Staff Working Paper ERSD-2006-06 **May 2006**

World Trade Organization

Economic Research and Statistics Division

SERVICES TRADE LIBERALIZATION AT THE REGIONAL LEVEL: DOES SOUTHERN AND EASTERN AFRICA STAND TO GAIN FROM EPA NEGOTIATIONS?

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Manuscript date: *May 2006*

SERVICES TRADE LIBERALIZATION AT THE REGIONAL LEVEL: DOES SOUTHERN AND EASTERN AFRICA STAND TO GAIN FROM EPA NEGOTIATIONS?

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- May 2006 -

Abstract:

This paper discusses the opportunities and challenges for Southern and Eastern African ACP countries of services negotiations in the context of European Partnership Agreements. The paper provides an overview of existing flows in services from and to Southern and Eastern Africa, an overview that suffers from the paucity of relevant data. Given the significant differences among services sectors, the paper provides a separate discussion for several of them, including financial services, tourism and business services. The latest developments in each sector are described and the issues that are at stake in trade negotiations. In this context the competitive position of Southern and Eastern African countries is compared with the position of the European Union and other global players. The paper attempts to identify possible export opportunities for Southern and Eastern African ACP countries and discusses the advantages and disadvantages of giving preferential access to EU suppliers in those services sectors where African countries are likely to import. Particular attention is paid to the role of mode 4 in the discussed services sectors.

JEL classification: F13, F15, O19.
Key words: regional trade agreements, trade in services, GATS, Africa.

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[1] The opinions expressed in this paper should be attributed to the author. They are not meant to represent the positions or opinions of the WTO and its Members and are without prejudice to Members' rights and obligations under the WTO. I thank Monia Mimouni for statistical assistance and Rolf Adlung, Pierre Latrille, Joscelyn Magdeleine, Calvin Manduna, Hildegunn Nordås and Lee Tuthill for comments on earlier versions of this paper. Any remaining errors are mine.

A. SERVICES SECTOR NEGOTIATIONS IN THE CONTEXT OF EPA: WHAT IS AT STAKE

The Cotonou Partnership Agreement (CPA), signed in 2000 and ratified in 2003 provides for Economic Partnership Agreements (EPAs) between the European Union (EU) and African, Caribbean and Pacific (ACP) countries to be extended to services. In principle ACP countries are not obliged to start EPA negotiations on services, but if they do the liberalization of services should be in accordance with the provisions of GATS. GATS Article V requires regional agreements to have "substantial sectoral coverage" and elaborates in a footnote that this "condition is understood in terms of number of sectors, volume of trade affected and modes of supply".[2] The requirements in GATS Article V concerning the sectoral coverage of regional agreements are drafted rather loosely. Nevertheless it should be expected that EPAs encompassing services are more ambitious in their objectives and go well beyond the GATS in terms of liberalization.

Although much of the analysis in this paper will be relevant for ACP countries in general, its focus is on ACP countries situated in Southern and Eastern Africa. Most of these countries are simultaneously pursuing multilateral negotiations for the services sector in the context of the Doha Development Round[3]. This is not the case for all of them, as Comoros, Eritrea, Ethiopia, Seychelles and Sudan are not currently Members of the WTO. One of the main questions this paper asks is whether preferential liberalization in the context of EPAs is likely to be preferable or not to multilateral liberalization. In general, different layers of regional and multilateral arrangements reduce transparency, raise transaction costs related to trade and create additional administrative costs.[4] This aspect is particularly relevant for Southern and Eastern African ACP countries as all of them are members of at least one African regional trade agreement.[5] The administrations of these countries also tend to face serious resource limitations. Concerns thus quite naturally arise about the costs for ACP countries of pursuing liberalization with EU countries at a different speed than multilateral liberalization.

On the other hand, process in the multilateral liberalization of services has so far been slow and preferential liberalization in the context of EPAs may be preferable to no liberalization. Indeed, Mattoo and Fink (2002) argue that, compared to the status quo, a country is likely to gain from preferential (e.g. regional) liberalization of services trade at any particular point in time – in contrast with the more ambiguous conclusions emerging for goods trade. In goods trade, where tariffs are the main instrument of protection, the trade-creating benefits of preferential liberalization could be offset by the costs of trade diversion reflected in a loss of tariff revenue. However, in services, trade barriers do not generate revenue for the government –import tariffs are rarely used to restrict trade – and barriers are often prohibitive. Consequently, there are few costs of trade diversion.

While the arguments in the previous paragraph hold for services trade in general, other arguments in favour or against preferential liberalization are sector specific. Mattoo and Fink (2002) emphasise the role of location-specific sunk costs in certain services sectors, like professional services, telecommunications, finance and distribution. They argue that in the presence of such fix costs the

[2] Also, in order to meet GATS requirements, agreements should not provide for the *a priori* exclusion of any mode of supply. The meaning of the word "substantial" has been a subject of intensive discussions and the paucity of existing data on services trade adds to the difficulty of interpreting this and other requirements with precision. See also the discussion in Stephenson (2002) and Feketekuty (2000).

[3] The Hong Kong Ministerial Declaration (2005) explicitly acknowledges that least-developed countries (LDCs) are not expected to undertake new commitments.

[4] See also the discussion in Stephenson (2002) and Mattoo and Fink (2002).

[5] This paper alludes to the economic implications for the services sector of overlapping regional arrangements within Africa, but will not discuss their legal and political implications. EU free trade agreements with third countries, like the MED Agreements with Mediterranean countries or the TDCA with South Africa, also affect the economic outcomes of EPA negotiations. See Ulrich (2004) for a discussion of the role of services in those agreements.

advantage given to regional providers in the context of regional liberalization may persist even if countries decide to liberalize multilaterally later on. The entry of more efficient service providers may be durably deterred if their competitive advantage does not offset the advantages conferred by incumbency. In other words, sequencing matters and may matter a lot when it comes to trade in services. How much it matters depends on whether the provider who benefits from preferences is the most efficient provider globally. In the context of the Southern and Eastern African ACP countries this comes down to asking the question whether it is costly to give preferential access to regional suppliers (e.g. Egypt, Mauritius, South Africa) and/or EU suppliers rather than opening markets to the entry of other suppliers like the US or Japan. This question will repeatedly be asked in this paper.

Another sector specific aspect discussed in this paper relates to regulation.[6] Regulation plays a role in most services sectors, but in some it appears to be easier to agree on global standards than in others. The International Telecommunication Union, for instance, sets global standards for the telecommunication sector and the Basel II framework developed by the Basel Committee on Banking Supervision defines widely accepted standards governing capital adequacy of internationally active banks.[7] In other services sectors, national standards are still prevailing. Stephenson (2002), for instance, argues that construction/engineering and professional services are often highly restricted sectors as they are subject to national standards for compliance that may set out quite restrictive criteria for the determination of the equivalence of qualifications by these service providers. According to Stephenson (2002) regional agreements can play a useful role in these sectors, as it should be generally easier to develop a common set of criteria for the recognition of the equivalence of standards and/or the equivalence of diplomas and educational and professional training for the granting of licences to practice various professional services when this is carried out among a smaller sub-set of member countries. A similar argument holds for social-type services, like educational and health services, where there is even greater need for similarity among countries that wish to come to a preferential agreement in these areas. The question, however, arises, whether ACP countries and EU countries are similar enough to make an argument in favour of regional liberalization on the basis of regulatory considerations.

The services negotiations in the context of EPA will follow a positive list approach along the line of GATS negotiations. Parties will thus attempt to come to agreements on which modes to bind in which sectors and under which market access and national treatment restrictions.[8] The "negative list" approach preferred by some observers, is therefore ruled out from the outset. Under that approach all services sectors are considered to be free of restriction unless included in lists of reservations. According to Stephenson (2002) the negative list approach promises to incite more commitments than the positive-list approach (nothing is bound that is not included).[9] Within the Western Hemisphere no fewer than 12 RTAs have adopted a "negative list" approach for carrying out services trade liberalization and these RTAs are, according to Stephenson (2002), much more transparent instruments for service providers than agreements that follow a positive list approach.[10]

[6] This aspect has, for instance, been emphasised in Stephenson (2002).

[7] The appropriateness of these standards for developing countries has, however, been questioned, in particular with respect to the Basel II framework. See, for instance, Bailey (2005).

[8] Binding the access to markets does not necessarily imply more liberalization as Members are in principle free to bind access at levels that are below (or equal to) the existing level of liberalization.

[9] See also Adlung and Roy (2005) on this issue.

[10] Mattoo and Wunsch (2004) make a similar argument but focus on services supplied under mode 1 and 2. They suggest that WTO Members should aim at eliminating existing limitations for GATS mode 1 and 2 and bind these two modes across the board. In this way, Members would give up the right to maintain or introduce new restrictions, but according to the authors not much would change in practice, because many covered services are already traded freely. They suggest to accompany such a broad forward-looking commitment by a closed list of exceptions, including any financial services involving the movement of capital and transport services that involving the movement of freight or persons.

Two aspects of the services negotiations that will be mentioned throughout this paper are the length of agreed transition periods and the scope for technical assistance.[11] Parties to the EPA negotiations have to agree on the length of transition periods, i.e. the duration between agreement on policy reform and its actual implementation. In particular in services sectors, these transition periods can play an important role, as successful liberalization often implies privatization at the national level and the introduction of an appropriate regulatory framework. Designing and implementing such a framework takes time and is often also costly. Given the financial restrictions many ACP countries face, the prospects for technical assistance specified in the Cotonou Agreement, can play an important role here. For instance, a commitment by ACP countries to open their markets to the entry of European banks could be tied to technical assistance with respect to regulatory design and institution building during the transition period stipulated in a hypothetical agreement.[12] It could also be considered to make liberalization conditional on the achievement of certain targets in the domain of regulation.

The terms liberalization, competition, deregulation and regulation can have different meanings in the literature depending on what type of liberalization (foreign, domestic) and what type of regulation is discussed. This paper uses the term liberalization when referring to the reduction of policy induced barriers to international trade in services. The term privatization is used when referring to the privatization of public entities accompanied or not by the introduction of competition at the domestic level. Privatization does not automatically imply the entry of new competitors, but given that the emphasis in this paper is not on domestic processes, the terminology is kept simple and most of the time no distinction is made between pure privatization and the introduction of competition at the domestic level. The word regulation will be used with a positive connotation and refers to prudential and supervisory regulation. When referring to governmental intervention that hampers the functioning of markets the paper uses the term stifling regulation or restrictive regulation. In practice the distinction between the two types of regulation is not always straight forward. Qualification requirements for service providers, for instance, can be considered to be prudential regulations. But depending on the design, e.g. the restrictiveness and the arbitrariness, of such requirements they may also be considered stifling regulation.

The remainder of this paper is organized as follows. The next section presents and discusses data on global trade in services, the role of Southern and Eastern African ACP countries in global trade and the importance of the different services sectors within each country. This is followed by a section that discusses a number of services sectors in more detail. In that section particular attention is paid to the role of different modes of services trade, the role of regulation in these sectors and, related to this, the potential role of transition periods and technical assistance. A separate subsection is dedicated to mode 4 liberalization, as services trade in mode 4 is generally regarded as a possible area of comparative advantage for developing countries.

