UNIT 3 INTERNATIONAL TRADE IN SERVICES, THE WTO, AND INDIA

Objectives

After studying this unit you should be able:

- to outline recent trends in service sector trade and investment flows with particular focus on India's prospects in this sector,
- to provide an overview of the GATS and recent developments in the GATS negotiations, and
- to discusses India's broad sectoral as well as cross-sectoral negotiating strategy in the GATS negotiations and associated domestic reform issues that need to be addressed if India is to realize its potential in services.

Structure

3.1 INTRODUCTION

The service sector today encompasses a wide range of areas and activities. It extends beyond the traditional areas of finance, insurance, transport, communication, and tourism to new and dynamic areas such as software and information technology services, environmental, and consultancy services. Over the past two decades, the service sector has expanded rapidly and has come to play an increasingly important role in national economies and in the international economy. Given the growing role of services in the Indian economy and India's emergence as a global player in services like software and health, globalization of services presents new opportunities and challenges for India. The WTO negotiations on services under the General Agreement on Trade in Services or GATS is thus of great significance as it provides India with a multilateral negotiating forum to address its trade and investment interests and concerns in the service sector.

3.2 GLOBAL TRENDS IN SERVICES

Around the world, there has been a structural shift away from primary activities and manufacturing towards services. Services today account for over 70 per cent of production and employment in many advanced countries with producer services such as transport, communication, and distribution alone accounting for 20 per cent of GDP. In developing countries, services have similarly risen in importance, accounting for 40 per cent or more of total output in some countries and also constituting a significant share of total employment.

The growth in service sector output and employment has also been accompanied by increased internationalization of service sector transactions, driven by rapid advances in information and communication technology, the growing presence of multinational corporations and outsourcing of activities, and deregulation of services. According to the WTO, the value of commercial services exports grew sevenfold between 1980 and 1999, from $ 358 billion in 1980 to US $ 933 billion in 1990 to $1.4 trillion in 2000 while trade in merchandise goods recorded a fivefold increase over this same period. Between 1990-2000, world exports of commercial services kept pace with the growth in merchandise exports, at an average rate of 6 percent per year.[1,2] FDI in services has also expanded considerably in the past decade. By the end of the 1990s, FDI in services constituted about 40 per cent of the global stock of FDI. It consistently exceeded FDI in manufacturing during the 1990s. Overall, services trade represents about 20 per cent of global trade flows.[3] Even this latter estimate is likely to underestimate the true value of services trade as it excludes the value of cross-border intrafirm services transactions, which have been rising rapidly in recent years.

Activity 1

Select any one service out of Financial Services, Hospitality Services, Telecommunication Services or Healthcare Services and find out the trends of growth in that sector. (You may refer to business magazines, Internet or any other Source).

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Characteristics of Services Trade[4]

Services have traditionally been viewed as being nontradable, intangible, and nonstorable. However, recent trends clearly indicate that services are tradable in various forms and that services trade is concentrated among certain countries, sectors, and activities. The following discussion highlights some of the main characteristics of services trade in terms of its modes of delivery, geographic, and sectoral profile.

A) Four Modes of Service Delivery

Services can be traded through various forms and modes of delivery, including transborder data and information flows and movement of capital, labour, consumers, and goods embodying services. The GATS conceives of services as being traded through four modes of supply, namely: cross border supply (mode 1) consumption abroad; (mode 2) commercial presence; (mode 3) and; movement of natural persons (mode 4).

i) Cross-border Trade: Mode 1

Cross-border trade is similar to the traditional notion of goods trade. In this mode, the service is embodied in a transportable media such as paper documents, computer diskettes, or digital form, and is transmitted via telecom links. In the balance of payments (BoP), mode 1 is represented mainly by services minus travel and government services, although this is not fully accurate due to overlap with other modes of services trade. Mode 1 based services trade has grown rapidly in recent years, in large part due to advancements in information technology and increased scope for transmission of information and transborder data flows. It grew faster than world GDP between 1985 and 1997. By 1997, cross border trade in services accounted for 3.1 per cent of world GDP and 13 percent of total world exports of goods and services. In value terms, it increased threefold during this period, from US $ 270 billion in 1985 to $890 billion in 1997. Even for countries with modest service exports, if one looks at indicators of relative specialization (ratio of mode 1 based services trade to total exports of goods and services), cross-border services trade features importantly. Given the growing potential for services trade via means such as e-commerce, telemedicine, and e-banking, mode 1 based services trade is likely to expand significantly in future.

