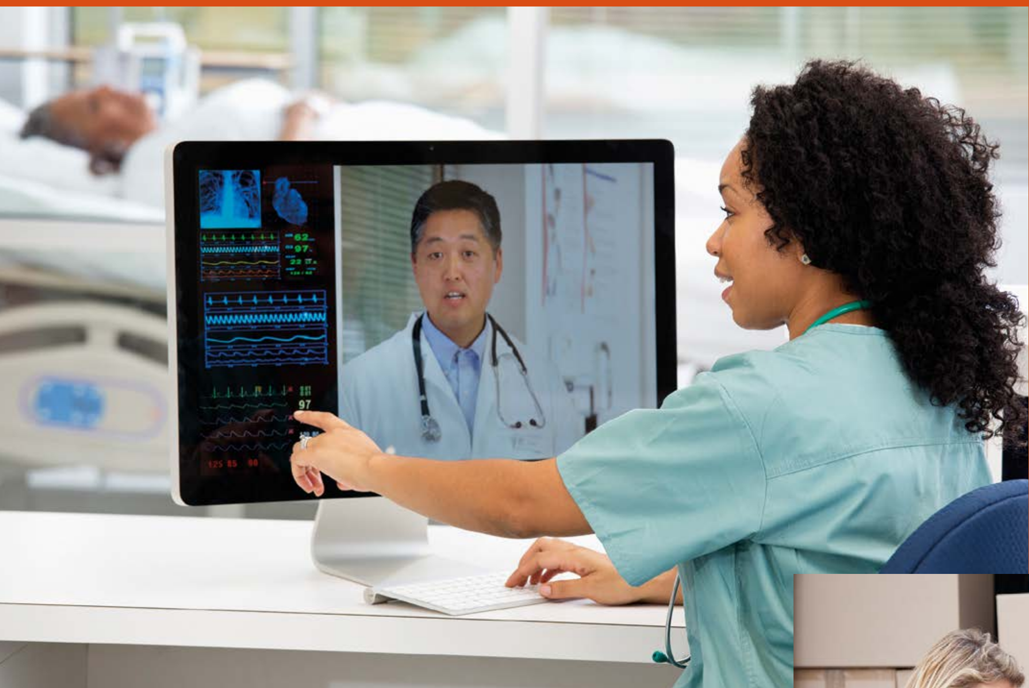
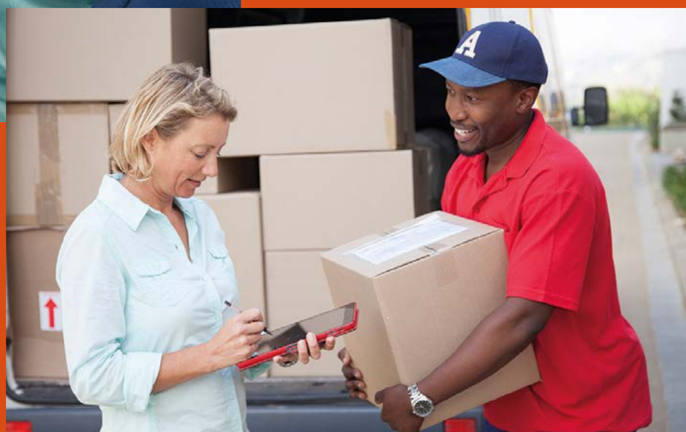
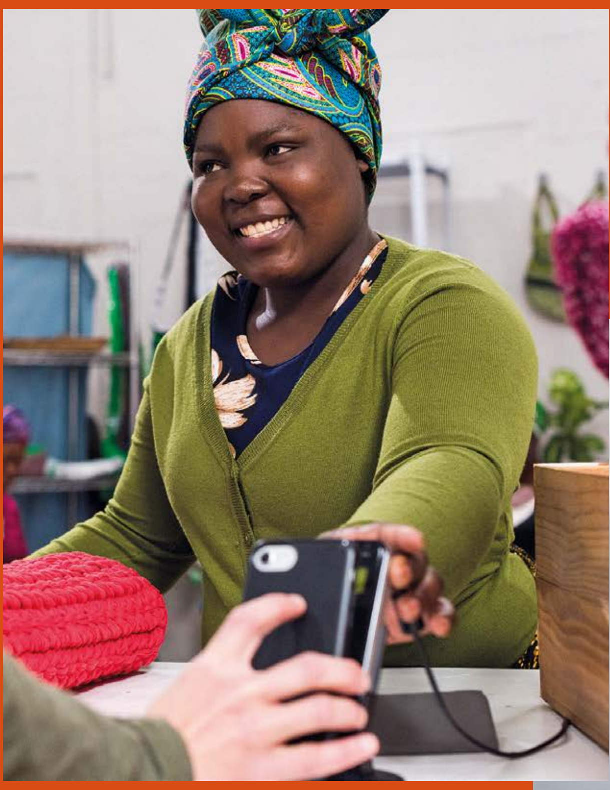
World Trade Organization

