Trade in Services in Latin America and the Caribbean: An Overview of Trends, Costs, and Policies

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Abstract

Trade in services is becoming increasingly relevant. Changing technologies have transformed the landscape, making international trade possible in sectors that were once considered nontradable. But the lack of consistent, reliable data prevents analysts from fully understanding and accurately describing trade in services. Despite this limitation, this report aims to outline Latin America and the Caribbean’s competitiveness in global services markets. It concludes that the region still focuses on traditional sectors like travel and transportation, despite some green shoots in nontraditional services, and that costs remain high in comparison with other regions of the world. Furthermore, the regulatory framework in the region is still weak, and although several modern trade agreements are already in place, there is still room for improvement. Sound policies to further develop trade in services and boost competitiveness in nontraditional sectors such as computer or business services would help the region to diversify its export baskets and build trade resilience.

JEL Codes: F1, F10, F14, F15.
Keywords: Trade, integration, services, exports, Latin America and the Caribbean.

* The views and interpretations in this study are strictly those of the authors and should not be attributed to the Inter-American Development Bank, its Board of Directors, or any of its member countries.

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Contents

Introduction ........................................................................................................................................ 7

1. The Outlook for Trade in Services .................................................................................................... 9
   The Rise of Trade in Services ........................................................................................................... 9
   LAC’s Competitiveness in Global Services Markets ......................................................................... 19

2. Barriers to Trade ............................................................................................................................. 26
   Services Trade Costs ....................................................................................................................... 26
   Policy Barriers for Services ............................................................................................................. 31
   Relationships Between Costs, Policy Barriers, and Services Exports .................................................. 36

3. Trade Policy .................................................................................................................................... 38
   General Agreement on Trade in Services ......................................................................................... 38
   Preferential Trade Agreements .......................................................................................................... 42

Conclusions ........................................................................................................................................ 48

References ......................................................................................................................................... 50
Introduction

Trade in services represents a window of opportunity for diversifying the basket of traded products and increasing countries’ resilience, which is especially appealing in the aftermath of the global recession caused by the COVID-19 pandemic and the measures adopted to mitigate it. The importance of the services sector has been growing as technological change has increased the tradability of many services that were once considered nontradable, while fostering the development of new services, such as software.

Indeed, the rapid uptake of digital technologies is creating a new host of opportunities for services exporters. The fourth industrial revolution, spurred by the adoption of new technologies such as artificial intelligence, cloud computing, 3D printing or the internet-of-things, is driving the “servicification” of manufacturing, whereby services are used as inputs, or bundled with material goods. Digitally enabled services have been growing in their own right, and their remote supply has recently exploded. Likewise, during the pandemic, large swaths of global demand have shifted to e-commerce channels. Meanwhile, digitally enabled services depend on cross-border data flows, which are developing exponentially, account for a growing share of the value of international exchanges and require new regulatory frameworks.

However, services are less tangible than physical goods and, consequently, it is more difficult to record commercial transactions correctly. The lack of consistent and reliable data with broad country coverage limits the breadth and depth of the analyses that can be carried out. Despite these challenges, this report outlines the region’s competitiveness in global markets and points to sectors with potential, as well as areas in need of policy upgrades.

The weight of trade in services in Latin America and the Caribbean (LAC) with respect to total trade has been on an upward trend and is particularly important for countries in the Caribbean and Central America. However, traditional services (such as tourism and related areas) continue to play a major role. In certain countries, some green shoots are starting to appear in nontraditional sectors like computer or business services. Digitally-enabled services are more dynamic and have shown greater resilience, since services that do not involve physical contact between buyers and sellers have been less impacted by the economic crisis caused by the COVID-19 pandemic.

Measuring trade costs is particularly challenging as many components are nontangible and hard to quantify. However, estimates point to the costs of trading services being substantially higher than those of trading physical goods, which in turn implies that trade in services faces higher barriers. In LAC, these costs are higher than those estimated for other regions of the world and are also above the world average in all the sectors that were analyzed, meaning that the region’s competitiveness is lagging. Services trade restrictiveness indexes show a more heterogeneous performance across sectors and even place Mexico and Costa Rica below the global average in digitally-enabled services.

A clear regulatory framework that sets the ground rules for international trade in services is a key factor for promoting such trade. Newer trade agreements do incorporate provisions regarding trade in services, but within LAC few go beyond what is established in the General Agreement on Trade in Services (GATS). Three good examples of modern agreements are the Pacific Alliance, which is noteworthy as an intraregional agreement with great sectoral openness, and the United States-Mexico-Canada Agreement (USMCA) and the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), as both include comprehensive, modern digital trade regulations.
The rest of this report is structured as follows. Chapter 1 provides an outlook on trade in services in LAC. Chapter 2 analyzes barriers that affect trade in services and provides estimates of the costs of trading. Chapter 3 contains an overview of the regulatory framework for trade in services for LAC countries and provides examples of modern trade agreements with wide coverage for services. These are followed by a series of conclusions.
1. The Outlook for Trade in Services

Trade in services has opened up a window of opportunity for diversifying the basket of traded products and increasing resilience to trade shocks. These benefits are especially valuable in the aftermath of the global recession caused by the impact of the COVID-19 pandemic and the measures adopted to mitigate its effect. LAC countries have mainly relied on traditional services relating to tourism or trade in goods, such as travel and transportation. These sectors were hit particularly hard during 2020 as stay-at-home orders and travel restrictions were put in place in countries around the globe. To successfully navigate the waves of uncertainty and prepare itself for the future, LAC needs to become more competitive and move toward trade in digitally-enabled sectors like computer and information services or business services, which have proved more resilient in recent trade downturns. Moreover, beyond resilience to a once-in-a-century pandemic, a more diversified and balanced portfolio will likely provide new growth opportunities, after a decade characterized by lackluster trade performance.

The Rise of Trade in Services

The importance of the services sector is undeniable. Its value-added as a percentage of world GDP has been close to 65% over the last decade, and it accounts for 50% of employment. Traditionally, most services were considered non-internationally tradable, but technological progress has facilitated the supply of many services across borders while also fostering the development of new ones. Trade in services not only includes services delivered remotely (which GATS refers to as cross-border trade or mode of supply 1), but also covers consumers obtaining a service while in another country (consumption abroad or mode 2), and the provision of services by foreign firms (commercial presence or mode 3) or foreign individuals (presence of natural persons or mode 4) (Table 1).

The lack of consistent and reliable data with broad country and sector coverage limits possible analyses of trade in services in LAC. However, some indicative figures reveal overall trends for the region and the rest of the world. If public policies that support the development of trade in services are to be designed and implemented, improving data collection and statistics should be a priority.

