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"CONCEPTUAL AND DATA ISSUES IN TRADE IN SERVICES"

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Foreword

These papers were presented at a seminar on "Conceptual and Data Issues in Trade in Services", held in Ottawa, February 13, 1986. This is the first seminar in an ongoing series on current issues in trade policy, sponsored by the International Economics Program at the Institute for Research on Public Policy and the Centre for the Study of International Economic Relations of the University of Western Ontario. The series aims to bring together policy practitioners from Canada and the United States for discussion of issues relevant to upcoming bilateral and multilateral trade negotiations.

Organizational support for the seminar was aptly provided by Lynda Lennon and Andrew Moroz of the Institute for Research on Public Policy.

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Some Reflections on the Current Trade in Services Debate[1]

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February 1986

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[1]This is a summary of a presentation at a CSIER/IRPP Symposium on Trade in Services held in Ottawa, February 8, 1986.

I. Background to Present Proposals for a Service Trade Negotiation

At the present time, there is active debate on both the prospects for and the possible content of a negotiation covering issues affecting trade in services.[1] The objectives of such a negotiation would be to bring under international discipline an area of international trade which is currently viewed as largely outside the coverage of the GATT, and to deal with what is seen as a rapidly growing area of trade. The impetus for such negotiations comes largely from the United States.

Perhaps the most important factor underlying the current U.S. drive for an active negotiation on service trade is the strong perception that the U.S. has a comparative advantage in service industries.[2] These cover such items as communications, banking, insurance, transportation, engineering, and consulting services. The U.S. view is that this is a rapidly growing and dynamic part of the economy, and an area which the U.S. has major potential export opportunities.

In part, this is a reaction to the inward penetration by rapidly growing newly industrialized countries such as South Korea and Brazil of the more traditional U.S. industries such as

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[1]For a recent discussion of this debate, see the recent monograph by Stalson (1985).

[2]See Shelp (1981) for an early view of the role of service industries in the U.S. economy.

steel and autos; which has been underway for some 10-15 years. The view is deeply entrenched that the future potential of the U.S. economy lies in these service industries, many of which are equated with high technology activities, and that this necessitates a strong orientation in trade policies towards these industries to achieve improved access to foreign markets.

This, however, is not the only source of U.S. pressure for negotiations. It is also widely believed that services constitute a large fraction of current U.S. international transactions. In documents, such as that prepared by the Special Trade Representatives' Office in the U.S. as part of the series of national studies which were done for the GATT working party on services, the claim was made that as much as 30 percent of international transactions that the U.S. engages in constitute services of one kind or another. While it is now agreed that this number is misleading since it includes dividends and interest, flows which in large part refer to income returns to assets rather than services per se, the fact that services are perceived as constituting such a large fraction of international transactions gives added impetus to a service trade negotiation. In turn, services are viewed as an item not covered by the GATT, although there are disagreements as to the precise legalities of current GATT coverage in the articles which enshrine national treatment and other provisions for goods trade.

A further factor accounting for the drive towards negotiations is the strong perception in the United States, and a perception shared by some other countries, that there is a major threat of new barriers being used in the future by various countries to impede the flow of service trade. Some of these concerns focus on communications technology where there have been proposals by various countries to tax the number of message units which flow through transmission devices such as satellites and other electronic media. Such proposals have raised substantial consternation. Intrusions of this type into what is seen as a relatively barrier free area of trade would, of course, generate major problems. This motivates the desire to put in place a series of international arrangements which will prevent the erection of such barriers.

In part, then, one has to be aware that entering a new round of negotiations on service trade may involve different issues than previous negotiating rounds under the GATT which have focussed on tariff and other barriers to visible trade. In earlier GATT rounds the approach was to negotiate down barriers which already existed. In the service trade case the negotiations are, in part, motivated by an attempt to prevent the introduction of new barriers.

Finally, one also has to be aware that a service trade negotiation is consistent with the so-called "bicycle theory" of the GATT. That is, that the process of trade negotiation has always to keep moving forward into new fields and to generate new areas of substantive trade liberalization, otherwise the cooperative outcomes which have characterized previous negotiations will be at risk. New negotiations, even if difficult or not concerned with matters of great substance, need to take place in order to protect the advances of previous negotiations. Without this hope that a further cooperative step is possible, countries will tend to revert to the protectionism of old.

When one looks at the liberalization which has taken place under the GATT since 1947, tariffs on manufacturing products have been, in effect, either significantly reduced or eliminated between major trading partners. Quantitative restraints and contingent protection measures such as countervail, antidumping, and safeguards, remain difficult to deal with. In part, present proposals to move trade liberalization attempts outside of its traditional focus on manufactures, and onto services can thus be seen as part of a continuation of a trend of (at least perceived if not actual) forward movement on the trade liberalization front. How far it will take us remains to be seen.

II. The Broad U.S. Framework Proposal

What then is a negotiation likely to contain and how could it proceed? At this point we are at an early stage of any negotiations, and whatever one says is largely speculative. From what has emerged thus far, it seems clear that there are three major elements to a broad framework proposal coming forward from the U.S.

The key element is a call for a standstill on new service trade measures. The view is that the service trade negotiations can be thought of as much akin to the negotiations on liberalization of trade in goods which has preoccupied the GATT from its inception in 1947. While many tend to think of the major trade liberalization under the GATT as having occurred under the Kennedy and Tokyo Rounds when tariffs were substantially cut, there was, in fact, an important prior period of negotiations. Early GATT negotiating rounds concentrated on binding of tariff rates, which were essential to provide the framework for subsequent negotiations. Particularly important were early attempts to convert existing trade restrictions into more transparent and commonly agreed negotiable barriers which could then be more openly discussed.

The United States sees a standstill on new service trade measures not only as a way of heading off new barriers to service trade, but also as the first step in an ongoing series of negotiations covering service trade matters. Clearly, any standstill will encounter major problems in defining what service trade measures actually are. Also monitoring and policing such an arrangement will be difficult.

A second element in a likely U.S. proposal would be that national treatment, which currently applies under the GATT to flows of goods, should also be extended to services. The principle of national treatment states that as soon as any item crosses a national border it should be treated on the same basis as comparable domestically produced items. The U.S. proposal is that the same principles as apply to goods be applied to services. This would seem to imply, for instance, that in the case of banking, insurance, and other financial activities, all regulatory constraints should be applied uniformly to domestic and foreign entities. If this occured it would lead to major changes for these sectors in the United States as well as in other countries.

The final element in the U.S. call is for right of establishment, namely that all foreign entities be allowed to establish themselves for the purpose of servicing domestic markets. This has been a particularly contentious issue in the area of insurance, where in order to sell insurance in certain countries it has been necessary to establish a local entity which can undertake and absorb the local risk. But if right of establishment is denied, entry into the local market is also denied.

III. Complications in Preparing for a Negotiation

Despite the broad U.S. framework proposal, there is no doubt that any multilateral or even bilateral negotiation on service trade is a substantial distance away and that negotiations would be extremely complicated. This is the case for many reasons.

Firstly, the service trade issues as they arise by sector are highly varied, and this makes a broad framework proposal difficult to both achieve and implement in a substantive way. The issues in communications, banking, insurance, transportation and engineering services are clearly different one from another. In the communications area, the concerns apply to potential barriers to transborder data flows. In banking, the current regulatory environment both within countries and within regions within countries largely prevents the international exchange of banking services through cross-border intermediation services. Most international activity involves the establishment of branches abroad. In insurance there are several instances where foreign insurance companies are prevented from selling into domestic markets. The complexities of these arrangements, reflect the subtleties of national regulatory environments, and any form of negotiation has to deal with these complexities in a concrete manner to make substantive progress.

A further difficulty is that the data that is currently available on service trade is extremely limited. The data that we have comes largely from balance of payments accounts, but these are in no way intended to give a representative view of what service trade flows actually occur. The balance of payments accounts separate the capital and current account, and on current account separate visible and invisible flows. The invisible flows contain interests, dividends, fees, and royalties. The capital account reports data on transborder capital flows. The underlying service related transactions which give rise to these financial flows are not fully recorded by type of service. And several service items (such as banking) give rise to financial transactions which appear in more than one place in these accounts.[1]

It is, therefore, not possible from existing data to reliably compile separate estimates of international flows of services in the key functional service categories. This not only makes negotiations difficult, since the negotiators will not have data on which to judge what constitutes a reciprocal exchange of concessions, but it also undermines the political will for a negotiation because of the ambiguity of the U.S. claim that services indeed constitute a large fraction of international transactions.

There is also the feature that a broad framework approach to services trade will inevitably encounter complex definitional problems. Since the service trade debate first got underway, there has been a substantial amount of agonizing as to what constitutes a service. Many commodity transactions have large service components associated with them, and what should be classified as a service is by no means clear. Also, the precise meaning of a standstill in this area has to be clarified; right of establishment has to be defined; and thus any broad framework approach itself raises further problems of definition which in turn may complicate the breadth of the framework.

In addition the linkages between service trade issues and the treatment of factor flows substantially complicate matters.

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[1]See the discussion in St-Hilaire and Whalley (1985).

Many of the so-called service trade issues are viewed by others as trade-related investment issues. Concerns over international barriers towards banking and insurance are frequently linked either to right of establishment or the requirement to establish. But these regulatory environments equally imply that these concerns may be alternatively stated as trade related investment questions; namely, that either establishment is denied, or if establishment is allowed it is only on discriminatory terms compared to national business. To what extent service trade negotiations inevitably implies negotiations covering trade related investment issues is at this stage unclear.

Equally, many of the service trade issues encounter complex linkages to questions affecting labour flows. Inherent in the discussions of barriers of free flow of engineering and consulting services is the right of individuals supplying such services to cross national borders. This in turn can involve countries' rights to control immigration procedures.

A final complication in preparing for a negotiation is how the linkages to other issues on either the multilateral or bilateral agenda relating to trade flows in goods can be made. There is a concern in many of the smaller developed countries, including Canada, and also in some of the developing countries, that an overly active negotiation on service trade may deflect both attention and negotiating energies from substantive negotiations on matters of more concern to such countries, which involve trade in goods. Questions involving contingent protection, such as safeguards and countervail, are matters which the smaller developed countries perhaps have more interest in than a service trade negotiation.

IV. Negotiating Issues

Despite these difficulties, the determination of the U.S. to proceed to a broad ranging negotiation on service trade makes it likely that some of negotiation will indeed take place. In contemplating a negotiation on service trade, one has to identify alternative approaches and look at the merits of them. And just as with trade in goods there are alternative approaches that can be taken.

