise trends in FDI flows, both inward and outward, show that all the South Asian countries barring Nepal experienced a significant increase in FDI inflows during 1990− 2008.

However, the growth in FDI flows in India is spectacular and absorbs about 85 percent of the region's FDI inflows. One of the exciting developments in recent years has been that FDI outflows from the region have also increased, particularly from India, Sri Lanka, Pakistan and Bangladesh. India, which accounts more than 99 percent of the region's FDI outflows, recorded FDI outflows from US$ 2billion in 2005 to US$17.6 billion in 2008. Available information on the composition of India's outward FDI indicates that services constitute around 40 percent of such flows, with non-financial services, including computer and business and professional services, constituting the bulk of outward FDI in services from India (Chanda 2009).

Information on intra-regional investment is scanty, and more so in the services sector. FDI flows from within South Asia account for a very small share of total FDI inflows in most South Asian countries, with countries outside the region (e.g., the US, the United Kingdom (UK), Japan and Singapore) being the major sources of FDI. The only noteworthy investor country is India, particularly in the case of Nepal and, to a smaller extent, Sri Lanka (UNCTAD 2009). Chanda (2009) argues that most of the incremental FDI inflows in Nepal, Bangladesh, Pakistan and Sri Lanka are directed to services. In Bangladesh,

Table 3.12 Migrants and remittance in South Asia, 2008

Country	Stock of migrant workers	Remittance-GDP ratio (%)	Average annual growth rate of remittance 2000−2008 (%)
Bangladesh	4885704	11.4	19.9
India	9987129	4.2	19.5
Maldives	1618	0.2	6.3
Nepal	753662	21.6	65.7
Pakistan	3415951	4.2	28.9
Sri Lanka	935599	7.2	12.0

Source: http://econ.worldbank.org

India and Pakistan, the most important subsectors are communication, energy and financial services and, to a lesser extent, construction and certain business services. In Sri Lanka, communication and business process outsourcing constitute the main sectors for FDI inflows, whereas in Nepal, Bhutan and the Maldives, the tourism sector accounts for a major share of FDI inflows.

3.6 Potential benefits and risks in service cooperation

The costs and benefits of an FTA are strongly premised on whether they are trade creating or trade-diverting. An FTA would be trade-creating if liberalization allows a member country to replace a higher-cost domestic supply by a lower-cost partner country supply. This creates enhanced efficiency and is, therefore, beneficial to the member countries. It would be trade-diverting if preferential liberalization by a member country leads to replacing the lower-cost supply from non-partner member countries by higher-cost supply from a partner country.

In most of the cases, these phenomena would simultaneously take place and whether a regional group is beneficial depends on its net trade-creating or net trade-diverting effects. Since the SAFTA Agreement does not include services or investment chapters, though it has identified them as a future area of cooperation, there is little vigorous analysis of the potential for services trade and investment among the South Asian countries.

The services sector is the largest productive sector in all the SAARC economies (except Afghanistan) accounting for more than half of output and an even larger share of growth. It is important that this sector is infused with new dynamism for sustaining the existing growth momentum. In all South Asian countries except Nepal, trade in services has seen robust growth, services have been a major source of economic growth, and services have attracted increasing FDI. The region has been emerging as an important source of FDI.

Similarly, there has been significant movement of workers within the region for providing services. Resource endowment and comparative advantage of individual countries indicate existing and potential complementarity in services trade in the region. In addition, cooperation in services would help to improve or create complementarity in trade in goods also (Banga 2009). Regional integration in services could enhance dynamism of services by providing the region's services suppliers greater opportunities abroad and generating competition at the domestic level to spur innovation.

The cultural, linguistic and geographic proximity between countries in South Asia makes it easier for trade in services to take place, particularly in the context of the requirement for interpersonal re-

Table 3.13 Share of intra-regional migration in total inflows and outflows, 2008

Country	Regional inflows of migration	Share in total inflows (%)	Regional outflows of migration	Share in total outflows (%)
Afghanistan	0	0.0	8823	0.4
Bangladesh	1022094	99.0	3460134	70.8
Bhutan	0	0.0	34125	87.2
India	5444418	95.5	2084802	20.8
Maldives	0	0.0	758	46.8
Nepal	766579	93.6	592354	78.5
Pakistan	0	0.0	1246683	36.4
Sri Lanka	364512	98.9	169943	18.1
Regional Total	7597621	67.6	7597621	34.4

Source: http://econ.worldbank.org

lations in services. Benefits of services liberalization within the region have also been advanced as a viable option for the slow progress at the multilateral level to liberalize trade, a policy measure to diversify export markets and products, a means to exploit economies of scale and efficiency to reduce input costs on business services for the manufacturing sector and gain competitiveness in global markets, an instrument to facilitate transition to multilateral liberalization—particularly in terms of understanding negotiating processes—a potent mechanism to develop supply-side capacity and regulatory system, and a means to strengthen the overall bargaining power of the region in negotiations with other regions and in multilateral negotiations. Regional cooperation can also help to overcome the limitations of national bodies in developing standards besides facilitating exchange of experiences in various aspects of development of service capabilities (SAARC 2009).

The SAARC region has already developed comparative advantage in some sectors, notably, IT, IT-enabled services and telecom services and, to some extent, professional services. Intra-regional services trade may give boost to global services trade. The companies that are already enjoying comparative advantage may facilitate the entry of new firms in the market through outsourcing activities within the region. In this process, the new entrants may acquire capability, consolidate and upgrade quickly to compete in the regional and global markets. Regional cooperation can lead to "flying geese" phenomenon in South Asia where countries specialize in different stages of the value chain. Moreover, sectors such as social services, including health and education, tourism, recreational and sporting services, infrastructure services, including telecommunications and transport, have been identified as potential sectors for greater economic cooperation. A regional arrangement for trade in services could facilitate greater FDI inflows as a lot of trade in services takes place through FDI (SAARC 2008, Banga 2009, Chanda 2009a).