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2 IDB Integration and Trade Sector with data from the World Bank.
3 An extensive body of policy-focused academic literature has emphasized the growing tradability of services, the structural transformations prompted by technological change, and the strategic and institutional implications of these trends. See, for example, Mattoo et al. (2007) for a discussion of the economic effects of the increase in trade in services; Hernández et al. (2014) for the disruptive impact on LAC’s economies; and Lund et al. (2019) for a discussion of the impact on international integration strategies in the future.
4 This chapter uses WTO data, where services are classified in accordance with the sixth edition of the IMF Balance of Payments Manual and, therefore, only those services reported in modes 1, 2, and 4 (respectively, cross-border supply, consumption abroad, presence of natural persons) are used, whereas mode 3 (commercial presence) is excluded. For an extensive review of the literature on the determinants of international trade in services and its economic impact, see Francois and Hoekman (2010).
5 The intangible nature of services poses challenges for measuring and recording, which gives rise to errors and omissions. Despite some progress, the quality of services trade data in LAC remains poor, especially when it comes to conducting a disaggregated analysis such as the one presented in this chapter. In particular, the disaggregated data for type of services exported is incomplete, while data for destination countries is virtually nonexistent, with the exception of a few countries. Moreover, there is wide variation in terms of the quality and availability of data in different countries, which hinders comparisons. It is therefore important to treat the results of this analysis as

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Table 1: Modes of Supply of Services

<table>
<thead>
<tr>
<th>Mode of supply</th>
<th>Description</th>
<th>Examples (country A is an importer and B an exporter)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1: Cross-border trade</td>
<td>Services flow from the territory of one member country into the territory of another member</td>
<td>A user in country A rents a digitally streamed movie from a company in country B</td>
</tr>
<tr>
<td>2: Consumption abroad</td>
<td>A service consumer moves into another member's territory to obtain a service</td>
<td>A national of country A travels to a resort in country B</td>
</tr>
<tr>
<td>3: Commercial presence</td>
<td>A service supplier from one member country establishes a commercial presence in another member’s territory to provide a service</td>
<td>A management consulting company from country B provides consulting services through its affiliate established in country A</td>
</tr>
<tr>
<td>4: Presence of natural persons</td>
<td>Natural persons from one member country enter the territory of another to supply a service</td>
<td>A surgeon from country B performs surgery in country A</td>
</tr>
</tbody>
</table>

Source: IDB Integration and Trade Sector adapted from the World Trade Organization (WTO).
Note: Modes of supply as defined by the GATS.

For LAC, the services sector represents an important source of income. Its value-added as a share of GDP has been around 58% during the last few years, and in 2019 it employed 64% of the labor force.

Trade in services in the region amounted to US$377 billion in 2019. Even though it has grown at an annual average rate of 6.1% between 2005 and 2019, the trend has fluctuated, in line with the global average (Figure 1). Traditionally, trade in services was more resilient than trade in goods. For example, in 2009, while world trade in goods fell 22.5%, trade in services only dropped 10.7%, and between 2012 and 2015, the slowdown in growth was also less pronounced. However, in recent years there has been a reversal, with trade in services growing less than in goods, particularly in LAC. Moreover, in 2020, global trade dropped dramatically as a consequence of the economic crisis that derived from the COVID-19 pandemic, which had a greater impact on services. The social distancing measures and travel restrictions adopted in many countries to mitigate the effect of the virus have hampered the provision of services that require physical contact between buyer and seller, such as travel and transportation.

Despite recent trends, trade in services in LAC has great potential and could be an engine for growth for many countries. Services exports relative to GDP have been steadily increasing: this ratio doubled between 2005 and 2019 (going from 1.9% to 3.8%, respectively) (Figure 2). However, by 2019, LAC services exports neared 15% of total exports, which is lower than the weight they have in the United States (US), indicative and subject to correction. For a recent complementary analysis, including an evaluation of progress in statistics gathering, see ECLAC (2017).

6 Trade is the sum of exports and imports reported by the WTO.
7 In the first half of 2020, global trade fell 13.3% year-on-year, and LAC exports decreased 16.1%. In the first quarter of 2020, at an early stage of the health crisis, global trade in services had already fallen 6.7% year-on-year and LAC services exports had dropped 11.5%. See Giordano et al. (2020).
Figure 1: Growth Rate of Total Trade
(Percentages, 2006–2019)

Source: IDB Integration and Trade Sector with data from the WTO.
Note: Total trade is the sum of exports and imports.

Figure 2: Exports of Services as a Share of GDP
(Percentages, 2005–2019)

Source: IDB Integration and Trade Sector with data from the WTO and the World Bank (WB).
The relative weight of services exports among LAC subregions varies widely, with the Caribbean standing out, foreign sales of services representing 42% of total exports (up from 30%). This subregion has specialized in offering tourism-related services. Unfortunately, the pandemic has halted activities in this sector, deeply damaging Caribbean economies. In Central America, services amount to 41%, but the portfolio is more diversified. Travel and transportation are also important, but other business services and manufacturing services are relevant as well. Services account for 21% of total exports in the Rest of MERCOSUR and are below 15% in all the remaining subregions.

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8 In the analysis of the export performance of the services sector, this chapter separates Brazil and Mexico and groups the other LAC economies as follows: Central America (Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, and Panama); Rest of MERCOSUR (Argentina, Paraguay, and Uruguay); Rest of Pacific Alliance (Chile, Colombia, and Peru); Intensive in Fuels and Energy (Bolivia, Ecuador, and Venezuela); and the Caribbean (Bahamas, Belize, Guyana, Haiti, Jamaica, Suriname, and Trinidad and Tobago).

9 For more on the economic impact of the pandemic in selected Caribbean countries, see The Economist (2020).
Figure 4: Exports of Services as a Share of Total Exports by Subregion (Percentages, 2010–2014 and 2015–2019)

Source: IDB Integration and Trade Sector with data from the WTO.

Note: For each five-year period, the average is constructed as the simple average of the period in question for each country. Subregions are constructed providing equal weight to each country. The composition of each subregion can be found in footnote 8. The group of Intensive in Fuels and Energy excludes Venezuela, and the Caribbean excludes Guyana due to a lack of data.

The trade balance in LAC for both goods and services is negative. For services, it widened to -1.1% of GDP in 2014, and in recent years it has shown some improvement, reaching -0.7% of GDP in 2019 (Figure 5). Its evolution has been less volatile than that of goods, which reached its lowest point in 2015, at -2.0% of GDP, while in 2019 it was above the trade balance of services (-0.4%).

Figure 5: Trade Balance of Goods and Services (Percentage of GDP, 2005–2019)

Both exports and imports of services are highly correlated, therefore, changes in the trade balance are explained by differences in growth rates, and not by trend reversals.
of services has followed a similar path to that of LAC, exports of goods have been above imports, with the differential reaching a maximum of 1.6% of GDP in 2015. Following the opposite trend, both the US and the EU have been net exporters of services for the past 15 years, with their trade balances being 1.3% and 2.0% of GDP, respectively.

Since services are embedded as inputs in the production of other goods, the figures stated above may undervalue the magnitude of trade in services, as only the value of final exports is taken into account. Although the data on value-added does not allow tradable and nontradable services to be disentangled, it does show that the services contained in exports of final manufactured products amount to 30%. Within LAC, the contribution of services varies considerably among countries. While in Brazil, Mexico, and Costa Rica this proportion is above average (36.6%, 35.5%, and 33.2%, respectively), for Chile, Colombia, Peru, and Argentina the reverse is true (30.1%, 28.2%, 24.3%, and 18.5%, respectively) (Figure 6). To put

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**Source:** IDB Integration and Trade Sector with data from the WTO and the WB.

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11 Data comes from Trade in Services Value Added (TiVA). The average is calculated as the simple average of the 64 countries present in the sample. The only LAC countries available are Argentina, Brazil, Chile, Colombia, Costa Rica, Mexico, and Peru. An alternative source is the EORA database produced by UNCTAD, which includes a larger sample of LAC countries. TiVA was preferred as it is in the process of being updated and the new figures would be directly comparable with those used in this study.
this heterogeneity in context, in 2015 the global sample ranged from 15.6% in Bahrain to 46.3% in Singapore, with the majority of countries displaying values between 20% and 30%. In Europe, specifically, it ranged from 25.4% in Greece to 53.6% in Luxembourg, with the majority of countries presenting values between 30% and 40%.

**Figure 6: Share of Value of Final Manufactured Goods Corresponding to Embedded Services**
(Percentages, 2010 and 2015)

![Graph showing the share of value of final manufactured goods corresponding to embedded services for different countries and years.](image)

*Source:* IDB Integration and Trade Sector with data from TiVA.