There is a choice between a broad or a sectoral approach, the relative merits of which are reasonably clear from the discussion above. The definitional problems associated with a broad framework approach are undoubtedly intimidating. The attractions of negotiating narrowly on individual sectors at first sight seem overwhelming; except that one immediately encounters the difficulties common to sectoral negotiations on goods trade, namely that the way in which tradeoffs between sectors can be accommodated is unclear. Typically the benefits in any one sector accrue disproportionately to one country or the other.

A further issue is how far bilateral negotiations might proceed before these issues are subsequently taken up in the multilateral framework. There is a view in many circles that the U.S. is actively pursuing bilateral trade negotiations, in part, to establish precedent setting framework agreements on services. The view is that these will largely define an eventual set of codes which will operate in the multilateral arena. The bilateral arrangement between the U.S. and Israel has a significant component which deals with service trade issues, and some are arguing that a possible interest of the U.S. in an active bilateral negotiation with Canada will be to further the same end.

The problem is that agreements entered into bilaterally need in no way represent the most appropriate form of multilateral agreement; but that any multilateral agreement will have to be compatible with prior bilateral agreements that participating countries have entered into. This is especially the case if bilateral negotiations continue to focus on a broad framework approach which may be inconsistent with approaches subsequently taken up multilaterally.

Another issue is how concessions on services can be traded for concessions on goods. Proposals for negotiations on services have concentrated largely on possibilities for trading concessions within the service category. One of the major strengths of the GATT negotiating framework is that it permits a mutual exchange of concessions which can span different categories of trade in goods. If the service trade proposal is to proceed, presumably there has to be a framework developed for a trading of concessions on goods for trading on concessions of services. And yet the barriers which apply to services are unclear. Even a standstill agreement itself would represent a concession to certain parties to the agreement.

A further complication is the role of the developing countries in such a negotiating process. Developing countries are currently hostile to the idea of an active negotiation on services, led by India and Brazil but joined by Yugoslavia, Egypt, and Argentina. The developing countries see an active service trade negotiation as a vehicle through which their own service industries will be dominated by those of the developed countries. There are, however, signs of disagreement among some of the developing countries themselves. Some, such as South Korea and Singapore, see their own comparative advantage as partly lying in certain service industries. Others which are major net importers of services, such as the African countries, view themselves in danger of becoming captive markets to other developing countries, and partially support attempts to liberalize service trade to allow the more efficient service suppliers from the developed world to enter. There is, however, a widespread suspicion in the developing world on the service trade issue, and the potential for a further major fracture in the global trading system which could result from a confrontational approach towards the developing countries on the service trade question must be borne in mind.

All of this leads to the obvious question. What should be the next step? If indeed a negotiating round is to take place on services, it does seem sensible to think in terms of the parallels between a service trade negotiation and the goods liberalization process which we have been through multilaterally under the GATT since 1947. This involved an initial binding of tariff rates, and these limits on their use provided the framework for subsequent negotiations. The analogue in the present case does indeed seem to be a standstill on new service trade measures. In turn, this would require some international framework or agency which would be empowered to deal with disputes between countries on service trade, even though the dispute settlement procedure would itself be very difficult. Perhaps a standstill arrangement with a multilateral dispute settlement procedure[1] is then the way for a service trade negotiation to proceed, although negotiating this may prove difficult.

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[1]See Stalson (1985) who makes a similar proposal.

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Statement of Peter Morici
Vice President, National Planning Association
on
U.S. Comparative Advantage and International Trade in Services
before the
Subcommittee on Economic Stabilization
Committee on Banking, Finance and Urban Affairs
U.S. House of Representatives
June 12, 1984

Mr. Chairman and Distinguished Members:

I am Peter Morici, Vice President of the National Planning Association here in Washington. I am honored to appear before you today to discuss how U.S. international trade in services relates to issues surrounding the evolution of U.S. comparative advantage generally and U.S. trade policy objectives. My comments will focus on this overall perspective, as I am sure you will be receiving from others a great deal of detailed and specific information on the services sector and problems of particular industries. Before proceeding further, let me state that the views I express are my own and are not necessarily the views of the National Planning Association.

INTRODUCTION

Over the past decade and a half, the U.S. private sector has had to adjust to many fundamental changes in the domestic and international economies. Important among these have been the increased prominence and sophistication of services in the United States and in economies around the world. With respect to the latter, services are an important potential source of export growth in their own right, and they also carry with them the potential for additional exports of U.S. goods.

To fully appreciate the role that services may play in our future economic growth and the international economic policy challenges they pose, an understanding is required of: (1) how they fit into the U.S.

international competitive position and (2) the consequences for U.S. income and living standards of the very formidable barriers U.S. exports of services face.

A GENERAL VIEW OF AMERICAN COMPETITIVENESS

During the 1970s, the post-War internationalization of the U.S. economy accelerated significantly. From 1950 to 1972, exports' share of GNP grew slowly from 5 percent to 6.5 percent and then jumped to 11.6 percent in 1979. This process advanced during a time of fundamental changes in the U.S. and international economies, which exacerbated the adjustments imposed by increased international competition on U.S. business and labor. Some of these changes were new, while others were the result of trends underway for several decades. Nevertheless, they converged during the 1970s and are now defining the types and scope of adjustments the U.S. private sector must achieve if the American economy is to remain competitive and U.S. living standards and employment opportunities are to be maintained and expanded. They include:

- The creation of a truly international marketplace for goods and services by tariff reductions, improvements in global communications and transportation, the need to spread ever larger product development costs, and other changes in the technology of production; the subsequent struggle between the leading trading nations and blocks—e.g., EC, United States-Canada, Japan, Singapore-Taiwan-Hong Kong-Korea, and Mexico-Brazil—for markets and employment opportunities.

- Shifting patterns of international competitiveness—

  - A general evening of capabilities in technology-intensive industries among the major advanced industrial countries (AICs). During the last 1960s and 1970s, Japan, followed by the major European economies, expanded their R&D capacities (as measured by scientists and engineers actively engaged in R&D) much more rapidly than Canada, who, in turn, expanded its capacity more rapidly than the United States.

- oo The broadening export capabilities of the Far East and Latin American NICs from labor-intensive products to many standardized-technology, capital-intensive manufactures such as steel, aluminum, copper and automotive parts.

- oo The emergence of a new wave of NICs emphasizing the labor-intensive industries, as the more prosperous NICs follow Japan into capital-intensive industries. For example, Malaysia, Thailand, the Philippines, Sri Lanka, and China are moving into apparel and footwear, toys and simple electronic assemblies. The process of older NICs graduating from and the newer ones entering these most labor-intensive activities will continue well beyond the end of the century.

- o The increased importance of competitive (perhaps combative) foreign industrial policies that seek to create comparative advantages.

- o Floating exchange rates, which since 1973 have greatly elevated the importance of exchange rate management and financial market conditions in determining competitive performance. Misaligned exchange rates are now a critical factor in the competitiveness equation.

- o An increased pace of technological progress—the advent of computer-aided design and manufacturing, flexible manufacturing systems, major breakthroughs in microelectronics, and the development of new materials are changing the way we manufacture products, the composition of goods and services we consume, and the materials we use to make them.

As this process advanced, U.S. competitiveness waned first in labor-intensive, mobile industries with standardized technologies and short production runs (e.g., apparel and footwear) and then in capital-intensive industries producing standardized goods on longer production runs (e.g., steel and automotive products).* The United States came to look to exports of agricultural products, technology-intensive manufactures requiring large

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* These market share losses often came with alarming speed. For example, import penetration in automobiles rose from 16.2 to 28.3 percent between 1977 and 1980, and in color televisions from 19 to 33 percent between 1975 and 1976. Such sudden shifts in competitive performance imposed burdensome adjustment costs, because they required firms and workers to adapt to change more rapidly than markets could permit at any reasonably attainable rate of economic expansion.

amounts of R&D and highly-skilled engineers and technicians, and services, as well as to the ability of U.S. firms and entrepreneurs to move into successive generations of newly emerging industries to pay for a rising tide of imports. In the decade ahead, however, this course may not prove as easy as proponents of a post-industrial America may believe.

Focusing on merchandise exports, the contribution of agricultural products to the total U.S. exports began to decline after displaying great promise during the mid-1970s (as a result of expanded Soviet and Eastern European grain purchases and increased imports by upper-income developing countries). In 1981, they stood at 18.4 percent of total merchandise exports, little more than the 17.0 percent recorded in 1970 and significantly less than the 22.9 percent achieved in 1965. Once the effects of the recent U.S.-Soviet grain agreement have been absorbed, potential growth in this area will likely be constrained by slow market growth and, to a more limited extent, by trade-distorting practices such as the EC's Common Agricultural Policy.

Meanwhile, traditionally export-oriented technology-intensive manufacturing industries face growing competition. U.S. leadership in areas such as machine tools and heavy machinery can no longer be taken for granted. Experience with the Japanese in computer chips and robots and with the Europeans in commercial aircraft indicate that the traditional U.S. strategy of relying on the most advanced branches of high-technology industries to maintain U.S. competitiveness and to generate needed exports may no longer be relied upon with certainty.

In 1981, R&D-intensive exports' share of total merchandise exports was 46 percent, little changed from 1969. This performance may be viewed only as adequate at a time when technology-intensive industries are a growing segment of all the major AIC economies. Therefore, net trade performance in this area should be examined to evaluate competitive performance.

Figures 1a and 1b present the frequently cited U.S. trade balance (exports less imports) in R&D-intensive industries for the 1960s and 1970s. They indicate that U.S. competitive performance has been improving; but these trade balance data may reflect the effects of general economic growth and inflation as much as they indicate changes in overall competitive performance. To correct for these factors, the annual data for the U.S. trade balances in R&D-intensive goods should be normalized to remove the effects of inflation and the real growth of trade. One way to do this is to divide these annual data for trade balances by the annual values of total R&D-intensive imports plus exports. These computations were performed and the results are charted in Figure 2. They indicate a trend of declining competitiveness in R&D-intensive industries even as U.S. competitiveness has waned in a widening range of labor- and capital-intensive industries.*

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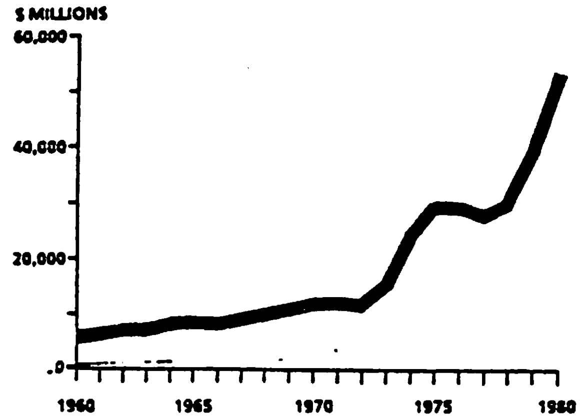
* Data for exports divided by imports indicate a similar downward trend.