Given the region's deficits in energy production resulting in frequent and widespread power outages and growing demand for energy in the region, an important area for regional cooperation is trade in energy services, which may address the energy security needs of the region. Studies have highlighted the scope of mutual benefits from generation sur-

Table 3.14 Intra-regional remittances, 2008

Country	Regional remittance inflows (million US$)	Share in total inflows (percent)
Bangladesh	1838	43.2
India	1775	7.4
Maldives	1	32.1
Nepal	631	52.1
Pakistan	642	15.0
Sri Lanka	126	7.9
Regional Total	4993	14.1

Source: http://econ.worldbank.org

Table 3.15 Trends in FDI flows in South Asia (million US$)

Country	Inward flows			Outward flows		
	1990−2000 (annual average)	2005	2008	1990−2000 (annual average)	2005	2008
Afghanistan	…	271	300	…	…	…
Bangladesh	218	845	1086	2	3	9
Bhutan	…	9	30	…	…	…
India	1705	7606	41554	110	2078	17685
Maldives	9	9	15	…	…	…
Nepal	6	2	1	…	…	…
Pakistan	463	2201	5438	5	44	46
Sri Lanka	159	272	753	7	38	62

Source: http://www.unctad.org

pluses from Bangladesh, Bhutan and Nepal to meet the demand of India and Pakistan. It may help reduce the region's dependency on fossil fuels and also address trade deficits of Nepal and Bangladesh with India (SAARC 2008, Chanda 2009a, World Bank 2008).

Services market integration may accentuate the existing problems of brain drain and mismatch in labour markets.

The efforts at regional cooperation in services could be marred by institutional and regulatory weaknesses in the region. One of the major risks is arising from lack of data to conduct in-depth studies on the impacts of liberalization on specific sectors and produce effective schedules which strike a right balance between the pace of liberalization and safeguard measures. In addition, the regulatory bodies in many SAARC countries have limited capacity to ensure the quality of services delivery, and health and safety standards, and in the coordination of rules.

Services market integration may accentuate the existing problems of brain drain and mismatch in labour markets as well as augment the stress in local culture (SAARC 2008, de Mel 2009). In addition, poor connectivity and lack of infrastructure, asymmetry in standards, lack of business information, and lengthy bureaucratic procedures and hidden costs in transactions in the region may prevent full realization of the potential of service cooperation (Kumar et al. 2008).

Chapter 4

South Asian countries' commitments under GATS

4.1 Introduction

The General Agreement on Tariffs and Trade (GATT) 1947, the predecessor of the WTO, did not cover trade in services, apart from a few services absolutely essential for the conveyance of goods. It is the GATS, which came into force as an integral part of the WTO on 1 January 1995 as an outcome of the Uruguay Round of negotiations, that extends internationally agreed rules and commitments, broadly comparable with those of the GATT, into trade in services.

The GATS provides a general MFN obligation (subject to exceptions) and a framework of obligations for scheduled services. However, the coverage of the GATS is far more comprehensive than that of the GATT.

First, the definition of trade under the agreement reaches far beyond cross-border flows to include three additional types of transactions or modes of supply, namely consumption abroad, commercial presence and movement of natural persons. Second, the application of the GATS is not confined to product-related measures, as provided for under the GATT, but covers producer-related laws and regulations as well.

Third, it has adopted two different sets of negotiable trade obligations, market access and national treatment, rather than replicating the GATT's exclusive reliance on tariff protection, which is generally impossible in services trade (Adlung and Roy 2005).

The coverage of the GATS in principle is universal and applies to all services, except those relating to air traffic rights and services supplied in the exercise of governmental authority. Article I (3) of the GATS defines the latter as services not provided on a commercial basis or in competition with other suppliers. This carve-out includes the activities of central banks and other monetary authorities, statutory social security and public retirement plans, and public entities using government financial resources.

The obligations enshrined in the GATS could be categorized into two groups: general obligations which apply directly and automatically to all members, regardless of the existence of sectoral commitments; and specific commitments whose scope is limited to the sectors, sub-sectors and/or modes of supply where a member has undertaken market access and/or national treatment obligations.

The application of the GATS covers producer-related laws and regulations as well .

General obligations are of two types: MFN treatment and transparency. Under Article II, members are held to extend immediately and unconditionally to services or services suppliers of all other members "treatment no less favourable than that accorded to like services and services suppliers of any other country". Derogations are possible in the form of so-called Article II exemptions. Members were allowed to list such exemptions before the Agreement entered into force. New exemptions can be granted only to new members at the time of accession or, to current members, by way of a waiver under Article IX:3 of the WTO

Agreement. All exemptions are subject to review; they should in principle not last longer than 10 years. Under Article III, Members are required, inter alia, to publish all measures of general application and establish national enquiry points mandated to respond to other members' information requests.

Market access and national treatment obligations are negotiated and specific commitments undertaken by individual members in specified sectors. Members are allowed to make market access commitments subject to one or more of six types of limitations enumerated in Article XVI(2). For example, limitations may be imposed on the number of services suppliers, services operations or employees in a sector, the value of transactions, the legal form of the services supplier, or the participation of foreign capital.

The flexibilities under the GATS have been reflected in the actual level of commitments under the GATS in terms of sectoral coverage and the limitations on market access.

In any sector included in its schedule of specific commitments, a WTO member is obliged to grant foreign services and services suppliers treatment no less favourable than that extended to its own like services and services suppliers, subject to the terms and conditions specified in its schedule. In this context, the key requirement is to abstain from measures which are liable to tilt the conditions of competition in favour of a member's own services or services suppliers.

Table 4.1 Services commitments: Sectoral coverage

Members	Average number of sub-sectors committed per member	Range (Lowest/highest number of sub-sectors per schedule)
Least-developed countries	24	1 – 111
Developing and transition economies	54	1 – 149
Transition economies only	104	58 – 149
Developing countries only	43	1 – 123
Developed countries	106	87 – 117
Accession since 1995	102	37 – 149
All members (N=151)	52	1 – 149

Source: Adlung and Roy 2005.