*Note:* The world average was 30.4% in both 2010 and 2015 and is constructed as the simple average of the sixty-four countries available.

Another characteristic of exports of services that highlights their importance as drivers of growth is that they have higher domestic content than exports of manufactures. Consequently, a larger portion of revenue stays in the exporting country as payments to labor and capital. In LAC, domestic value-added in services represents 92.1% of the total, while in manufactures it stands at 77.7% (Figure 7). The US is the only other region studied in which the share of domestic content is even larger both for services (95.9%) and manufactures (84.4%).

LAC exports of services are concentrated in travel, which represents 40.5% of total foreign services sales, well above the world average of 23.4% (Figure 8). Transportation takes third place, amounting to 18.4%. These sectors were severely affected by the crisis in 2020, as confinement measures and travel restrictions in many countries have paralyzed the hospitality industry and curtailed trade in goods. Even though prohibitions are becoming less restrictive, businesses are still only allowed to operate at a lower capacity.

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12 Mexico is excluded from the LAC total because this would distort the distribution by category, as official statistics report data for travel, transportation, insurance, and pensions and financial services consistently, while data for the other categories is not broken down adequately and may be incomplete.
than previously to ensure that proper social distancing is maintained. Moreover, additional sanitation procedures must be in place, which has increased the cost of doing business. Not only is supply being altered, but demand has also dropped significatively: on the one hand, business travel has halted since companies have moved to home-based work, and on the other hand, tourism is severely reduced as fear of contracting COVID-19 is deterring people from unnecessary travel.\textsuperscript{13} The subregions of LAC where the weight of travel is higher than the regional average are the Caribbean (82.2\%) and the group of countries that are Intensive in Fuels and Energy (65.7\%). Transportation is particularly important for this last subregion (21.8\%) as well as for the Rest of the Pacific Alliance (24.6\%) and Central America (21.2\%).

\textbf{Figure 7: Share of Value-Added in Manufactures and Services by Origin (Percentages, 2015)}

\begin{itemize}
  \item The subregions of LAC where the weight of travel is higher than the regional average are the Caribbean (82.2\%) and the group of countries that are Intensive in Fuels and Energy (65.7\%). Transportation is particularly important for this last subregion (21.8\%) as well as for the Rest of the Pacific Alliance (24.6\%) and Central America (21.2\%).
\end{itemize}

Source: IDB Integration and Trade Sector with data from TiVA.

Note: LAC is composed of Argentina, Brazil, Chile, Colombia, Costa Rica, Mexico, and Peru.

\textsuperscript{13} The number of commercial flights worldwide dropped by close to 80\% between late February and mid-April 2020; see WTO (2020).
Figure 8: Composition of Services Exports by Sector
(Percentages, 2018)
Figure 8: Composition of Services Exports by Sector (continued…)
(Percentages, 2018)

Source: IDB Integration and Trade Sector with data from the WTO.

Note: LAC excludes Barbados and Venezuela (lack of data) and Mexico (lack of disaggregation). Totals may not add to 100% due to the existence of a heading for unclassified services.
Exports of other business services represent 22.6% of total foreign sales of services. Unlike transportation and travel, this sector has shown more resilience. It includes professional and management consulting services, research and development services, and technical, trade-related, and other business services. Technology allows for the remote delivery of many of these services, so the higher the digital preparedness and literacy of a business, the more likely it is to survive in extraordinary market conditions. Similarly, another sector with potential is computer and information services. Its weight in the export basket for LAC is 4.6%, which is close to half the proportion it represents globally (8.6%). Brazil and the Rest of MERCOSUR stand out among LAC subregions in both categories. In Brazil, the shares of other business services and computer and information services account for 46.3% and 5.7% of total exports of services, respectively, while for the Rest of MERCOSUR these same shares are 24.6% and 10.8%.

**LAC’s Competitiveness in Global Services Markets**

The region needs to position itself competitively in less traditional and more dynamic segments of world trade and, in this respect, there is room for improvement. This report analyzes competitiveness by taking into account two dimensions: change in market share and growth in global demand. Combining these two variables gives rise to four distinct groups for categorizing exports. The *strategic* segment contains sectors in which market share is increasing and demand is growing above the average global rate. Sectors in which market share is increasing but demand is growing at a below-average rate fall into the *mature* segment. *Untapped* sectors are those in which market share is declining despite dynamic demand. Finally, in the *declining* segment, market share is falling and growth in demand is below average.

Between 2013 and 2018, LAC’s market share increased in sectors that accounted for half of total services exports. However, almost all of this improvement corresponded to the mature segment (Figure 9). Travel accounted for 94% of this category and insurance for the remainder (Figure 10). The most attractive category, the strategic segment, was the smallest of the four, represented 1% of total services exports, and contained a single sector: charges for the use of intellectual property, which grew at almost twice the speed of the world average. This contrasts with the weight of the strategic segment in other regions like the EU, Asia, and the US, where it represented 47%, 28%, and 24%, respectively, and other business services and computer and information services dominated.

LAC lost market share in the other half of services exports, although the distribution among the remaining two segments was more balanced. The utmost attention should be paid to the untapped segment since

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14 Business services include: i) research and development services; ii) professional consultancy services; and iii) technical services relating to trade and other business services (including architectural, engineering, and scientific services, and those relating to agriculture and mining, among others).

15 The first application of the methodology used in this analysis to trade in services can be found in López et al. (2014), which only considered the data available to 2009. It should be noted that although the category names have been modified to simplify the discussion, the underlying concepts are similar and thus the results are comparable. A more recent application can be found in Giordano et al. (2019).

16 For the competitiveness analysis, data for the last available year (2018) was used. A five-year window was taken as a reference (2013–2018) to calculate change in demand and market share. To summarize, in LAC the four segments contain the following sectors: *strategic*—charges for the use of intellectual property; *mature*—insurance and pension services, travel; *untapped*—other business services, goods-related services, computer and information services; *declining*—financial services; construction; personal, cultural, and recreation services; telecommunications; and transportation.
this contains sectors in which demand is dynamic and in which the region is falling behind. The untapped segment represented 26% of total services exports, among which other business services stood out, accounting for close to three-quarters of the entire category. Despite the global dynamism of this sector, LAC’s market share fell from 0.31% to 0.24%, whereas those of the EU, the US, and Asia increased. Computer and information services accounted for 15% of the category. This sector has great potential as its growth was close to four times the global average and the services it entails can be delivered digitally, making it more resilient than other sectors in the current economic context. LAC’s market share for the sector fell slightly, dropping from 0.15% to 0.14%. The dominant player, the EU, was the only region to experience an increase in its market share, which went from 44.6% to 56.1%.

Finally, the declining group accounted for 23% of LAC’s total foreign services sales. Transportation contributed close to three-quarters of the group, while financial services and telecommunications were a distant second and third (representing 9% and 8% of the category, respectively).

The performance of LAC’s subregions varied widely. Brazil stands out as 12% of the value of its services exports corresponded to the strategic group. Computer and information services accounted for half of these, goods-related services for a third, and charges for the use of intellectual property for the remainder. The group of untapped segments was the largest (46%) and was made up entirely of other business services, the largest sector of services exports for Brazil. Developing this sector is therefore a major opportunity that should not be missed. The declining segment represented 39% of total exports (mainly travel and transportation), while the mature segment accounted for 3% of the total (mainly telecommunications and insurance and pensions services).