ii) Consumption Abroad: Mode 2

Consumption abroad refers to services trade where the consumer of the service moves to the country that produces the service, as in the case of tourism. Mode 2 refers mainly to travel services, as given in the BoP, although there is likely to be some underestimation due to reasons such as e-commerce which make it difficult to separate out modes 1 and 2. In 1997, exports of travel services have increased faster than for mode 1, rising from US $120 billion in 1985 to US $ 430 billion, or 20 per cent of total services trade. Consumption abroad as measured by the travel services component of the BoP accounted for 1.5 per cent of world GDP and 6.3 per cent of global exports of goods and services.

iii) Commercial Presence: Mode 3

Commercial presence is when services trade involves the establishment of service operations in the consuming country as in the case of setting up bank branch offices or law offices overseas. It is analogous to foreign direct investment. Mode 3 covers juridical persons and legal entities that share characteristics of corporations, joint ventures, partnerships, and representative offices and branches. In existing BoP statistics, commercial presence is recorded in the form of data on international FDI flows and income stocks in financial accounts.

However, FDI information alone does not provide an accurate picture of the total value of operations by service firms overseas. For instance, if a foreign affiliate is treated as a resident in the host country, the value of its services is not recorded in the BoP. An important supplementary measure of mode 3 based services trade is provided by the Foreign Affiliates Trade in Services (FATS) statistics. The FATS collects both inward and outward information on commercial presence through indicators such as sales, employment, and value added of majority owned enterprises located in foreign countries. Inward FATS statistics deal with the value of services provided by foreign affiliates established in the home country while outward FATS statistics deal with the value of services provided by foreign affiliates owned abroad by residents of the home country[5]. Gross output of foreign affiliates for 1997 is estimated at $ 820 billion, or about 38 per cent of total services trade. The value of production by foreign affiliates constituted 2.9 per cent of world GDP and 12.1 per cent of world exports of goods and services.

iv) Movement of Natural Persons: Mode 4

This mode involves the delivery of the service through the temporary cross-border movement of service suppliers as in the case of software and construction services. There are two categories of such service providers, the self-employed and employees. The self employed are individual foreign service suppliers who go overseas on their own to supply services. Employees are foreign natural persons employed by service suppliers to provide services, where the employer could be from the home or third countries. At present, mode 4 based services trade is captured in the BoP accounts under compensation for those established abroad. By this measure, world income from the compensation of employees stood at $ 30 billion in 1997, or 1 per cent of total services trade and a meagre 0.1 percent of world GDP. These values are small relative to those associated with other modes of supply. Mode 4 based services trade is less than 4 per cent of the value of cross border trade in services.

While the relative insignificance of mode 4 based trade reflects the smaller volume of trade via movement of natural persons, due to various restrictions on cross-border labour mobility, it is also due to problems in capturing the extent of such trade. Measures of mode 4-based services trade are the most problematic. The compensation category does not capture compensation to service providers who are temporarily abroad for more than one year, since by the BoP definition, such persons are defined as residents of the host country. This lends a downward bias to the estimates.

Activity 2

Classify the following services, as per the classification given above:

- Financial Services

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- Hospitality Services

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- Telecommunication Services

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- Healthcare Services

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B) Geographic Profile

Services trade is highly concentrated among a few developed countries and a few regions of the world. Developed countries account for 70 per cent or more of global services trade and this predominance holds across all four modes of supply. [6]Developing countries are relatively smaller players in services trade than in merchandise trade. Services trade between developed and developing countries occurs mostly in the context of modes 3 and 4 which relate to cross border flows of capital and labour, respectively. The latter reflects the importance of capital and labour endowments in determining comparative advantage and the direction of trade and factor flows in services.

C) Sectoral Composition

Trade data on commercial services is collected in the BoP for three broad categories of services, namely. travel, transport, and other services. Based on available BoP statistics, transportation services account for about one quarter of total services trade, travel services for about one third, and other commercial services for the remaining 40 per cent. A look at the relative growth performance of the three sub sectors further indicates a shift in composition towards “other” services and away from transport and travel services, with the former category recording relatively higher annual growth rates in recent years. Within the miscellaneous “other” services category, other business services, which include a variety of professional services such as advertising, legal, accountancy, technical, repair and maintenance, and other supporting services (many of which go unreported) account for 50 per cent of trade. Individual activities such as communication, finance, and insurance occupy a much smaller share of trade in this category.

