

Dangers in liberalization of services and investment in EPAs

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Services and investment in EPA negotiations

The current trade negotiations between the European Union (EU) and groups of African, Caribbean and Pacific (ACP) countries for Economic Partnership Agreements (EPAs) are set up to become free trade agreements (FTAs). As in many FTAs, liberalization of trade in services as well as liberalization of investments might become an important aspect of the EPA negotiations. The EU is very interested in including liberalization of services and investment and is pushing the ACP to negotiate on these issues. While the ACP are in principle not obliged to start negotiations, the EU and ACP have already agreed together that EPAs would cover liberalization of services and investment.

Trade in services

Services are for instance: wholesale trading and distribution (e.g. supermarkets), tourism, banking and insurance (financial services), transport, making translations, health care, water distribution, education and music production. The services sector thus covers a large and diverse range of economic activities. Some of these activities are informal in many developing countries, such as small informal shops around the corner.

Liberalization of "trade in services" has already happened to a limited extent by developing countries in the World Trade Organization through the Agreement on Trade in Services (GATS). The GATS definition of "trade in services" will be used in the EPA negotiations. There are four different ways ("modes") which are used to classify trade in services:

- ❑ (mode 1) **services cross the border** e.g. a translation is transmitted through e-mail to an other country from where the client pays for the translation;
- ❑ (mode 2) **consumption of a service abroad** e.g. a patient goes to a hospital in a foreign country; an EU tourist goes on holiday in an ACP country;
- ❑ (mode 3) **establishment of a foreign service company**, e.g. a foreign bank establishes new branches where people can deposit their money savings, a foreign

water company buys up a privatized water distribution company and provides water distribution services at commercial rates;

- ❑ (mode 4) **movement of service personnel** e.g. a nurse works temporarily in a hospital abroad.

Note that much of trade in services is covered by mode 3, which in fact is about investment; in other words, EPAs that include liberalization of trade in services will in fact also liberalize foreign direct investment in the services sector. Developing countries are officially in favour of mode 4 liberalization because they have more migrant labour but the EU fears too much migrants.

What are the problems when liberalizing 'trade in services'?

The services sector is highly developed in the EU and provides for most of the EU's jobs, income and economic growth. The EU is the world's major exporter and importer of services¹ and a major investor around the world. It has many very large service multinationals that operate worldwide. The ACP countries are exporting little services (1.5% of world exports in 2000²), mainly tourism (mode 2), and do not have many services' investors abroad. Although services play an important role in many developing countries, they are mostly for national use and are not so highly developed as in the industrialized countries. This means that EPAs which would include trade in services would provide much less potential export benefits to the ACP than to the EU. There would be **unbalanced trade in services between the ACP and the EU**.

Liberalization of services and importing new services means that a country allows foreign services and their providers to enter the national market and has to eliminate measures that discriminate between foreign and national services (providers). This is a **complex** process, which has not only benefits such as new and efficient services, but also negative effects. Problems caused by foreign service providers are for instance that they:

- ❑ focus on rich clients and neglect of poor consumers (e.g. in health and financial services),
- ❑ rapidly dominate the market and closing of local service providers,
- ❑ only work with big suppliers (e.g. foreign supermarkets mainly source their products from large farms and large industries),
- ❑ focus on short term profits, and repatriate their profits to the headquarters abroad.

In case services are liberalized, the right **regulations** need to be introduced or to be in place and supervisory instruments need to ensure their implementation so that consumers are

¹ WTO, World Trade Report 2004, p. 21 (Appendix Tabel IA.2)

² D. W. te Velde, Special and differential treatment in Post-Cotonou Services negotiations, Trade Negotiations Insights, ECDPM, May 2004, p. 4-5.

protected. This is costly, needs time as well as the necessary expertise, which is often lacking in developing countries (and even in the industrialized countries).

What are the problems of negotiating trade in services in EPAs?

If EPAs will liberalize services as in the GATS, this might result in rules that prevent governments and parliaments to take certain measures because they are considered to 'restrict trade' in services. Such rules **limit the way how governments and parliaments want to regulate** services industries as they see best for their country and population.

Negotiating services liberalization needs to be based on democratic choices and consultation with different ministries, parliamentarians, NGOs, consumers, small businesses, etc. This is time consuming which needs a lot of expertise. However, the ACP need to make progress in further liberalization of services in the current GATS negotiations at the WTO by December 2005. This means **that ACP negotiators in trade in services need to intervene in the WTO and EPA negotiations at the same time**. As many ACP countries lack the expertise and financial or human resources to do so, this is very problematic, especially if the EU wants the ACP to liberalize more in EPAs than in the GATS negotiations.

The GATS agreement has an article (Art. 5) that says that free trade agreements must **liberalize a substantial part** of the services sectors of the countries involved. Developing countries do not need to liberalize all services sectors in an FTA, according to this GATS article, and do not need to open up as much as the EU should do (non-reciprocity). However, it is not clear how much services sectors can be excluded from the EPAs. The EU intends the EPAs to open up ACP markets for services from the EPA region and for services from the EU. The interests of the EU are amongst others to open up maritime transport/shipping, financial services, and water distribution. The EU is interested to get market opening in more ACP service sectors than the ACP have opened in the GATS agreement.