Central America gained market share in 82% of its total services exports. The strategic segment represented 11% of this total and was composed of other business services. It is noteworthy that the subregion is increasing its market share in a sector that is more resilient to the current global health shock than traditional sectors. The mature segment accounted for 71% of total services exports and mainly consisted of travel and transportation. Goods-related services represented more than two-thirds of the untapped segment (12% of the total), and the remainder corresponded to computer and information services.

The performance of the group of countries that are Intensive in Fuels and Energy was poor, as it lost market share in 93% of its services exports, largely due to the group’s concentration in the least dynamic sectors. The declining segment represented 92% of the total and was dominated by travel and transportation, accounting for around three-quarters and one-quarter of the segment, respectively. The untapped segment, which provides more growth opportunities, only accounted for 1% of the total, with goods-related services predominating. The strategic segment represented 5% of the group’s total services exports. Two-thirds of the segment corresponded to other business services, and one-third to computer and information services. Although still small, these two segments could boost the subregion’s competitive positioning in global markets. Last, the mature segment (2% of the total) was made up entirely of financial services.

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17 In order to avoid misleading policy implications, it is important to acknowledge that this analysis only provides a bird’s-eye view of the competitiveness of the export supply. The allocation of public policy incentives and private investment should also take comparative advantages and supply constraints into consideration.
Mexico increased its global presence in all services exports. However, this was concentrated in the mature segment, which saw below-average growth in demand.18 Travel dominated this group, accounting to close to 80% and experiencing an important increase in market share, followed by insurance and pension services and transportation.

The strategic segment in the Rest of MERCOSUR represented 4% of the group’s total services exports. Goods-related services accounted for more than half of this segment, and charges for the use of intellectual property for the remainder. Although both sectors exhibited high global growth in demand, the increase in market share was particularly large for goods-related services. Within the untapped segment (35%), other business services accounted for 70%, followed by computer and information services (30%). In both cases, the loss of market share was substantial. The declining segment was the largest of the four (56% of total services exports), within which travel accounted for the lion’s share (71%) and transportation contributed close to one-quarter. In the mature segment, telecommunications and personal, cultural, and recreational services were the most relevant sectors.19

The countries of the Rest of the Pacific Alliance gained market share in half their services exports and lost it in the other half. However, the strategic segment only accounted for 1% of the total, driven by charges for the use of intellectual property. Within the mature segment (53% of the total), travel represented close to 90%. This sector was already growing at a slower-than-average pace and is expected to decline further due to the impact of the pandemic. The group’s focus should be on the untapped segment (20% of its total services exports), especially in other business services, which accounted for 87% of the category, and computer and information services (12%). Transportation made up most of the declining segment (27% of total services exports).

Most of the Caribbean’s services exports also corresponded to the mature segment (84%), and as travel accounted for 80% of this category, the subregion is facing the same challenges as the Rest of the Pacific Alliance but on a greater scale, given how much its countries depend on tourism. Opportunities also lie in other business services and computer and information services, which represented 93% and 7% of the untapped segment (8% of total services exports).

18 However, the categorization of the export basket should be considered incomplete, as the composition of service exports from Mexico may be distorted, due to the fact that travel, transportation, insurance and pensions, and financial services are reported consistently, but those for the remaining categories are not adequately disaggregated and could be incomplete.
19 Personal, cultural, and recreational services include i) audiovisual and related services; ii) health services; iii) education services; iv) heritage and recreational services; and v) other personal services.
Figure 9: Composition of Services Exports by Competitive Segment
(Share of total services exports, percentages, 2018)

Source: IDB Integration and Trade Sector with data from the WTO.
Note: Due to a lack of data, the group of countries that are Intensive in Fuels and Energy excludes Venezuela, and the Caribbean excludes Barbados. Records for Mexico may be incomplete, distorted by inaccuracy, and are likely to be inconsistent with respect to breakdown by category. The share of total exports is reported for 2018, but the change between 2018 and 2013 is used to assign sectors to segments. Totals may not add up to 100% due to rounding.
Figure 10: Relevance and Competitive Positioning of Services Exports by Sector (Percentages, 2018)
Source: IDB Integration and Trade Sector with data from the WTO.

Note: The world average for demand growth between 2013 and 2018 was 29%. The size of the bubble represents the weight of the sector in total exports for each region.
In sum, even though the lack of high-quality data on trade in services prevents a deeper, more detailed analysis from being carried out, this report outlines LAC’s competitiveness in global markets and points to sectors with potential. Traditional services like travel and transportation continue to play a major role in the region. However, these were not the most dynamic sectors even in the years running up to the COVID-19 pandemic, which has had a severe impact on them. Other areas like computer and information services or businesses services have displayed greater dynamism. They now have even greater potential, as services that can be delivered without contact between buyers and sellers have proved more resilient to the pandemic. In the wake of a global recession, it is crucial for LAC to position itself competitively in strategic sectors with the potential to deliver opportunities for growth, hence the need to shed some light on investments and policies that could promote the development of these sectors, in tandem with efforts to improve the collection of high-quality services data.\(^\text{20}\) One of the challenges that must be addressed to achieve this is lowering trade costs, which is explored in the next chapter.

\(^{20}\) For an analysis of policy recommendations for developing services exports, see OECD (2017), UNCTAD (2017), and WTO (2019a). For a discussion focused on the specific needs of Latin America and the Caribbean, see Hernández et al. (2014) and Aboal et al. (2015). For an example of sector-specific and horizontal export promotion plans in a specific country in LAC, see García and Capobianco (2012).
2. Barriers to Trade

Trade in services faces many barriers that need to be addressed to lower costs and unlock potential gains. In fact, the costs of trading services are substantially higher than those of trading goods, which points to a tangible opportunity for lowering barriers. LAC’s costs for trading services are higher than those of other regions, hampering its ability to compete in global markets. Therefore, policymakers need to identify the barriers to investment attraction and design sound policies to create a more favorable business environment.

Services Trade Costs

In general, trade costs are driven by both tariffs and nontariff barriers, as well as all expenses associated with shipping or transmitting the product or service from the seller to the buyer. Measuring such costs is challenging, as not all components are directly observed. Given the nontangible nature of services and the lack of complete, high-quality data, these difficulties are particularly onerous when it comes to estimating the costs of trading services.

Multiple approaches have been applied to quantify trade costs. These can be broadly divided into direct and indirect measurement techniques. Direct measures tend to be inaccurate and incomplete due to aggregation biases and a lack of data. Costs derived from policy barriers—such as tariffs, quotas, or other regulations—are not only partially observed but frequently do not translate easily into ad valorem cost equivalents. Finally, data regarding other factors like transportation, transaction, or distribution costs is hard to obtain due to its private nature.

Indirect measures try to infer costs by connecting unobservable variables to observable ones. There are two main approaches, which entail inferring costs from either trade flows or prices, respectively. Moreover, efforts can be divided into theory-based models and estimations. Within the category of models using trade flows, Novy (2013) proposes a method to derive an analytical solution for costs from the gravity model in Anderson and van Wincoop (2003). Trade costs are expressed as a geometric average of the costs of trading between two countries relative to domestic trade costs. To calculate these, only data on bilateral trade flows and domestic usage is required. Other efforts to derive closed-form solutions rely on strong assumptions, such as symmetric costs between two countries, or choose specific functional forms for costs.