D) Data Issues in Services

While existing data clearly indicate the predominance of certain countries, subsectors, and forms of delivery in services trade, it is important to note that service sector data are subject to many shortcomings due to statistical, conceptual, and methodological difficulties in measuring this sector. There are major discrepancies between national income accounts and balance of payments statistics for the service sector. Such measurement problems and the resulting lack of comprehensive and accurate data on services are a major constraint to analysing services trade and investment flows.

3.3 INDIA'S OPPORTUNITIES AND CONSTRAINTS IN THE SERVICE SECTOR

Over the past two decades, the service sector has replaced agriculture as the dominant sector in India. The service sector's share in India's GDP has risen from 36 per cent in 1980-81 to around 56 percent in 2002-03 while the share of the primary sector has fallen over this period, from 38 per cent to 24 per cent. The share of manufacturing has remained stagnant at about 22 per cent of GDP.[7] This aspect has been discussed in detail in the previous unit.

India has witnessed considerable growth in service sector trade, particularly during 1990s. Net inflows of invisibles stood at $16 billion in 2002-03. Net invisibles receipts from non-factor services were an estimated $ 6 billion and net receipts from software services stood at $8.8 billion in 2002-03.[8] The service sector accounts for about one quarter of total trade in goods and services, with services exports and imports each constituting about 25 per cent of total exports and total imports, respectively. Close to 80 per cent of this trade is in transport, travel, and other business services.[9] The most notable expansion has been in the software services sector. Exports of software services have risen from a few hundred million US dollars in the early 1980s to around $ 9.6 billion in 2003-03 and are expected to reach $ 50 billion by 2008.[10] Today, India's presence as well as its future potential in the global software industry is well recognized, at home and abroad. In several other areas such as construction and engineering services, health services, telecommunications, and financial services, there is growing recognition in India and abroad of the country's trade and investment potential.

Activity 3

Identify those Services in India which have grown during the last 4-5 years. Also think about the possible reasons for growth.

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Characteristics of India's Service Sector Trade

Trade statistics for India's service sector are highly aggregate in nature. BoP data are available for only a few services, including, travel, transport, insurance, and other business services including software services. Several categories, including important sectors such as communication, construction, finance, computer and information services, and personal, cultural, and recreational services, are not covered in India's BoP statistics or are subsumed within broader categories, reflecting the problems in collecting information on specific service activities. Tables 3.1 show trends in the value of India's service sector exports and imports.

Table 3.1: India's Services Trade (US $ million)

Items		1990-91	1995-96	2000-01	2002-03
1)	**Travel, net**	1,064	1,546	294	-438
	Receipts	1,456	2,713	3,168	3,029
	Payments	392	1,167	2,874	3,467
2)	**Transportation, net**	-110	-158	-1,257	- 3
	Receipts	983	2,011	1,913	2,544
	Payments	1,093	2,169	3,170	2,547
3)	**Insurance, net**	23	36	135	57
	Receipts	111	179	257	371
	Payments	88	143	122	314
4)	**Miscellaneous, net**	161	-1,405	2,990	6,511
	Receipts	1,986	2,411	12,875	18,735
	Payments	1,825	3,846	9,885	12,224
	Of Which :				
	Software Services, net	N.A.	N.A.	5,750	8,863
	Receipts	N.A.	N.A.	6,341	9,600
	Payments	N.A.	N.A.	591	737

Source: RBI Annual Reports (www.rbi.org)

The data clearly indicate that India's services trade has undergone a major expansion during the last few years. This expansion, however, has not been uniform across subsectors. The composition of India's services trade has shifted away from traditional service activities such as travel and transport towards other services, and in particular, towards other business services. The share of transport and travel services in total services trade has declined considerably. This structural change in India's services trade mirrors the structural changes in global services trade where there has been a similar shift from traditional sectors towards business and professional services. The latter shift is due in large part to the growth in information technology and software services with their enabling impact on many business activities.

However, as noted earlier, the BoP statistics should be interpreted with caution. The categories are very broad and heterogeneous. There is considerable overlap across activities and sectors and many services may be altogether excluded from India's BoP statistics for lack of information and systematic compilation of data. The BoP figures also exclude FDI in India's service sector, which is likely to result in under-representation of subsectors such as communications, transport, and financial services where FDI plays a greater role.