B. STRUCTURE OF ACP COUNTRIES' TRADE IN SERVICES

1. The role of services in Southern and Eastern African ACP countries

The contribution of the services sector to a country's GDP and its trade flows depends on a number of factors, including its level of development, its size and its comparative advantage. It has been observed that the role of agriculture and subsequently manufacturing in economic activity tends to decline in the process of economic development. This phenomenon is also reflected in the data

[11] Another aspect that may play a role in services negotiations is the distinction between entry through acquisition and greenfield entry in the context of mode 3 liberalization. This aspect will not be elaborated in this paper. See Mattoo and Fink (2002) for a discussion of this issue.

[12] Adlung and Mattoo (forthcoming) refer to the need to establish a link between market-opening negotiated at the WTO and additional assistance for complementary reform that is vital for successful liberalization.

presented in Table 1. The first column represents the weight of the services sector in countries' overall GDP. The table includes the Southern and Eastern African ACP countries that are the focus of this paper. As indicated in the table, all of them are a member of at least one regional agreement within Africa, i.e. the Common Market for Eastern and Southern Africa (COMESA) and/or the Southern African Development Community (SADC). Table 1 also gives information for Egypt and South Africa, that are not ACP countries but members of COMESA in the case of Egypt and SADC in the case of South Africa. In order to evaluate the position of the Southern and Eastern African countries, the indicators are compared with the relevant indicators for the ACP group as a whole and a number of industrialized economies. The lower average share of services value added in GDP in the COMESA and SADC countries compared with Japan, the EU and the US reflects different levels of economic development. In individual ACP countries the share of services' value added can, however, be very high. It is, for instance, above 80 per cent in Djibouti, due to the economy's dependence of the activities of its port, that acts as a transit port for the region and an international transhipment and refuelling centre.

While services value added represents around two thirds of economic activity in the industrialised countries the ratio of the value of commercial services trade to GDP is very small.[13] In the EU, one of the world's leading services exporters, the ratio of services exports to GDP is less than 4 per cent. In the Seychelles, instead, this ratio is above 40 per cent and in Mauritius it is around 25 per cent. This difference reflects two things. Smaller economies tend to be more reliant on trade and the ratio of trade to GDP therefore tends to decrease with countries' size. If a high export to GDP ratio is combined with a specialization in services exports, like in the case of Mauritius and the Seychelles, then the ratio of services exports to GDP can turn out to be very significant. Although the numbers in table 1 do not imply that 40 per cent of economic activity in the Seychelles is concentrated in the exports of services, it is safe to say that services exports play an important role for the overall economic activity of the island.[14] In countries like the Seychelles, any change in the country's export performance in the relevant services sector(s) can therefore have important repercussions on overall economic performance. Countries like the Seychelles and Mauritius are, however, the exception in Southern and Eastern Africa. The average ratio of commercial services trade to GDP is 4.8 in SADC and 7.0 in COMESA and thus significantly lower than in the two mentioned island economies. For SADC and COMESA countries the ratio is, however, higher than in the three industrialized economies represented in the table.

At this stage it is important to point out that there is no perfect overlap between the coverage of the services trade data presented in this section and the coverage of GATS. In particular the data for trade in services reported in balance of payment statistics do not cover mode 3 trade.[15] If a EU company, for instance, provides port handling services in the harbour of Djibouti, this would according to GATS definitions represent a mode 3 import of maritime services by Djibouti from the EU. The mode 3 imports, however, are not captured by Djibouti's balance of payments as they represent transactions by a company resident in Djibouti. Accordingly, the value of the company's transactions would be included in Djibouti's national accounts or business statistics. Data on services trade based on balance of payments information are therefore only of limited use as a measure for services trade covered by GATS.

[13] The concept "commercial services" excludes government services, a category that is associated with the public sector and refers, among other things, to expenditure by embassies and consulates. Throughout this paper the term "services" only refers to "commercial services".

[14] Trade is measured on the basis of the value of traded goods and services, whereas only the value added of production is taken into account for the calculation of GDP. As a consequence the ratio of trade to GDP can exceed 100 per cent, as is for instance the case in economies like the Seychelles but also in countries like Luxembourg and Singapore.

[15] Sectoral definitions are also different in balance of payment statistics and the GATS. See for instance discussions in te Velde (2004) and Mattoo and Wunsch (2004).

Table 1
The role of services in economic activity and trade, averages 2000-2002, percentages

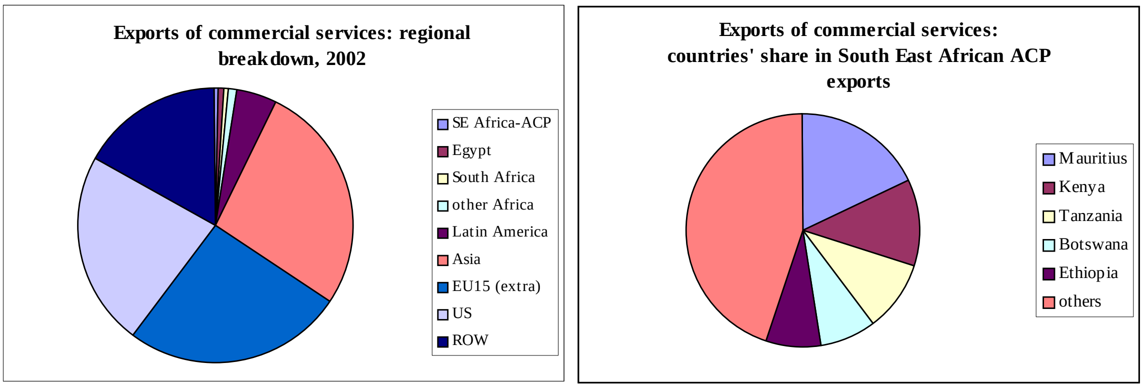
	Services value added % of GDP	Commercial services trade to GDP ratios		Commercial services trade % of total trade	
		exports	imports	exports	imports
Angola[1,2]	23.6	2.3	29.2	2.9	46.4
Botswana[2,3]	50.1	6.8	9.8	12.8	23.7
Burundi[1]	31.2	0.4	5.1	6.3	24.1
Comoros[1]	47.2	13.2	10.0	65.3	34.1
Djibouti[1]	82.1	12.9	9.2	69.2	20.9
Eritrea[1]	61.2	14.7	4.0	72.4	4.7
Ethiopia[1]	44.2	6.4	8.1	46.3	26.9
Kenya[1]	62.9	6.7	5.8	27.9	17.2
Lesotho[2,3]	40.1	4.3	5.3	10.7	5.5
Madagascar[1]	55.7	5.8	8.9	25.0	30.8
Malawi[1,2]	47.1	2.4	10.6	9.2	27.1
Mauritius[1,2]	62.2	25.4	17.2	40.8	28.6
Mozambique[2]	45.6	8.5	14.7	34.0	32.6
Namibia[1,2,3]	59.5	6.8	8.3	15.6	16.9
Rwanda[1]	37.5	2.6	6.7	36.8	33.3
Seychelles[1,2]	68.1	44.1	27.3	56.8	32.3
Sudan[1]	41.8	0.4	5.0	3.0	28.9
Swaziland[1,2,3]	37.9	11.4	15.1	13.2	15.5
Tanzania[2]	39.3	6.4	6.7	43.5	29.9
Uganda[1]	44.4	3.7	8.3	31.4	32.5
Zambia[1,2]	52.1	3.3	9.5	13.1	25.0
Zimbabwe[1,2]	57.8	2.2	3.5	12.5	16.7
Egypt[1]	50.2	9.6	6.8	56.6	31.6
South Africa[2,3]	64.8	4.0	4.6	12.9	16.7
SADC	52.5	4.8	7.1	14.2	22.2
COMESA	44.4	7.0	7.7	32.6	29.6
ACP	47.1	7.2	8.8	19.5	23.8
Japan	67.5	1.6	2.6	14.6	25.6
United States	74.6	2.7	2.1	27.4	15.1
EU(15)	61.9	3.6	3.4	24.4	23.0

Sources:
GDP: World Bank, WDI 2005 online
Commercial services trade: WTO, SDB online
Note: EU(15) trade refers to extra-EU trade, the value in the first column for Djibouti is the value for the year 2000, for the United States the average for 2000-2001.
Footnote 1 refers to COMESA members, footnote 2 to SADC members and footnote 3 to SACU members. Kenya, Tanzania and Uganda are besides members of the Commission for East African Co-operation (EAC).

2. Southern and Eastern African ACP countries as exporters

At the global level Southern and Eastern African ACP countries only play a minor role as exporters of commercial services as illustrated in chart 1. They only represent around half a percentage point of total world exports in commercial services. This is only slightly more than the share of South Africa alone and slightly less than the share of Egypt. The European Union and the United States each represent around one quarter of total world exports in commercial services.[16] Within the group of countries discussed here, Mauritius is the most important services exporter, its exports representing close to 20 per cent of Southern and Eastern African commercial services exports. It is followed by Kenya (12.7 per cent), Tanzania (10.5 per cent), Botswana (8.5 per cent) and Ethiopia (7.8 per cent). The exports of Burundi, Lesotho, Malawi and Rwanda, instead, each represent less than one per cent of Southern and Eastern African commercial services exports.

Chart 1: Southern and Eastern African countries' share in world services exports



Source:
Commercial services trade: WTO, SDB online

Europe is Africa's main trading partner for commercial services. More than half of Africa's commercial services went to Europe in 2003.[17] To some extent this can probably be explained by geographical closeness and colonial links, two variables that have found to be important determinants for bilateral trade flows in the empirical literature.[18] Africa, instead, is only a minor trading partner for the European Union, as only 6.6 per cent of its imports were sourced from that region in 2003. The sectoral breakdown of EU services imports from African ACP countries differs significantly from the breakdown of imports from the world in general.[19] Transport and travel together represent around three quarters of EU services imports from African ACP countries. The picture for Africa as a whole is similar and Egypt relies even more heavily on exports from these two services subsectors. In contrast, travel and transport only represent around one half of services imports from the world as a whole. This illustrates the significance of transport and, in particular, tourism for services exports of African ACP countries.

[16] For reasons of data availability and comparability, data for the European Union in this section are data for the fifteen member countries before the enlargement in 2005.

[17] This percentage is based on data from two different databases. The value for total African commercial exports was taken from the WTO's SDB database and the value for African exports to the EU is based on data for EU(15) commercial services imports from Africa taken from Eurostat. It was necessary to rely on mirror data as bilateral data for services exports from African countries are not available. Due to likely asymmetries in the data the calculated percentages should be taken with caution.

[18] For an overview of this literature see Piermartini and The (2005).

[19] Data for bilateral trade between the EU(15) and Southern and Eastern African ACP countries as a group was not available from EUROSTAT. It would be possible to obtain more detailed information by using bilateral trade data for individual EU member countries.

Table 2: EU(15) services imports by region
totals (millions euro) and sectoral breakdown (percentages), 2003.

	Imports from				
	World	Africa	ACP-Africa	South Africa	Egypt
EU (15) Imports					
Commercial Services	293050	19326	10039	3497	3172
of which (in percentages)					
Transportation	25	33	33	30	33
Travel	28	47	43	46	58
Communications services	2	3	2	2	1
Construction services	2	2	3	1	1
Insurance services	2	1	1	2	0
Financial services	3	1	1	2	0
Computer and information services	2	0	0	1	0
Royalties and license fees	8	0	0	0	0
Other business services	25	12	16	15	6
Personal/ cultural and recreational services	2	0	0	1	0

Source: Eurostat and own calculations
Note: World trade refers to extra-EU(15) trade

This reliance is further illustrated in Table 3 that gives an indication of the sectoral specialization of the different East African ACP countries within services. The table confirms the high concentration of exports in only two subsectors: travel and transport. At the global level travel and transportation together represent slightly more than 50 per cent of total commercial services exports.[20] For most of the African countries discussed here the share of these two sectors is far above 50 per cent. In Botswana, Lesotho, Malawi, Mauritius, Namibia, Rwanda, the Seychelles, Sudan, Tanzania and Uganda tourism alone represents more than 50 per cent of total commercial services exports. In Ethiopia and Kenya more than half of commercial services exports fall under the transportation subsector. But more disaggregated data show that those transportation services exports mainly refer to passenger air travel, probably linked to the tourism industry. This adds to the weight of the tourism industry in the services exports of these countries.