As mentioned above, the GATS does not impose the obligation to assume market access or national treatment commitments in a particular sector. In scheduling commitments, WTO members are given a wide range of choices and they are free to tailor the extent of the commitments they schedule in accordance with national policy objectives. They can decide to open markets fully and adopt no limitations on market access and national treatment for their services activities; they can go to the other extreme and make no commitments; or they can make partial commitments in specific sectors and particular modes of delivery (subject to scheduled limitations that in turn become legally binding).

However, once a sector or subsector is scheduled, members assume the obligations concerning, inter alia, the objective administration of domestic regulations and the avoidance of restrictions on international payments and transfers. It means that the GATS opted for a very cautious "positive list" approach with respect to market access and national treatment. This type of "bottom-up" approach to the undertaking of sector-specific access obligations (nothing is bound that is not included) is likely to incite less commitments than a negative-list approach (everything is bound unless explicitly excluded) (Adlung and Roy 2005).

The flexibilities under the GATS have been reflected in the actual level of commitments under the GATS in terms of sectoral coverage and the limitations on market access. WTO members have, overall, included no more than one third of the 160 or so subsectors in their schedules. However, there is significant diversity of commitments across groups of members.

The sectoral coverage of commitments tends to depend on the level of development, higher for developed countries, followed by transition economies, developing countries and least-developed countries (LDCs). It is worth noting that

Table 4.2 Average level of commitments by WTO members (in %)

	Cross-border			Consumption abroad			Commercial presence		
	Full	Partial	Unbound	Full	Partial	Unbound	Full	Partial	Unbound
Market Access									
All (n=148)	37	34	30	53	38	9	20	76	4
Developed	26	48	26	47	52	1	23	75	2
Transition	45	27	28	62	36	2	31	66	2
Developing	29	33	38	46	36	17	10	87	3
LDC	66	20	14	70	19	10	24	67	10
Acceding	47	30	24	62	36	2	30	67	3
National Treatment									
All (n=148)	33	38	29	44	45	11	13	81	6
Developed	15	59	26	30	68	1	0	98	2
Transition	35	42	24	41	56	3	14	85	2
Developing	32	30	38	43	36	20	10	81	9
LDC	68	21	11	76	15	9	46	45	9
Acceding	33	45	21	42	54	4	18	79	3

Note: Based on a sample of 37 sub-sectors deemed representative for the services concerned.
Source: Marchetti and Roy 2008.

acceding countries in spite of their status as developing countries or LDCs have on average undertaken commitments on the same number of subsectors as developed countries, and the maximum number of subsectors opened for commitments for acceding countries is 149 (Table 4.1). This is probably explained by the asymmetric nature of accession negotiations, where prospective members are asked by existing members to make concessions in exchange for membership (Marchetti and Roy 2008).

The number of sectors included in members' schedules is only one of several possibilities to describe the current state of bindings under the GATS. The inclusion of a sector in the schedule of commitments is far from granting full access to one's own market across all modes. It does not provide information on the limitations and conditions for individual mode of supply for scheduled sectors/ sub-sectors.

Distinguishing commitments in various modes of supplies as full commitments (entry scheduled for a particular mode as "none"), full discretion ("unbound"), and the intermediate case of "partial" commitments which are subject to limitations, the average level of commitments on selected services sectors for both market access and national treatment is presented in Table 4.2. The Table shows that the inclusion of any sector in the schedule does not imply full access to one's market across all modes. In fact, the majority of commitments in Mode 1 (cross border trade) and Mode 3 (commercial presence) for the selected sectors are either "unbound" or having "partial" commitments.

In particular, schedules show a high proportion of non-bindings under Mode 1 while Mode 3 is scheduled with many limitations and conditions resulting in a high proportion of "partial commitments". However, for Mode 2 (consumption abroad), most of the commitments are without limitations. With regard to country groups, the pattern of commitments is similar across the groups but LDCs have made more liberal commitments in the sectors scheduled, though lower in number, compared to other groups of countries. (Adlung and Roy 2005, Marchetti and Roy 2008).

The asymmetric nature of accession negotiations probably explains the high degree of commitments undertaken by acceding countries.

While a significant degree of unilateral services liberalization and regulatory reform has occurred in the last decade, the GATS has in fact played little or no role in this process, nor has it yet locked in the results of unilateral liberalization. Indeed, with the exception of WTO agreements on telecommunications and financial services, no multilateral liberalization has occurred under the GATS framework for more than one and a half decades (OECD 2002).

4.2 GATS commitments of South Asian countries

In South Asia, the level of commitments in GATS is the highest for Nepal, followed by Pakistan, India and Sri Lanka.

Among South Asian countries, Bangladesh, India, the Maldives, Pakistan and Sri Lanka are the original members of WTO and Nepal is a newly acceded member, whereas Afghanistan and Bhutan are negotiating their accession. Reflecting the mirror image of the GATS commitments at the global level, original South Asian countries have relatively lower level of commitments than acceded countries both in terms of sectoral/ sub-sectoral coverage and limitations and conditions specified in the schedules.

The level of restrictiveness (or openness) of SAARC countries' commitments in GATS is presented in Table 4.3. The indices show that the level of commitments in GATS is the highest for Nepal followed by Pakistan, India and Sri Lanka. Bangladesh has scheduled in 2 sectors, India in 4, Maldives in 1, Nepal in 11, Pakistan in 6, and Sri Lanka in 2. The restrictiveness in market access is consistently higher than in national treatment for all the countries. The indices also indicate that South Asian countries have taken a cautious approach in making commitments.