Using the mode-wise classification of services trade, all four GATS modes appear to be important in India's service trade. Consumption abroad or mode 2 is an important mode of supply given the significant share of travel services in both services exports and imports. Cross border supply or mode 1 is also important given the recent growth in business process outsourcing and back office activities in India and the growing scope to deliver services cross border through electronic and telephonic means. India also relies heavily on movement of natural persons for its services exports, reflecting its comparative advantage in exporting labour-intensive services. The importance of cross border labour mobility is evident from the growing role of other business services in total services trade, since many of these professional services require movement of professional service providers to the overseas market. The predominant subsector within this segment is software services which relies on cross border movement of software service providers to provide on-site and customized software services in overseas markets. It is difficult, however, to gauge the significance of this mode in India's services trade since data on compensation of employees and on transfers and remittances and the usual proxy measures for mode 4 are not available separately for service activities and because there is no separation of temporary from permanent movement of labour. Nevertheless, if private transfers and remittances are any indicator of the importance of revenues from cross border labour mobility, inflows amounted to a significant $12 billion in 2001-02 and $14.8 billion in 2002-03 while outflows have been very small in comparison at $ 67 million and $ 367 million respectively. Through the 1990s, India has been a net recipient of labour income as indicated by positive net transfers, indicating the role of cross-border labour mobility in India's services exports.

On the import side, the main mode of interest to India is commercial presence, or mode 4. Data available from the RBI's Annual Report indicate that services receive a large share of FDI in the country. For instance, between August 1991 and upto July 2000, FDI inflows totalled $16.5 billion in the telecommunications sector, $10.7 billion in the financial sector, and $ 6 billion the transport sector. Within services, financial and telecommunications services account for the bulk of FDI. Given impending deregulation and liberalization of many state monopoly sectors such as insurance, telecommunications, and air transport, and relaxation of foreign equity norms in view of the need for major capital investments in many areas, the role of FDI in India's services trade is likely to grow.

Constraints to India's Trade in Services

There are many policy-related, infrastructural, and other constraints to India's trade in services. On the export front, India's exports of professional services are adversely affected by external barriers such as immigration and labour market regulations, recognition and licensing provisions, and discriminatory treatment with respect to taxes, subsidies, and government procurement policies. For instance, Indian professionals are subject to entry quotas, cumbersome administrative procedures for issuance of visas and work permits, wage parity requirements, economic needs tests, and nationality and residency conditions. In professions like health, architecture, and accountancy services, credentials of Indian professionals are not recognized in major countries due to the absence of mutual recognition agreements, which either requires them to undergo further training in the host country or restricts their scope of practice. Deficiencies in domestic standards of training and infrastructure and quality of manpower also affect India's' exports of professional services.

On the import front, there are again numerous domestic regulatory barriers. For instance, India's imports in key infrastructure services such as energy, banking, insurance, and telecommunications are constrained by restrictions on foreign equity participation, authorization and approval requirements, and restrictions on the scope of activity and form of legal entity. Such barriers not only affect competitiveness and efficiency in the sector concerned, but also have larger economy-wide implications for export prospects in other sectors, given their vital input role. For example, regulatory barriers in the air transport services sector affect India's export potential in tourism services. There are also licensing and nationality based restrictions arising from regulatory capture in various professional services, which affect market access by foreign firms and individual service providers, consequently hurting quality, cost competitiveness, and the scope for technology and skill transfer in such services.

3.4 GATS : AN OVERVIEW

One of the most significant achievements of the Uruguay Round of negotiations from 1986-1993, was to broaden the scope of world trade rules to cover services. Services negotiations were conducted on a separate track from those on goods, under the aegis of the Group for Negotiations on Services (GNS).[11] The resulting agreement, GATS, establishes multilateral rules and disciplines to govern international trade and investment in services.

Key features of the GATS

The GATS is a comprehensive legal framework of rules and disciplines covering 161 service activities across 12 classified sectors. These include activities as wide ranging as telecommunications, financial, maritime, energy, business, education, environmental, and distribution services. It excludes services supplied in the exercise of governmental functions.[12]

The GATS has three main elements. The first is a set of general concepts, principles, and rules, which are applicable across the board to measures affecting trade in services. Some of the key provisions include obligations concerning transparency, domestic regulation, restrictive business practices, behavior of public monopolies, and Most Favoured Nation (MFN) treatment.[13] The second element is a set of sector-specific or cross-sectoral commitments on national treatment and market access which are applicable to those activities listed in a country's schedule of commitments. The third important element TS is a series of attachments including annexes to the agreement which pertain to sectoral specificities and Ministerial Declarations regarding GATS' implementation. This three tier structure reflects the need to have:

1. General principles applicable to all services to advance overall liberalization in services;
2. National schedules to enable countries to proceed at their own pace in liberalizing services; and
3. Sectoral agreements to ensure that trade liberalization in some sectors is supported by the establishment of compatible regulatory regimes or modification of existing ones.