[20] See Chart 2.

Table 3: Sectoral shares in total exports of commercial services, 2002.

COUNTRY NAME	transportation	travel	other commercial services
Angola	8.1	17.9	74.0
Botswana	12.6	72.7	14.7
Burundi	23.1	30.6	46.3
Comoros	20.1	62.9	17.0
Djibouti	75.6	11.3	13.1
Eritrea			
Ethiopia	55.6	16.0	28.4
Kenya	58.0	37.4	4.6
Lesotho	1.3	64.0	34.7
Madagascar	26.8	22.9	50.3
Malawi	32.7	67.3	0.0
Mauritius	24.0	53.4	22.6
Mozambique	30.3	18.7	51.0
Namibia	16.7	79.3	4.1
Rwanda	25.7	65.3	9.0
Seychelles	39.4	55.3	5.2
Sudan	12.8	82.9	4.3
Swaziland	9.4	23.3	67.3
Tanzania	10.1	71.8	18.2
Uganda	16.7	76.5	6.8
Zambia			
Zimbabwe			
Egypt	30.6	41.2	28.1
South Africa	22.3	63.9	13.8

Source: WTO, SDB database. Empty cells represent missing data.

3. Southern and Eastern African countries as importers: who are the most competitive suppliers?

The European Union is also a major trading partner for Africa when it comes to imports of commercial services. In 2003, the African continent sourced 42 per cent of its commercial services imports in the EU(15).[21] Table 4 reveals that African countries in general, and ACP African countries in particular, import relatively more transport services and construction services from the EU than the rest of the world does. In contrast, ACP African countries import relatively less travel services and other business services.

[21] This percentage has been calculated using the value for total commercial services imports by Africa (WTO, SDB data base) and the value of commercial services exports from the EU(15) to Africa (Eurostat). See also footnote 14.

Table 4: EU(15) services exports by region of destination totals (millions euro) and sectoral breakdown (percentages), 2003.

	Exports to				
	World	Africa	ACP-Africa	South Africa	Egypt
EU(15) Exports					
Commercial Services	317838	18066	12507	3452	1323
of which (in percentages)					
Transportation	24	31	32	26	32
Travel	19	19	15	17	18
Communications services	2	2	1	2	1
Construction services	3	10	10	3	5
Insurance services	5	3	5	8	1
Financial services	7	3	7	6	2
Computer and information services	5	4	4	10	3
Royalties and license fees	5	2	2	6	1
Other business services	28	27	23	21	36
Personal/ cultural and recreational services	1	1	1	1	0

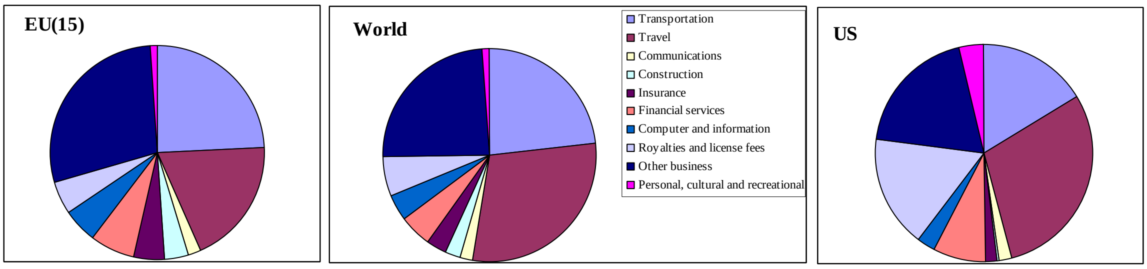
Source: Eurostat and own calculations
Note: World trade refers to extra-EU(15) trade

It has been discussed before that the gains and risks of regional liberalization in services trade in the context of EPA depend to a large extent on the characteristics of the sector at stake and on the global competitiveness of the European suppliers in that sector. In sectors where the EU is a superior supplier at the global level, ACP countries may not run a significant risk if regional integration with the EU precedes multilateral liberalization. Chart 2 gives some information as to the competitive position of EU services suppliers at the global level, by comparing the EUs sectoral breakdown of commercial services with the world's average and the sectoral breakdown of US exports, one of the leading world exporters in services.[22] It illustrates that the US has an important role as an innovator at the global level as the share of licences and royalties is significantly higher than for the world average.[23] When compared to the European Union travel is also more important. The share of all the other sectors in EU exports is more or less equal or higher than in the case of the US. This could be interpreted as the EU being a relatively competitive supplier of those services at the global level. This is notably the case in the insurance sector.

[22] South Africa is likely to be one of the most competitive services suppliers at the regional level, but data for South African exports are not available for a comparable sectoral breakdown. In particular, no data are separately available for exports of financial services and of computer and information services.

[23] A significant share of the transactions covered by the item "royalties and licence fees" in the balance of payments is likely not to fall under the definition of services trade under GATS. In balance of payments statistics the item "royalties and licence fees" comprises international payments and receipts of franchising fees; the royalties paid for the use of registered trademarks; and international payments and receipts for the authorised use of intangible, non-produced, non-financial assets and proprietary rights and with the use, through licensing agreements, of produced originals or prototypes. Only franchising in the context of distribution services is covered by the GATS according to the services sectoral classification list specified in WTO document MTN/GNS/W/120.

Chart 2: Sectoral breakdown of EU(15), world and US commercial services exports, 2003.



Sources: Eurostat, OECD and WTO estimates.

The EU is a net exporter of services and is at the global level one of the main services exporters. This could be seen as an indication that ACP countries would not run a significant risk if they offer preferential access in services to the EU before liberalizing at the multilateral level.[24] The following discussion at the sectoral level provides a more nuanced picture. ACP countries should also take into account what happens if they do not include the services sector in EPA and multilateral negotiations but do, instead, liberalize services trade within the African region. African suppliers may then be able to get a head-start, which may not be the preferred option from an efficiency point of view.[25] The discussion in the next section indicates that this may already be happening in certain sectors, like finance and insurance, where providers from, for instance, South Africa or Mauritius are entering other African markets.

C. EPA NEGOTIATIONS EXPORT OPPORTUNITIES, GAINS FROM IMPORTS AND ADJUSTMENT TO CHANGE

The section tries to identify in which sectors Southern and Eastern African countries are likely to have export potential and in which they are likely to face increased imports if trade in the sector is liberalized.[26] Where relevant, positive spill-overs from increased imports on the rest of the economy will be discussed. For import competing sectors the section also addresses the question whether the option of giving preferential access to EU suppliers is more likely to have advantages or disadvantages compared to the option of multilateral liberalization. Issues of appropriate transition periods and regulation, of the potential role of foreign technical assistance and the need to distinguish different modes of trade will also arise.[27]

[24] In the case of a regional EPA agreement, third country suppliers, e.g. U.S. suppliers, could in principle establish in the E.U. and serve African markets from there, thus taking advantage of EPA provisions. GATS Article V.6 allows for this possibility, provided that the third country supplier engages in "substantive business operations" in the territory of the parties to an agreement. This implies that efficient third country suppliers are not necessarily excluded from a regional market as a result of a preferential agreement.

[25] It could maybe be possible to argue in favour of such a development from a regulatory point of view or using an infant industry argument. Only the first of these issues will be discussed in the following section.

[26] The definition of the sectors discussed in this section neither follows GATS definitions nor the definitions used in balance of payments statistics, but rather uses terminologies common in the public debate.

[27] The discussion embraces the four modes of services trade. It particular, it includes mode 3 even though that mode was not covered by the balance of payment data presented in the previous section.

1. Financial sector

(a) Banking

The banking sector is a sector in which most Southern and Eastern African ACP countries do currently not appear to have strong export potential. Two possible exceptions are Mauritius and Botswana. Mauritius has a relatively large and well-developed domestic financial system and a growing offshore sector.[28] Mauritian banks have expanded their activities to African countries (e.g. Malawi, Mozambique, Madagascar and Seychelles) but also to India and France.[29] Also Botswana has a relatively active financial sector. The government of Botswana has chosen to focus on financial services as an area of growth in the economy. Although the domestic market is small, the government is trying to attract investment in an International Financial Services Centre (IFSC) to act as a conduit for funds from South Africa and the rest of the world into other parts of Africa. The aim of the IFSC is to increase employment and expertise in financial services in the country in order to make Botswana a financial hub for Sub-Saharan Africa, by encouraging companies falling under the IFSC to provide financial services to clients located outside of Botswana. [30] At this stage it is too early to evaluate the success of this project.[31]

In general, though, Southern and Eastern African countries, are more likely to be importers than exporters of financial services. The question therefore arises whether Southern and Eastern Africa could gain from further opening its markets to the foreign supply of banking services and, if yes, whether preferential access for EU player has clear advantages or disadvantages when compared to multilateral liberalization.

The banking sector is crucial for economic development in general and plays an important role for trade. Improved provision of financial services allows greater efficiency in nearly all other sectors: by expanding the range and quality of financial services; by allowing transactions that would otherwise not occur and by facilitating firm entry and competition in other sectors. A well-functioning banking sector is also vital for international trade as the possibility to take loans facilitates international transactions or the expansion of production for local exporters.[32] The empirical literature shows that an efficient financial services sector enhances economic growth.[33]

In many developing countries, including a number of countries discussed here, the financial sector is not well developed and subject to strong government intervention. Indeed, until recently minority or majority government ownership of banks was frequent, credit allocation quotas often existed and governments imposed controls on interest rates and/or barriers to entry in the banking sector. These interventions often resulted in high interest rate spreads harming both lenders and borrowers and resulting in a shallow financial market. Besides directed credit programs and publicly owned banks were not necessarily channeling funds into the most profitable investment opportunities for the economy resulting in high default rates on loans.[34]

Many African countries embarked on more or less ambitious privatization programmes in the late 1980s or 1990s with the intention to increase the efficiency of their banking sector.[35] Although this

[28] IMF (2003).
[29] Information available on the website of the State Bank of Mauritius.
[30] Botswana IFSC website (http://www.botswanaifsc.com/).
[31] EIU Botswana (2004).
[32] See WTO(2004) and Bacchetta and Jansen (2003) for the role of the financial sector for international trade.
[33] See Levine (1997) for an overview.
[34] Collier and Gunning (1999) mention default rates in the 40-95 percent rates for publicly owned banks in Africa.
[35] See, for instance Chirwa (2001), Kasekende (2003), Ikhide and Alawode (2001) and Beck et al (2005) on financial sector reforms in Malawi, Uganda and Nigeria respectively.

has in many cases improved the prevailing situation, the financial sector remains weak in many countries and government intervention continues to exist. In most African countries still only a small fraction of the population has access to deposit and credit facilities and other financial services provided by formal financial institutions. For example, in Tanzania, only about 6 per cent of the population has access to the banking sector (4 per cent in rural areas).[36] In recent years, systems of microfinance institutions (MFIs) have developed outside the formal sector in a number of African countries in order to offer financial services to a larger part of the population. These institutions already play an important role in entrepreneurial activities in some of these countries. In Tanzania the activities of MFIs reached around 6 per cent of the population in 2002. MFIs held about 60 per cent and 11 per cent of total commercial bank deposits and credits, respectively. The appropriate integration of the microfinance sector into the regulatory system is therefore an important challenge for many ACP countries.

