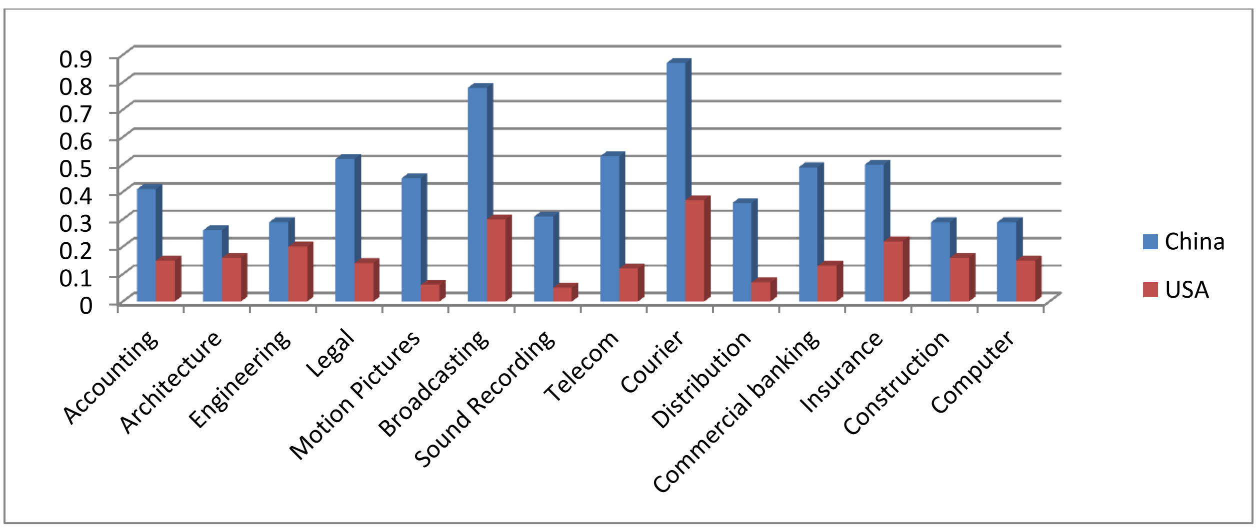
Foraging for Service Industry Growth in China

Linda Schmid,[i] September 14, 2015

China can rebalance export oriented growth with a more open and productive services economy. China's 2001 accession to the World Trade Organization (WTO) included commitments to liberalize services. China also assumed important transparency obligations. After 14 years as a member of the WTO, China's services economy remains significantly restricted. An opaque regulatory climate persists. State Owned Enterprises (SOEs) eclipse the services economy. A reduction of barriers to trade in services, a greater commitment to transparency, and a reboot of competition policy can help China build a diversified services economy.

China has taken steps to open its services economy. China's WTO services commitments span 93 service sectors.[1] For example, China's WTO Schedule of Specific Commitments allows the provision of online services in many sectors without limitations. Firms wishing to establish a presence in China must form joint ventures in most sectors. Computer and related services are free to establish without restriction. Environmental service providers are restricted to joint ventures with foreign majority ownership permitted. Despite these steps to liberalize, the OECD Services Trade Restrictiveness Index[2] notes significant barriers (figure 1). In 2015, China did amend restrictions on education, entertainment, financial, health, legal, and telecommunications under the Industry Catalogue for Foreign Investment.[3] China can do more to reduce barriers.

Figure 1 OECD Services Trade Restrictiveness Index, May 2014



Source: OECD Trade Restrictiveness Index (http://www.oecd.org)