The GATS defines services trade as occurring through four modes of supply, modes as discussed earlier. This modal breakdown addresses the complex nature of international transactions in services and the diverse forms in which services are embodied, in consumption, production, and distribution-related activities and in the form of goods, human capital, and information. It also brings into the purview of GATS, regulatory issues concerning investment policies and immigration and labour market legislation, hitherto outside the domain of the multilateral trading system.

The GATS' commitment structure and framework is distinct from that of other WTO agreements. Countries make commitments on market access and national treatment for specific sectors in sectoral schedules of commitments and across sectors in horizontal schedules of commitments. The former are applicable to the particular sector at hand while the latter relate to all sectors and could compliment, override, or qualify the sectoral commitments. Countries are free to decide which service sectors they wish to schedule, i.e., table for negotiations, and thus subject to market access and national treatment disciplines. The latter has also been termed as a positive list approach to liberalization. These market access and national treatment commitments are made for each of the four modes of supply, i.e., there are in all eight commitments per subsector or activity in both the sectoral and the horizontal schedules. In addition, countries also specify in their schedules, the limitations and exceptions they wish to maintain which violate market access and national treatment, again by mode of supply. Limitations listed in the horizontal schedules typically include general laws and policies, which restrict the use of a mode of supply by foreign suppliers, independent of the sector concerned. Countries may also choose to inscribe additional limitations or qualifying conditions to their commitments.

Under the market access obligation, a country must accord treatment to foreign service providers which is no less favourable than that provided for under the terms, limitations, and conditions specified in its commitment schedule. These limitations take the form of restrictions on the number of foreign service suppliers, the value of transactions or assets, the total quantity of services output, the number of natural persons who may be employed, the type of legal entity, and the extent of foreign capital participation.

Table 3.2 below illustrates the typical format of the horizontal and sectoral schedules of commitments.

Table 3.2: Sample Schedule of GATS Commitments

Commitments	Mode of supply	Conditions and limitations on market access	Conditions and qualifications on national treatment
Horizontal commitments (i.e., across all sectors)	Cross-border supply	"None"	E.g., "None" other than tax measures that result in differences in treatment with respect to R&D services.
	Consumption abroad	"None"	"Unbound" for subsidies, tax incentives, and tax credits
	Commercial presence	E.g., "Maximum foreign equity stake of 49 percent"	E.g., "Unbound" for subsidies. Approval required for equity stake over 25 percent.
	Temporary entry of natural persons	E.g., "Unbound" except for the following: Intra-corporate transferees of executives and senior managers; specialist personnel subject to economic needs test for stays longer than one year; service sellers for upto three months	E.g., "Unbound" except for categories of natural persons referred to in the market access column.
Specific commitment	Cross-border supply	E.g., "Commercial presence is required"	E.g., "Unbound"
E.g., Architectural services	Consumption abroad	E.g., "None"	E.g., "None"
	Commercial presence	E.g., "25 percent of senior management should be nationals	E.g., "Unbound"
	Temporary entry of natural persons	E.g., "Unbound, except as indicated in Horizontal Commitments	E.g., "Unbound, except as indicated in Horizontal Commitments".

Source: Hoekman in (eds.) W. Martin and A. Winters (1995).

The national treatment obligation requires a country to accord treatment to foreign service suppliers which is no less favourable than that accorded to its domestic service providers, except as specified in its limitations and conditions under its national treatment commitments. Typical violations of national treatment include differential treatment of foreign service providers in the case of subsidies, taxes, government procurement policies, and provision of various benefits.

An entry of "none" in the above schedule means that a member binds himself not to have any measures, which violate market access and national treatment for a specific sector and mode of supply. These are also termed full commitments. Unbound implies that no commitment is made for a particular mode of supply. The rest of the entries, which include specification of some conditions and limitations are known as partial commitments. Thus, the GATS not only gives countries the discretion to choose sectors for negotiations but also gives them the flexibility to decide the degree of liberalization which they wish to commit in these tabled sectors.