Foreign banks do not play an important role in the micro finance sector and this is not expected to change in the future. Foreign suppliers tend to focus on lending to the manufacturing sector rather than households and within the manufacturing sector they seem to have a preference for serving large clients. This phenomenon has also been referred to as "cherry picking" in the literature. As a result, domestic banks in developing countries may be driven out of the wholesale and large enterprise segments and obliged to focus on retail operations only, albeit with improved efficiency (Clarke et al., 2001). It is often feared that by stripping the higher end customers from existing banks, the entry of new foreign banks will fragilize the whole sector, but Pomerleano and Vojta (2001) argue that, on the contrary, foreign entry is beneficial for the effectiveness of the banking sector at the top end with no negative, or even positive, effects on the lower segment of the market.

Other empirical studies on the subject confirm that foreign bank entry increases competition and efficiency in the domestic bank sector. Using data from a sample of 80 countries, Claessens, Demiriguc-Kunt and Huizinga (2000) show that foreign entry reduces the profitability of domestic banks and enhances their efficiency. The empirical work by Unite and Sullivan (2001), Barajas et al. (2000) and Clarke et al. (2000) on the Philippines, Colombia and Argentina, respectively, also indicates that foreign entry exerts competitive pressure on domestic banks triggering cost reductions in domestic banks with resulting increases in profitability.[37] The empirical literature has mainly analysed the effects of foreign entry (mode 3) on the competitiveness of domestic banks.[38] Presumably both mode 1 and mode 3 liberalization would induce increased competition and efficiency improvements in the local banking sector.

In the case of mode 1 liberalization foreign banks or other financial actors are allowed to offer their services from their home country to clients in the liberalizing African economy. In the case of mode 3 the foreign bank opens a branch or subsidiary in the liberalizing African economy and serves its clients from there. There are two reasons to believe that the positive effects of mode 3 liberalization

[36] Basu et al. (2004).

[37] On the other hand, the evidence regarding the impact of foreign entry on the quality of domestic banks' loan portfolios is mixed (Clarke et al., 2002). Goldberg et al (2000) examine the lending behaviour of foreign and domestic banks in Argentina and Mexico in the period 1994 to 1998. They concluded that foreign banks exhibited stronger loan growth with lower associated volatility compared to all domestic owned banks, and thereby contributed to greater stability in credit. The onshore presence of foreign banks may also foster stability of the deposit base by allowing domestic depositors to do their "flight to quality" at home (Clarke et al., 2000). Indeed, Demergüç-Kunt et al. (1998) found evidence suggesting that increased participation of foreign banks tends to lower the probability of banking crisis. On the other hand, it has been argued that the decision of a number of foreign banks to leave Argentina at the beginning of its financial crisis may have exacerbated the situation and that these events challenge the notion that foreign banks are a stabilizing force in developing countries' banking sector (Clarke et al., 2002).

[38] Besides this research does not distinguish between the productivity increases due to changes in the market structure of the banking industry versus those due to technology transfers between foreign banks and domestic banks. See Goldberg (2003).

would be higher than mode 1 liberalization.[39] First, information and communication costs may be lower for African clients dealing with foreign banks established in their country than with banks established abroad. As a consequence foreign banks established in the country will be able to reach out to more clients leading to a stronger competition effect. Second, to the extent that demonstration effects, human capital spill-overs or other spill-overs exist between foreign banks and domestic banks, they are likely to be stronger when the foreign bank is established in the country.

The positive effects of mode 1 liberalization on the financial sector's efficiency may thus be weaker than in the case of mode 3 liberalization. At the same time, mode 1 liberalization may induce more risk to domestic financial systems. Firstly, it is easier for domestic regulators to control the behaviour of foreign banks established within their borders than those established abroad. This is in particular the case if foreign banks establish in the form of subsidiaries and are thus, in principle, subject to the prudential regulation in the host country. Second, for most banking services mode 1 trade explicitly implies cross border capital flows.[40] As a consequence mode 1 liberalization only makes sense for countries that are willing to open their capital account. Foreign direct investment, i.e. mode 3 flows, may instead also take place in the context of only limited openness of the capital account. Indeed, some observers have suggested that developing countries may consider restricting certain types of capital flows only to banks or other financial institutions based in the home country.[41] The developing host country could also consider imposing quantitative limits on banks' lending to non-residents and prudential limits on banks' open foreign exchange position.[42] It could also be stipulated that only banks are allowed to use derivatives and related instruments implying cross-border transactions.[43]

The literature is unanimous on the need for appropriate financial regulation in order for financial markets to function smoothly. There is less agreement on - and maybe even insufficient understanding of - the exact characteristics of "appropriate financial regulation". Many developing countries, besides, face important capacity constraints which may make it difficult for them to appropriately regulate and supervise the financial sector. Some conclude from this that developing countries may consider pursuing only a restricted level of Mode 1 liberalization combined with significant liberalization of Mode 3 as long as their regulatory capacity is weak.[44] Such a cautious approach could be combined with deeper integration at the regional level within Africa.[45]

Overall the liberalization of financial services appears to be a complicated process, where mistakes can have significant negative consequences for the economy. Foreign assistance, in terms of money and technical assistance, in this process can be extremely useful. It has also been argued in the literature that developing countries conducting trade negotiations should take care of involving both trade representatives and representatives of regulatory agencies in the negotiations, in order to ensure that the pace and pattern of liberalization is appropriate for the country's level of regulatory framework.[46] The successful building of an efficient financial sector is likely to have huge positive spill-overs on the economy. The entry of foreign companies can play a very positive role in this context. The difficulty of the task ahead should therefore not refrain African governments from opening up their financial sector to foreign competition. On the contrary, credible commitment to liberalization in the context of EPA negotiations or at the multilateral level could put the necessary

[39] See also Kono and Schuknecht (2000) on this point.

[40] See the discussion in Kono and Schuknecht (2000).

[41] See the more extensive discussion in Ishii and Habermeier (2002).

[42] See Ishii and Habermeier (2002).

[43] See, for instance, Garber (2000) on how derivatives can be used to evade risk-control or prudential regulation and circumvent capital controls.

[44] See for instance Kono and Schuknecht (2000).

[45] Jansen and Vennes (2006) argue the combination of full regional and less ambitious multilateral liberalization could be supplemented with a harmonized regulatory system within regions and the creation of regional institutions in charge of supervision and control of the financial sector. In both COMESA and SADC efforts for further financial integration within the region exist. See Jansen and Vennes (2006) for a discussion.

[46] Vander Stichele (2003)

pressure on domestic players to take the process of domestic privatization, deregulation and introduction of prudential regulation serious.

Among the Eastern and Southern African countries discussed here Botswana, Burundi, Djibouti, Madagascar, Namibia, Rwanda, Swaziland, Tanzania, Uganda and Zambia have made no commitment at all under GATS in the financial sector. Comoros, Eritrea, Ethiopia, Seychelles and Sudan could be added to this list, as they are not WTO members. This does not imply however that foreign banks are not active in the countries that did not make any GATS commitments in the financial sector. Banks with UK ownership are, for instance, active in a number of Southern and Eastern African countries including, Botswana and Zambia. The most striking observation is however that South African banks are very active in the region. This is, for instance, the case in Angola, Botswana, Malawi, Mozambique, Tanzania, Zambia and the three SACU countries (Lesotho, Namibia and Swaziland).

In this particular sector opening up to European companies before opening up at the multilateral level does not appear to bear a big risk of getting stuck with "inferior suppliers" as European banks are very competitive at the international level.[47] It may, indeed, be an economically attractive idea to allow for entry of banks from third countries that represent an additional element of competition vis-à-vis expanding South African banks. Making concessions in this sector could, besides, help to obtain concessions in other areas from the EU. According to the arguments presented above ACP countries should consider encouraging mode 3 imports from the EU rather than mode 1 imports.

(b) Insurance

The insurance sector comprises a range of very different activities including personal property insurance (e.g. automobiles, homes), life insurance and health insurance. An insurance contract typically implies that in exchange for periodic payments from the insured, the insurer agrees to pay the insured a sum of money upon the incurrence of a specific event, for instance an accident. The main purpose of insurances therefore is to reduce risk for the policyholders. But taking an insurance policy contains a risk in itself, i.e. the risk that the insurance company does not have enough reserves to pay the promised sum when the specified event occurs. Insurance activities therefore also require surveillance by independent, typically governmental bodies. In particular, governments need to make certain that insurance customers have access to sufficient information to enable them to make informed, independent judgements as to (1) an insurer's financial condition and (2) the value of its products.[48]

A strong insurance sector promotes financial stability of firms and individuals and reduces the anxiety of experiencing unexpected losses or harms, by indemnifying policy holders if hardships occur. As a consequence insurance facilitates trade and commerce as it fosters entrepreneurial activity in environments that may be perceived as highly risky.[49] Insurance, especially life insurance, also mobilizes savings and enhances the efficiency of the financial system, by complementing banks in the role of financial intermediaries. Through these channels of risk transfer, indemnification and financial intermediation the insurance sector can therefore have very positive effects on economic growth. It could be argued, however, that the insurance sector is more likely to fulfil this role in countries at a relatively advanced stage of economic development.

The potentially positive and negative effects of opening the insurance sector to international competition are similar to the ones discussed in the context of the banking sector. International liberalization can entail increased investment and improved capitalization, the sector can take

[47] See chart 2.
[48] Skipper (2001).
[49] Skipper (1997)

advantage from the know-how and technical capacity of foreign insurers and increased competition is likely to enhance efficiency. To the extent that the activity of foreign insurers involves cross border flows of capital, liberalization may increase the risk of financial instability, but as is the case in the banking sector, the level of this risk depends on the type of trade involved (e.g. cross-border versus commercial presence) and can be controlled by appropriate prudential regulation at the national level.

Although international liberalization of the insurance industry may not be an immediate priority for all of the countries discussed here, the development of an adequate regulatory and supervisory framework for insurances together with the development of such a structure for the banking sector has clear advantages. This would among others impede that operators that have been rejected by banking authorities seek refuge in the insurance sector thus endangering this segment of financial intermediation with potential spill-overs on commercial banks.[50]

With respect to existing commitments to liberalization in the insurance sector, the situation is comparable to the one in the banking sector, to the extent that the countries not committing the banking sector under GATS also did not commit the insurance industry. As in the case of the banking sector, South African companies are the most competitive players at the regional level and are already active in a number of African countries including Botswana and Mauritius.[51] While the discussion in this paper may not be sufficient to conclude on the desirability *per se* of including insurance services in EPA negotiations at this particular point in time, Chart 2 indicates that Southern and Eastern African countries should not be worried about opening their doors to the wrong player. European companies are highly competitive in the insurance sector and a number of them belong to the most efficient and most active actors at the global level. In this respect making commitments to the EU in the context of EPA negotiations before making similar commitments at the multilateral level is unlikely to have significant trade distorting effects, neither in the short nor in the long run.