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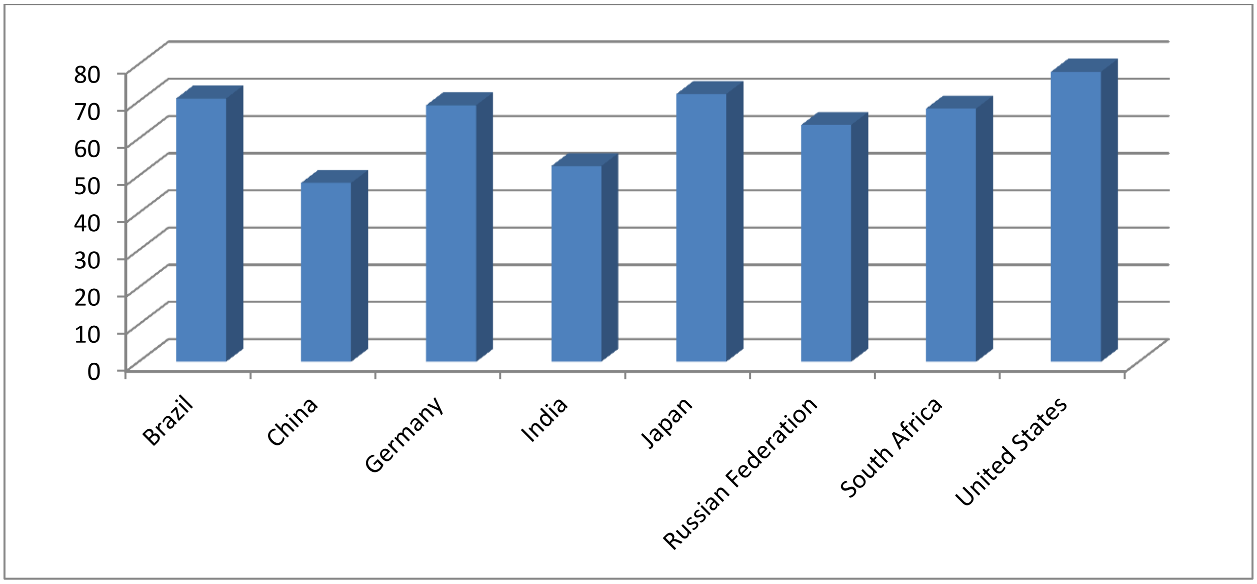
[1] WTO Trade Profile China, September 2014 (http://www.wto.org)

[2] The Index measures limits on equity share, access to public procurement, and statutory monopolies. Nationality restrictions and licensing requirements are also taken into account. OECD, STRI Scoring Methodology, (http://www.oecd.org/tad/services-trade/STRI_scoring_methodology.pdf)

[3] WTO, Report to the TPRB from the Director-General on Trade Related Developments, July 2015 (WT/TPR/OV/W/9)

China restricts trade in services while domestic production of services is modest. Services represent 48.1% of gross domestic product in China (figure 2). China's restrictive trade stance reduces the benefits of high quality services to the marketplace. For example, services contribute to the quality of the business environment. Efficient financial services governed by sound prudential regulations contribute to the qualified expansion of credit and a lower cost of borrowing. Insurance enables enterprises and individuals to mitigate risk and reduce exposure to unanticipated events. Accountancy adds rigor to corporate health as well as public sector accountability. Environmental services protect against air, water, and ground pollution. A reduction of trade barriers coupled with institutional and administrative transparency can boost these sectors.