WORLD TRADE REPORT 2019

The future of services trade







What is the World Trade Report?

The World Trade Report is an annual publication that aims to deepen understanding about trends in trade, trade policy issues and the multilateral trading system.

What is the 2019 Report about?

The 2019 World Trade Report examines how trade in services is likely to evolve in response to some major trends, such as demographic changes and the impact of digital technologies.

Find out more

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Acknowledgements

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Disclaimer

Foreword by the WTO Director-General

Services are often largely overlooked in discussions on global trade, yet they account for the majority of trade in many developed economies and are growing rapidly in many developing economies as well. This is perhaps because services are less tangible and the issues surrounding services trade are often more complex. This report therefore sets out to demystify trade in services. It aims to shed new light on this essential part of global trade, provide a detailed picture of trade in services today and consider how it might evolve in the coming years, particularly as new technologies make some services increasingly tradeable.

The Report deepens our understanding in a number of ways, including through presenting new data. By looking more closely at services delivered by a company that has an office or subsidiary in a foreign country, we have found that trade in services is significantly larger than previously thought. In fact, when this “commercial presence” is accounted for, trade in services was actually worth US$ 13.3 trillion in 2017 – therefore accounting for a share of overall global trade 20 percentage points higher than traditionally estimated. On average services trade has grown 5.4 per cent per year since 2005, which is faster than trade in goods, at 4.6 per cent on average. Distribution services and financial services are the most traded services globally, accounting for almost one-fifth of trade in services each, followed by telecommunications, audio-visual and computer services, which together account for 13.2 per cent. Trade in other sectors, such as educational, health, and environmental services, although currently relatively small, is rising rapidly.

Developing countries’ share of global services trade has grown by more than 10 percentage points since 2005, reaching 25 per cent of world services exports and 34.4 per cent of world services imports in 2017. However, services trade is concentrated, with the same five developing economies ranking both as leading services exporters and importers. Together these five economies accounted for more than 50 per cent of developing countries’ services trade. Least-developed countries accounted for 0.3 per cent of world services exports and 0.9 per cent of world services imports in 2017, although this does represent an increase since 2005.

One key message from the report is that services trade is evolving fast. Digital technologies, demographic changes, rising per capita incomes and climate change will all act as disruptors, potentially reducing trade costs, creating shifts in demand, and creating new markets, for example in environmental services. Digital technologies are likely to have a particularly significant impact as they change the ways that companies do business, allowing them to access a global marketplace and creating new channels through which to deliver services which were once provided face-to-face.

Digital technologies can be a driver of inclusivity in services trade, by dramatically cutting costs and lowering barriers to entry. This is true for developing countries, and it is true for smaller businesses. Micro, small and medium-sized enterprises (MSMEs) that offer services are on average two years younger when they start exporting as compared to manufacturing MSMEs. New technologies have facilitated this faster access to international markets as MSMEs’ participation in services trade is frequently in digitizable services, such as professional and scientific activities. There is also a potential opportunity here to support women’s economic empowerment, as services play a prominent role in women’s employment. However, so far women are under-represented in the most traded service sectors. Groups of WTO members recently launched discussions on leveraging trade to support MSMEs and women’s economic empowerment. Services trade is clearly relevant in both cases.