2. Telecommunication

Telecommunications is a key sector for economic performance and overall development. It directly and indirectly influences the profitability of the majority of trade activities. An efficient telecommunications sector reduces communication costs for all market participants and can, as a consequence, have significant and positive effects on overall economic performance.

The telecommunication sector has undergone drastic changes in the past decades. Around the globe countries have privatized state-owned telecommunication companies and have opened their markets for competitors. Technological changes have been significant and continue to advance rapidly in the sector. As a consequence policy makers in the telecommunication sector face making decisions in a rather complex environment.

In most Southern and Eastern African countries telecommunications were in the hand of a state monopoly in the beginning of the 1990s but many of them have since initiated reform of the sector. There has been a tendency to adopt a gradual adjustment approach, which reflects to some extent hesitations to move quickly in an uncertain market.[52] Gradual adjustment was probably also the approach favoured by incumbents, who may have put pressure on the government not to change the market at a too rapid pace. Governments may also have thought that gradual changes would give them more time to build the regulatory capacity that is crucial for the market to function well and that it would be the best approach to reach appropriate levels of investment.

[50] Ryba (1998). See also the concerns expressed by the IMF on prudential regulation in the non-bank financial sector in Botswana (IMF, 2004).

[51] WTO (2003) and Vittas (2003) respectively. Two other insurance companies in Mauritius are subsidiaries of Indian companies.

[52] Hodge (2003).

Gradual or managed liberalization typically started by the separation of the incumbent monopoly from the ministry. The new private company was often granted an exclusivity period during which it could prepare itself for competition, while a foreign equity partner was sought for to inject capital and technical know-how. In the next step a second national operator was allowed to enter the market, with competition often being allowed on a facilities-basis only. In particular, voice resale competition has been expressly prohibited in many African countries during the first and second phase of the transition process. Resale competition and the entry of additional competitors have only been allowed at a later stage of the process. Progress in this transition process has tended to be slow. In numerous countries, there is still only one fixed-line operator active (e.g. Botswana and Malawi), while others, like South Africa, only recently allowed for the entry of the second operator.[53]

In the mobile phone sector, the approach has been to begin with one or two licences, because it was originally felt that this was a small luxury market in Africa and that only a few players would be viable. Instead the mobile phone market has experienced impressive growth rates and in 2005 several countries in the region counted three or more operators. This is for instance the case Uganda, Mauritius, Zambia, Zimbabwe and South Africa. The number of operators thus resembles the number in much wealthier countries like France (three), Japan (three) and the United Kingdom (four).

The market for satellite-based services has also been evolving steadily with numerous companies based in countries like Kenya, Tanzania, South African and Zambia offering their services in the region.[54] So far there has not been much of a systematic co-ordination in the area of wireless technologies in general and satellite technology in particular in the region. But initiatives like the TRASA Guidelines on Wireless Technologies Policy and Regulation published in 2004 are slowly but surely changing this picture.[55]

Overall the impression arises that technology and markets are moving much faster than governments in many African countries. Public intervention at the regulatory level is crucial in the telecommunication sector that requires appropriate regulation in order to function well. External assistance to build up regulatory capacity could therefore certainly be useful. In the meantime, however, it does not seem to be a good policy to continue to protect the monopolies of national telecom operators as this may happen at the expense of affordable and universally accessible services.[56] Indeed, one reason to protect national monopolies was to stimulate increased investments in fixed lines in order to ensure universal access to telecom services. Yet the evolution in the mobile market has shown that fixed line providers are no longer the providers of universal access. New wireless technologies such as mobile messaging and telephony, WIFI, WIMAX, and wireless local loop can offer affordable access to telecom services to poor customers. It is important for Southern and Eastern African countries to give the sector sufficient flexibility to exploit such bearers of new opportunities.

Overall strong arguments can be made for further liberalization of the telecommunication sector in African economies, including liberalization at the international level. Basic telecommunication services are mainly provided through GATS modes 1 and 3, but mode 4 is a consideration for the intra-corporate transfer of personnel. It has been mentioned before that several African companies are already providing their services in neighbouring countries. Preferential liberalization of the telecommunication sector within the region, for instance in the context of SADC and COMESA, therefore has a strong potential of increasing intraregional trade. Yet the risks of regional

[53] See Li and Xu (2004) for a recent contribution to the empirical literature on telecommunication reform. They find that countries that implemented more aggressive programs of reforms – full privatization and competition in both fixed-line and mobile sectors – experienced significantly more performance gains than countries that implemented less aggressive reform policies.

[54] See, for instance, Hamilton and TeleGeography (2004).

[55] TRASA refers to the Telecommunications Regulators Association of Southern Africa.

[56] See TRASA (2004).

liberalization alone, discussed before, are likely to be highly relevant in the telecommunication sector. The limited number of licences typically provided and the fact that there are first-mover advantages in facilities-based supply, means that favouring a regional firm may well leave the country with a less efficient provider that is difficult to dislodge.[57] It is therefore preferable to issue wholly open tenders to seek out the most competitive global suppliers.

Indeed interest is likely to be high among African countries to liberalize the telecommunication sector at the multilateral level, having largely missed out on the WTO basic telecom negotiations in the mid-1990s.[58] African interest in ICT development may also be an important factor. In addition, negotiating pressure may be brought to bear, at least, on the larger markets such as South Africa and Nigeria and possibly others who could bind their recent reforms. So far few countries in the region have made any commitments in the WTO. Most industrialized countries, instead, have fully liberalized their markets already and the large developing countries have committed to significant liberalization at the WTO. By committing merely to the current level of liberalization, many African countries can already improve their existing WTO offers in this sector dramatically.[59] But the arguments in favour of commitments exceeding current levels of liberalization are rather strong.[60]

In the context of the discussion in this paper, the question arises whether there is any scope for preferential liberalization with the European Union. The answer is likely to be no. Although European companies are strong competitors in the global telecommunication markets, they are not necessarily more competitive than a number of US or Asian companies.[61] Besides, this is a fast moving market where new competitors are emerging constantly. Telecommunication companies based in Arab companies have for instance already entered the African market.[62] At the same time South African companies are trying to enter markets in the Middle East. It may therefore make sense for Southern and Eastern African countries to pursue telecom liberalization at the multilateral level, in particular in order to stimulate mode 3 direct investment inflows into the region.[63] Mode 3 imports in this sector today may well be the basis for future increases in mode 1 or mode 2 exports in this service sector or others, like the tourism sector or the business service sector.

3. Transport

Transport costs can represent a major barrier to trade and this appears to be the case in many of the countries discussed in this paper. Indeed, a World Bank study has shown that for the majority of Sub-Saharan African countries, transport cost incidence for merchandise exports (the share of international shipping costs in the value of trade) is five times higher than tariff cost incidence (the trade weighted *ad valorem* of duty actually paid).[64] Transport costs also play an important role for the tourism industry, the most important sector for services exports in most ACP countries discussed here. The GATS services sectoral classification list distinguishes nine types of transport services: maritime

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[57] Hodge (2003).

[58] Sub-Saharan African countries that made basic telecom commitments are: Côte d'Ivoire, Ghana, Kenya, Mauritius, Senegal, South Africa and Uganda.

[59] Hodge (2003).

[60] See also Ndulo et al. (2005).

[61] A UK company, Vodafone, is the world's leading mobile phone operator in terms of turnover, while a Chinese company, China Mobile, was number one in terms of subscribers in December 2004 (see http://www.itu.int).

[62] In 2005 MTS Kuwait, Kuwait's largest mobile telephone service provider took over Celtel, a firm holding strong positions in nearly all West and East African countries (E-Magazine, 21/09/2005, Credit Suisse)

[63] It has been argued in the literature that countries may consider to maintain certain conditions concerning foreign ownership, like the obligation for a partial local participation in investment projects, as such conditions pursue specific goals of developing domestic capital and entrepreneurship that can be defended in terms of GATS Article IV (e.g. Hodge 2003).

[64] World Bank (2001).

transport services, internal waterways transport, air transport services, space transport, rail transport services, road transport services, pipeline transport, services auxiliary to all modes of transport and other transport services. This section will only discuss maritime and air transport and the related auxiliary services.

(a) Maritime transport

The international maritime transportation industry consists of three types of activities (Fink, Mattoo and Neagu (2001)): international transport services (freight and passengers); auxiliary services related to cargo manipulation in ports and on ships; and port services.[65] Transport services are further disaggregated into liner shipping, or regular lines, and tramp shipping, or transport performed on an irregular basis depending on the demand of the moment. Liner shipping usually carries processed commodities using containers, whereas tramp shipping typically carries raw commodities in bulk. Liner shipping has been subject to government restrictions and to cartel-types of agreements between private operators, while tramp shipping is generally considered fairly competitive. Private liner shippers are organized in "conferences" which allow them to cooperate on technical and commercial matters, on price-setting in particular[66]. Even though the power of those conferences to set international prices for transportation has eroded after the entry of large competitors (mostly from newly industrialized countries), some argue that their influence is still felt.

In the past governments often imposed cargo reservation schemes which required the flying of the national flag to obtain a significant share of the cargo capacity, unless bilateral or multilateral agreements had been reached with other states. Such cargo reservation schemes significantly restrained trade in the past, but their effect has decreased. The way in which the access to and use of port services is handled can also affect the costs of maritime transport. Many ports use the "first-arrived-first-served" rule that was devised in the early 1990s. This system, however, seems no longer in tune with modern developments and ships now often reserve a "window" of berthing in "common user" terminals.

Auxiliary activities in ports have tended to be monopolized either by the government directly or through a public authority. Private sector involvement, if not full privatization, of these activities can greatly foster efficiency in harbours. Indeed economic studies have demonstrated quick and massive productivity gains after privatization. This is the case, even though some activities, like cargo handling, require huge initial investments. Depending on their size, many ports can therefore only accommodate one or two suppliers and competitive pressure remains limited even after privatization.

Given the nature of the different activities in the maritime transportation industry, liberalizing maritime transport services mainly involves allowing for mode 1 trade in maritime transport services and for mode 3 and/or mode 4 trade in auxiliary services and/or port services. Mode 3 can also play a role for maritime transport services as companies active in liner shipment may want to establish commercial offices to build and maintain links with clients.

The area of international transport services (passenger and freight) does not seem to be an area of interest for most ACP countries discussed here, as the size of Southern and Eastern African countries' fleet is very small in the global context and also when compared with the size of the European fleet. According to UNCTAD (2004) the world's merchant fleet equalled 856.974 thousand deadweight ton

[65] International transport services would fall under the GATS section "maritime transport services" and auxiliary services would fall under "services auxiliary to all modes of transport". Port services embrace a range of different activities, some of which fall under "maritime transport services", whereas others would fall under "services auxiliary to all modes of transport".

[66] OECD (2001) reports that there are over 300 liner conferences, with memberships varying between 2 and 40 companies.

(dwt) in 2003, of which around 15 per cent were carried by vessels registered in a EU(15) country.[67] The fleet of the countries discussed here summed up to a mere 1014 thousand dwt, more than half of which are registered in Comoros (599) followed by Ethiopia (101), Seychelles (70) and Mauritius (60). In other words, the fleet of the countries discussed here corresponds to 0.2 per cent of the total world merchant fleet. According to UNCTAD(2003) the average age of the sub-Saharan fleet, excluding open registers, is 22.1 years, considerably more than the average age of the world fleet -- 12.6 years. This could imply that some of the ships involved may not meet environmental standards in industrialized countries.