Figure 1

U.S. TRADE BALANCE IN R&D-INTENSIVE MANUFACTURES: 1960-80

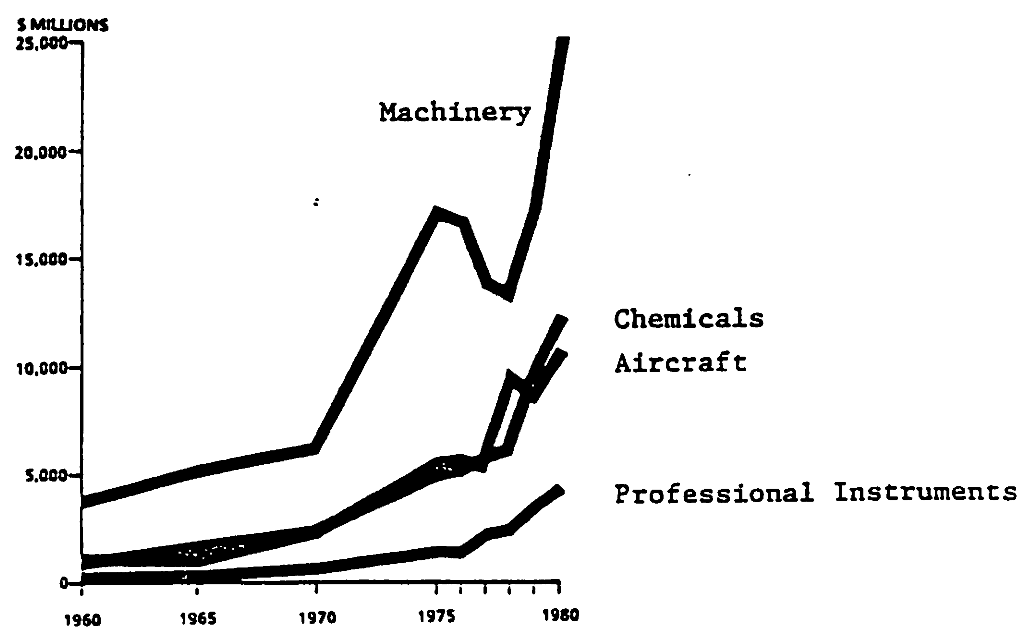
All R&D-Intensive Manufactures

U.S. TRADE BALANCE IN R&D-INTENSIVE MANUFACTURED PRODUCT GROUPS



Selected R&D-Intensive Product Groups

U.S. TRADE BALANCE IN SELECTED R&D INTENSIVE PRODUCT GROUPS



Source: United States Trade Representative, Twenty-sixth Annual Report of the President of the United States on the Trade Agreements Program (November 1982), Figures 14 and 15, pp. 26 and 29--reproduced.

Figure 2

U.S. TRADE BALANCE IN R&D-INTENSIVE PRODUCTS DIVIDED BY R&D-INTENSIVE EXPORTS PLUS IMPORTS: 1960-81

Source: Derived from United States Trade Representative, Twenty-sixth Annual Report of the President of the United States on the Trade Agreements Program: 1981-82 (November 18, 1982), Table A-14, page 156; Survey of Current Business, various issues; the National Science Foundation.

It is important to note that the gains achieved by U.S. competitors in technology-intensive industries have been the result of substantial investments in R&D and hard-fought efforts to increase innovative capabilities in other AICs. However, these gains have also been the result of concerted foreign government efforts to encourage their technology-intensive industries through subsidies, industry targeting and other measures designed to assist their firms close technological leads achieved by U.S. companies through decades of R&D investments.

Turning to services, their recorded contribution to U.S. export earnings has expanded only modestly over the last two decades. The international transactions statistics published by the Department of Commerce in the Survey of Current Business divides service transactions into five categories: (1) travel (tourism, food, lodging, etc.); (2) transportation of goods or people; (3) investment income derived from U.S. assets abroad (including among other things stocks, bonds and interest earned by U.S.-based banks on foreign loans); (4) a broad category of other services (e.g., banking, insurance, advertising, accounting, legal services, brokerage, and construction engineering); and (5) government service receipts. The first four constitute recorded private sector service exports, and it is the fourth category that includes the kinds of activities to which we usually refer when we discuss expanding service exports.

According to the international transactions statistics, services accounted for 33 percent of U.S. export earnings in 1973, unchanged from a decade earlier. By 1983, they stood at 36 percent but most of this growth was caused by increases in earnings from foreign investments (in particular, interest earned by U.S.-based banks). Of course, measurement problems for service exports is an acknowledged area of difficulty. Nevertheless, there is concern that the growth of service exports has been slower than would be anticipated given several underlying structural factors that are expected to favor rapid expansion of U.S. sales abroad.

First, the growing importance of R&D-intensive products, such as computers, telecommunications equipment and heavy electrical equipment are accompanied by expanding markets for complementary services; we expect expansion of U.S. R&D-intensive exports to be followed by increased service exports. Second, tradeable services require large amounts of highly skilled labor, an abundant and rapidly expanding resource in the United States vis-a-vis our trading partners. Third, rapid growth and development in oil-exporting developing countries, the NICs and emerging NICs has created a rapidly expanding market for tradeable services; on the basis of comparative advantage, this process should create a rapidly increasing market for service exports from the United States and other AICs, especially as developing countries continue to expand their export capabilities in standardized manufactures. Fourth, the United States and Canada have well-developed expertise in many tradeable services as a by-product of the development of an integrated and relatively independent continental economy; construction engineering, banking, insurance, international law, and telecommunications are examples of significant home-grown expertise.

However, the export of services presents special problems. These emerge from the nature of the products involved and foreign practices that limit U.S. service exporters' market access abroad.

BARRIERS TO U.S. SERVICE EXPORTS

International trade in goods is fairly straight forward—goods are produced in one country and are moved across an international border to another. Goods may be simply put in the hull of a ship and moved; international commerce in goods is guided by conventionally understood relationships among traders, and government practices are constrained at least to some degree by the GATT. In contrast, tradeable services take many forms: they may be embodied in goods (e.g., blueprints, software, films); others are provided by individuals either traveling abroad or through global communications systems (e.g., legal, banking and consulting services); still others require the access to or establishment of extensive capital facilities (e.g., shipping, commercial aviation and telecommunications). Trade in services are not generally covered by the GATT and, because of their amorphous character, they are prone to a wide range of difficult to regulate and control discriminatory practices in addition to many of those applied to goods.

Many service exports require (or their marketing is greatly enhanced by) physical proximity between producers and consumers. The consumer travels to the producers (e.g., tourism and educational services), or the producer seeks to establish an entity in foreign markets (e.g., advertising, accounting, banking, and wholesale and retail trade). When U.S. firms seek to establish a branch abroad, they encounter the difficult problems associated with the regulation of foreign investment. Specifically, they often encounter quantitative restrictions on market access and investment performance requirements. The relationship between market access for services and foreign investment makes efforts to improve access in developing countries particularly difficult. These countries often view attempts by developed nations to liberalize trade in services as a Trojan horse for increasing foreign investment.

Tradeable services are often provided by industries that governments choose to regulate within their domestic economies for reasons relating to consumer protection (e.g., natural monopolies, standards of competence for professional services, and public health), national security, domestic sovereignty, and nationalistic cultural concerns. Examples include broadcasting, telecommunications, transportation, advertising, and professional services. Countries tend to think of these industries, unlike those producing goods, in domestic as opposed to international terms. While many regulations are in place to achieve reasonable domestic objectives, others often have the intended effect of discriminating against foreign suppliers in pursuit of nationalistic economic goals. Barriers may take many forms such as denying or delaying necessary licenses; discriminatory taxation; discriminatory government procurement; limits on access to foreign exchange; restricted access to imported equipment and intermediate services; restrictions on the composition of management; domestic employment and sourcing requirements and other performance requirements; and outright limits on market shares. Some of these practices can be real nuisances: in Brazil, all accountants are required to have a degree from a domestic university and, in Argentina, television commercials made outside the country are banned.

IMPLICATIONS FOR THE UNITED STATES

Referring back to my earlier comments about the evolution of comparative advantage, the United States is in difficult competitive box.

On the one hand, import penetration has grown in an expanding group of mature industries. On the other hand, accelerated export growth is not assured in three important areas of U.S. strength: agricultural products, technology-intensive manufactures, and services. In all three of these areas discriminatory trade practices are important constraints with important consequences for U.S. incomes.

We are all aware of the concerns expressed about the quality of employment opportunities in the services sector. While being the principal new source of jobs in recent years and of employment opportunities in many high-skilled occupations, many entry level service positions do not pay as well as jobs in industry requiring comparable skills. Exportable services do require many highly skilled workers, and foreign trade restrictions are depriving Americans of important job opportunities.

Further, it may be that, as presently constituted and applied, the rules of international trade work to the disadvantage of the United States. U.S. comparative advantages are more dispersed among (implying greater potential reliance for export growth on) agriculture, rapidly evolving high technology industries and services; meanwhile other major AICs in Europe and Japan and the NICs have comparative advantages that are to varying degrees more concentrated in industrial products and manufactures. The GATT has been most effective in liberalizing trade in industrial products and manufactures; its rules have only limited effects on agricultural trade practices and very limited applicability to trade in services. Further, many of the measures other countries employ to catch up with U.S. competitors are some of the most difficult to cope with under GATT rules. Hence, GATT rules may do a better job of opening up markets for our competitors than for the United States. However, such asymmetry in trade liberalization across tradeable goods and services has been tempered in recent years by the increased use of trade management devices and subsidies in many basic labor- and capital-intensive manufacturing industries—e.g., apparel, footwear and steel. To the extent that trade liberalization has been in the past or is in the future asymmetrical, it has the potential to adversely affect U.S. terms of trade and living standards.

All of this implies that U.S. efforts to bring services within the GATT, as well as efforts to liberalize trade in high technology and agricultural products, are important to ensure that the United States receives a fair share of the benefits from trade liberalization.