Services exports support a huge number of jobs around the world, but there is tremendous untapped potential. A further expansion of services trade will be reliant on a number of factors. The quality of institutions in the importing country is particularly significant. Driving new services trade reforms through trade agreements is also important, although progress in this area has often proved difficult. WTO members continue to pursue multilateral negotiations on services trade, and a group of members recently launched an initiative towards greater cooperation on domestic regulation of services. How these efforts – and those in other fora, such as regional trade agreements – evolve, only time will tell.

What is clear is that services represent a highly significant part of global trade – one which will be increasingly important in determining economic growth, development and job creation around the world. This report is a crucial step in increasing our understanding of this vitally important part of global trade – and therefore I want to thank the authors and contributors for their excellent work. Building on the contribution made by this report, the WTO will continue to improve its services data and is launching a biannual Services Trade Barometer to provide a real-time indicator of the strength of services trade globally. It is time that services took its rightful place front and centre in the global trade debate.

Roberto Azevêdo
Director-General

Key facts and findings

- Trade in services has expanded faster than trade in goods between 2005 and 2017, at 5.4 per cent per year on average.
- When commercial presence in another country (mode 3) is accounted for, trade in services was worth US$ 13.3 trillion in 2017.
- Commercial presence is the dominant mode of supply for trading services globally, representing almost 60 per cent of trade in services in 2017.
- Distribution and financial services are the services most traded globally, each accounting for almost one-fifth of trade in services. The share of other services, such as education, health or environmental services, is rising rapidly, but currently accounts for a negligible proportion of overall trade in services.
- The contribution of developing economies to trade in services grew by more than 10 percentage points between 2005 and 2017, but is mainly concentrated in five economies. The share of least-developed countries remains small, although it has increased significantly since 2005.
- In developing economies, micro, small and medium-sized enterprises trading in services start exporting more quickly than manufacturing firms. However, they export less than 5 per cent of total sales, a share three times lower than large services firms.
- Firms owned by women are under-represented in services exports, although less so than in manufacturing.
- Services value-added accounts for close to half of the value of international goods and services trade.
- Trade in services creates welfare gains for society through a more efficient allocation of resources, greater economies of scale, and an increase in the variety of services on offer.
- In addition, some service sectors, such as infrastructural services, play a critical role in the functioning of the entire economy while others affect the productivity of the economy's factors of production.
- An important avenue through which services trade benefits societies is the improvement in firms' competitiveness, both in the services and manufacturing sectors.
- Because services providers must often be present in the area where the service is delivered, the quality of institutions in importing countries is of greater importance in services trade than in goods trade.
- A large number of jobs is supported by services exports, but the effect of services trade on the level and structure of employment has so far been minimal. Services trade may help to reduce economic inequality for women and for micro, small and medium-sized enterprises.
- Trade costs in services are almost double those in goods, but they fell by 9 per cent between 2000 and 2017 thanks to the spread of digital technologies, the lowering of policy barriers, and investment in infrastructure.
- Four major trends will affect services trade in the future: digital technologies, demographic changes, rising incomes, and the impact of climate change. These trends will create new types of services trade, affect the demand for services, and disrupt trade in some services while creating new markets in areas such as environmental services.
- According to the WTO Global Trade Model, the share in global trade of the services sector could increase by 50 per cent by 2040. If developing countries are able to adopt digital technologies, their share in global services trade could increase by about 15 per cent.
- Despite the reforms that most economies have undertaken over the past few decades, trade in services remains subject to higher barriers than trade in goods.
- Driving new services trade reforms via trade agreements has proven difficult.
- Accompanying market-opening negotiations with greater international cooperation focused on domestic regulatory measures may be one way to harness the potential of services trade.

Executive summary

A. Introduction

Services have become the backbone of the global economy and the most dynamic component of international trade.