Econometric estimations using trade flows to determine the costs of trading are carried out using an application of gravity equations. Basically, costs are determined by a series of standard gravity variables (such as geographical distance between countries, whether there is a shared border, common language, shared currency, common legal system, or common religion, among other factors), and an indicator is included to identify if trade flows are internal or external. Again, trade costs are expressed as relative to domestic trade costs. Among the limitations of using econometric estimations based on gravity equations

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21 Tariffs can be quantified but the impact of regulatory barriers is hard to measure.
22 For an extensive review of the literature on trade costs, see Anderson and van Wincoop (2004).
23 Although the analytical solution is for the model in Anderson and van Wincoop (2003), the author shows it can also be derived from other trade models, like the Ricardian model in Eaton and Kortum (2002) and the heterogeneous firm models in Chaney (2008) and Melitz and Ottaviano (2008).
24 For example, the model in Anderson and Wincoop (2003) assumes a functional form for costs where it depends on two variables: a border barrier and geographical distance. One drawback to this model is that it is not well suited to capturing time-varying effects. Likewise, it can also be misspecified and miss other factors that determine costs.
25 See, for example, Walsh (2006) and Anderson et al. (2018) for applications of gravity equations to services trade.
is the fact that true costs are often confounded by noise in the data, which makes estimators hard to interpret, and that a form for the cost function needs to be assumed.

An alternative way of inferring trade costs uses prices instead of trade flows. Using price data to pin down costs is particularly challenging for services, given the wide heterogeneity of services that are provided and the lack of a consistent approach to classifying these. Both the trade literature and the macro literature have used evidence from prices to estimate trade costs, primarily for goods. The first strand of literature compares import prices to domestic wholesale prices.\(^\text{26}\) Conceptually, the difference in prices represents costs. However, a portion of trade costs is actually borne by the exporter and passed on to the importer, which is not captured by the price comparison. Indeed, other nontariff barriers might not be reflected in the comparison at all, despite the emergence of novel techniques (Cadot et al., 2018). Consequently, this approach might underestimate the magnitude of trade barriers. The macro literature compares retail prices of similar goods across countries and is based on concepts like purchasing power parity.\(^\text{27}\) The main limitation to this approach is the lack of a good theoretical foundation for linking price differentials to trade barriers.

To calculate tariff-equivalent costs, this report follows the methodology proposed by Novy (2013) given its simplicity and the relatively low data requirements. While that article focuses on trade in goods, Lanz et al. (2009) and Miroudot et al. (2013) apply the methodology to trade in services.\(^\text{28}\) As mentioned before, trade costs are expressed as a geometric average of the costs of trading between two countries relative to domestic trade, and only data on bilateral trade flows and domestic usage are required, which in this case are obtained from the TiVA database.

Ad valorem tariff equivalents of costs of trading services in LAC are higher than in other regions (Figure 11, panel a). Although these costs have been decreasing in recent years, falling from 259% in 2005 to 251% in 2015, they are still well above those of Asia (203%), the EU (192%), the US (151%), and the Rest of the World (214%). Remarkably, trading services is more costly than trading manufactured goods. Although moving physical products around the globe might be perceived intuitively as more costly than providing services, transportation only accounts for a small portion of total costs for trading services, which are heavily influenced by other factors, such as regulatory matters.

Costs in LAC countries differ widely (Figure 11, panel b). Brazil stands out since its costs of trading services (225%) have followed a downward path, overtaking Argentina to become the lowest in the region by 2015. Argentina has the second-lowest costs (233%), despite showing an upward trend in recent years. Chile and Mexico follow, with the latter on a steady downward path (247% and 241%, respectively). Although Peru is among the three countries with the highest costs of trading services, it has shown a remarkable improvement: costs fell from 282% in 2005 to 259% in 2015, overtaking those of Costa Rica (272%). Colombia’s costs are at the top of the distribution (286%).

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\(^{26}\) See Deardorff and Stern (1998) for a review of studies using price comparisons to estimate trade barriers.

\(^{27}\) See for example Engel and Rogers (1996) and Obstfeld and Taylor (1997) for analyses of price differentials across countries and estimates of trade barriers.

Figure 11: Ad Valorem Tariff Equivalent of Trading Costs (Percentages, 2015)

Source: IDB Integration and Trade Sector with data from TiVA.
Note: Costs are calculated according to the methodology described in Novy (2013), and regions are constructed as simple averages of the countries.

Costs differ widely among services sectors, but LAC faces costs that are higher than the world average in all sectors (Figure 12). The highest costs are associated with services that are deemed less tradable, such as construction, health and social work, and government-related services (average ad valorem equivalents for LAC of 485%, 402%, and 355%, respectively). Trading services in certain other sectors in LAC also entails
costs that end up almost quadruplicating the price of the service in question: this is true of financial and insurance activities (293%), telecommunications (269%), other business-sector services (272%), and information and communication services (252%). The sectors with the lowest costs are transportation and storage (206%) and IT and other information services (208%).

**Figure 12: Ad Valorem Tariff Equivalent of Trading Costs by Sector**
(Percentages, 2015)

Nontraditional services like business services and IT and other information services are becoming increasingly significant and may bring opportunities for LAC countries. However, for many of these countries, the costs are still high in comparison with the world average. For other business services, among the economies of the region for which data are available, costs in Mexico are the highest, at 338% (Figure 13, panel a). Colombia, Peru, and Chile follow, with costs of 306%, 278%, and 271%, respectively. The LAC
Figure 13: Ad Valorem Tariff Equivalent of Trading Costs in Selected Services Sector (Percentages, 2015)

a. Other business-sector services

b. IT and other information services

Source: IDB Integration and Trade Sector with data from TiVA.
countries where these costs are lowest, albeit still above the world average, are Brazil, Argentina, and Costa Rica (225%, 235%, and 250%, respectively). The costs for IT and other information services are lower, and the gap with the world average is narrower. Remarkably, the cost of trading IT and other information services from Argentina (174%) are below the global average (183%), which puts the country in an advantageous position to compete in global markets (Figure 13, panel b). Costa Rica and Brazil also have competitive costs, at 185% and 208%, respectively. At the other end of the distribution, Colombia reports the highest costs in the region (230%), closely followed by Chile, Peru, and Mexico (225%, 218%, and 217%, respectively).

The tariff-equivalent cost measures described above are comprehensive and reflect all costs associated with trading services. However, disentangling the specific weight of those induced by restrictive policies is fundamental to guide sound policymaking.

**Policy Barriers for Services**

Given the less tangible nature of trade in services in comparison to trade in goods, customs officials are less able to observe international transactions in services, and tariffs cannot be used as a tool for trade protection. Therefore, regulations are commonly set in place to achieve this goal. Such regulations are difficult to compile and quantify consistently across countries. As a result, estimating their impact on trade flows is challenging. Moreover, differentiating discriminatory regulations that aim to deter trade from those necessary to ensure proper market stability and quality standards is no trivial matter.

Certain efforts in the literature have centered around studying trade barriers and creating comparable cross-country indexes that summarize the restrictiveness of policies affecting trade in services. In particular, the Organisation for Economic Co-operation and Development (OECD) has constructed the Services Trade Restrictiveness Index (STRI) for 22 sectors and 46 countries, five of which belong to LAC. Restrictions are collected and classified into five groups, namely restrictions on foreign entry, restrictions on the movement of people, other discriminatory measures, barriers to competition, and regulatory transparency. Each regulation receives a score between 0 and 1, where 0 is the least restrictive and 1 the most. The weighting methodology takes into account the fact that policies have different effects according to sectors, and expert judgment is applied to come up with a scoring system.

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29 For an extensive review on the different methodologies used to measure restrictions to trade in services, see McGuire (2003). Hoekman (1995) was the first to construct an index to measure restrictions on trade in services, which he did by developing a weighting system to assess the openness of GATS commitments. For other early studies applying similar methodologies, see, for example, Hardin and Holmes (1997), Mattoo (1998), or Kemp (2000). This chapter reports the index constructed by the OECD based on the methodology described in Geloso Grosso et al. (2015).