Efforts to liberalize trade in services will be slow and difficult. Trade distortions vary considerably among industries, and often, owing to the nature of these industries, foreign governments are generally more heavily involved in regulating markets and market access in services than in manufacturing. Nevertheless, the United States should make every effort to negotiate extension of the GATT principles of national treatment and most-favored-nation treatment to trade in full range of services and with as many countries as possible.

SYMPOSIUM: DATA ON TRADE FLOWS AND BARRIERS

EFFORTS TO IMPROVE DATA ON U.S. TRADE IN SERVICES

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Efforts to Improve Data on U.S. Trade in Services

Briefing Material: February 1986

Introduction

The inadequacies of data on U.S. international trade in services are well recognized. U.S. Government agencies are presently attempting to develop improvements in the data.

This paper explains the importance of the data, what is lacking, why it is lacking, and what is being done to develop better information.

Background

A. What is meant by the term "services"?

For purposes of data collection, the term "services" includes, but it is not limited to,

-- banking
-- insurance
-- transportation

-- communications
-- data processing
-- education
-- health care
-- tourism

-- advertising
-- accounting
-- architectural, engineering, and construction services

-- management consulting
-- professional services
-- entertainment
-- franchising

In general, these services consist of economic activities whose outputs are other than tangible goods.

B. What constitutes international trade in services?

International trade in services may take place in numerous ways, such as:

(1) Cross-border transactions, including the transmission of voice, video, data or other information and the transportation of goods and passengers from one country to another;

(2) Contractual arrangements transmitting rights to use intellectual property, technology, or other services (e.g. patents, trademarks, franchises, book, film, broadcast and recording rights);

(3) Travel of individual consumers to another country (e.g., services provided to non-resident tourists, students, and medical patients);

(4) Travel of individual producers to another country (e.g., services provided to foreign clients by business consultants, engineers, lawyers, etc.); and

(5) Sales of services (e.g., accounting, advertising, insurance) through branches or other affiliates.

Importance of Trade in Services

Employment and output in service industries are growing at faster rates than in manufacturing, mining and agriculture. Services now account for over 70 percent of employment in the United States and nearly two-thirds of the gross national product. Scientific and technological advancements, particularly in computers and communications, are making it easier to perform services internationally. The United States is giving high priority to services in trade policy because of its growth potential and because sales of services are needed to offset the growing deficits in merchandise trade in our balance of payments.

Importance of Services Trade Data

The liberalization of world markets for trade in services should lead to economic gains similar to those achieved in merchandise trade. At present, such efforts on services cannot draw upon a statistical base comparable to that for merchandise trade. More comprehensive and detailed data are needed to examine the specific effects of services trade and to place issues in proper perspective. Clearly, an improved data base would facilitate international discussions of services trade aimed toward resolving existing and emerging trade problems. In addition, trade data are needed by Government and industry for market analysis, to find business opportunities, and to promote exports of services. Thus, data improvement is a vital part of the trade program.

What Data Are Available

The primary sources of U.S. data on services trade are the balance-of-payments surveys and the international investment surveys conducted by the Bureau of Economic Analysis of the U.S. Department of Commerce.

A. Balance-of Payments Survey

Aggregate data for service transactions are available according to the following balance-of-payments classifications: travel, passenger fares, transportation, royalties and fees, private miscellaneous services, and U.S. Government miscellaneous services. The available data have been used primarily for analyzing international payments and receipts and for developing appropriate policies to assist the balance-of-payments adjustment process. Balance-of-payments statistics, designed for these purposes, provide inadequate detail on the value of services exported and imported by service industry, by type of transaction, and by country.

B. International Investment Surveys

The international investment surveys cover direct investment abroad by U.S. companies and direct investment in the United States by foreign companies. The surveys provide, not only the data necessary for preparing the direct investment estimates for the balance-of-payments accounts, but also extensive amounts for of other financial and operating data on U.S. companies and their foreign affiliates and on U.S. affiliates of foreign companies.

The surveys (both balance-of-payments and investment) show high potential for obtaining relevant detailed data on specific services.

Data Inadequacies

Data for trade in services are not on a par with data on trade in goods. While there are more than 10,000 categories for merchandise trade data, there are only six major categories for services in balance-of-payments data and fewer than two dozen in investment survey data. Not only are services trade data lacking in specific sector or industry detail and in geographic detail, they also lack the frequency of reporting of merchandise trade (i.e., monthly).

The inadequacies of services data have been recognized for some time. Several years ago the U.S. Government commissioned two studies by private consulting groups to determine what improvements were needed. These groups examined existing data and gaps in U.S. information on international trade in services.

One analysis, conducted by Economic Consulting Services Inc. (ECS) identified official and unofficial data on U.S. international services transactions for 16 selected service industries with an important stake in trade. Based on that data, ECS attempted to estimate independently the value of U.S. companies' foreign-source revenues for 1980. The estimates indicated that current official data substantially understate the extent of services trade. While the estimates were limited to data for only one year and were not comparable conceptually to official U.S. statistics, the results demonstrated the need for more comprehensive data to fully reflect U.S. international trade in services.

A second analysis was performed by Evelyn and Walther Lederer and Robert L. Sammons, who examined many of the conceptual problems in defining trade in services and developed a series of specific proposals for obtaining the needed data through Government collection and reporting. Some of the proposals dealt with ways in which balance-of-payments type data could be made more useful for non-balance-of-payments purposes and could be combined with other types of data to analyze the international services business of a country.

These two studies helped to lay the groundwork for further efforts to develop more comprehensive and detailed data.

What Is Being Done To Improve The Data

As a first step in this effort, a U.S. Government interagency task force was established in 1982 to review the existing statistics and to examine the specific needs of data users. Other functions of the task force are to:

(1) help plan the development of a comprehensive data collection and reporting system, including improvements in existing data;

(2) coordinate the work of the various U.S. agencies with an interest in the data;

(3) coordinate with the private sector to develop needed information and to assess the feasibility, cost, and burden of collecting the data;

(4) identify technical, legal, administrative, and financial problems arising from the data improvement program; and

(5) recommend ways of resolving these problems.

A private sector counterpart also was established by the U.S. Chamber of Commerce to work with the Government task force by coordinating the views of individual companies in various service industries on data needs and the means of obtaining the data without undue cost and burden.

Steps Taken

Steps already have been implemented to improve existing data. These involve the benchmark and annual surveys of direct investment, the survey of foreign contract operations, and the in-flight survey of travel and tourism.

A. Benchmark Survey of Direct Investment

The first benchmark survey, conducted by the Commerce Department's Bureau of Economic Analysis, covers data for the year 1977. The second benchmark survey, recently completed, covers data for 1982. The survey for 1982 seeks detailed data for 12 service industries not previously reported separately. The industries are: metal mining services; travel agents; franchising; research and development and commercial testing laboratories; management, consulting, and public relations services; equipment rental and leasing services, excluding automotive and computers; employment agencies and temporary help supply services; computer and data processing services; automotive rental and leasing, without drivers; health services; legal services; and educational services.

In addition, the insurance industry was split into three groupings: (1) life, (2) accident and health, and (3) other. The survey also requests, for the first time, a separate break-down or estimate of sales of services, as distinct from sales of goods, by whether the sale was to a U.S. person or a foreign person, and whether the person is affiliated or unaffiliated. The survey forms (covering calendar year 1982) were mailed in March 1983 to U.S. companies having direct investments abroad. The results of the survey, which is usually taken at 5-year intervals, became available toward the end of 1985 and some of the data were included in the December 1985 issue of the Survey of Current Business.

B. Annual Survey of Direct Investment

A new annual survey of direct investment abroad (to supplement the 5-year benchmarks) was instituted in 1984. Questionnaires for the first annual survey were mailed in August 1984. Data for calendar year 1983 became available toward the end of 1985. Some of the data are included in the January 1986 issue of the Survey of Current Business.

C. Survey of Foreign Contract Operations

Beginning in 1983, the Commerce Department's annual survey of foreign contract operations of U.S. technical and other services firms, which covers service transactions between unaffiliated parties, also was expanded to permit recording the transactions on a gross basis. In addition to data previously collected on net receipts, information is now requested on gross income or operating revenue, merchandise exports included in gross income, and foreign outlays and expenses. Also, a concerted effort is being made to increase the number of respondents to this survey.

D. Tourism and Travel In-Flight Survey

In the fourth quarter of 1982, the U.S. Travel and Tourism Administration of the U.S. Department of Commerce instituted an in-flight survey of non-U.S. citizens departing from the United States. Collection of information from U.S. citizens departing from the United States began in January 1983. The survey provides estimates of total expenditures, disaggregated by type of purchase, such as lodging, transportation, meals, entertainment, and gifts. Almost all of the resulting information is sold on a subscription basis, mainly to businesses and to tourism promotion agencies of State, local, and foreign Governments. The data on expenditures in the United States by foreign residents will be used in compiling the balance of payments, and the expenditures abroad by U.S. residents are being evaluated for possible use at a later date.

E. Staff Paper

In September 1984, the Commerce Department's Bureau of Economic Analysis (BEA) published a staff paper on U.S. International Trade and Investment in Services: Data Needs and Availability. The paper describes and evaluates available data, discusses recent efforts to improve the data, and makes suggestions for further improvement.

Further Improvements

BEA is planning to conduct a survey to obtain comprehensive information on selected service transactions between U.S. companies and unaffiliated foreign residents. This benchmark survey, which will be the first of its type, will obtain data on sales and purchases of services, by type of service, from both goods-producing and services-producing U.S. companies. It will cover services that are now covered by BEA through sample surveys, as well as services that are essentially outside the scope of those surveys.

Examples of Data Collection Problems

Among the problems in obtaining data on service trade are the method of collection, the coverage of transactions, the classification of certain service activities, and the kinds of data needed for analysis.

(1) Method of Collection

Unlike merchandise trade, which is counted as an export and import in Customs documents when goods cross national boundaries, the vast majority of service transactions is not accompanied by documents which are collected for statistical purposes by government offices at border points. In the absence of documents on individual transactions, data on trade in services generally are derived from questionnaires which are completed periodically by respondents from their own records. Similar transactions will have to be reported consistently from one company to the next. Complete and consistent reporting of transactions will depend upon the manner in which records are kept by respondents as well as clear and uniform understanding of the types of transactions to be included. This will require diligence on the part of both the statistical collection agency and the reporting businesses. Diligence will also be necessary to avoid duplication of reporting on the various survey forms.