Trade in services has been expanding rapidly, at a faster pace than trade in goods since 2011. Services currently account for around three quarters of GDP in developed economies, up from 40 per cent in 1950, and many developing economies are becoming increasingly services-based. In some cases, this is occurring even more rapidly than in developed economies.

Technology is making it easier to trade services.

Much services trade until recently required producers and consumers to be in physical proximity. But in the current services economy, it is becoming significantly easier to trade in services, thanks in large part to digitalization. The growing cross-border tradability of services is opening new opportunities for national economies and individuals.

Fulfilling the potential offered by the internationalization of services requires finding new pathways to advance international trade cooperation.

While technology plays an instrumental role in expanding services trade, it is not sufficient. Various obstacles continue to hinder trade in services. Finding new ways to overcome these obstacles may be necessary if governments are to realize the full potential offered by the growing internationalization of services.

B. Services trade in numbers

World trade in services has been growing faster than trade in goods, reaching US$ 13.3 trillion in 2017.

Traditional statistics on trade in services do not cover all four of the modes of services supply, as defined by the General Agreement on Trade in Services (GATS). However, a new WTO experimental dataset includes GATS mode 3 – commercial presence in another country – for the first time, thereby capturing the total value of services trade. Using these new estimates, trade in services was worth US$ 13.3 trillion in 2017. Services trade grew 5.4 per cent annually on average from 2005 to 2017, faster than goods trade.

Distribution and financial services are the most traded services globally.

Distribution and financial services each account for almost one-fifth of trade in services, while trade in computer services and research and development have recorded the most rapid average annual growth from 2005 to 2017 (above 10 per cent). Some services, such as education, health or environmental services, account for a negligible share of trade at present but are rising rapidly.

Commercial presence (GATS mode 3) is the dominant mode for trading services globally.

Commercial presence, i.e. the supply of services through foreign affiliates (GATS mode 3) accounted for 58.9 per cent of services trade in 2017, followed by cross-border services transactions (mode 1), at close to 30 per cent. Commercial presence represents an even more important share of trade in the finance and distribution sectors. However, increased digitalization is reshaping business models, opening more possibilities for cross-border supply in these sectors too.

Developing economies have increased their share in services trade, albeit unevenly; the share of least-developed countries remains small, but has increased significantly since 2005.

The share of world services trade by developing economies has grown by more than 10 percentage points since 2005, reaching 25 per cent of world services exports and 34.4 per cent of world services imports in 2017. However, services trade is very concentrated, with the same five developing economies ranking both as leading services exporters and importers, accounting together for more than 50 per cent of the developing group's services trade in 2017. Least-developed countries accounted for 0.3 per cent of world services exports and 0.9 per cent of world services imports in 2017. While these shares are small, they are significantly higher than in 2005.

The participation of micro, small and medium-sized enterprises (MSMEs) in services trade has been facilitated by new technologies.

In developing economies, MSMEs operating in the services sector are less internationalized than MSMEs operating in manufacturing. The trade participation of services-based MSMEs in developed economies varies across countries. However, starting to export is easier in the services sector: services-based MSMEs are on average two years younger than manufacturing-based MSMEs when they start exporting. Technological progress and the spread of the internet appear to have played a key role in giving services-based MSMEs faster access to international markets. The type of services trade in which MSMEs frequently participate is digitizable services, such as professional and scientific activities.

There is much potential for women to benefit from services trade, but so far they are under-represented in the most traded services sectors.

Services have played a prominent role in steadily increasing women's participation in the workforce. However, except for wholesale and retail trade, women's employment is concentrated in the least traded sectors, such as education, health and social services. Firms owned by women are also underrepresented in services exports, although less so than in manufacturing.

Services represent an important source of value-added in total trade.

Measuring the role of services in international trade has become more complex as global value chains and technological change have blurred the distinction between services and goods activities. Statistics based on trade in value-added capture the importance of services as inputs to all sectors in the economy, revealing that services play a bigger role in international trade than gross statistics suggest. Services value-added accounts for close to half of the value of international goods and services trade.