Raising the efficiency of maritime transport in ACP countries can above all be achieved by increasing the efficiency of ports. Ports play an essential role in facilitating international trade, constituting as they do the main interface between the various modes of transport and the only gateway to international trade. The level of infrastructure development and the quality of port services are major factors in the cost of transporting goods. Thus improvements in port performance will contribute to improvements in a country's foreign trade as has been shown in a number of recent studies. Clark et al. (2004) find that port efficiency is an important determinant of ocean freight costs. They estimate, for example, that maritime transport costs in Brazil or India would fall by over 15 per cent if their port efficiency was at the level of France or Sweden. Their findings also suggest that if a country like Peru or Turkey was to improve sea port efficiency to a level similar to Iceland or Australia, it would be able to increase trade by roughly 25 per cent. Limão and Venables (2001) find that own infrastructure explains 40 per cent of transport costs for coastal countries and Nordås and Piermartini (2004) find that port efficiency is the single most important infrastructure variable when estimating the impact of different infrastructure variables on bilateral trade flows.

In recent years African port supervisory authorities have undertaken reforms and involved the private sector in varying stages. Generally speaking the first step has been to implement institutional reforms giving ports the status of an independent enterprise managed along commercial lines. In a considerable number of cases, countries have then brought in private enterprises to operate and manage the ports. Mozambique led the way: privatization began in the late 1990s and has since spread to all the ports in the country.[68] In 2003 there were three countries in the region, where the private sector –chiefly international multi-port operators – was fully involved in port management and development: Djibouti, Mozambique and Tanzania. In Tanzania management of the container terminal of the port was assigned to a consortium involving Philippine participation. In Mozambique's port of Maputo port management was assigned to a consortium involving UK, Swedish and Russian participation. Given the importance of port efficiency and the size of the investments involved in improving port efficiency, the question naturally arises whether ACP countries want to consider opening up auxiliary and port services to trade in mode 3 linked or not to mode 4.

The maritime industry is one of the few services sectors for which the Cotonou Agreement contains rather specific provisions. It states (in Part 3, Title II, Chapter 4: Trade in Service, Article 42) that the parties "undertake to promote the liberalisation of maritime transport and to this end apply effectively the principle of unrestricted access to the international maritime transport market on a non-discriminatory and commercial basis (paragraph 2)" and that "each Party shall grant, inter alia, a treatment no less favourable than that accorded to its own ships, for ships operated by nationals or companies of the other Party, and for ships registered in the territory of either party, with respect to access to ports, the use of infrastructure and auxiliary maritime services of those ports, as well as related fees and charges, customs facilities and the assignment of berths and facilities for loading and

[67] The EU percentage would be significantly higher if the distribution was based on ownership rather than registration. Greece, for instance, is the most important maritime country based on vessel ownership. But only around 25 per cent of its ships are also registered in Greece (UNCTAD, 2004). Registering abroad, for instance in a country with an open registry, may have advantages with respect to taxation, adherence to safety and other standards and with respect to the wage costs of manning ships.

[68] UNCTAD (2003).

unloading (paragraph 3)."[69] The agreement thus mainly refers to the facilitation of mode 1 imports. Facilitation of mode 1 imports of maritime services is, indeed, in the interest of Southern and Eastern African countries, but it is likely to be more beneficial for countries in the region to bind this mode of maritime services trade at the multilateral level rather than the regional level.

(b) Air transport services

International air transport is a complex industry, that in addition to the transport of people and cargo includes various ancillary services, such as airport, ground handling, leasing and catering (WTO, 2005). The air transport industry has traditionally been characterized by significant government interventions, including public ownership and entry restrictions. In the past decades OECD countries have made substantial progress in liberalizing ownership and market access in air transport. But the industry remains characterized by significant levels of state ownership and pervasive controls on entry, capacity and tariffs.[70]

In 2001, Africa's share of the total number of international passengers carried was around 4 per cent at the global level, while its share in the world's air cargo traffic was 1.6 per cent. In the same period Africa accounted for around 2 per cent of world GDP, but 13 per cent of the world population. The low level of development of the air transport sector is therefore striking, even when the continent's low level of GDP is taken into account. African air transport does not only fare badly when compared to the rest of the world but also when compared to other modes of transport in Africa. Air trade among African countries was estimated only 6.4 per cent of the overall African cargo market in 2001.[71] This low level of the intra-African cargo traffic illustrates an underdeveloped intra-regional trade pattern and serious deficiencies in air infrastructure. The limited number of regional hubs and the lack of a well-developed network of domestic airports are likely to be serious barriers to the growth of both merchandise trade and services trade, in particular tourism. In Southern and Eastern Africa, South Africa and, to some extent, Kenya are exceptions to this rule, but elsewhere there is very little intermodal competition and road transport dominates both passenger and cargo transport.

Easy access to tourist destinations in terms of international transport and facilities is considered to be a prerequisite for the development of tourism. This includes an extended domestic air network, frequent flight schedules and linkages through hubs. As for merchandise trade, the air transport sector is of particular importance for the transport of fruits, vegetables, cut flowers and fish, that are export products for a number of countries in the region. Also apparel, textiles and fabrics are exported via air. Air imports are dominated by computers and peripherals, telecommunication and transport hardware and pharmaceutical goods. Flights to and from Europe dominate the inter-continental air traffic, largely due to Europe's proximity to Africa and its long-standing historical and investment ties with the region. In 2001, for instance, out of inter-continental cargo traffic in Africa, 65% related to trade with Europe and 14% to trade with the Middle East.[72] Europe is also the most important sender region of tourists to Southern and Eastern Africa, thus explaining Europe's role in passenger air transport.

The efficiency of a region's air transport network is mainly determined by three aspects: the availability, size and efficiency of airports; the efficiency of air companies serving the region; and the

[69] Reference to the importance of a "safe and clean marine environment" is made in the first paragraph of Article 42 and paragraph 4 states that "The Community shall support the ACP States' efforts to develop and promote cost-effective and efficient maritime transport services in the ACP States with a view to increasing the participation of ACP operators in international shipping services."

[70] Another particularity is the existence of an international regime with specific international organizations and institutions. See WTO(2005) for a discussion of IATA (International Air Transport Association) and so-called code-sharing agreements from a competition policy point of view.

[71] ATAG (2003).

[72] ATAG (2003).

governing market access conditions that determine competition in the sector. The positive effect trade liberalization can have on each of this three aspects will briefly be discussed in the next paragraphs.[73]

A number of countries, including South Africa and Tanzania, have already privatized their on-ground aviation services. Other countries should consider to do so swiftly, as privatization and increased competition is expected to lead to improvements in the quality of services, that are crucial, in particular for the tourism sector.[74] Like in the case of harbour services, countries may want to consider to allow for the entry of foreign companies into the market of on-ground services.

State owned companies still dominate air transport in the region, although many countries allow for some level of competition from private domestic companies. Foreign companies also serve local markets but in most cases their access to that market is limited. Indeed, if the sector was fully opened at the global level, most state-owned airlines would not be able to survive in their present form. Restructuring and privatization is therefore necessary and desirable, but this is a rather contentious issue, as it has also been in many industrialized countries. Donor assistance may be helpful for the successful implementation of a privatization strategy.[75] In parallel, African countries could consider to allow for certain levels of foreign participation in domestic airlines.[76]

Market access in international air transport is defined by a number of variables, including the designation of carriers, the entry of these carriers on specific routes and the flexibility to establish capacity and prices on routes. The industry has defined eight different types of international air traffic, which it has called freedoms. These range from the first freedom to overfly another country to the right to carry freight and passengers on domestic routes in a foreign country. The failure to agree on a multilateral approach to traffic rights has implied that they are most of the time negotiated at the bilateral level. The granting of the first two freedoms has typically not been controversial.[77] Similarly, the third and fourth freedom have often been granted in the context of bilateral agreements, although the terms and conditions of access have traditionally been quite restrictive.[78] In 1992, the United States signed an agreement with the Netherlands that went further that the typical existing bilateral agreements and included, among others, the fifth freedom, i.e. the right to carry freight and passengers between two countries by an airline of a third country on route with origin/destination in its home country. Other innovative aspects of the agreement were that it allowed companies from the partner country to determine price, capacity and frequency of their flights and about the routes they would take to connect the two countries. This agreement therefore induced a significantly higher degree of competition than previous bilateral agreements. It was referred to as an "open skies" agreement and this term has since then been used for similar agreements.[79]

The traffic rights granted to other countries thus determines to a large extent the level of competition domestic companies face in their market. If, for instance, Tanzania grants the fifth freedom to US or South African airlines, those airlines can take passengers in Tanzania and bring them to Kenya on a

[73] Note that the region has also major safety problems (e.g. IATA, 2005).

[74] Ndulo et al. (2005).

[75] See the discussion in Goldstein (1999).

[76] See WTO (2005) for an overview of foreign ownership regulations in air transport in a number of countries belonging to different regions in the world. Most countries impose limits on the extent of foreign participation in domestic airlines in order to ensure that the control over national carriers remains in the hands of nationals. See also the related discussion in Goldstein (1999) of the Kenyan experience with privatization and foreign participation.

[77] The second freedom refers to the possibility to make a technical stop in another country. See the discussion in WTO (2005).

[78] The third freedom refers to the right to carry freight and passengers from the home country to the partner country and the fourth freedom to the right to carry freight and passengers from the partner country to the home country.

[79] See WTO (2005) for a more detailed description of the characteristics of "open skies" agreements.

route US/South Africa-Tanzania-Kenya. This is likely to increases competition for Tanzanian airlines on routes within the African region.[80]

Efforts exist to create one "open sky" for the entire African region, or at least large parts of it. It is expected that this would lead to increased competition at the regional level, probably triggering a series of mergers and/or the creation of consortia. In an ideal scenario, the region would end up with fewer but more efficient carriers and would see its bargaining power increased when negotiating air traffic rights with partners outside the continent.[81]

The most important project of this type in terms of countries involved was borne out of the Yamassoukro Declaration (YD) in 1988. This Declaration was signed by 52 African countries including most of the Southern and Eastern African countries discussed here. The declaration was reviewed in 1994 and new impetus was given to the project by the 1999 "Decision on the implementation of the Yamassoukro Declaration concerning the liberalization of air transport and market access." Implementation of the Declaration would imply increased and unified market access for participating countries and the Yamassoukro has been referred to as an "open skies" agreement for Africa. Implementation was supposed to take place within 2 years but in 2005 only a subgroup of countries, i.e. the East African Community (Kenya, Uganda, Tanzania), had announced that its Bilateral Air Services Agreements had been aligned to the provisions of YD and that it had thus become the first subregion in Africa to accept YD. South Africa, Kenya, Zambia and Zimbabwe have in the meantime opted for a somewhat lighter form of liberalization and agreed to allow for unlimited flights with multiple designations of airlines allowed between one country and another.[82]

The United States has shown interest in the African air transport market, among others by launching the "Safe Skies for Africa" initiative in 1998. By October 2005 the United States had concluded 72 bilateral opens skies agreements, among them six countries of the group discussed in this paper: Ethiopia, Madagascar, Namibia, Rwanda, Tanzania and Uganda. The European Union only recently managed to agree that open skies agreements are a regional rather than a bilateral matter, although significant limits to the jurisdiction of the Community exist, which has led to a certain level of confusion among member states and third countries.[83] In a communication from March 2005 the European Commission outlines the agenda for its external aviation policy. In contrast to Asia, Africa does not appear to be a priority region for the European Commission. The continent is rather referred to as a region which stands to "gain economically and/or politically from aviation negotiations with the EC", through, for instance regional co-operation in terms of exchange of regulatory know-how and/or technical assistance. The impression arises that the issue of market access is considered to be of minor importance when it comes to Africa. This may however reflect that Europe currently has a privileged access to the African air transport sector for historical reasons.