(2) <u>Coverage</u>

Full coverage of international trade in services requires data collection for all types of transactions, including the five basic types listed above. Because not all of the transactions would enter the balance-of-payments accounts, additional information will be required covering such items as sales abroad by foreign affiliates. Where available, such data can be reviewed in conjunction with balance-of-payments-type data to give a more complete picture of a country's total international services business--including sales through each of the channels mentioned above.

In services, a substantial portion of trade is conducted through foreign affiliates, partly because it is often necessary, for legal or marketing reasons, to establish a presence in a foreign market in order to do business there. To isolate the cross-border or home office content of the affiliate's final sales, it will be necessary to secure information on the value of services performed by the home office for the affiliate. It is highly unlikely that such information would be available for each transaction. Rather, it would be recorded on an annual basis. The detail available will vary according to individual company practices and the manner in which records are kept. Some companies may charge different accounts, as for example, "auditing" "management services", "fees and royalties", or "advertising", other companies may simply charge an account called "business support services". While the data may not be entirely consistent in detail, it is essential to determine the equivalent home office content of sales by overseas affiliates to derive a total for all types of cross-border transactions.

Services transactions between unaffiliated firms present other problems. Such transactions are likely to be distributed across a much larger number of firms trading in relatively small volume and to be more sporadic. Transactions between unaffiliated firms furthermore tend to be less intensively surveyed than transactions between affiliates.

Many business enterprises produce both goods and services. It is intended that all service transactions be covered in the data regardless of the industry in which an enterprise is classified, i.e., a goods-producing or service-producing industry.

In addition, a problem in all types of surveys is the difficulty of locating all possible respondents, including newly established companies.

(3) Classification

The delineation of boundaries between individual sectors is complicated by the nature of some service activities which include or overlap activities of other sectors. Conceivably, for example, "telecommunication" services could encompass, not only the transmission and reception of video, voice, and data, but also the material that is broadcast (news, information, entertainment, data processing) and the activities that provide the means of communication (launching of satellites, laying of undersea telephone cables). Other examples of sectors with overlapping service activities are franchising (a primary activity for some firms, but secondary for others principally engaged in such services as hotel management, auto rental, and fast-food restaurants, etc.); tourism (encompassing the activities of several individual industries -- travel agencies, transportation, travel insurance, hotels, restaurants, entertainment, etc.); and educational services (performed primarily by schools, but also by insurance companies, financial advisors, management consultants, data processing companies, accountants, tax preparers and even manufacturing firms, which may offer specialized forms of instructional services related to their own products).

Goods and services sold or provided jointly in a package also present problems of classification. Examples include goods sold with service contracts, guarantees and warranties; the cost of providing temporary engineering assistance and maintenance and the cost of training workers to operate machinery; and tourist expenditures which include purchases of goods, such as souvenirs and gifts, as well as services, such as transportation and lodging.

Classification requires practical decisions to be made based on intended uses of the information. If the basic information is available in sufficient detail, it can be combined in a variety of ways to satisfy different needs.

(4) Kinds of Data

Sales (or, for some industries, total revenues) and purchases may well be the standard items used in valuing international services transactions for all industries. However, for most industries, other types of data will be needed for analytical purposes. Advertising agencies usually report total billings, including the cost of advertising space, time, and materials, as opposed to revenues accruing to their firms. Insurance companies report total insured values as well as premiums, but net amounts (after deducting claims paid) may also be necessary. Measurement of banking services requires distinguishing between interest, other portfolio income, and non-interest income. For the construction industry, the value of contract awards may be needed in addition to gross or net revenues received when various stages of construction jobs are completed.

Decisions as to what additional information is needed will have to be made on the basis of the analytical requirements of each industry where the standard measures are judged insufficient.

International Comparability

The United States and other countries report balance-of-payments data to the International Monetary Fund (IMF). The IMF Balance of Payments Manual provides guidelines and definitions to facilitate international comparability of the reported data. In an annual publication, the IMF converts data reported in local currencies into a common unit -- Special Drawing Rights (SDRs). The data published by the IMF, however, do not show separately the value of trade in individual service industries.

As countries seek to develop more comprehensive and refined data on international trade in services, the need to attain international comparability of data should be recognized. Comparability problems already exist, partly because of the vast amount of economic activity covered by balance-of-payments data and the complicated nature of modern business transactions. Cooperation and exchange of information among countries are needed to assure the maximum international comparability of statistics. An exercise of this kind currently is underway in the Organization of Economic Cooperation and Development (OECD).

Conclusion

No country or international organization compiles data in a manner that fully and accurately measures services trade activities and disaggregates the data to reflect the activities in individual service sectors. Considerable work by individual countries lies ahead in developing the methodology and data collection systems for improving the services data base.

The United States will continue to work toward more comprehensive and detailed data coverage of international service transactions. Of all the numerous refinements described, perhaps the most crucial are: determining, by sector, how trade in services should be measured; developing the necessary intelligence and strategy for surveying the appropriate universe or samples of services transactions; and refining the survey questions so as to generate the information needed to separate the home office (U.S.) content from the overseas affiliate content in the value of services performed. To establish a more useful and meaningful body of data for services trade, cooperation with the private sector is essential.

During the process of developing data improvements, the United States will exchange information and ideas with other countries so that a greater degree of international comparability can be achieved.

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Some Estimates of Trade Flows in Banking Services[1]

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I. Introduction

Those who advocate including services in a future GATT negotiating round base their case, in part, on the alleged growing importance of trade in services. These claims are based on estimates of service trade derived from balance of payments (BOP) data, even though it is widely recognized that individual service items cannot be identified in these accounts since they are recorded both as part of merchandise trade estimates and as part of the broader receipts and payment of fees, royalties, and investment income (i.e., invisibles).

This paper presents some estimates of international trade in one key service category, banking services, obtained using an alternative method. In the process, we also raise the conceptual issue as to what the measurement of international trade in banking services should include and perhaps more importantly not include. This issue, it turns out, has substantial relevance to the wider debate on trade in services.

We use IMF data on assets and liabilities of both domestic banks and non-banks with foreign banks, and of foreigners with the domestic banking system to construct measures of the volume of transactions on which banking intermediation services are provided across national borders. We then use estimates of the spread between borrowing and lending rates for depositors and borrowers with the financial institutions involved to estimate the value of international flows of intermediation services. We apportion these estimates between depositors and borrowers; and on this basis, make calculations of the value of financial intermediation services traded across national boundaries.

Estimates are presented for three years in the early 1980's for three countries: the U.S., the U.K., and Canada. For the early 1980's, our calculations suggest that the value of international trade flows in banking services is small. For the U.S., exports are perhaps around $3-5 billion per year.

Our approach to measuring trade in banking services recognizes that the main service which banks provide is one of financial intermediation between depositors and borrowers. Depositors and borrowers both use banks to economize on transactions costs in locating one another for the purpose of effecting mutually advantageous trades. Depositors postpone consumption in return for interest payments by borrowers on their deposit. They also pool risks of default, reducing the variance of their expected returns on their savings. International flows of banking services occur where banks located in one country provide financial intermediation services to borrowers or depositors located in other countries.

This may seem to be a relatively straightforward concept on which to base a measure of international flows of banking services, but in the literature on service trade which has appeared thus far, international flows of banking services are often equated with the foreign source income of domestic banks. These, of course, are quite different. Our estimates of exports of banking services by the U.S. of $3-5 billion in the early

1980's with estimates of foreign source income accruing to U.S. banks of $23.2 billion for 1977 (the latest year for which official estimates are available; see Whichard (1984)).

The implication for the debate on trade in services is that international flows in banking services may be relatively small; but since the importance of the service trade issue is to a great extent measured in terms of foreign affiliate revenues it may well be overemphasized. The fundamental issue with trade in services which many authors have raised is whether the main issues for service industries in fact relate to questions of establishment rights and discriminatory regulations such as those faced by banks in their international operations. Strictly speaking, these are investment rather than trade- related issues, and our estimates seem to confirm this.

II. Services, Balance of Payments Data, and the Treatment of Banking

In attempting to measure international trade in banking services, the wider issues involved in measuring trade in services are readily apparent. There is little, if any, consensus as to what constitute traded services, and available data is very limited. Definitions of service trade vary between two extremes; one restricted to services which actually cross national borders, the other incorporating all non-merchandise and non-transfer items reported in the Balance of Payments current account.

Nevetheless, the most widely used estimates of service trade flows are all based (in one way or another) on Balance of Payments data. These accounts, reported on a national basis, record all transactions between residents of a country and the rest of the world (i.e., flows of real resources, transfers and change in assets or liabilities). The current account of the BOP reports merchandise trade and trade in invisibles.[2] The capital account records all financial transactions.

Table 1 summarizes the main BOP items from the IMF Balance of Payments Manual. Invisibles include a number of more readily identifiable service categories such as travel, transportation and freight. Remaining services appear in one miscellaneous category which includes insurance, fees, commissions, royalties and copyrights, construction services, communications and advertising (see the right-hand inset in Table 1).

Listing these items in this way demonstrates the difficulties in separating service transactions on a functional basis. Various services generate fees, royalties, copyrights and commissions. BOP data does not provide any information on the specific activities from which these arise. Constructing estimates of international services flows for such categories as accounting, data processing, education, engineering, franchising, health care, leasing and renting, management consulting, public relations, law and other professional, marketing and technical

[2]It is important to note that invisibles refer to transactions which relate neither to goods flows nor to capital movements.

Table 1

Items Included in Typical Country Balance of Payments Accounts

A. Goods and Services (Items 1 through 8)
 1. Merchandise
  1.1 Exports f.o.b., Imports
  1.2 Other merchandise (net)
 2. Nonmentary gold
 3. Freight and insurance on international shipments
  3.1 Freight
  3.2 Insurance
 4. Other transportation
  4.1 Passenger fares
  4.2 Time charters
  4.3 Part expenditures
  4.4 Other
 5. Travel
 6. Investment income
  6.1 Direct investment income
  6.2 Other dividends
  6.3 Other
 7. Government, not included elsewhere
  7.1 Military transactions
  7.2 Nonmilitary transactions
 8. Other services
  8.1 Nonmerchandise insurance
  8.2 Other

  Memorandum item: factor income
   (item 6 and part of items 7 and 8

B. Transfer Payments (Items 9 plus 10)
 9. Private[1]
  9.1 To and from foreign governments
  9.2 Other
 10 Central government
  10.1 Intergovernmental
  10.2 Other

Other Services Includes
 1. Nonmerchandise insurance (1.1 through 1.4 = item 8.1)
  1.1 Premiums on direct insurance
  1.2 Claims on direct insurance
  1.3 Premiums on reinsurance
  1.4 Claims on reinsurance
 2. Other (2.1 through 2.12 = item 8.2)
  2.1 Personal income
  2.2 Management fees
  2.3 Underwriters' commissions
  2.4 Agents' fees
  2.5 Construction activity
  2.6 Communications
  2.7 Advertising
  2.8 Subscriptions to press
  2.9 Film rentals
  2.10 Copyrights and patent royalties
  2.11 Real estate rentals
  2.12 Other
 3. Total (1 plus 2 = item 8)
 4. Memorandum item:[2] factor income

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[1] All residents other than the central government.