Liberalizing investment

The main argument used in favour of investment liberalization agreements is that it creates conditions that attract foreign investment to developing countries. Foreign investment is said to be "much needed" to build infrastructure and develop industries and services sectors. However, no study has given evidence that investment liberalization agreements have resulted in more or better foreign direct investment (FDI)³ for developing countries.

³ S. Szepesi, Comparing EU free trade agreements: Investment, ECDPM InBrief 6D, Maastricht, 2004, p. 2

Liberalizing investment means that foreign investors are allowed to establish themselves, or to buy up national companies. In practice, investment liberalization agreements mean that **governments have to take certain measures in order to protect foreign investors and not discriminate against foreign investors**. These measures are for instance:
(1) national treatment i.e. a government cannot treat foreign companies "less favourably" (i.e. they can be treated more favourably!) than national ones, and
(2) equal treatment of all foreign investment (Most Favoured Nation clause/MFN principle): a treatment given to a foreign investor from one particular country has also to be given to investors from all other foreign countries.

In the current the EPA negotiations, dealing with investment issues aims at introducing regulations that **eliminate discrimination** between investors of an EPA region and to **improve transparency in national investment regulations**⁴. It is very likely that if the regions negotiate such investment protection measures, in the long term they will also apply to EU investors. This means that the EPA negotiations might discuss and negotiate investment issues which the ACP have rejected to negotiate with the EU in the current WTO Doha round of negotiations.

Problems related to investment liberalization

Measures of non-discrimination between foreign investors and national investors, or among foreign investors, means that a country cannot promote one particular company. While this might avoid corruption, it also means that a country cannot support the development of a national industry or a particular foreign company that better suits the needs of the country.

The EU is also interested in measures that liberalize the movement of capital. Investors want to repatriate their profits freely out of the country without obligations to reinvest in the country. They also want to make all kind of payments with other countries. Such free movements of capital can have a negative effect in the stability of a country's currency and thus the economy of a country.

In the EPA negotiations as in other investment agreements, the issue of misbehaviour towards workers or towards consumers by foreign investors are not covered. Cases of abuse have to be dealt with at the national level and with national regulations. However, for many countries it is difficult to deal with foreign investors who can threaten to leave the country when stricter laws or measures are being introduced.

⁴ See for instance: European Commission, EPA Negotiations: Rules related issues, viewed at http://europa.eu.int/comm/trade/issues/bilateral/regions/acp/rules_en.htm

EPA negotiations on services and investment

In the current EPA negotiations, different groupings of ACP countries ("regions") included discussions and potentially negotiations about liberalization of services and investment with the EU from 2005 or 2006 onwards. The EPA negotiators might first discuss how these issues will benefit the development of the ACP regions and strengthen the economies of the countries in the regions. However, at the end, the EU will also negotiate how to get more access in the ACP regions for European services, European service companies and European investors which are mainly big European multinationals.

Many options for the EPA negotiations are still open:

- ❑ The negotiators could decide that liberalization of services and investment is not very beneficial for ACP countries and should not be included in the EPAs. In the agreement between the EU and South Africa, for instance, there is a provision that such liberalization might be discussed in the future.
- ❑ There might be no agreement on liberalizing services but (additional) resources for the development of the ACP services sector and ACP services exports.
- ❑ There might be an agreement on liberalizing services and investment. The level of the "substantial" degree of liberalization is to be decided by the negotiators but could be more than what the EU and the ACP have already agreed at WTO. The EU is willing to liberalize more than the ACP.

Conclusion

Different options for the negotiations are still possible, from refusal to negotiate on services and investments to including liberalization measures. The planned impact assessments need to urgently explore the effects of those different options, not only based on economic criteria but also social and environmental criteria. Such assessments should take place with inputs from different stakeholders. The negotiations should become more transparent and better mechanisms for information provision to parliamentarians, civil society and small producers should be set up. Most of all, such comprehensive assessments should be taken into account during the discussions and negotiations on the different EPAs.

As long as the wider impact of EPA provisions on liberalization of services and investment is not assessed and publicly discussed, they should be excluded from EPAs. Once liberalization of services are included in an EPA, Art. 5 of GATS applies and it might become difficult to exclude many services sectors from the EPA liberalization process.

Other options and alternatives to services and investment liberalization should be explored and identified to guarantee that foreign and domestic investments, development of services

and trade in services contribute to sustainable development, better access by the poor, the needs of the economy and society of the host countries, and improvement of quality.

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For more information, see : **Liberalization of investment and service in EPA negotiations: options and dangers**, by Myriam Vander Stichele (November 2004, see: <http://www.epawatch.net/general/text.php?itemID=253&menuID=6>).

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