GATS Commitments

Liberalization has been limited thus far under the GATS. Given the discretionary nature of the commitment process, countries have typically not scheduled the more sensitive and regulated service sectors. More commitments have been forthcoming in sectors like tourism and software which are relatively open and unregulated as opposed to services like education, health, distribution, and transport where there may be equity, employment, and government monopoly related considerations. Moreover, even in sectors that have been scheduled, often the coverage of subsectors and activities is quite limited. Commitments are mostly partial in nature and tend to bind less than the status quo, especially in the case of developing country commitments on commercial presence. Hence, existing policies have often not been locked in through commitments. Liberalization in mode 1 has also been limited as commitments in this mode are mostly unbound for reasons of technical infeasibility, indicating the uncertainty about telecom based delivery of services and e-commerce at the time of the Uruguay Round. However, the most strikingly limited liberalization has been in the case of mode 4 where countries have refrained from making sector specific commitments and have made broad horizontal commitments for select categories of service suppliers, namely those associated with commercial presence and at higher skill and professional levels. Moreover, even these horizontal commitments have been subject to a large number of restrictions relating to immigration and labour market policies, recognition requirements, nationality and residency conditions, and differential treatment in terms of taxes, subsidies, and procurement policies. Thus, the interest of developing countries in exporting labour based services, especially through cross border movement of semi-skilled and unskilled service providers, has been completely unmet.

India has made limited commitments in the Uruguay Round. It did not schedule major sectors like energy, distribution, accountancy, and legal services and even in sectors like financial services, which it did schedule, its commitments did not extend to subsectors like life insurance. India's commitments are largely uniform across sectors and are more restrictive than existing policies, reflecting the fact that India did not try to address sector-specific interests and concerns and took a conservative approach to the negotiations. Its commitments in modes 1, 2, and 4 are mostly unbound and commitments in mode 3 are subject to a foreign equity ceiling and local incorporation requirement. Overall, India has not used the GATS negotiations to lock in its existing policies in various service sectors. It has also not benefited from greater market access in other countries given the limited liberalization in its key modes of interest, namely modes 1 and 4.

GATS 2000 Negotiations

Talks resumed in GATS 2000 as mandated during the Uruguay Round and are currently underway. The objective of this round is to deepen the existing commitments through a request-offer process, to strengthen and develop various provisions in the GATS, and to establish mechanisms for better implementation of these provisions.

The request-offer process and India

As of June 30, 2002, many countries have put forward their sectoral and horizontal requests to other member countries. Developed country requests largely reflect their interest in liberalizing capital-intensive sectors like telecommunications, financial, energy, and distribution services through improved market access commitments in mode 3, as well as their interest in improving transparency in regulation and in administrative procedures in developing countries. Requests by developing countries are mainly focused on labour-intensive services and on improving market access under mode 4, through coverage of a wider range of skill categories and of independent and contractual service providers, who are de-linked from commercial presence.

India has received requests from all major developed countries. The thrust of these requests has been to commit to full market access in a variety of infrastructure services like insurance, banking, telecommunications, and energy services and to reflect India's FDI liberalization and regulatory reforms in these sectors in its commitments. Greater market access has also been sought for commercial presence and movement of intracompany transferees and business visitors in business services like legal and accountancy services. India has in turn made requests to all its major trading partners. These requests have mainly focused on India's export interests in mode 4. In this regard, India has made a bold proposal on mode 4, also endorsed by several other developing countries, to institute a streamlined GATS or service provider visa for intracompany transferees, business visitors, contractual service providers, and independent professionals for a uniform one year period. This visa would be distinct from normal immigration visas, so as to effectively separate temporary from permanent movement of labour. India has further proposed that entry quotas, wage parity requirements, social security taxes, economic needs test and other such restrictions be eliminated for those qualifying for a service provider visa. The GATS or service provider visa would be characterized by:

i) Strict time frame for issuance (2-4 weeks maximum);

ii) Flexibility in issuance on shorter notice for select categories of providers and border availability;

iii) Transparent and streamlined application process;

iv) Mechanisms to find status of application, rejection, requirements;

v) Easier renewal and transfer procedures;

vi) Safeguard mechanisms to prevent entering permanent labour market and abuse;

vii) Scope to challenge rejections, delays, and unfair practices under the dispute settlement mechanism.

India has also requested due recognition of qualifications for its service providers and improved enforcement of GATS provisions for facilitating entry into Mutual Recognition Agreements.

Initial offers have been forthcoming as of March 31, 2003. There are more full commitments in mode 1. This is of significance to India as it ensures liberal and predictable market access through cross border supply and thus for business process outsourcing and back office service exports by India. There is also some improvement in the offers on commercial presence, with removal of limitations such as economic needs tests and authorization/approval requirements and relaxing of limits on foreign equity participation. However, improvements in mode 4 have been very limited. A few offers, such as by the EU and Canada, cover new categories of service providers such as graduate trainees, independent professionals, and contractual service suppliers that are of export interest to developing countries like India. These offers also increase the length of stay and relax associated conditions on stay and entry. However, these offers still do not distinguish between temporary and permanent movement of labour. They continue to subject GATS related movement which is temporary to the usual immigration and labour market regulations which are applicable to permanent migration. Moreover, limitations in the form of entry quotas, differential taxes and subsidies, economic needs tests, and discretionary application of recognition norms continue to hold. Hence, so far, India does not have much to gain from the offers in this mode.