However, the level of restrictiveness varies across countries and sectors. Although Bangladesh has scheduled only two sectors, the level of openness is high in the scheduled sectors but for other SAARC countries, except for Nepal, despite higher sectoral coverage, the level of the commitments in terms of

Table 4.3 GATS commitments restrictiveness index for SAARC countries

Sectors	Bangladesh	India	Maldives	Nepal	Pakistan	Sri Lanka
Overall index	3.36	6.69	2.33	33.34	8.97	5.64
Market access	2.24	5.46	2.33	29.19	8.90	4.57
National treatment	4.47	7.91	2.33	37.49	9.05	6.71
Business services	0.00	2.52	8.03	30.32	7.32	0.00
Communication services	26.68	12.08	0.00	15.68	16.42	6.16
Construction/engineering services	0.00	4.02	0.00	14.73	4.02	0.00
Distribution services	0.00	0.00	0.00	54.45	0.00	0.00
Educational services	0.00	0.00	0.00	40.76	0.00	0.00
Environmental services	0.00	0.00	0.00	68.75	0.00	0.00
Financial services	0.00	6.19	0.00	47.58	6.57	16.93
Health/social services	0.00	6.38	0.00	25.53	14.89	0.00
Tourism/ travel services	33.09	18.20	0.00	66.73	24.26	38.60
Recreational/ cultural services	0.00	0.00	0.00	28.65	0.00	0.00
Transport services	0.00	0.00	0.00	13.25	0.00	0.00
Other services	0.00	0.00	0.00	0.00	0.00	0.00

Source: World Bank 2009.

openness is low. Nepal, being an acceded country, stands out in terms of making liberal commitments in South Asia.

During the Uruguay Round, India made very limited commitments. It did not schedule many sectors and even when it did table important sectors such as financial and telecommunication services, key subsectors and activities such as insurance or international long-distance telephony were not scheduled. Moreover, the commitments typically bound less than the status quo creating a gap between existing market access conditions and the level of commitment under the WTO.

For most of the sectors, Mode 1 and Mode 2 were unbound. Mode 3 was subject to FDI ceiling of 49 percent or lower even when existing FDI regulations permitted a higher ceiling, and Mode 4 was unbound except for a few categories of services providers. Thus, India's commitments on services reflected a conservative approach and provided no additional market access opportunities for trading partners (www.wto.org).

However, India made significant improvements on its Uruguay Round commitments in the Doha Round of negotiations on services by tabling offers in several new sectors and subsectors and also signaling that it was willing to remove commercial presence restrictions in key areas which it had autonomously liberalized since the Uruguay Round. Its revised offer covered 11 sectors and 94 subsectors and includes commitments in new areas such as education, distribution, accountancy and environmental services, among others, and also improvements on previously scheduled sectors such as telecommunications, financial and health services, making multilateral commitments closer to unilateral liberalization (See Chanda 2009a for details).

Pakistan made commitments in six sectors, namely business services, financial services, communication services, health and related services, construction and related engineering services, and tourism and travel-related services in the Uruguay Round. A total of 42 sub-sectors were scheduled. However, Pakistan kept Mode 1 and Mode 2 unbound for most of the scheduled subsectors, and capped foreign equity at 51 percent (www.wto.org).

In the Doha Round, Pakistan has offered to undertake commitments in new areas such as distribution services, educational services, and environmental services. In the sectors scheduled during the Uruguay Round, Pakistan has proposed to increase foreign equity limit in engineering services, add subsectors in telecommunication, financial and tourism services and remove Mode 1 and Mode 2 limitations in construction and related services. It has substantially improved subsectoral coverage in business services by including legal, accounting, auditing and bookkeeping services, architectural services, and medical services by including veterinary services and services provided by midwives, nurses, physiotherapists and para medics. Furthermore, computer-related services, research and development services, rental and leasing services, printing and publishing, agriculture storage facilities and rangeland services have been offered (Uddin 2009).

In the Doha Round, Pakistan has offered to undertake commitments in new areas

Sri Lanka's initial commitment in the GATS was limited to tourism in 1994 and included hotel and lodging services and travel and tour operating services in the schedule. However, with the conclusion of agreements on telecommunications and financial services in 1997, Sri Lanka included telecommunications and financial services in its schedule. In these two sectors, Sri Lanka included almost all subsectors in its schedule but has kept unbound Mode 1 and Mode 2 for financial services. It has also put economic needs test or quota allocation for foreign services providers with a foreign equity cap (www.wto.org). Compared to the existing level of unilateral liberalization that has been undertaken in Sri Lanka, its multilateral commitments were substantially low. Furthermore, the level of commitment in the listed sectors is lower than the actual level of liberalization evident in the country (de Mel 2009).

The GATS schedules of Bangladesh and the Maldives cover a very limited number of sectors. The Maldives has scheduled accountancy, auditing, bookkeeping under professional services and computer hardware consultancy, software implementation, data processing and data base services under computer services with no limitations on market access or national treatment affecting all mode of supplies (www.wto.org).

South Asian countries in general have made commitments below the level of locking in unilateral services liberalization.

Bangladesh has undertaken commitments in almost all telecommunications services and only five star hotel and lodging services under tourism and travel-related services. However, Bangladesh has inscribed limitations and conditions in terms of the technicalities in providing services as well as the number of service providers in telecommunication services. In tourism services, Bangladesh has kept Modes 1 and Mode 2 unbound.

Being an acceded member of the WTO, Nepal's commitment in the GATS is more comprehensive compared to other SAARC countries. Nepal has scheduled altogether 11 services sectors and 77 sub-sectors which constitute 48 per cent of all the subsectors of WTO categorization. However, Nepal has listed a few limitations and conditions on both market access and national treatment. There is a foreign equity cap of 80 percent for two sectors, namely telecommunications and computer services, while for other sectors the cap is between 51 percent and 66 percent. Similarly, Nepal has inscribed limitations on national treatment by maintaining the right to provide subsidies only to the services provider wholly owned by Nepali citizens, and limitations on the employment of foreign nationals.

Fully exploiting the flexibilities provided by the GATS, South Asian countries in general have made commitments below the level of locking in unilateral services liberalization. The level of commitments in terms of sectoral coverage, except for Nepal, is lower than the average of their respective groups. However, India and Pakistan have improved their schedules of commitments during the ongoing Doha Round services negotiation by including new sectors or relaxing the limitations on previously scheduled sectors. Despite all these developments, the GATS commitment of Nepal is the most liberal in South Asia.