30 Data is available from 2014 to 2019. Additionally, the WTO and the World Bank have jointly created the Services Trade Policy Database (STPD). Although their country coverage is wider (the database includes 68 countries, 11 of which belong to LAC), the most recent year for which data is available is 2016. See Borchert et al. (2019) for methodological details on the STPD.

31 It is worth noting that indexes are a way of translating qualitative information into quantitative data by applying certain scores and weights. In order to construct them, information on restrictions first needs to be collected and classified, and then a weighting methodology needs to be defined and applied to compute the indexes in specific sectors of an economy. One of the main challenges is that the impact of a particular barrier can vary widely among different sectors or modes of supply, and judgment needs to be applied. Additionally, different degrees of restriction...
The STRI shows that the average restrictiveness by sector varies widely (Figure 14). The most restrictive industries are air transportation, legal, and accounting. In all three, the weight of restrictions to foreign entry is particularly high. While for air transportation barriers to competition are highly relevant, for legal and accounting services, restrictions on the movement of people represent a challenge.

**Figure 14: World Average Services Trade Restrictiveness Index by Sector**
(Index, 2019)

Source: IDB Integration and Trade Sector with data from the OECD.

Note: The index ranges from 0, representing no restrictions, to 1, corresponding to the highest restrictions. The world average is calculated as the simple average of all countries in the sample. Policy areas are weighted differently for each sector, according to their relative importance and based on expert judgment.

The average level of restrictiveness of LAC is higher than the world average in half the services sectors in the sample (Figure 15). In all logistics subsectors, policies are more restrictive in LAC than globally. This is because a barrier need to be translated into a specific number that is not easy to determine. For example, it is not clear if setting a maximum duration of stay of 12 months for temporary services suppliers is twice as restrictive as setting it at 24 months. Moreover, a barrier can have different effects in different countries, or some restrictions might not be set in place if they are not relevant for that economy, such as if a certain sector does not exist.
particularly true for logistics customs brokerage, for which LAC’s index is 68% higher than the world average, with Mexico standing out as having the most restrictive policies (Figure 16). Easing barriers in such sectors would not only improve trade in services but would also have a positive spillover on trade in goods, as their costs would decrease with more efficient customs-related services.

Financial services are also more affected by restrictions in LAC than in the world as a whole. The regional index for commercial banking is 24% higher than the global average, while that of insurance services is 6% higher. In both cases, Brazil has the most restrictive policies in LAC, while Chile and Costa Rica have the least.

Within the audiovisual sector, LAC broadcasting services are particularly restricted by policy, with an index 43% higher than the world average. This is particularly driven by Colombia and Mexico, whose indexes are more than twice global levels, while Chile and Costa Rica apply fewer policy barriers.

On the other hand, professional services in LAC are less restricted. The index for legal services is close to 50% of the world average and is likewise low for accounting, architecture, and engineering services (75%, 85%, and 93% the global average, respectively). In all four professional services categories, Chile and Colombia have lower levels of restrictiveness than the world average, while Costa Rica has low restrictions in legal services but higher ones in the remaining categories. In contrast, Brazil and Mexico impose more policy restrictions on trade in professional services than the global average.

Transportation services also face fewer policy barriers in LAC than the world in general, with the exception of road freight transportation. The index for air transportation is 71% of the world average, which all LAC countries are below. For rail freight, this index is 89%. For maritime transportation, it is similar to the world average, whereas for road freight transportation it is 29% higher. Chile stands out as being the least restrictive country for all transportation modes, and the same is true of Colombia for road and rail freight. In contrast, Mexico particularly restricts trade in road freight and air transportation, while Brazil restricts insurance services.

Finally, in other industries like computer services, telecommunications, and distribution services, policy restrictiveness in LAC is in line with the world average. Brazil imposes harsher restrictions on all three of these industries than other LAC countries, while Mexico does so for computer and distribution services. Chile and Colombia are the two countries in the region where these industries face the fewest restrictions.
Figure 15: World vs. LAC Average Services Trade Restrictiveness Index by Sector (Index, 2019)

Source: IDB Integration and Trade Sector with data from the OECD.
Note: The index ranges from 0, representing no restrictions, to 1, corresponding to the highest restrictions. The world average is calculated as the simple average of all countries in the sample. LAC contains Brazil, Chile, Colombia,
Costa Rica, and Mexico. Policy areas are weighted differently for each sector, according to their relative importance and based on expert judgment.

**Figure 16: Services Trade Restrictiveness Index by Sector and LAC Country**
(Index, 2019)

![Services Trade Restrictiveness Index by Sector and LAC Country](image)

*Source:* IDB Integration and Trade Sector with data from the OECD.

The nature of trade in services is evolving thanks to technological change and greater connectivity, and services are being delivered increasingly through digital channels. To reap the benefits that these less traditional services can bring, it is key to understand the policy barriers that specifically hinder trade in these sectors. The OECD’s Digital STRI focuses on cross-cutting impediments that affect services traded through electronic networks.\(^{32}\) Barriers affecting trade are categorized into five areas: infrastructure and connectivity, electronic transactions, payment systems, intellectual property rights, and other barriers affecting trade in digitally-enabled services.

Remarkably, Costa Rica topped the list of 44 countries in the Digital STRI database, meaning that it was the country with the least restrictive policies (Figure 17). Indeed, its only restrictions fell into the category of electronic transactions. With its strong telecommunications infrastructure and data protection laws, among other factors, Costa Rica has been able to position itself as a key services provider in global value chains. It started with call centers in the 1990s, then other sectors like software or back-office gradually started to develop.\(^{33}\) Mexico’s policy restrictiveness index was also below average—it ranked 20th. However, policies affecting infrastructure and connectivity, electronic transactions, and payment systems,

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\(^{32}\) See Ferencz (2019) for details on the methodology. The database contains 44 countries, of which six belong to LAC, namely Argentina, Colombia, Brazil, Chile, Mexico, and Costa Rica.

\(^{33}\) See Marin-Odio (2014) for a description of Costa Rica’s insertion in global value chains in services.
as well as other barriers, are still present there. The indexes for the remaining LAC countries are higher than the average, reflecting the weight of restrictive policies. Brazil, Colombia, and Argentina are at the bottom of the distribution, ranking 38th, 39th, and 40th, respectively, while in 34th place, Chile fares a little bit better. While the infrastructure and connectivity and electronic transactions components are important in all these countries, restrictions affecting intellectual property are also a factor for Brazil and Chile.

**Figure 17: Digitally-Enabled Services Trade Restrictiveness Index**
(Index, 2019)

![Graph showing digitally-enabled services trade restrictiveness index for various countries.](image)

*Source:* IDB Integration and Trade Sector with data from the OECD.

*Note:* The index ranges from 0, representing no restrictions, to 1, corresponding to the highest restrictions. The world average is calculated as the simple average of all countries in the sample. Policy areas are weighted according to their relative importance and based on expert judgment, with infrastructure and connectivity being the area with the highest weight.

**Relationships Between Costs, Policy Barriers, and Services Exports**

The natural question that follows the above discussion is what the relationship between policy restrictiveness and trade costs is. Several studies have tried to estimate this elasticity, such as Miroudot and Shepherd (2016), who distinguish between trade in final and intermediate services. They find that a
10% increase in the STRI is associated with 2.7% and 3.1% increases in trade costs for final and intermediate services, respectively. That is, more restrictive policies are related to higher trade costs.34

Another important link is the one between policy barriers and services exports. The main question is how much trade in services would increase by following a decrease in policy restrictiveness. Van der Marel and Shepherd (2013) find that a 10% drop in the STRI would imply a 4.9% growth in exports.35 Although the results for different sectors vary, this shows that making efforts to lower services trade barriers can have a positive effect on exports. However, a more recent study points to the fact that estimates of this sort might be overstating the positive impact by up to 78%.36

In general, estimates point to links between costs, policy barriers, and services exports. As higher-quality data with broad coverage of trade in services and barriers becomes available, estimates will become more accurate and reliable. Such information will be a valuable asset for policymakers, as a clear understanding of the impact of alternative sets of regulations is paramount when it comes to designing and implementing sound policies with positive effects on services exports.