It is expected that the offers would be finalized by the end of 2004 and would become part of a new round of WTO negotiations. Although the initial commitments to date show only marginal improvements in terms of market access and conditions of operation relative to the earlier Uruguay Round commitments, there has been much greater willingness on the part of developing countries to negotiate further liberalization of services. India, which had earlier resisted the inclusion of services in the multilateral trading system, is today one of the most vocal proponents of improving multilateral guidelines under the GATS and for increasing market access for developing country service providers. This shift in position on services reflects the growing awareness of the significance of this sector to the country's overall reform and liberalization agenda, its wider implications for growth and productivity, and the realized comparative advantage in selected services.

Activity 4

Write your understanding of GATS in 50 words.

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3.5 NEGOTIATING STRATEGY AND DOMESTIC REFORMS

In order to benefit from the GATS negotiations, India needs to have a coherent external and domestic strategy. It needs to: (a) identify the country's strengths, weaknesses, and trade potential and requirements in individual service sectors; (b) identify the concessions India would like to obtain in specific service sectors and from specific markets; (c) determine what it could concede in turn; (d) recognize the political economy constraints and limitations it would face in liberalizing services; and (e) identify the domestic reforms and measures it would need to implement to support its negotiating strategy.

The thrust of India's strategy in *infrastructure services*, where it is primarily an importer, has to be on opening up the domestic market to greater competition and in particular, to foreign direct investment. India should consider liberalizing its earlier commitments on market access and national treatment, keeping in mind needs such as capital infusion, technology upgradation, synergies with other sectors, and the larger economy-wide impact on efficiency and competitiveness. The commitments have to be framed in the larger context of ongoing regulatory reforms and liberalization in these sectors and must reflect policy intentions. Overall, it must:

1. Bind the status quo at a minimum so as to reflect the current regulatory environment and recent reforms, signal predictability of its policies, and reduce the scope for backtracking.
2. Expand the coverage of its commitments by including new subsectors and activities which were previously not bound, by including more sectors which were not previously scheduled, and by increasing the scope of the existing commitments by removing or relaxing various limitations.
3. Pre-commit to further liberalization so as to signal future intentions, particularly where the course of future policy and a timetable for phasing in has been declared and use the transition period to undertake necessary domestic measures on regulatory capacity and institutional frameworks.
4. Leverage across sectors by offering greater market access through FDI in sectors like insurance and telecommunications which are of interest to major developed countries like the EU and the US in return for improved market access under cross border supply and movement of natural persons for services like IT, health, BPO, and others where it has export potential.

India's strategy in the area of *professional services* has to be both outward and inward oriented since these are services where India has both export and import interests. Given its comparative advantage in labour and knowledge-intensive services, India needs to obtain more liberal commitments from key export markets, particularly for modes 1 and 4. In this regard, India needs to advance with its proposal on mode 4 through its developing country coalition, "Friends of mode 4", for the institution of a separate GATS or service provider visa and its model schedule of commitments for mode 4. The introduction of a GATS visa to separate temporary from permanent labour would also facilitate the removal of social security taxes, economic needs and other necessity tests, and other restrictions. In addition, India would also need to insist on discussing issues relating to classification of service providers and transparency in administrative procedures.

In view of India's recent emergence as an outsourcing hub, its negotiating strategy also needs to put sufficient emphasis on liberalizing market access through cross border supply. Recently, India has proposed a horizontal formula for mode 1 whereby countries would make a full commitment in this mode across all sectors, barring those like financial services where there may be concerns of financial stability and fraudulent practices arising from unrestricted cross border flows of capital. This approach has been motivated by the protectionist backlash to BPO and back office services in developed countries and would help pre-empt future protectionism in the private domain by guaranteeing unrestricted market access under mode 1. Although India cannot challenge the latest US bill which bans offshoring of US government contracts, given the carve out clause for government services under the WTO, it needs to re-think its position on government procurement under the WTO. It needs to assess the market access implications of government procurement restrictions. As noted earlier, it would be India's interest to advance the proposals on both modes 1 and 4 through a quid pro quo negotiating strategy of offering greater market access in sectors of commercial interest like banking and insurance through commercial presence for improved market access in these two modes.