Chapter 5

Status of SAFAS negotiations

5.1 Introduction

The services sector in South Asia have emerged as the most dynamic sector of the economy and its growth has surpassed the growth in other sectors. As a result, its contribution in GDP is higher than the combined share of agriculture and industry. Much more importantly, the growth in services trade is much higher than the growth of services GDP as well as the growth of trade in goods. It implies that South Asian services growth is driven by the exports of services. At the regional context, some of the South Asian countries are having comparative advantage in high-skill and technology-intensive services while some in low-skill and labour-intensive services, indicating strong potential complementarities in services trade in the region. The potential of intra-regional services trade is further strengthened by the fact that some of the South Asian countries have been emerging as an important source for FDI and migrant workers.

Despite the prevalence of economic and non-economic rationales for closer cooperation on trade in services in the SAARC region, it was only in 2005 that SAARC Heads of State or Government at the Thirteenth SAARC Summit (Dhaka, 12–13 November 2005) first recognized the potential of cooperation on trade in services. Thereafter, the Declaration of the Fourteenth SAARC Summit (New Delhi, 3–4 April 2007) specifically stated the need to integrate services into the SAFTA Agreement and called for a collective vision of South Asia with a free flow of goods, services and ideas. The Declaration also called upon member countries to work towards an early conclusion of the SAFAS. In March 2008, the SAFTA Ministerial Council directed the senior officials of member countries to draft the SAFAS, and the Fifteenth SAARC Summit (Colombo, 2–3 August, 2008) endorsed the decision of the Ministerial Council. The SAFTA Ministerial Council entrusted the Research and Information System for Developing Countries (RIS), New Delhi to prepare a draft of the SAFAS. Taking the RIS draft, the SAFTA COE started negotiations on the SAFAS in November 2009 and since then various rounds of meetings of CoE have been held. This chapter critically reviews the latest draft of the SAFAS.

SAARC first recognized the potential of cooperation on services trade in 2005.

5.2 Contours of the SAFAS

As explained in Chapter 2, EIAs covering services concluded so far as well as the GATS have adopted key disciplines to regulate intra-regional services trade. The key characteristics of such EIAs include the scope and coverage of the agreements, approach in liberalizing regional services or the scheduling approach, MFN treatment, rules of origin (ROO), mechanism for dispute settlement, disciplines on domestic regulation, treatment of subsidies and emergency safeguard measures, treatment of investment, treatment of labour mobility, and treatment of government procurement. Irrespective of the approach adopted, the ultimate objective of any trade agreement is to promote international trade and the objective can be achieved in three ways: by reducing barriers to foreign participation, by making trade policies more transparent, and by enhancing the credibility of the trade regime or reducing the risk of policy becoming more restrictive (Fink and Molinuevo 2008). An assessment is made in this section as to what extent the SAFAS promotes trade along these three dimensions.

The SAFAS has been an adjunct to the SAFTA Agreement (SAARC 2004), has, by and large, adopted key features of the GATS and has been closely modelled on the GATS. In addition to the preamble, the agreement consists of 32 Articles. Analogous to the GATS, the agreement primarily contains provisions on definitions, objectives, principles and guidelines, scope, general obligations of MFN treatment and transparency, market access, national treatment, domestic regulations, recognitions, treatment of monopolies and exclusive services suppliers, safeguards including restrictions to safeguard BOP, subsidies, special and differential treatments, general and security exceptions, denials of benefits, and dispute settlement mechanism. The following subsections deal with the major provisions in the SAFAS, including those which deviate from the GATS or major non-NAFTA-type EIAs.

SAFAS covers any services in any sector except services supplied in the exercise of governmental authority.

Scope and coverage

The agreement covers any services in any sector except services supplied in the exercise of governmental authority. It has adopted the sectoral coverage of the GATS but has provided flexibilities to add any sector during the course of sector-specific negotiations, reflecting specific needs and requirements of the region. As in the GATS and most of the EIAs, it disciplines the measures taken by the central, regional or local government and authorities, and non-governmental bodies exercising powers delegated by central, regional or local governments or authorities in respect to the purchase, payment or use of a service, the access to and use of services generally offered to the public and presence of juridical and natural persons of member countries for the supply of services.

Market access

The aim of any EIA is to seek to liberalize trade progressively, not to establish a free trade regime immediately. It is so because governments wish to exempt certain activities from the coverage of trade disciplines or maintain certain trade-restrictive measures for economic, social or political reasons. Flexibilities are sought either through the exclusion of certain sectors from negotiations or exemption of certain measures from the disciplines established in the agreement.

As in most EIAs and the GATS, the SAFAS also carves out transportation and non-transportation air services, including domestic and international services and related services in support of air services other than aircraft repair and maintenance services, the selling of air transport services and computerized reservation system services from the scope of the agreement. The agreement also does not apply to government procurement, and measures affecting natural persons seeking access to the employment in foreign markets and measures related to citizenship, residence or employment on a permanent basis (Article 3)

The aim of the agreement is to promote and enhance trade in services among the member countries in a mutually beneficial and equitable manner by progressively covering liberalization of trade in services with broad-based and deeper coverage of the majority of services sectors/sub-sectors (Article 2). In order to liberalize services trade in the region, it has adopted, as in the GATS and other EIAs, a positive-list approach with specific commitments for progressive liberalization to be based on “request-and-offer” approach. The agreement specifically states that initial offers of the WTO-member contracting states shall be in addition to their existing levels of multilateral commitments with substantial sectoral and modal improvements over those commitments (Annex 1). However, given the different levels of commitments of member countries in the WTO, such an approach may contribute to nullify the objective of providing real and effective market access in an equitable manner, as stated in the principles for negotiations.

In the positive-list approach, only the sectors that members have expressly identified are subject to market opening undertaking. Members are allowed to inscribe market access "terms, limitations and conditions" and national treatment "conditions and qualifications" with respect to four different modes of supply: cross-border trade, consumption abroad, commercial presence and movement of natural persons.