[2] Item specified for reconciliation with national accounts.

Source: IMF Balance of Payments Manual, 1966, Tables A & VIII service is simply not possible from BOP. Service transactions in the BOP are recorded by type of service only in a small number of cases (i.e., travel, transportation, insurance). The rest are classified according to the type of payment associated with services provided (e.g., royalties, fees, and commissions). Even the receipts and payments of investment income in effect include a service component.[1]

Banking is a good example of these problems. In the U.K. BOP,[2] for instance, the receipts from overseas operations of national banks include the net receipts of banks from services provided to "non-related" customers, (including arbitrage as well as banking charges and commissions); the net receipts for services rendered to overseas branches, subsidiaries and associates of national banks; the net receipts on lending and borrowing involving overseas residents; and the interest, profits and dividends accruing to nationals from overseas branches, subsidiaries and associates of national banks. The first two items are included in "other services", and the second two as

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[1]Stalson (1985) refers to "intractable conceptual difficulties" in both collecting and interpreting U.S. data on services.

[2]UK Central Statistical Office, United Kingdom Balance of Payments 1963-73, London. Her Majesty Stationery Office, 1974, p. 70.

part of investment income.[1]

These items, however, do not provide a measure of international trade in banking services, since the service provided by banks is that of financial intermediation. In most cases there is no explicit charge for this service, except for fees and commissions which are relatively minor. The charge for the service is implicit in the difference between the interest rate charged to borrowers, and the rate of interest paid to depositors. The BOP data record estimates of the income flows generated by banks from their international activities and (the value of intermediation services actually traded internationally (except for fees and commission)) is an unidentified portion of these estimates.

Moreover, for the most part, the activities included in the BOP do not relate to transactions which occur between countries. A U.S. bank affiliate acting as a financial intermediary between two non-residents is generating investment income for the parent bank, not engaging in international trade. While one can argue that it is establishing a presence abroad that allows such transactions to occur; and therefore some element of the income return should be included as trade, it is impossible to distinguish the trade element from the investment element.

What is required is a more direct measure of the value

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[1]This treatment is approximately the same in the BOP accounts for the U.S. and Canada. The U.K. BOP treatment is described here because of the clear description of sources and methods of construction provided for these accounts.

of banking services actually traded internationally. Ideally this estimate should include all fees and charges accruing to domestic banks from non-residents, including their foreign affiliates, plus an imputed financial service charge covering the value of intermediation services traded between non-residents; much the same as that used in the National Accounts to measure the value of services rendered by national banks to domestic residents.

III. An Estimate of International Trade Flows in Intermediation Services Provided by Banks

Because the BOP estimates do not distinguish the various commponents of receipts and payments associated with banking activities, we have used an alternative method to construct estimates of international trade in intermediation services provided by both domestic and foreign banks. We have done this for three countries (the U.S., the U.K., and Canada), for the years 1982-84.

The method we use involves applying estimates of the spread between deposit and lending rates both for U.S., U.K., and Canadian banks, and banks in their largest partner countries to corresponding data on assets and liabilities of both domestic banks with non-residents, and non resident banks with residents. These yield an estimate of the value of intermediation services provided by domestic banks to both depositors and borrowers abroad, and by non-resident banks to domestic depositors and borrowers. The combined financial intermediation charge is apportionned between the parties to calculate the internationally traded component.

International Financial Statistics (1985) provides data on inter-country asset and liability positions of resident and non-resident banks. Estimates of intermediation services exported by countries are based on the sum of foreign non-bank deposits with domestic banks (cross-border bank deposits of non-banks by residence of borrowing bank); loans to foreign non banks (cross-border bank credit to non-banks by residence of lending bank); and loans to foreign banks (cross-border inter-bank claims by residence of lending bank). Intermediation services imported by countries are based on the sum of deposits of domestic non-banks with foreign banks (cross border bank deposits of non-banks by residence of depositor); loans to domestic non-banks by foreign banks (cross border bank credit to non banks by residence of borrower); and loans to domestic banks (cross-border inter-bank liabilities by residence of borrowing bank).

Table 2 reports both the consolidated claims and liabilities of domestic banks and non-banks with foreigners, and claims and liabilities of foreign banks involving domestic residents. Data on rate spreads from OECD Financial Statistics Monthly are reported in Table 3. These clearly have to be interpreted with caution; but for the purposes of the calculation we make, are unfortunately all that is available. Data on rate spreads in Japan, for instance, are distorted by domestic financial regulation. Also, the variance in rate spreads by country

Table 2

Claims and Liabilities, Domestic and Foreign Banks,

U.S., U.K., and Canada, 1982 - 1984

(Billions of U.S. Dollars)

	United States			United Kingdom			Canada		
	1982	1983	1984	1982	1983	1984	1982	1983	1984
Claims and Liabilities of Domestic Banks with Foreigners									
Foreign Non-bank Deposits	45.55	58.83	67.45	137.61	149.66	147.08	18.99	25.00	27.18
Loans to Foreign Non-banks	107.95	121.23	118.61	142.79	149.67	144.85	7.13	7.76	7.44
Loans to Foreign Banks	294.06	308.74	324.21	320.08	335.53	344.78	31.02	33.21	34.04
TOTAL	447.56	488.80	510.27	600.43	634.86	636.71	57.14	65.97	68.66
Claims and Liabilities of Foreign Banks with Domestic Residents									
Domestic Non-bank Desposits	152.36	167.91	161.49	17.72	20.48	20.76	10.98	11.38	12.76
Loans to Domestic Non-banks	57.54	56.52	68.24	13.75	15.98	13.84	11.18	10.61	11.01
Loans to Domestic Banks	208.91	246.93	269.47	349.19	365.62	384.39	38.81	36.36	34.83
TOTAL	418.81	471.36	499.2	380.66	402.08	418.99	60.97	58.35	58.60

Source: International Financial Statistics, 1985 Yearbook, p. 64-75, IMF, Washington, D.C.

Table 3

Interest Rate Spreads Between Depositors and Borrowers By Country

1982, 1983, 1984

Countries for which Trade in Intermediation Services are Calculated

	1982	1983	1984
United States			
1) Large time deposits	12.27	9.07	10.47
2) Prime rate	14.86	10.79	12.05
Implicit service charge	1.29	0.86	0.79
United Kingdom			
1) Sterling certificates of deposit	12.21	10.08	9.88
2) Overdraft (minimum rate)	12.93	10.79	10.68
Implicit service charge	0.36	0.35	0.40
Canada			
1) 90-day deposit receipts	14.06	8.25	9.98
2) Chartered banks prime lending rate	15.99	11.23	12.09
Implicit service charge	0.96	1.49	1.05
Other Partner Countries			
Germany			
1) Time deposits (3 months)	7.54	4.56	4.86
2) Discount credits	9.53	6.00	6.09
Implicit service charge	0.99	0.72	0.61
Switzerland			
1) 3-month deposits	4.29	3.35	3.81
2) Commercial bank's overdraft	7.14	5.82	5.91
Implicit service charge	1.42	1.23	1.05
Japan			
1) Time deposits (1 year)	5.75	5.75	5.50
2) Standard rate	6.00	5.92	5.50
Implicit service charge	0.12	0.08	0
France			
1) Time deposits (up to 6 months)	9.31	8.24	7.66
2) Bank's prime lending rate	13.62	12.25	12.15
Implicit service charge	2.16	2.01	2.24
Belgium			
1) Overdrafts with commercial banks	16.93	13.68	14.41
2) 1-year cash certificates	9.00	8.79	8.96
Implicit service charge	3.97	2.44	2.72

Source: Financial Statistics Monthly, OECD, January 1983, 1984, 1985.

Table 4

Estimates of International Trade in Financial Intermediation Services, U.S., U.K., and Canada 1982-84

	United States			United Kingdom			Canada		
	1982	1983	1984	1982	1983	1984	1982	1983	1984
Domestic Implicit Service Charge for Intermediation (%)	1.29	0.86	0.79	0.36	0.35	0.40	0.96	1.49	1.05
Foreign Implicit Service Charge for Intermediation (%)	0.79	0.67	0.61	1.49	1.11	1.05	0.99	0.68	0.64
Estimate of Bank Services Exports[1] (Billions of US dollars)	5.77	4.20	4.03	2.16	2.22	2.55	0.55	0.98	0.72
Estimate of Bank Services Imports[1] (Billions of US dollars)	3.31	3.16	3.04	5.67	4.46	4.40	0.60	0.40	0.42

[1]Assuming intermediation costs are borne equally by depositors and borrowers.

reflects both differences in financial regulation across countries, and the form of financial transactions in which the various national banks engage. Spreads are smaller for the U.K. than for most other countries because charges for bank-to-bank intermediation services are smaller per dollar transacted than for bank-to-non-bank intermediation and U.K. banks engage in more bank-to-bank intermediation activity.

Despite these problems this data on rate spreads has been used along the consolidated country data on inter-country claims and liabilities reported in Table 2 to estimate the value of intermediation services traded by the U.S., the U.K., and Canada for each of three years. These are reported in Table 4. In making these calculations the value of intermediation services has been apportioned between borrowers and lenders using an equal weighting assumption. Because the number of partner countries is so large in each case, we use data on rate spreads for only the more important countries displayed in Table 3, and construct weighted averages using the country composition of assets and liabilities.

While clearly dependent on the interest rate spreads used, the striking feature of these estimates of international flows of banking services from Table 4 is their relatively small size. For the U.S., for instance, international trade flows in banking services are in the range of $3-5 billion per year in the 1980's. This contrasts with estimates of foreign affiliate sales of U.S. banks of $23.2 billion for 1977 (the latest year available). This difference emphasizes that foreign investment income accruing to U.S. parent banks as a result of operations abroad does not appear to necessarily indicate large international trade in intermediation-type banking services. Service trade, as it relates to banking, may be an important investment issue, but does not appear to be that important a trade issue.