On the domestic side, India should also consider scheduling more professional service sectors and opening up these services to foreign commercial presence and service suppliers. Such an approach would be conducive to the needs of greater efficiency, competition, higher quality and standards in many of these services and would help overcome the regulatory capture that exists in the home market in some of these professions.

These negotiating strategies have to be supported by various domestic reforms and measures. More liberal market access conditions in infrastructure services need to be supported by initiatives to encourage private participation in such services. This would require liberalization of FDI policies, divestment of the government's share in related public sector enterprises, and creation of an appropriate regulatory structure to ensure transparency, fairness, and a level playing field without jeopardizing consumer and national interests. The fallout in terms of displacement of labour and associated reforms in labour laws and in legal and institutional frameworks, would also need to be addressed. Similarly, in the case of professional and manpower based services, India will not be able to realize its export potential unless it undertakes steps to improve quality, standards of training and infrastructure, and regulatory mechanisms to enforce standards. Investments in telecom infrastructure and supporting facilities and amendments to domestic laws and acts affecting competitiveness in such services may also be required.

Activity 5

Talk to some corporate people from a service organization and ask them about their understanding of implications of GATS for India. Summarize your interviews in 50 words.

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3.6 SUMMARY

Service sector trade and investment are likely to grow rapidly in the coming years. The prospects for further liberalization of these flows are also promising given heightened awareness about the importance of a competitive and efficient service sector and much greater willingness on the part of governments across developed and developing countries to deregulate and liberalize services autonomously. The GATS framework provides countries with the opportunity to lock in their liberalization in the service sector. India is likely to emerge as an important player in both exports and imports of services. So far, India has taken a very cautious and conservative approach to the GATS negotiations. But if India is to realize significant market access gains in sectors and modes of interest, then it must also be willing to make substantial market access commitments in services and to overcome its defensive posture in these negotiations.

3.7 SELF ASSESSMENT QUESTIONS

1. What are the four modes of service delivery? Explain by taking examples.
2. What is your understanding of GATS and its implications for India?
3. In what specific Services sector, India has core competence, which can be strategically exported. Give Justifications.

3.8 FURTHER READINGS

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3.9 REFERENCES

1. Warren and Findlay (2000), p.5.
2. WTO Annual Report (1999 and 2000).
3. Stern and Sauve (2000) and Karsenty (1999).
4. Estimates for the different modes of supply were obtained from Karsenty (1999). The latest available estimates are for 1997 for such a mode-wise allocation of services trade.
5. There are differences, however, between the GATS and the FATS concepts of foreign affiliates and related service trade statistics. GATS refers to all foreign affiliates while the FATS only refers to the majority owned affiliates. GATS covers services provided by service and manufacturing companies while the FATS covers the output of companies by primary activity. Since FATS proxies service products with total production of companies in service sectors and leaves out the value of service activities undertaken by

companies in agriculture or manufacturing, it may result in some underestimation. At the same time, since the service sector also produces goods, FATS may overestimate the value of service activity.

6. Statistics on the geographic profile of services trade are from the WTO Annual Report (2000).
7. RBI Annual Report (2002-03).
8. Ibid 7.
9. IMF, Balance of Payments Statistics (1999).
10. Nasscom (2000).
11. During the course of the discussions, it was decided, however, that services would be part of a single legal undertaking, the WTO, and would be subject to the same principles, i.e., those of Most-Favoured Nation treatment, national treatment, and transparency.
12. This carve out clause would apply to sectors such as health and education services which are typically in the public sector domain. However, due to lack of clear terminology in this carve out provision and given the growing role of private delivery in even such sectors, it is often difficult to determine which activities can be covered by GATS and which are excluded.
13. Article VI on domestic regulation establishes disciplines to ensure that regulations such as qualification requirements, technical standards, and licensing procedures are based on objective and transparent criteria, are not more burdensome than required for ensuring the quality of the service, and do not constitute restrictions in themselves. Article VII on recognition which establishes procedures for mutual recognition of licenses, education, and experience and calls for equal opportunities to other countries to negotiate accession to bilateral or plurilateral mutual recognition agreements. Article III on transparency requires countries to establish enquiry points to provide specific information on laws, regulations, and administrative practices with bearing on services trade. There are also several safeguard type provisions which permit a country to introduce restrictions for BoP reasons or to safeguard public morals, law and order, consumer interests, security, and privacy.