Countries are free to maintain or impose trade-restrictive measures in non-scheduled sectors, although those measures may still be subject to the agreement's general disciplines such as on MFN treatment and transparency. But members have the right to express reservations on the MFN obligation. It also allows for horizontal commitments, which apply to all listed service sectors, unless the wording of a sectoral commitment unambiguously indicates otherwise.

Although the agreement aspires to provide real and effective market access by progressively covering the liberalization of trade in services with broad-based and deeper coverage of majority of services sectors/sub-sectors, (Annex II) the modality adopted by the agreement do not require members to make bindings commitments at the level of actual openness.

In fact, they have full flexibilities to be less liberal than the status quo, creating the so-called "binding overhang". Such an approach runs the risk of creating uncertainty in the market because governments can restrict foreign participation in their domestic services market at any time as long as they honour the commitments.

Investment

Unlike NAFTA-type FTAs, the SAFAS has adopted the GATS approach in the treatment of investment under the mode of commercial presence. It does not have separate chapters on disciplines regulating investment at the horizontal level. The definition of commercial presence is substantially narrower. The disciplines cover FDI in services only where the investor of the member country is engaged in substantive business operations and holds more than 50 percent of the equity interest or exercises control over the invested enterprise. Foreign investments with a minority equity stake and no exercise of control are not covered by the services disciplines (Article 1 and Article 25).

Rules of origin/ Denial of benefits

Unlike NAFTA-type FTAs, the SAFAS has adopted the GATS approach in the treatment of investment under the mode of commercial presence.

In most EIAs, trade benefits are extended to the members, thereby resulting discriminatory treatments to non-members. Therefore, defining the eligibility for preferential treatment so that only the goods, services or services providers originating in the members have access to the preferential market is vital. Trading arrangements have resolved this issue through ROO. Compared to the case of goods trade, where ROO is determined by the share of imported intermediate products in the final products, defining ROO in services trade, where the services agreement applies to both services and services providers, is broader.

In principle, questions of origin arise in three different contexts: (a) when the imported service relies on the provisioning of intermediate service imported from non-member countries (origin of services), (b) when the juridical person of a member seeking commercial presence or exporting services through other modes is partly owned by a non-member country in a member country (origin of service suppliers in the form of juridical persons) and (c) when persons supplying the service through movement to the consumer country is not a national of a member country but has special ties with it (origin of services suppliers in the form of natural persons).

It seems that the agreement has, in general, replicated the provisions of the GATS. With regard to the first issue of what constitutes a service of another member, the agreement expressly allows a member to deny benefits if it establishes that the service is supplied from or in the territory of a non-member.

It means that as long as a service originates within the territory of an exporting member country, it would be eligible for preferential treatment. However, in the case of maritime transport services, services provided by a vessel registered under the laws of a non- member or by a person operating and/or using a vessel of a non-member country are not eligible for preferential access.

The SAFAS does not provide any insights to settle the multilaterally unfinished agenda of domestic regulations at the regional level.

The agreement lays down two conditions for defining the origin of services suppliers: the service-providing entity is required to be "owned" or "controlled" by a person of a member country; and it should have "substantive business operations" in the territory of a member country (Article 25).

The first requirement, though ill-defined in terms of ownership or control, recognizes the regional cumulation whereas the second discourages "mailbox" companies that do not have any commercial interest in the country of establishment but merely seek to exploit the regional trade preferences.

On the issue of the origin of services suppliers in the form of natural persons, the agreement has taken on a restrictive approach. Unlike in the GATS and other PTAs, which have accepted economic ties as a major criterion in defining a natural person, it has defined a natural person as a person who resides in the territory of the member country or elsewhere and who under the law is a national of the member country (Article 1).

Domestic regulations

In general, protection to domestic services providers is bestowed through discriminatory regulations vis-à-vis foreign services or services suppliers. Therefore, in most trade agreements, including the GATS, one finds disciplines on domestic regulations so that internal government measures do not unnecessarily undermine the market opening offered by the core obligations on national treatment, MFN treatment and market access.

The SAFAS does not provide any insights to settle the multilaterally unfinished agenda of domestic regulations at the regional level, but carries away the provisions of the GATS, and members agree to review the provisions taking into account of the developments in the GATS. It provides that generally applicable measures that affect trade in the services sector in which a member has made commitments must be applied reasonably, objectively and impartially. Members must not apply licensing and qualification requirements and technical standards that nullify or impair specific commitments. However, members are free to take measures for legitimate regulatory purposes such as such as protecting consumers, remedying market failures, and ensuring the quality of services. It also obliges members to maintain or institute judicial, arbitral or administrative tribunals or procedures which provide for the prompt review of, and where justified, appropriate remedies for, administrative decisions affecting trade in services (Article 11).

Recognition

Analogous to the GATS, the agreement urges members to recognize the educational and other qualifications of services suppliers from members. But while GATS allows the governments to negotiate agreements among themselves for mutual recognition, the SAFAS has entrusted their respective professional bodies to negotiate and conclude mutual recognition agreements on education, or experience obtained, requirements met, or licences or certifications granted in the services they regulate. It has also made responsible the professional, standard-setting or self-regulatory bodies to settle the disputes arising out of or under the agreements or arrangements for mutual recognition concluded by them. One striking feature of the SAFAS is that it also encourages members to work in cooperation with relevant inter-governmental and non-governmental organizations towards the establishment and adoption of common regional standards and criteria for recognition and common regional standards for the practice of relevant services trades and professions (Article 12).

Subsidies

In the area of subsidies, the GATS does not establish any special disciplines. It merely provides for a negotiating mandate to develop necessary disciplines to avoid the "trade-distortive" effects of subsidies. In the absence of special rules, subsidies in services are subject to all obligations under the GATS, most importantly national treatment. In other words, in sectors where specific commitments are undertaken and unless national treatment limitations with respect to subsidies are inscribed, government aid offered to domestic services suppliers has to be extended on a non-discriminatory basis to foreign services suppliers also.