In sum, the costs of trading services in LAC are well above those observed in other regions, which means the region’s competitiveness is lagging. Although costs have been on a downward trend in recent years, change has been slow, and LAC should fast-track reforms to avoid being left behind. Remarkably, trading services is more costly than trading manufactured goods in all regions of the world, which points to the fact that there is ample room for improvement. Conversely, metrics to estimate the restrictiveness of trade in services across countries show considerable variations between sectors. In comparison with the world, LAC fares well in professional services and transportation but poorly in logistics and financial services. Overall, the region should focus on policies that facilitate trade and boost competitiveness to lower costs and increase exports.

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34 Miroudot and Shepherd (2016) estimate an econometric model with trade costs as the dependent variable and the STRI as the key independent variable. Other gravity-like variables that are assumed to affect costs are also incorporated, such as distance, common language, or common colonial heritage.

35 Van der Marel and Shepherd (2013) use a functional form for costs that includes several independent variables: STRI (collected from the WB database), a dummy to indicate if two countries share a regional trade agreement, and gravity-like variables such as distance, a shared border, a common colonial heritage, and a common language. This expression is used in an econometric model in which the dependent variable is services exports and the explanatory variables are a set of fixed effects for both the exporter and importer, and costs.

36 Shepherd (2020) shows that cross-sectional gravity models overstate the effects of policies on services trade since they do not account for the simultaneity bias generated by unobserved country-pair characteristics.
3. Trade Policy

A clear regulatory framework that sets the ground rules for international trade in services is a key component for promoting such trade. However, the nature of services is different from that of goods, and their intangibility presents challenges when it comes to developing sound regulations. The fast pace of technological change has enabled trade in sectors that were once considered nontradable, and, as often happens, the law adapts slowly. Newer trade agreements incorporate provisions regarding trade in services, but in LAC few go beyond what is established in the GATS. Going forward, agreements covering new areas relating to e-commerce will be key modernizing factors that are needed to boost trade in services.

Modern regulatory frameworks need to deal simultaneously with services and investment provisions. A clear set of rules governing the provision of services is of paramount importance to attract foreign direct investment in sectors that are bound to grow above average in the future. Investment protection treaties, investment provisions in free trade agreements, and double taxation treaties are indeed emerging as key components of successful services development strategies.

Although this chapter does not provide a deep, exhaustive analysis of the current state of services trade agreements, it presents a broad overview of these and discusses three treaties that contain modern provisions and could serve as a starting point for countries when undertaking negotiations. These are the Pacific Alliance, an intraregional agreement marked by great sectoral openness, and the United States-Mexico-Canada Agreement (USMCA) and the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), which both contain comprehensive modern digital trade regulations.

General Agreement on Trade in Services

The General Agreement on Trade in Services (GATS) is a WTO treaty that was created to extend the multilateral trading system into the services sector. It entered into force in January 1995, as a result of the Uruguay Round, and was inspired by the General Agreement on Tariffs and Trade (GATT), the multilateral trading system for merchandise. Members of the WTO recognized the increasing importance of trade in services for the growth and development of their economies and agreed to create a framework to expand such trade under conditions of transparency and progressive liberalization, taking the needs of developing countries into consideration.

The GATS serves as a base for other agreements on services signed by its members. It defines four modes of supply for services and states that the agreement covers any service in any sector except for those supplied in the exercise of governmental authority.

Certain general obligations apply to all members and services sectors. The most important of these is that they must provide unconditional most-favored-nation treatment—that is, treatment cannot be less favorable than the treatment given to similar services and service suppliers of any other member. Likewise, members are required to act transparently, publishing all relevant measures of general

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37 For a companion piece focusing on the impact of policy measures on trade in services see Trachtenberg (2021).
38 All 164 WTO members are also members of the GATS.
39 See table 1 in chapter 1 for a description of the four modes of supply. Additionally, the GATS does not apply to air traffic rights and services directly related to the exercise of traffic rights.
application and reporting any new laws or regulations which significantly affect trade in services covered by GATS or any changes to existing legislation in this regard.

Each member decides which sectors to include in its Schedule of Specific Commitments, as well as which modes of supply. For those services, the GATS establishes two main obligations. The first is **market access**. Each member shall provide no less favorable treatment to services and services providers of other members than that specified in the schedule. In sectors where market access commitments are undertaken, members shall not adopt measures such as limiting the number of services suppliers, limiting the amount of the total value of the service, limiting the number of employees in a sector, or limiting the participation of foreign capital, among others. The second obligation is **national treatment**. Members shall provide no less favorable treatment to services providers of other members than that provided to their own services and services providers. The objective of these obligations is to ensure fair and equitable treatment for all participants.

Tourism and travel services is the sector for which the largest number of countries have schedules of specific commitments—23 countries in LAC and 133 in the rest of the world. It is a sector that has long been open to international trade, is well consolidated, and is of vital importance for LAC given its contribution to employment and the fact that is a source of foreign currency (Figure 18). Financial, business, and communication services are the next sectors for which countries have the most commitments both within the region and outside it. On the other hand, few LAC countries have commitments regarding environmental, distribution, and health and social services. The development of environmental services is fairly recent, and the sector has experienced a boom in recent decades due to growing awareness and more stringent environmental regulations. However, the number of countries with commitments is still low, as these services are typically provided by public entities. Distribution services are key for both domestic and international trade, as this sector links producers and consumers. Moreover, it is an important source of employment and growth. Further liberalizations would boost competition, lowering costs and creating greater economic returns. International trade in health and social services has been growing in recent years as health professionals have started moving to other countries and foreign investment in the industry has increased. More countries including commitments relating to these sectors in their GATS schedules could benefit LAC significantly.

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40 According to the WTO, environmental services includes sewage services, refuse disposal, sanitation and similar services, reducing vehicle emissions, noise abatement services, nature and landscape protection services, and other environmental services.

41 According to the WTO, health and social services includes hospital services and other health services as ambulance services and residential health facilities, but it does not include medical and dental services, veterinary services and the services provided by nurses, midwives, etc (these are grouped separately under "professional services").
Figure 18: General Agreement on Trade in Services Commitments by Sector
(Number of countries, 2020)

Source: IDB Integration and Trade Sector with data from I-TIP.
Note: The database includes the 163 individual countries that are members of the GATS, 25 of which are from LAC. The Bahamas is the only LAC country that is not a member.
There is wide heterogeneity among LAC countries regarding the sectors for which commitments are specified (Figure 19). Panama stands out for having commitments in all sectors. Mexico and Ecuador follow, with commitments in all sectors, except for environmental and recreational, cultural, and sporting services in Mexico’s case, and educational and other services in Ecuador’s. At the other end of the distribution, Paraguay only lists financial services and tourism and travel in its schedule. Belize has commitments regarding business, communications, and health-related and social services, while Suriname only lists communications, tourism and travel, and transportation services. It is worth noting that LAC countries have room to include more sectors in their schedules: in the region, the median number of sectors for which there are commitments is 6 out of 12, while in the Rest of the World it is 8.5.

Source: IDB Integration and Trade Sector with data from I-TIP.