Overall, the air transport sector does not seem to be a sector in which Southern and Eastern African countries stand to gain by giving privileged access to the European Union. There is no a-priori reason, why it would be more efficient for African countries to open up their on-ground services and/or their airlines for foreign direct investment from Europe rather than also allowing for FDI from other regions. Concerning traffic rights, it would in principle be interesting to reach an "open skies" agreement between the two regions, in particular taking into account the role of Southern and Eastern Africa as a tourist destination for Europeans. Although such an agreement would probably be mutually beneficial, it is unlikely for it to be put in place in the near future. Official EU documents on the matter show that there is no serious interest in the African region for the time being. This may

[80] It also increases competition for all the other African countries, e.g. Kenya in this example. Agreement of third countries therefore needs to be obtained for each individual route in order to actually apply the fifth freedom.

[81] See Goldstein (1999).

[82] See press release from IPPmedia from October 26, 2005: http://www.ippmedia. com.

[83] Commission of the European Communities (2005).

change if the open skies agreements existing among some of the Southern and Eastern African countries would be expanded to the entire region. But even if this was the case, the competence of the European Commission to negotiate such agreements is not entirely clear and would probably imply the involvement of directorate generals other than the one in charge of trade negotiations.

4. Business services

Cross-border trade in business services, especially the so-called "IT-enabled services", is today among the fastest growing areas of international trade. While the industrial countries are the largest exporters of such services, some of the most dynamic exporters are developing countries. Three factors are responsible for this phenomenon.[84] First, advances in technology have made cross-border trade possible in a number of services that were previously only tradable through the movement of providers. Second, thanks to substantial investments in education a number of developing countries are endowed with significant pools of skilled labour, and the absence of commensurate employment opportunities has ensured their availability at relatively low wages.[85] Finally, innovations in business practice have led to the out-location of service activities by multinational enterprises in the manufacturing and services industry to offshore operational units or their outsourcing to foreign third-party suppliers.

Activities commonly outsourced to developing countries include abstracting and indexing, data capture and processing, data warehousing, electronic publishing, legal transcription, litigation support, mailing list management, medical records management, medical transcription, remote secretarial services, technical writing, telemarketing, teleservices and website design and management.[86] Most people think of India when they hear the word "outsourcing". A recent study by A.T. Kearney (2003) confirms that India is the most attractive location for offshoring business processing from the U.S., followed by Canada, Brazil, Mexico. No African country is among the top eleven outsourcing locations in this study. Although the export of "other business services" represents a sizeable share of services exports in a small number of countries in our sample, it is safe to say that so far the offshoring boom has largely ignored Africa. But exceptions exist.

South Africa is developing into an attractive alternative to India for outsourcing, where well educated speakers of French, English and German are staffing growing calling centres catering mainly to European companies. Bowman International Sports, operating under a UK licence, built a 200 job call centre in Mauritius in 1996 and an Israeli company has been piloting data processing in Zimbabwe.[87] There are also examples of African companies successfully entering e-commerce independently. An UNCTAD Report described in 2001 the success of Ethiogift, a company operating out of Addis Ababa and offering 48-hour delivery of sheep, cakes, flowers and liquor within Ethiopia.[88] The site targets the large, affluent Ethiopian diaspora in Europe and the US implying mode 1 exports from Ethiopia to Europe and the US.

The before-mentioned report by A.T. Kearney (2003) discusses the determinants of competitiveness as an outsourcing location. They include cost of labour, management and infrastructure costs, tax or treasury impact, intellectual property security, geographic proximity, cultural compatibility, country

[84] Mattoo and Wunsch (2004).

[85] Skilled labour wages may be low when compared with the wages of skilled labour in industrialized countries but high when compared with other wages within the developing country. Indeed, many developing countries have experienced increases in the wage premium for skills in recent years (see, for instance, Hoekman and Winters 2005) indicating that there may be scope for further investments in education.

[86] Nielson and Taglioni (2004).

[87] Nielson and Taglioni (2004) and te Velde et al. (2004).

[88] UNCTAD Press Release TAD/INF/PR/35 from 20th November 2001: "From Selling Sheep to Transcribing Tapes".

infrastructure, risk (economic political, government support), employee retention, language barriers and literacy rates, education level of workforce, size of labour market, outsourcing experience. The main drawback of many Southern and Eastern African countries as outsourcing locations may currently be linked to insufficiencies in infrastructure, in particular telecommunication, and the lack of adequate trade-supporting services such as insurance and business information. But to the extent that such impediments are overcome ACP countries could move into the export of business services. In this context, it has been argued in the literature that it could be in the interest of developing countries to encourage the introduction of binding commitments in modes 1 and 2 across a broad range of services sectors.[89]

5. Tourism

For a number of Southern and Eastern African countries the tourism sector is an important sector in terms of employment generation, contribution to GDP and to export earnings.[90] More importantly it is in many cases a growing sector and the annual growth rate in international tourist arrivals in Africa has tended to outperform the growth rate for the world as a whole over the past decade. In particular it is the only region that was able to record positive growth rates in 2001, 2002 as well as 2003, three years that have been particularly difficult for the tourism industry.[91]

In 2003, international tourist arrivals in Africa originating from the same region amounted to 13.2 million or 43 per cent of the total, making it the region with the lowest percentage of intraregional traffic in the world. As for interregional traffic, flows are largely dominated by Europe which accounted for three quarter of arrivals from outside the region and 33 per cent of all arrivals. Though still predominant in terms of interregional flows to Africa, traffic from Europe lost three percentage points in terms of market share between 1990 and 2003.[92] Simultaneously there was a reinforcement of the relative weight of arrivals originating from Asia and the Pacific. In 2003, the share of European tourism was 30 per cent in Eastern Africa and only 20 per cent in Southern Africa. In both regions intraregional arrivals are predominant, but Europe is the most important sender of tourists from outside the region. The share of arrivals from Asia and the Pacific in total arrivals was less than ten per cent in both regions in 2003.

Africa is widely recognized for the quality of its resource endowment for tourism, but notwithstanding the promising growth figures from recent years, the industry is far from reaching its full potential.[93] The reasons for this are numerous and vary across countries. They include poor infrastructure, such as roads, electricity and water supplies; insufficient accommodation; unsatisfactory public health services; poor telecommunication facilities; and in a number of cases security problems. Furthermore, delays in applying more efficient management systems and the persistence of practices that impede their competitiveness have contributed to slow development of the tourism industry.[94] The air distribution channels that deliver tourists to and from the region have also been identified as an important restriction on the flow of tourists to Africa. For a number of reasons, arguably including the anti-competitive behaviour within the air transport industry and among tourism distributors, airfares to Africa remain very high, thus limiting the pool of middle to lower-income tourists able to afford a holiday in Africa.[95]

[89] Mattoo and Wunsch (2004).
[90] Gauci et al (2002).
[91] World Tourism Organization (2005).
[92] WToO (2005).
[93] Christie and Crompton (2001).
[94] Gauci et al. (2002) and Christie and Crompton (2001).
[95] Gauci et al. (2002) and Christie and Crompton (2001).

In theory, the quantity and quality of accommodation supplied could be increased by attracting foreign investors. But the private sector will respond to the environment it finds. The greater business confidence, the higher investment is likely to be. Conversely, a weak business environment will spawn low investment or enclave investment that discourages participation by local populations, a common complaint about tourism. A mix of development assistance to help address these issues, which would benefit a range of economic activities, and private sector investment will be required to enable African destinations to compete in the international tourism market.[96]

Among the main broad service sectors subject to WTO negotiation in the past, tourism has drawn by far the highest number of commitments.[97] This is true if all WTO Members are taken together and is also true for the group of developing and least-developed countries. The high number of commitments in tourism services from developing countries is fairly easy to explain, taking into account that most of these countries seem to enjoy a comparative advantage in this area, and access conditions to the main activities (e.g. hotel and restaurants) are fairly liberal worldwide. Other more "sensitive" areas, such as travel agencies and guides, are more often reserved to nationals. Overall the level of commitments, in terms of bound access opportunities, by African countries appears to be below the average of WTO Members. Nevertheless significant levels of commitment exist for both consumption abroad and commercial presence. A possible explanation for the latter is that African countries are keen to open to the commercial presence of foreign tourism enterprises because they either do not have the resources or the knowledge to direct tourism development in their own territories, relying instead on external expertise.

Although several Southern and Eastern African countries have made significant commitments in the tourism sector at the multilateral level there is room for further liberalization and as a consequence it is possible to conceive an approach leading to deeper integration between EU and ACP countries than at the multilateral level. Taking into account that most extra-regional tourists come from Europe, it is, indeed, possible to argue that in this particular sector preferential liberalization in the context of EPA negotiations could be mutually beneficial. Mode 3 and mode 4 imports from the EU could create a supply of accommodation and tourism services specifically targeting European customers. Mode 1 liberalization would facilitate African travel agencies and guides to offer their services to European customers, for instance via the internet. All this leading to increased mode 2 exports from Southern and Eastern Africa to the European Union.

Mode 4 flows could also go in the other direction, in particular if they are not limited to high skilled workers. European tourism areas experience sharp short-term increases in labour demand during the tourism season and it is not rare for this demand to be satisfied by foreign labour. Mode 4 liberalization would give African workers a chance to provide their services in Europe. The experience they gather and the skills they obtain during their temporary stays abroad could be useful upon their return to their home countries if they continue to work in the tourism sector and attend European tourists. It should be noted in this context that the potential for mode 4 exports from Africa to the European Union in this sector depends to some extent on the definition of mode 4. GATS Article 1 defines Mode 4 trade as the supply of a service "by a service supplier of one Member, through presence of natural persons of a Member in the territory of any other Member." It appears that foreign workers employed by a locally-owned firm are not covered by the definition of mode 4 under GATS.[98] This would, for instance, imply that African waiters employed in a restaurant in Europe and owned by a European would not fall under Mode 4. Yet, EPA negotiators are not obliged to adopt the GATS definition and may want to opt for a broader definition of Mode 4.

[96] Christie and Crompton (2001).

[97] Marchetti (2004).

[98] In the services negotiations in the context of the Doha Round a number of countries have nevertheless requested commitments on foreign employees of domestic companies (Marchetti, 2004).

6. Health

Trade in health services can take place in all four modes.[99] Cross-border delivery (mode 1) includes shipment of laboratory samples, diagnosis, and clinical consultation via traditional mail channels, as well as electronic delivery of health services, such as diagnosis, second opinions, and consultations. Many cross-border telemedicine initiatives have emerged in recent years. They tend to imply exports of services from relatively wealthy to less wealthier countries. Consumption abroad (mode 2) refers to the movement of consumers to the country providing service for diagnosis and treatment. Under this mode, affluent patients in developing countries seek specialized high-quality treatment abroad in hospitals in industrialized countries. But also developing countries, like Cuba, India, South Africa and Thailand export health services via consumption abroad.