C. Why services trade matters

Trade in services can help economies achieve more rapid growth, enhance domestic firms' competitiveness, and promote inclusiveness in terms of skills, gender and the location of economic activity.

As with trade in goods, trade in services creates welfare gains for society. Trade in services promotes a more efficient allocation of resources and greater economies of scale. It can lead to an increase in the variety of services available to consumers and producers, and it can set in motion processes by which the more productive services firms can expand and grow.

Beyond these usual sources of gains, some services sectors have special or unique features that may amplify how an economy can benefit from trade in services. For example, transport, telecommunications, finance, and water and electricity distribution, generally known as infrastructural or producer services, play critical roles in the functioning of the entire economy. Other services sectors have an outsized impact on factors of production, like labour. For example, the productivity of an economy's labour force depends on how educated, skilled and healthy it is, attributes which hinge crucially on the quality of that economy's educational and health systems.

Allowing greater access to foreign services is one way to improve efficiency, with potentially large payoffs for the economy.

The available empirical evidence from the literature shows that increased openness in a number of economies and in sectors such as financial services, telecommunications, electricity distribution, transport and healthcare have led to a variety of positive outcomes – better quality services at a lower cost, greater efficiency, and faster GDP growth rates. The survey of the empirical evidence included in Section C is complemented with country case studies of successful developmental outcomes as a result of an expansion of trade in services. These studies show that trade in services can have a significant impact on employment, wages and economic growth.

Increased trade in services can affect the welfare of the average consumer.

The report shows the meaningful contribution of trade in services to the economic welfare of many economies. The computable general equilibrium (CGE) modelling literature suggests that welfare gains from opening up trade in services range between 2 and 7 per cent. For the period 2000 to 2014, one method suggests that trade in services led to an average 6.3 per cent increase in GDP per capita for some 148 economies, with some of the biggest gains in developing and least-developed countries.

One important way in which services trade benefits economies is the improvement in firms' competitiveness.

An increase in firms' competitiveness manifests itself in three ways. Firstly, the competition engendered by services trade increases the productivity of services firms. A second and indirect way is by increasing the productivity of manufacturing firms and other services firms that employ services as production inputs. Finally, product differentiation also helps to increase competitiveness, for instance by bundling the provision of services with a manufactured product.

The quality of institutions in the importing country is of greater importance to services trade than to goods trade.

The primary reason for the amplified role of institutions in the importing country is that services providers must often be present in the area where the service is delivered; this consideration is of less importance in goods trade. Consequently, the quality of local institutions affects a services exporter's decision as to whether or not to operate in a particular economy, and impacts the gains from trade if this decision is made.

The growing importance of services shows itself not only in trade statistics but also in labour market statistics.

As services trade has come to be a major part of the export mix of various economies, a large number of jobs is supported by services exports. For instance, the information and communications technology sector in India employs around 3.5 million workers.

However, the effect of services trade on the level and structure of employment has been small so far.

Most evidence suggests that total employment and average wages have not been significantly affected by services trade, although some studies report positive effects. In contrast, services trade has affected the composition of the workforce, with several studies suggesting that high-skilled workers in cities tend to be the main beneficiaries in both developed and developing countries. Nevertheless, these effects have been quantitatively small.

Services trade can help to reduce economic inequality.

Services trade may also benefit women in the labour market, as services sectors are more balanced in terms of gender than manufacturing or mining. Services may also help to level the playing field for micro, small and medium-sized enterprises (MSMEs), as services exhibit smaller fixed costs of production. For instance, relatively lower physical investments necessary to run a business in services imply that a reduced access to finance is less limiting to MSMEs in the services sector than to MSMEs in manufacturing. Through these channels, services trade can contribute to reducing inequalities.

D. Services trade in the future

Predicting how services trade is likely to evolve in the future is not an easy task.

Various factors affect how trade patterns may change. Technology, factors of production and consumer preferences are key drivers of trade. In addition, both firms and individuals may leverage comparative advantage of the host country if they are trading services through a commercial presence abroad (GATS mode 3) or through the temporary movement abroad (GATS mode 4).