In contrast to the provision of the GATS, the agreement has carved out subsidies or grants, whether or not such subsidies or grants are offered exclusively to domestic services, services consumers or services suppliers, from the scope of services disciplines. But if such subsidies or grants adversely affect the commercial interest of other members, subsidies-providing members are urged to accord sympathetic consideration to the request for consultations, though a member does not have the right to invoke the dispute settlement mechanism for such consultations. The agreement also provides a provision to review the treatment of subsidies when relevant disciplines are developed by the WTO (Article 16).

Safeguard mechanism

In order to encourage members to undertake commitments to liberalize services trade, it is necessary that some safeguard mechanism in terms of the flexibility to temporarily depart from their commitments be provided in the case of an unanticipated surge in services imports with harmful effects on domestic services suppliers. During the Uruguay Round, such emergency safeguard measures were considered but no consensus could be achieved. The GATS merely calls for negotiations "on the question of emergency safeguard measures based on the principle of non-discrimination". The SAFAS emulates the provision of the GATS on safeguard measures and members agree to conduct a review of the provisions on safeguard measures so as to incorporate the results of WTO negotiations (Article 15).

The SAFAS recognizes that the LDCs of the region need to be accorded special and differential treatment commensurate with their development needs.

Special and differential treatment

The SAFAS recognizes that the LDCs of the region need to be accorded special and differential treatment commensurate with their development needs (Preamble) and contemplates special and more favourable treatment to LDC member countries. Although "best endeavour" in nature, the agreement urges members to provide special concessions to LDCs while undertaking commitments. It also accords flexibilities for LDCs in terms of opening fewer sectors, liberalizing fewer types of transaction and progressively extending market access in line with their development situations.

The provision on technical assistance is strongly worded compared to the SAFTA Agreement. It obliges members, bilaterally or through subregional/ regional projects, to provide technical assistance to LDC member countries "for enhancing their supply capabilities in service sectors and infrastructure development; for research and capacity building programmes; and for catering to the institutional and regulatory needs with a view to strengthening their domestic service capacity, efficiency and competitiveness" (Article 22).

Regional cooperation

The SAFAS contemplates regional cooperation in three areas, namely development of regulatory capacity, collection and exchanges of statistics, and GATS negotiations. It envisages constituting working groups for specific sectors of interest comprising national authorities and stakeholders for facilitating cooperation in the identified areas. Although the agreement calls upon members to cooperate and coordinate their positions in GATS negotiations, such cooperation and cooperation are not obligatory.

SAFAS' dispute settlement mechanism is weak.

Labour movement

Since the provisioning of many services requires the physical proximity of services providers and consumers, freeing the flow of certain categories of labour is crucial in expanding regional services trade. The SAFAS has adopted the definition of Mode 4 (presence of natural persons) as "the supply of service by a service supplier of a Contracting State, through presence of natural persons of a Contracting State in the territory of the other Contracting State" (Article 1).
Some commentators have argued that such a definition includes independent services providers, the self-employed and foreign individuals employed by foreign companies established in the territory of a member but excludes foreign individuals employed by domestic companies (See, for example, Nielson 2003, Chaudhuri et al. 2004).

However, the SAFAS has expressly carved out two types of measures from its scope: measures affecting access to the employment market of a member and measures regarding citizenship, residence, or employment on a permanent basis. The agreement also does not prevent members from regulating the entry of natural persons provided that regulations are not applied in such a manner as to nullify or impair the benefits accruing from specific commitments made by the members (Article 3).

Dispute settlement mechanism

Rules, rights, obligations, and commitments established in trade agreements are of limited value if they are not supported by an instrument capable of determining when they are being infringed upon and compelling parties to abide by them. However, compared to the GATS and other EIAs, the dispute settlement mechanism in the SAFAS, which has been adopted from the SAFTA Agreement, is weak. The SAFTA Agreement has provisions for lodging complaints, bilateral consultations, decisions by CoE and the right to appeal to the SAFTA Ministerial Council, with a time period prescribed for each process. However, the requirement of consensual decision-making in the SAARC may turn the whole dispute settlement mechanism into a farcical process. In addition, it does not cover investor-to-state disputes, which find a prominent position in other EIAs.

The SAFAS, modeled on the GATS, has adopted a very cautious approach to services liberalization. To start with, it is a positive development in the region, though very conservative in liberalizing trade compared to other EIAs among developing counties. Nonetheless, the negotiated schedules based on "requests and offers" would be a litmus test to assess the success of the agreement in liberalizing services.

Chapter 6

Conclusions and recommendations

This paper reviews the trends in services trade in South Asia, explores the potential for cooperation on services trade and suggests the architecture of services trade liberalization under the regional arrangement taking into account the level of commitments of South Asian countries in the WTO and the developments in the negotiations on the draft SAFAS.

The paper argues that if the dynamism of South Asian economies, in particular in the services sector, the role of the sector in the national economies, the differential comparative advantages among the countries of the region and the externalities to be generated by services sector cooperation are taken into consideration, regional cooperation on services will not only promote services trade in the region but also may help create complementarities among the economies as well. However, the modalities of liberalization of services trade should be unique and region specific, taking into account of the development needs of member countries, the institutional capacity to regulate the sectors and the distributional implications of benefits among the members.

There exists a positive relationship between economic growth and services liberalization as the latter removes the bottlenecks in infrastructural services, lowers prices in liberalized services, and improves the range and quality of services provided. An appropriately timed and sequenced liberalization of the services sector provides welfare gains by reducing, if not entirely eliminating, the wedge between domestic and foreign prices, as well as by permitting the rationalization of services activities along the lines of comparative advantage. In addition, there are certain dynamic gains from trade consequent upon additional competition, and the consumers would benefit from the availability of a broader product variety of specialized producer services as well as enhanced product quality.

In recognition of the role of services in international trade as well as in economic growth and the need for further liberalization, services have been included in the multilateral trade architecture of the WTO in the form of the GATS and services feature prominently in recently concluded EIAs. South Asian countries have also initiated negotiations on the SAFAS to broaden the coverage of the SAFTA Agreement.

The services sector is the largest productive sector in South Asia.