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FEBRUARY 1986

CANADA'S INTERNATIONAL TRADE IN SERVICES

STATISTICS CANADA

BUSINESS SERVICES*
AS PERCENTAGE OF GNP,
SELECTED YEARS

	RECEIPTS	PAYMENTS
	%	
1965	0.5	0.9
1970	0.8	1.4
1975	0.9	1.3
1980	1.1	1.6
1984	1.0	1.5

* INCLUDES MINOR AMOUNTS OF TRANSACTIONS SUCH AS EARNINGS OF MIGRANTS' WORKERS.

CANADA'S CURRENT ACCOUNT

	1984 Receipts	1984 Payments
	$ Million	
I MERCHANDISE TRANSACTIONS	112,118	91,450
II NON-MERCHANDISE TRANSACTIONS	22,507	40,623
A. SERVICE TRANSACTIONS		
Travel	4,416	6,542
Interest & Dividends	1,839	13,093
Freight & Shipping	4,647	3,979
Other Service Transactions		
- Government transactions	616	1,102
- Miscellaneous income	3,257	5,913
- Business services and other transactions	4,416	6,518
Withholding Taxes		1,100
B. TRANSFERS	3,316	2,376
III TOTAL CURRENT ACCOUNT	134,626	132,073

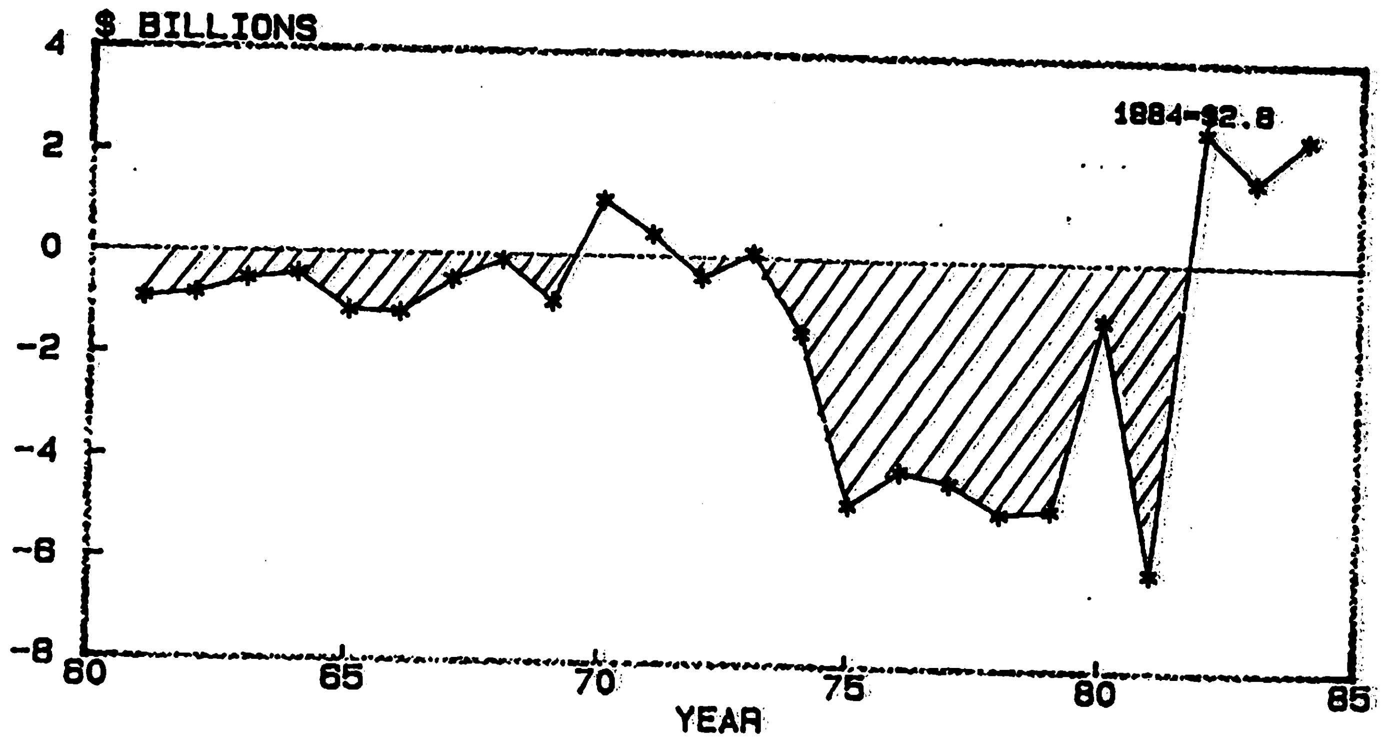
CANADA'S CURRENT ACCOUNT

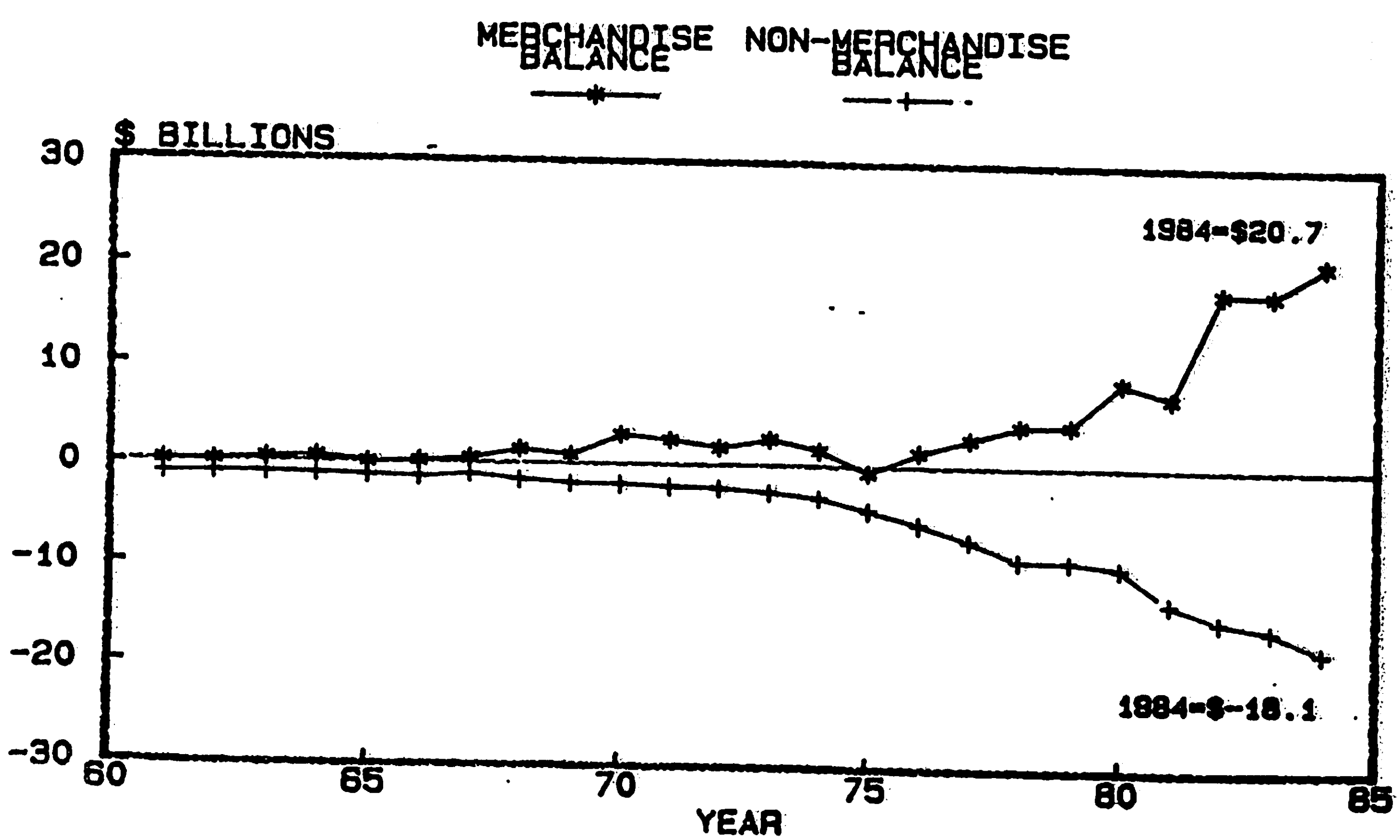
% SHARE OF SELECTED COMPONENTS

	1961	1971	1984
RECEIPTS	100.0	100.0	100.0
Merchandise	74.5	77.6	83.3
Non-Merchandise	25.5	22.4	16.7
Investment Income	3.8	4.1	3.8
Services	18.2	14.5	10.4
(Business Services)	(2.6)	(3.2)	(3.3)
Transfers	3.5	3.8	2.5
PAYMENTS	100.0	100.0	100.0
Merchandise	64.7	67.7	69.2
Non-Merchandise	35.3	32.3	30.8
Investment Income	10.3	10.0	14.4
Services	21.0	19.6	14.6
(Business Services)	(4.4)	(5.8)	(4.9)
Transfers	4.0	2.7	1.8