Trade costs are key to determining whether an economy trades and how much it trades.

This report uses a novel approach to estimate trade costs and breaks them down into their components: information and transaction costs, governance quality, trade policy and regulatory differences, and technology and transport costs.

Trade costs in services are almost double those in goods, but they fell by 9 per cent between 2000 and 2017.

Trade in services has traditionally faced higher costs compared to trade in goods, largely due to the "proximity burden" of services trade (i.e. the necessity for suppliers and consumers of services to be in close physical contact), and of more complex policy regimes than those applied to the goods trade. Declining trade costs are allowing more services to be traded through cross-border supply (GATS mode 1), in particular, a trend that can be particularly benefitting developing countries and MSMEs.

Several factors have contributed to the fall in services trade costs.

Technology is one of the factors that has led to a decline in trade costs in services. A key effect is that global exports of services enabled by information and communications technology have more than doubled between 2005 and 2018. A second factor is policy reforms that, on average, have reduced barriers, although new trade restrictions in some sectors, especially in digitally-enabled services, have emerged. The third factor is investment in physical and digital infrastructures and policies to enhance competition, including foreign participation, which has helped to bring down transport costs and increase connectivity.

Digital technologies will affect services trade even further in the future.

First, by enabling cross-border trade for services that have traditionally needed face-to-face interaction, digital technologies are likely to reduce the cost of trading in services. Second, digital technologies will blur the distinction between goods and services activities. Third, they will allow firms to reach larger numbers of digitally connected customers across the globe and to facilitate the outsourcing of activities. These trends will increase the importance of data flows, intellectual property and investment in digital infrastructure.

Demographic changes will play a key role in affecting the composition of the future demand for services and the patterns of specialization.

A population's age structure is a key factor in determining the composition of demand for services and patterns of specialization: an ageing population in developed countries will demand more health services and a growing young population in developing countries will demand education and digital services. Trade in services will be key to satisfying these demands. Digital technologies may facilitate the imports of education services into developing countries, with potentially positive development effects.

Demographic changes will increase the demand for online services.

Millennials (those born between 1980 and 1996) and Generation Z (those born between 1997 and 2012) represent an increasing share of the world's population. These two groups currently constitute more than 50 per cent of major users of social media platforms, and spend more than two and a half hours per day on social media, on average, compared to one hour a day for Baby Boomers (those born between 1945 and 1964). This demand is providing new opportunities, especially for certain types of services providers, such as creative industries in developing countries.

Convergence in incomes per capita between developed and developing countries will change patterns of trade in services.

As the income of a country grows, richer consumers spend increasingly larger amounts on skills-intensive services, such as financial and insurance services, and richer countries tend to specialize in the production of these services. Therefore, if countries converge in income, a larger number of countries will participate in services trade.

Climate change will modify the nature of some services sectors.

Climate change is likely to disrupt some services and their trade. In tourism services, climate change is likely to make some destinations less appealing to tourists or more vulnerable to natural disasters. In terms of transportation, climate change is likely to disrupt some traditional routes, and may open new ones. For example, extreme weather conditions may lead to more frequent port closures, but warmer winters could reduce the amount of sea ice in many important shipping lanes, extending the shipping season. However, under the pressure from consumers, services industries are also adapting to become more environmentally friendly; for example, there is growing demand for ecotourism, especially from the Millennial generation.

Climate change will also increase the demand for trade in environmental services.

The market for environmental services is expected to grow significantly in the future (for example, project consultancy services for the construction of wind power systems, or the transportation and installation of materials required for its construction) as populations seek to adapt to and mitigate climate change.

The share of services in world trade is likely to grow by 50 per cent by 2040.

In order to get a sense of the potential quantitative impact of these major trends on services trade, this report uses the WTO CGE model and runs a number of simulations. It examines the combined impact of three trends: (i) generally lower services trade costs due to digital technological innovation; (ii) a reduced need for face-to-face interaction in services trade; and (iii) a lowering of the policy barriers to services trade. The simulations project that, under these scenarios, the services sector share of global trade will grow by 50 per cent by 2040. If developing countries are able to adopt digital technologies, their share in global services trade will increase by about 15 per cent.