Figure 2 Services, etc., value added (% of GDP) 2014



Source: World Bank World Development Indicators Database

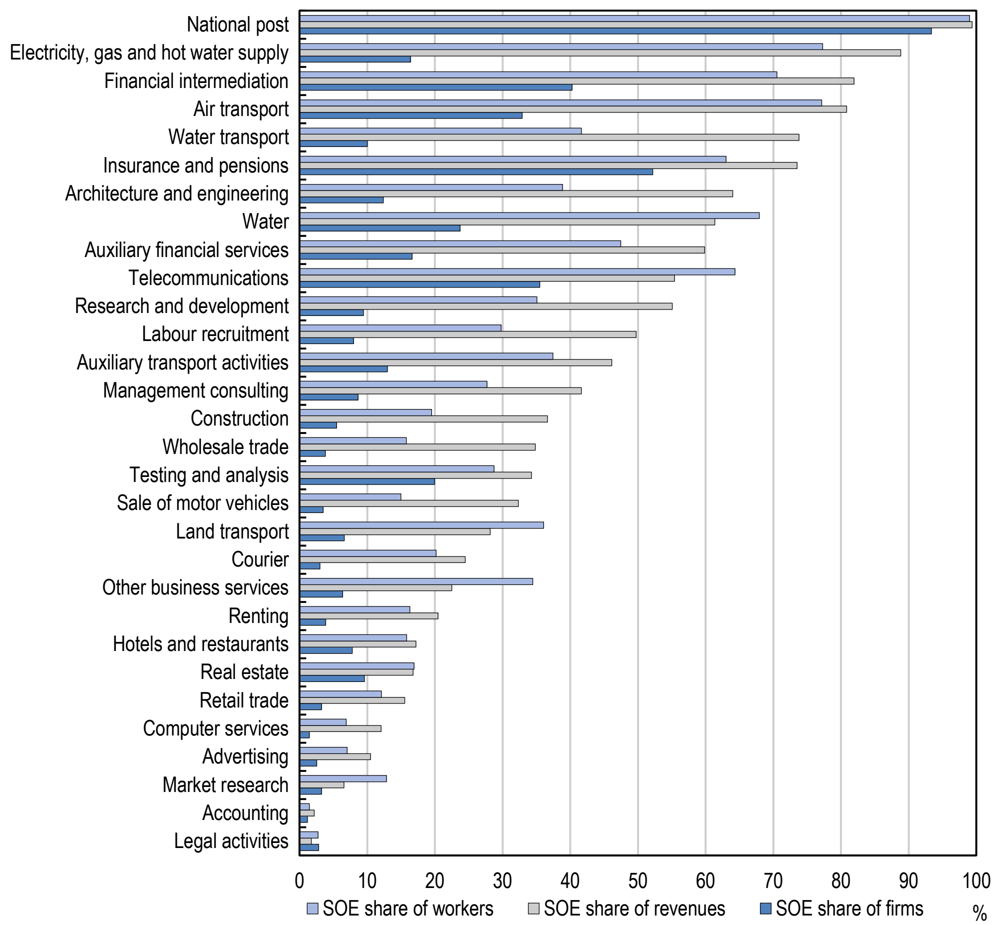
China assumed important transparency obligations in the WTO. For example, China has undertaken general provisions on transparency to publish and make readily available laws, and regulations pertaining to trade in services.[4] China has committed to allowing public comment on laws, regulations, or other measures bearing on trade in services.[5] In line with its commitments, China has established an enquiry point[6] where such information is made available upon request. In addition to procedural and institutional transparency, many WTO members maintain domestic measures that emphasize access to accurate market information. For example, mandated corporate disclosure and survey requirements generate market information and quality economic data. Such practices create confidence in the marketplace.

State owned enterprises (SOEs) eclipse China's services economy. SOEs dominate revenues in finance, insurance, and telecommunications (figure 3). Many WTO members have retooled competition authorities to reduce distortions in price, quality, and innovation in the services

4 WTO, Accession of the People's Republic Of China, November 23, 2001 (WT/L/42)
5 WTO, Accession of the People's Republic Of China, November 23, 2001 (WT/L/42)
6 Ministry of Commerce People's Republic Of China, http://english.mofcom.gov.cn/

economy. For example, authorities assess the structure and activities of SOEs; increase penalties for anticompetitive practices, and define and expand business misconduct. Competition authorities also host academic and business representatives to study competition issues, train officials with case studies, and coordinate with counterparts abroad. China can curtail SOEs dominance in the services economy using the experiences of other WTO members.

Figure 3: Chinese State Owned Enterprises share of services workers, revenues, firms (2008)



Source: OECD Economic Surveys: China, March 2015. (Statlink http://dx.doi.org/10.1787/888933198604)

China can build a robust services economy with a focus on liberalization, transparency, and competition policy. China can reduce trade restrictions on services by easing foreign equity share limitations, opening public procurement, and streamlining administrative procedures. China can fully implement transparency obligations and expand transparency practices to generate market information and quality economic data. Attention to competition policy can help China's services economy evolve. Deeper engagement in the WTO and collaboration with WTO members can help China rebalance growth.

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