The services sector is the largest productive sector in all the SAARC economies (except Afghanistan) accounting for more than half of domestic output and an even larger share in economic growth. South Asian countries except Nepal have witnessed robust growth in trade in services, surpassing the rate of overall economic growth, during the last two decades, implying that the growth in services in South Asia is export driven. Services are attracting increasing amounts of FDI, and the region has emerged as an important source of FDI in recent years. Similarly, South Asia is major source of migrant workers and there has been a significant movement of workers within the region for providing services.

Resource endowment and comparative advantage of individual countries indicate existing and potential complementarities in services trade in the region. Regional integration in the services sector could enhance the dynamism of services by giving to region's services suppliers greater opportunities abroad and generating competition domestically to spur innovation. It may also help to improve or create complementarities in trade in goods. In addition to the economic rationale for closer cooperation in South Asia, non-economic factors such as the cultural, linguistic and geographic proximity between countries in South Asia may foster regional cooperation in services. It may also help to improve the region's regulatory, institutional and supply capacity regarding services.

Energy should be defined as a service under SAFAS.

South Asia is characterized by high asymmetries among countries in services output, services trade, technological development and the extent of trade liberalization measured by the level of multilateral commitments. Such asymmetries demand special and different treatment to the weaker countries in the process of trade liberalization, in addressing their trade and development needs as well as in developing their regulatory and supply capacities.

The SAFAS, which is under negotiation, modelled on the framework of the GATS, has incorporated almost all major provisions of the GATS. With the adoption of a "positive list" approach along with a "request and offer" modality in services liberalization, South Asian countries are treading cautiously on the path of regional trade liberalization. The agreement looks more conservative in trade liberalization than the EIAs among other developing countries.

Recommendations

Taking into account the needs of reducing barriers to regional participation, ensuring fair distribution of the gains from services trade liberalization, developing the regulatory and supply capacity of the weaker members, and enhancing the credibility of the trade regime, the following recommendations are made.

a. The general understanding on the principles and guidelines of the SAFAS for negotiation proposes has adopted The WTO Secretariat's Services Sectoral Classification List as a basis for the sectoral coverage of the sector specific commitments, but it has also opened the window for the addition of sectors/subsectors of significant interest for the countries of the region.

   In this context, given the fact that there will be increasing pressure of energy demand with economic growth in the region and there is a huge potential for hydroelectricity production in Nepal and Bhutan and natural gas production in Bangladesh, an important area for regional cooperation is trade in energy and related services, including transmission services. Therefore, it is suggested that energy be defined as a service for the purpose of the SAFAS, and included in the sectoral classification list.

b. One of the benefits of a trade agreement is that it encourages transparency in trade policy and enhances the credibility of the trade regime. However, the positive-list approach to trade liberalization allows members to undertake commitments at a level below the status quo, thereby creating "binding overhang".

   One argument in favour of allowing binding overhang in trade agreements is that countries with unilateral liberalization have yet to assess the full impact of liberal policies on the national economy as well as on specific sectors, and the risks associated with status quo binding would be high. Given the fact that all the

South Asian countries have been gradually embarking on a liberal economic regime by opening up goods and services since the last two decades and have not yet felt the need for substantially rolling back policies, the risks of undertaking commitments to bind unilateral liberalization at the regional level seem minimum. However, some flexibility should be provided on a case-by-case basis on specific sectors where high risks of status quo binding could be established.

c. Commercial presence of services providers in service-consuming countries is one of the most important modes of services trade in many service sector/subsectors. Therefore, many EIAs provide dual coverage through commercial presence and investment provisions at the horizontal level. As some of the countries of South Asia have been emerging as major sources of FDI, liberalization of investment only through commercial presence may not be sufficient to attract regional investment, especially when competing destinations are providing better protection and procedural facilities. In this context, incorporation of a chapter on investment assuring investment protection and simplification of procedures for investment would go a long way towards increasing intra-regional FDI flows.

Similarly, liberalization of the movement of unskilled and semi-skilled workforce, starting with select services categories, could be made a horizontal obligation. Such provisions would not only address the mismatch in the demand and supply in the labour market but also help ensure fair distribution of benefits of services liberalization among the member countries.

Liberalization of the movement of unskilled and semi-skilled workforce could be made a horizontal obligation.

d. The agreement recognizes the problems of LDCs and proposes special and differential treatment only in the liberalization process and technical assistance. Special and differential treatment is conspicuously missing in the "rule" areas in the draft agreement. Providing more favourable treatment to LDCs on the definitions "rules of origin" and "juridical person of other contracting parties" would help them to attract extra-regional FDI.

Endnotes

[1] Afghanistan joined SAARC in April 2007.

[2] The available information/data on services trade are from balance-of-payments (BOP) statistics which greatly underestimate the value of services trade flows. This is because BOP statistics provide only a partial picture of trade in services, only reflecting cross-border trade and consumption abroad, but ignoring the supply of services through the presence of juridical and natural persons.

[3] See also McGuire (2002), Lücke and Spinanger (2004) and WTO (2004).

[4] Existing database on services based on BOP accounts underestimates the actual trade flows in services as it does not capture all the modes of supply. Recent estimates by the WTO Secretariat underline the important role of Mode 3 for services trade. Trade through commercial presence represents 50 percent of total services trade and cross-border supply 35 percent. The role of the other two modes is much smaller: 10 percent to 15 percent for consumption abroad and only 1 percent to 2 percent for the presence of natural persons (Fink and Jansen 2007).

[5] The formula applied here is RCA = (Xik / Xiw) / (Xwk / Xw), where Xik is country i's world exports of service k, Xiwk is country i's exports of goods and services; Xwk is world exports of service k, and Xw is world exports of goods and services. If the estimated RCA index of a sector is found to be greater than one, then it is considered as globally competitive (Balassa 1965). The RCA index measures "revealed" comparative advantages rather than actual or potential comparative advantages, therefore it suffers from the limitations at the conceptual level. These limitations are further compounded in measuring the RCA index in services sectors by lack of reliable and detail statistics.

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