E. What role for international cooperation on services trade policy?

Policy barriers to trade in services are much more complex than in goods trade.

Policy barriers in services trade are essentially regulatory in nature, rather than tariffs, as in goods trade. At the same time, in view of the pervasiveness of market failures in many services markets, most services regulation does not aim to restrict trade, but rather to pursue public policy objectives. For instance, education and training requirements are imposed on service providers to ensure their competence in instances where the complexity of the service being supplied makes it very difficult for consumers to appreciate quality or safety prior to consumption (i.e. a market failure due to “asymmetric information”).

Over the past three to four decades, most economies have embarked on far-reaching reforms targeted at opening up their services markets to competition, including from foreign suppliers.

Most reforms were not propelled by trade negotiations, with the notable exception of WTO accessions, but were undertaken by governments in an autonomous manner. Those transformations proved to be a driving force behind greater international cooperation in the services arena, which culminated, in 1995, in the entry into force of the GATS. The GATS provides rules-based, transparent and predictable conditions under which services firms can operate.

Opening services markets unilaterally does not allow economies to reap all the potential benefits.

First, there is a risk of policy reversals. Second, several trade barriers have proven impossible to remove based on purely domestic processes. Third, regulations set by countries independently of one another are likely to result in heterogeneity, and thereby to be a source of unintended trade costs for services suppliers. International cooperation on services trade policy enables countries to secure their unilateral reforms, and those of their trading partners, more fully, by binding them in trade agreements, thereby guaranteeing that global services markets will remain open, and may also contribute to regulatory convergence.

Economies have collaborated, both in the WTO and in regional trade agreements, on lowering services trade barriers and on regulatory measures.

Collaboration has not been fully exploited to deliver on its potential, however, as testified by the overall low levels of market openings committed in the WTO (except on the part of economies that acceded to the WTO after its creation) compared to the actual level of openness of services regimes. The generally modest state of WTO commitments stands in stark contrast to the breadth of the levels of access bound in regional trade agreements. Regional trade agreements have also made deeper inroads into establishing disciplines, in particular on GATS domestic regulation, services e-commerce, telecommunications services and the movement of individuals supplying services (GATS mode 4).

However, multilateral as well as bilateral/regional services trade agreements have so far found it difficult to drive services trade reforms.

One likely explanation for the difficulty in driving services reforms is the pervasive role that regulation plays in services markets and the essential role that well-designed regulatory policies and appropriate domestic regulation play in delivering welfare-enhancing trade-opening. Nevertheless, the findings of this report point to a number of factors that might increasingly motivate governments not only to open up their services markets, but also to seek mutual openings on the part of their trading partners.

Accompanying market opening negotiations with greater international cooperation focused on domestic regulatory measures may be one avenue to harness the potential of services trade.

In most services sectors, market openings need to be supported and enhanced by adequate domestic regulatory measures, while strengthened regulatory measures and governance are a necessary condition for trade-openings to deliver on their potential economic benefits. Technical assistance and capacity-building would be crucial in this regard, enabling countries to respond to the challenges and opportunities brought about by technology and the ensuing changes in services trade patterns.

On-going deliberations in the WTO point to the areas where the members concerned feel that international cooperation is worth pursuing further.

Current services discussions in the WTO are focused mostly on regulatory aspects, and specifically on GATS domestic regulation, the services trade-related aspects of electronic commerce and the relevant elements of investment facilitation. The services component of the WTO Work Programme on Electronic Commerce remains active, particularly with respect to sharing of information and experiences. However, much of the discussion on the three topics is taking place in plurilateral groups of 70+ members, also known as Joint Statement Initiatives, in meetings open to all members. These Initiatives do not necessarily reflect the issues, or the only issues, where deeper collaboration would be desirable, but rather demonstrate a meeting of minds amongst the members concerned that WTO discussions on these topics can be valuable.