Commercial presence involves the establishment of hospitals, clinics, diagnostic and treatment centres and nursing homes and the services trade in this mode typically implies imports by developing countries from industrialized countries. Concerns have been raised about the likelihood for foreign investors to focus on certain segments of the health sector resulting in a two-tiered system where the corporate sector concentrates on the treatment of wealthy patients and does not address broader social needs.[100]

Health services are also traded via the movement of health personnel, including physicians, specialists, nurses, paramedics and midwives. Mode 4 flows in health services are most commonly associated with nurses and doctors from developing countries offering their services in industrialized countries, that in many cases suffer from shortages in the supply of this type of services. In this context concerns have been expressed that mode 4 flows may result in a brain drain problem, i.e. the problem of people leaving their country to offer their services elsewhere after having enjoyed an education in their home country. On the other hand it is acknowledged that home countries often take advantage of such flows as suppliers of health services send money back to their home country. It should also be taken into account that mode 4 trade mainly refers to temporary stays of service suppliers abroad.[101] The brain drain could therefore in principle rather take the character of "brain circulation", as services suppliers return to their home country with increased professional experience.

In the context of multilateral trade liberalization the health sector is one of the sectors with the lowest level of commitments by WTO Member countries. While over 90 per cent of WTO Members undertook some form of commitment on tourism services and about 70 per cent included financial or telecommunication services in their Uruguay Round schedules, less than 40 per cent made commitments on education and health. It also appears unlikely that the scope and content of current commitments on health services will change significantly as a result of the Doha Round negotiations.[102] This may reflect the concern that governments in general seem to have with the liberalization of "social-type" services. Indeed, it has been argued in the literature that liberalization in these sectors is more likely among relatively similar countries or within the context of regional agreements.[103]

Assuming that liberalization at the multilateral level remains limited, is there scope for more significant liberalization between Southern and Eastern African countries on the one hand and the EU on the other hand in the context of EPA negotiations? If trade in health services was fully liberalized the most likely outcome would be that African countries in the region start importing services via mode 3, possibly accompanied by some mode 4 inflows of relatively skilled health service providers. These inflows would favour the expansion of the private health sector in the importing country. If the

[99] See discussion in Chanda (2002).
[100] See for example Chanda (2002) and Kinuthia (2002).
[101] Although the definition of "temporary" is not very precise in the GATS.
[102] Adlung and Carzaniga (2001).
[103] Stephenson (2002).

newly created entities target European patients, mode 3 imports could in turn lead to mode 2 exports. Southern and Eastern African countries are, however, not particularly well positioned for this type of exports. Geographical vicinity to the targeted markets is likely to be an important determinant of mode 2 flows in health services and Northern African countries, like Morocco and Tunisia, are better positioned to serve the European market. The prevalence of contagious diseases in the Southern and Eastern region may also be an important concern to potential customers.

The possible expansion of a private sector serving domestic patients or foreign patients from Africa has raised distributional concerns, as mentioned before. Yet, as pointed out in Adlung and Carzaniga (2001) appropriate regulation in the home country can help to limit possible negative effects and stimulate positive spill-overs from mode 3 inflows to the overall population. A country may, for example, require all private hospitals to reserve a minimum percentage of beds for free treatment for the needy, to offer some basic medical services in remote rural areas, or to train beyond the number required for the purpose of these institutions.[104]

In addition to mode 3 inflows the liberalization of health services in the context of EPA could lead to the export of services via mode 4. Potentially such flows could involve service providers of different skill levels. Indeed, the emigration of nurses from Sub-Saharan Africa, is a long-existing phenomenon and one that has recently become more important as the numbers have increased significantly.[105] In 2003 the "top 20" source countries of nurses into the UK (excluding those coming from the EU) included six of the countries discussed here and the number of nurses migrating has increased significantly (see Table 3). Note also that South Africa sends significant numbers of nurses abroad. This country in turn receives nurses from surrounding African countries like Ghana, Malawi and Zambia.[106]

Entry of foreign nurses into the UK has been facilitated in the past by the fact that the nursing sector has been categorized as a sector of recognized skill shortage in the UK. In such sectors it was easier to obtain working permits than in other sectors. Recently the UK has also introduced sectoral schemes facilitating the entry of workers in the hospitality sector and the food manufacturing sector. Many of these workers, including those reflected in Table 3, do not necessarily fall under the concept of Mode 4 trade according to the GATS definition, in particular if they are employed by UK companies or in the public sector.[107]

Table 3: Overseas-trained nurses registered in the UK 1998-2003 (excluding those coming from the European Union)

	1998-1999	2002-2003
Botswana	4	42
Kenya	19	152
Malawi	1	57
Mauritius	6	60
Zambia	15	135
Zimbabwe	52	493
South Africa	599	1480
Total	3440	12298

Source: Munjaja et al. (2005).

[104] Adlung and Carzaniga (2001) point out that such regulation is also possible at the multilateral level and would not normally be in conflict with GATS provision even

[105] Munjaja et al. (2005).

[106] See also Buchan et al. (2005).

[107] Governmental services are not covered by the GATS.

7. Mode 4

Services trade in mode 4 is generally regarded as a possible area of comparative advantage for developing countries and therefore deserves a separate discussion. Mode 4 liberalization has so far been limited in the context of GATS and rather biased toward highly skilled personal. Besides, liberalization under GATS currently reflects a strong link with the wider objective of attracting foreign investment, as the highest number of commitments has been made for intra-corporate transferees.[108] Despite their alleged interest, developing countries as a group have found it difficult to articulate a collective position on the issue of mode 4 in the ongoing Doha-negotiations. The first collective proposals on mode 4 were submitted in July 2003 and March 2004 by a group of 14, respectively 18 developing countries.[109] The only African country in this group was Egypt, that is not an ACP country. Egypt has also submitted a request with respect to mode 4 liberalization to Australia and the European Union. The latter is also the case for Kenya. This ambivalent attitude towards mode 4 liberalization can also be observed at the regional level within Africa, where many impediments to the temporary movements of natural persons exist, including the non-recognition of the qualification of foreigners and the requirements for up-front payments by foreigners who wish to provide a service.[110]

Currently the expectations for any significant breakthrough with respect to mode 4 liberalization at the multilateral level are rather low.[111] It is also likely that further liberalization at the multilateral level continues to concentrate on high-skilled services rather than low-skilled services in which numerous developing countries arguably have a comparative advantage. Some observers indeed suggest that GATS negotiations are more likely to be fruitful if they focus on the high skill segment, for which there seems to be an emerging international market.[112] Greater progress on the movement of low-skilled labour, instead, may be possible at the bilateral or regional level and promises significant gains for home and host countries.[113] Examples of bilateral labour agreements that have to some extent improved access for the low-skilled exist, like those between Spain and Ecuador, between Canada and the Caribbean and between Germany and Eastern Europe.[114]

Increased access for Southern and Eastern African service providers through mode 4 to EU markets and vice versa thus appears to be a natural element of EPA negotiations. The advantage of liberalizing Mode 4 movements within the context of Economic Partnership Agreements, is that the terms and conditions of such liberalization can be agreed upon by a smaller number of trading partners than at the multilateral level. It is, for instance, likely to be easier to design specific temporary work permits for EPA members, than to agree on the design of a more general "GATS-visa" at the multilateral level. Existing bilateral or regional schemes, like the NT-visa in the context of NAFTA, could be used for guidance.

In the design of such a scheme it would be in the interest of African countries to de-link mode 4 flows from mode 3 and from the nationality of the employer in the destination country. More generally, it would be possible to deviate from the potentially restrictive definition of mode 4 under GATS. The literature also provides guidance as to the characteristics of such a scheme that would facilitate acceptance of the scheme by potential host countries. Mattoo (2005), for instance, suggests that source countries should accept certain obligations including pre-movement screening and selection,

[108] See for instance WTO (2004).

[109] Marchetti (2004).

[110] Tanzania, for instance, requires a payment of $15,000 from any foreign architect who wishes to provide services there (Ikiara, 2000)

[111] Marchetti (2004).

[112] See Mattoo (2005) on the possible characteristics of politically feasible liberalization commitments.

[113] See for instance Winters and Walmsley (2005).

[114] Mattoo (2005). See WTO (2004) for information on the number of temporary workers moving to Germany in the context of bilateral agreements.

accepting and facilitating return, and commitments to combat illegal migration. He argues that co-operation at the source can help address security concerns, ensure temporariness and prevent illegal labour flows in a way that host countries are incapable of accomplishing alone. As a result this cooperation could according to Mattoo (2005) constitute a service for which the host may be willing to pay by allowing increased access.

Several observers have pointed out that governments may be reluctant to make ambitious and binding commitments on mode 4 because of the cyclicality of labour market movements.[115] Demand for certain types of workers may go up during some periods and fall dramatically during other periods. Making binding commitments at constant levels may therefore face stiff political resistance at the national level. To avoid this, Mattoo (2005) suggests to design mode 4 commitments in such a way that host countries are allowed to vary the level of access depending on the state of the economy. He refers to the example of the bilateral agreement between Germany and certain Eastern European countries, under which the quota on temporary migrants increased (decreased) by 5% for every one percentage point decrease (increase) in the level of unemployment.

Southern and Eastern African countries may want to consider requesting that temporary access for their service providers be given across services sectors. Sectors in which European countries are most likely to face (temporary) excess demand that could be filled by African service providers include the tourism sector, social-type services (e.g. health, child care, care of the elderly), construction, transport and distribution. It could be an alternative to focus negotiations on these sectors of excess demand, if a comprehensive arrangement on Mode 4 movements is considered to be out of reach.[116]

D. CONCLUSIONS

Many Southern and Eastern African countries are simultaneously engaged in trade negotiations at the multilateral level and at the regional level in the context of the EPA negotiations with the European Union. Trade negotiators thus face the difficult decision which extent of liberalization to pursue at which level. Based on arguments developed in the literature this paper contends that preferential liberalization in certain services sectors can be beneficial for Southern and Eastern African countries and may be the preferred option when regulatory aspects and the prospects of technical assistance are taken into account. It is, however, crucial not to give preferential access in sectors where third country suppliers hold a comparative advantage at the global level or are likely to develop it in the near future. Although this is an argument that holds in general, it is particularly relevant in the services sector.

Based on the above, the paper argues that countries in the region may stand to gain from including the financial sector and the tourism sector in the EPA negotiations. They may also stand to gain from including mode 4, in particular if EPAs use a broader mode 4 definition than the one in GATS. Mode 4 liberalization is more likely to be successful in a regional than in a multilateral setting and ACP countries may have a potential to export services in this mode. Trade flows in general and tourism in particular would benefit from an open skies agreement between the African and the European region, but such an agreement seems unlikely to be concluded in the near future.

The Cotonou Partnership Agreement that forms the basis for the ongoing negotiations provides for the possibility of combining liberalization with technical assistance from the European Union. Such assistance could be directed towards the sectors and/or modes that are subject to negotiations. In the financial sector it could be directed towards the improvement of prudential regulation and in the tourism sector assistance could be used to address environmental concerns, to expand the supply of

[115] See, for instance, Marchetti (2004) and Mattoo (2005).
[116] See also Adlung and Mattoo (forthcoming) on this issue.

and improve the quality of accommodation and to assist marketing efforts by African countries. With respect to mode 4, assistance could be used for creating the legal and institutional set-up in sender countries to ensure that only adequately qualified service providers move abroad and to ensure that their stays in host countries are temporary.

For a number of services sectors, though, a multilateral road seems to be more appropriate than a regional approach. This is, for instance, the case for telecommunication and certain transport and business services. The question therefore arises whether an EPA that only embraces a limited number of services sectors is consistent with the condition in GATS Article V that regional agreements ought to have "substantial sectoral coverage".

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