CURRENT ACCOUNT BALANCE

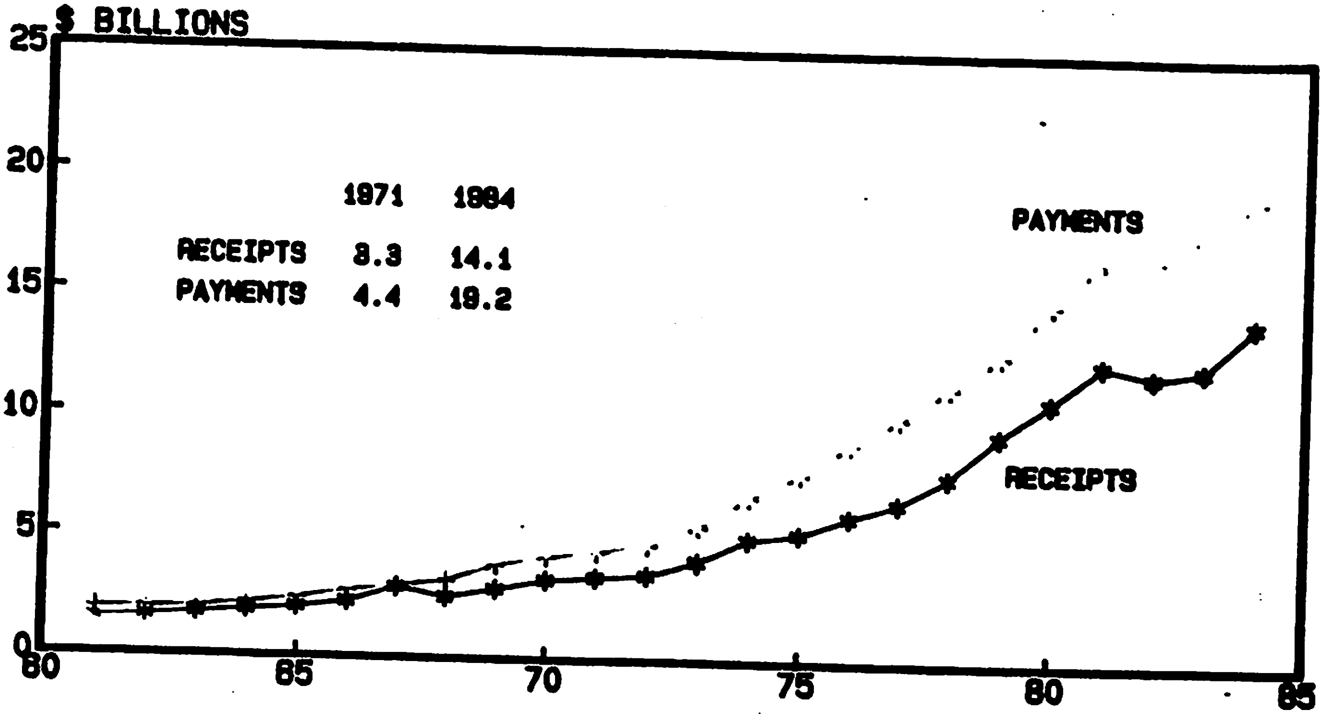
1961 TO 1984





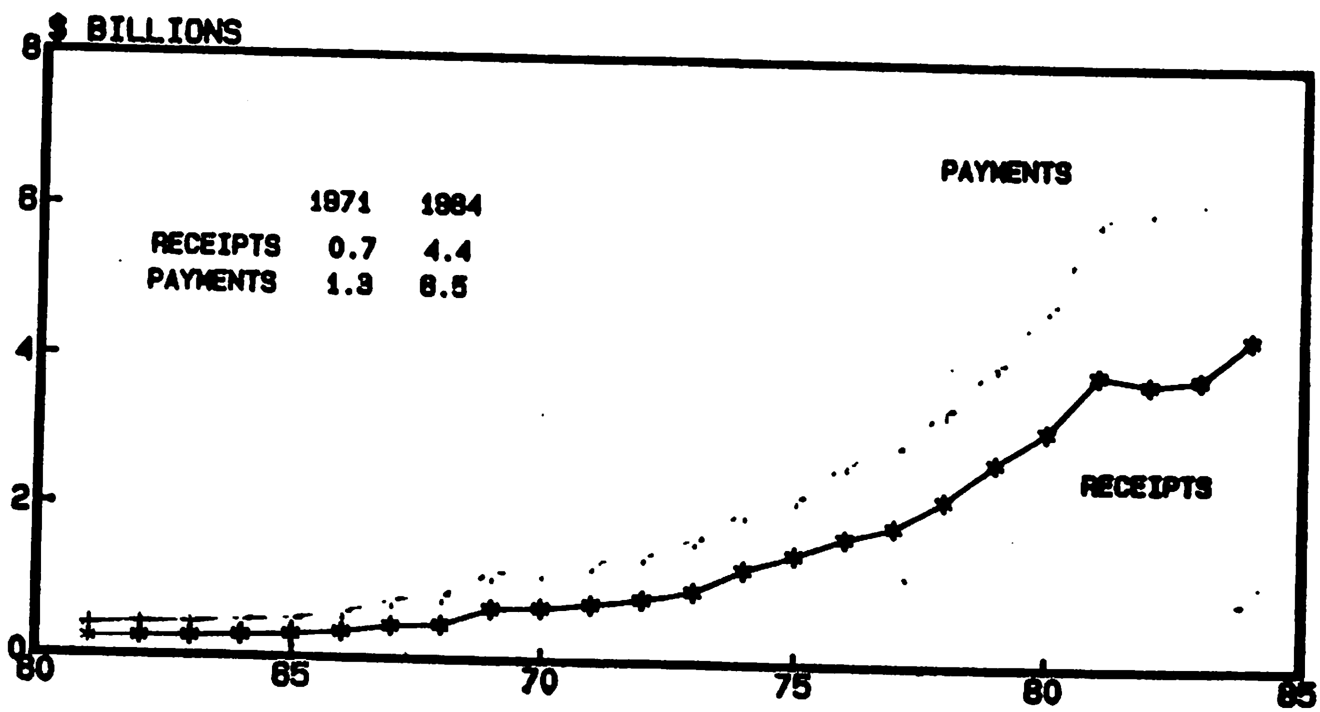
CANADA'S INTERNATIONAL TRADE IN SERVICES

TOTAL*



* EXCLUDES INVESTMENT INCOME TRANSACTIONS

BUSINESS SERVICES & OTHER TRANSACTIONS



CANADA'S INTERNATIONAL TRADE IN BUSINESS SERVICES AND OTHER TRANSACTIONS

1981

	RECEIPTS	PAYMENTS
	($ MILLION)	
. QUADRENNIAL SURVEY RESULTS: TOTAL	2,011	3,622
- CONSULTING AND OTHER PROFESSIONAL SERVICES		
- INSURANCE TRANSACTIONS		
- MANAGEMENT AND ADMINISTRATIVE SERVICES		
- SCIENTIFIC RESEARCH AND PRODUCT DEVELOPMENT		
- COMMISSIONS		
- ROYALTIES, PATENTS, TRADEMARKS AND FILM RENTALS		
- ADVERTISING AND SALES PROMOTION		
- COMPUTER SERVICES		
- EQUIPMENT RENTALS		
- FRANCHISES AND SIMILAR RIGHTS		
- OTHER SERVICES		
. OTHER	1,904	2,387
BUSINESS SERVICES AND OTHER TRANSACTIONS	3,915	6,009

CANADA'S INTERNATIONAL TRADE IN BUSINESS SERVICES

ADDITIONAL DETAIL

1. By Type of Service
   - Geographical (US, UK, Other EEC, Japan, Other OECD, Other)
   - Industry (selected)
   - Country of control (US, UK, Other)
   - Affiliate - non-affiliate

2. At aggregate level
   - Province of head office
   - Industry

CANADA'S INTERNATIONAL TRADE
GEOGRAPHICAL DISTRIBUTION IN PERCENTAGE
1984

	U.S.	U.K.	Other EEC	Japan	Other OECD	Other	Total
Receipts:							
Merchandise	76	2	4	5	2	11	100.0
Services (1)	58	7	7	5	4	19	100.0
Business services	54	8	9	3	4	23	100.0
Payments							
Merchandise	72	3	6	6	3	10	100.0
Services (1)	66	8	9	2	4	12	100.0
Business Services	74	8	6	2	3	8	100.0

(1) Includes: Travel, Freight and shipping, Business services and other transactions.

TRADE IN BUSINESS SERVICES

MANUFACTURING AND OTHER INDUSTRIES, 1981

PERCENTAGE

INDUSTRY	RECEIPTS	PAYMENTS
	%	
MANUFACTURING	22	36
OTHER	78	64
TOTAL	100	100

TRADE IN BUSINESS SERVICES

BY COUNTRY OF CONTROL, 1981

PERCENTAGE

COUNTRY OF CONTROL	RECEIPTS		PAYMENTS
		%	
CANADA	71		50
UNITED STATES	24		45
OTHER COUNTRIES	5		5
TOTAL	100		100

CANADA'S INTERNATIONAL TRADE IN BUSINESS SERVICES

CURRENT AND FUTURE DEVELOPMENTS

A) CLASSIFICATION

B) COVERAGE

C) FREQUENCY

BUSINESS SERVICES

BREAKDOWN

- Business Services
  - Equipment Rentals
  - Advertising and Sales Promotion
  - Tooling and Other Automotive Charges
  - Transportation
  - Consulting & Other Professional Services
  - Management & Administrative Services
  - Commissions
  - Scientific Research & prod. Development
  - Royalties, Patents & Trademarks
  - Films and Broadcasting
  - Franchises and Similar Rights
  - Computer Services
  - Communications
  - Financial Services
    - insurance
    - other financial services
  - Other

CANADA'S CURRENT ACCOUNT PRESENTATION

CURRENT	PROPOSED
I MERCHANDISE TRANSACTIONS	I MERCHANDISE TRANSACTIONS
II NON-MERCHANDISE TRANSACTIONS	II NON-MERCHANDISE TRANSACTIONS
A. SERVICE TRANSACTIONS	A. SERVICE TRANSACTIONS
INCLUDING INVESTMENT INCOME	EXCLUDING INVESTMENT INCOME
	B. INVESTMENT INCOME
	INTEREST
	DIVIDENDS
	OTHER
B. TRANSFERS	C. TRANSFERS
III. TOTAL CURRENT ACCOUNT	III. TOTAL CURRENT ACCOUNT

CANADA'S INTERNATIONAL TRADE IN BUSINESS SERVICES

COVERAGE & FREQUENCY

. COVERAGE

- OTHER SURVEYS AT STATISTICS CANADA
- ADMINISTRATIVE DATA
- OTHER

. FREQUENCY

- CURRENTLY:
  QUADRENNIAL
- STARTING WITH THE 1985 REPORTING YEAR
  ANNUAL (?)

ANALYTICAL STUDIES

CHARACTERISTICS OF SERVICE EXPORTING/IMPORTING FIRMS

. CURRENTLY

(QUADRENNIAL)

- EXPORT-IMPORT OF SERVICES FOR ABOUT 20 CATEGORIES
- GEOGRAPHICAL DISTRIBUTION:

  U.S. U.K. JAPAN OTHER E.E.C. OTHER O.E.C.D. OTHER
- INDUSTRY OF EXPORTERS-IMPORTERS
- AFFILIATION
- PROVINCIAL DISTRIBUTION

. POTENTIALLY

(BY RELATING TO OTHER DATABANKS IN STATISTICS CANADA)

- TOTAL SALES OF FIRMS
- ASSETS
- EMPLOYMENT
- SIZE
- MERCHANDISE IMPORTS OF SERVICE IMPORTING FIRMS
- MERCHANDISE EXPORTS OF SERVICE EXPORTING FIRMS (DEPENDS ON THE CODING OF MERCHANDISE EXPORT FILE)
- OTHER

SYMPOSIUM PAPER SERIES INDEX

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