Except for commitments in “other services not included elsewhere.”
Preferential Trade Agreements

There are 97 regional trade agreements (RTAs) in force in LAC that have been notified to the WTO, of which 71 cover both trade in goods and services, and 26 only cover trade in goods (Table 2). However, there is wide heterogeneity among countries. With 30 RTAs in place, Chile is the economy with the most in the region, while Haiti has just one. Moreover, there are eight intraregional RTAs in LAC, that is, agreements signed only by LAC countries, five of which contain provisions regarding trade in services (Table 3).\(^{43}\) These are the Pacific Alliance, Mexico–Central America, Colombia–Northern Triangle, Dominican Republic–Central America, and MERCOSUR. Not surprisingly, the most recent treaties are the ones whose coverage includes services, of which the Pacific Alliance is the most complete.

Table 2: Regional Trade Agreements in Force and Notified to the WTO by LAC Country (Number, 2020)

<table>
<thead>
<tr>
<th>Country of LAC</th>
<th>Goods</th>
<th>Goods &amp; Services</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Argentina</td>
<td>7</td>
<td>1</td>
<td>8</td>
</tr>
<tr>
<td>Bahamas</td>
<td>2</td>
<td>2</td>
<td>4</td>
</tr>
<tr>
<td>Barbados</td>
<td>2</td>
<td>2</td>
<td>4</td>
</tr>
<tr>
<td>Belize</td>
<td>2</td>
<td>2</td>
<td>4</td>
</tr>
<tr>
<td>Bolivia</td>
<td>4</td>
<td>4</td>
<td>4</td>
</tr>
<tr>
<td>Brazil</td>
<td>8</td>
<td>1</td>
<td>9</td>
</tr>
<tr>
<td>Chile</td>
<td>8</td>
<td>2</td>
<td>22</td>
</tr>
<tr>
<td>Colombia</td>
<td>3</td>
<td>10</td>
<td>13</td>
</tr>
<tr>
<td>Costa Rica</td>
<td>2</td>
<td>11</td>
<td>13</td>
</tr>
<tr>
<td>Dominican Republic</td>
<td>1</td>
<td>3</td>
<td>4</td>
</tr>
<tr>
<td>Ecuador</td>
<td>5</td>
<td>1</td>
<td>6</td>
</tr>
<tr>
<td>El Salvador</td>
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<td>Guatemala</td>
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<td>Guyana</td>
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<td>3</td>
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<td>Haiti</td>
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<td>1</td>
<td>1</td>
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<td>Honduras</td>
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<td>Jamaica</td>
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<td>Mexico</td>
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<td>Nicaragua</td>
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<td>Peru</td>
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<tr>
<td>Suriname</td>
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<td>2</td>
<td>2</td>
</tr>
<tr>
<td>Trinidad and Tobago</td>
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<td>2</td>
<td>3</td>
</tr>
<tr>
<td>Uruguay</td>
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<td>2</td>
<td>8</td>
</tr>
<tr>
<td>Venezuela</td>
<td>3</td>
<td>3</td>
<td></td>
</tr>
</tbody>
</table>

Source: IDB Integration and Trade Sector with data from the WTO.

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\(^{43}\) Refers only to agreement signed by more than two countries. In addition, there are 28 bilateral agreements between LAC countries.
Table 3: LAC Intraregional Trade Agreements in Force and Notified to the WTO

<table>
<thead>
<tr>
<th>Regional Trade Agreement</th>
<th>Coverage</th>
<th>Date of Entry into Force</th>
<th>Signatories</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pacific Alliance</td>
<td>Goods &amp; Services</td>
<td>1-May-16</td>
<td>Chile; Colombia; Mexico; Peru</td>
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<tr>
<td>Mexico - Central America</td>
<td>Goods &amp; Services</td>
<td>1-Sep-12</td>
<td>Costa Rica; El Salvador; Guatemala; Honduras; Mexico; Nicaragua</td>
</tr>
<tr>
<td>Colombia - Northern Triangle (El Salvador, Guatemala, Honduras)</td>
<td>Goods &amp; Services</td>
<td>12-Nov-09</td>
<td>Colombia; El Salvador; Guatemala; Honduras</td>
</tr>
<tr>
<td>Dominican Republic - Central America</td>
<td>Goods &amp; Services</td>
<td>4-Oct-01</td>
<td>Costa Rica; Dominican Republic; El Salvador; Guatemala; Honduras; Nicaragua</td>
</tr>
<tr>
<td>Southern Common Market (MERCOSUR)</td>
<td>Goods &amp; Services</td>
<td>29-Nov-1991(G) / 07-Dec-2005(S)</td>
<td>Argentina; Brazil; Paraguay; Uruguay</td>
</tr>
<tr>
<td>Andean Community (CAN)</td>
<td>Goods</td>
<td>25-May-88</td>
<td>Bolivia, Plurinational State of; Colombia; Ecuador; Peru; Venezuela, Bolivarian Republic of</td>
</tr>
<tr>
<td>Latin American Integration Association (LAIA)</td>
<td>Goods</td>
<td>18-Mar-81</td>
<td>Argentina; Bolivia, Plurinational State of; Brazil; Chile; Colombia; Cuba; Ecuador; Mexico; Paraguay; Peru; Uruguay; Venezuela, Bolivarian Republic of</td>
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<tr>
<td>Central American Common Market (CACM)</td>
<td>Goods</td>
<td>4-Jun-61</td>
<td>Costa Rica; El Salvador; Guatemala; Honduras; Nicaragua; Panama</td>
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</table>

Source: IDB Integration and Trade Sector with data from the WTO.

Note: The list excludes bilateral treaties and only includes treaties whose members are all countries from LAC.

The Pacific Alliance is a trade bloc formed by Chile, Colombia, Mexico, and Peru. It entered into force in May 2016, making it the most recently signed RTA among LAC countries. It is the most complete RTA regarding trade in services. The Additional Protocol to the Framework Agreement (hereafter, the Additional Protocol) contains chapters on trade in services, financial services, maritime transportation, telecommunications, and investment, as well as a specific chapter on e-commerce.\(^{44}\)

The chapter on services applies to modes 1, 2, and 4, as mode 3 is covered in the investment chapter. It does not apply to financial services, air services, services supplied in the exercise of governmental authority, government procurement, or subsidies or grants conceded by one party or a state enterprise. The Additional Protocol uses a negative list approach and grants market access, most-favored-nation treatment, and national treatment.\(^{45}\) Local presence is not required as a condition for providing cross-border services.

The Additional Protocol constitutes a major step toward liberalization in comparison with the GATS.\(^{46}\) Under the latter, Chile has schedules with partial coverage of five sectors.\(^{47}\) Under the Additional Protocol, Chile has fully liberalized the following sectors or subsectors: distribution and tourism and travel services; within business services: computer services, real estate services, and rental/leasing services without

\(^{44}\) For a recent overview of the internationalization of the services sector in the Pacific Alliance as a whole and within its individual member countries, see Palacio Valencia and Sauvè (2017).

\(^{45}\) A negative list approach implies that all sectors or subsectors that are not explicitly listed are, by default, liberalized, whereas in a positive list approach, all sectors or subsectors that are not explicitly listed are, by default, not liberalized.

\(^{46}\) For a detailed description of the Additional Protocol to the Framework Agreement, as well as a comparison with GATS commitments, see WTO (2019b).

\(^{47}\) Chile has schedules for business, communication, financial, and tourism and travel-related services, and transportation services.
operators; within communication services: other communication services; and within recreational and cultural sporting services: other recreational and cultural sporting services. It has also liberalized several other subsectors, while maintaining the possibility of applying quantitative restrictions, such as postal and courier services; sewage, refuse disposal and sanitation and similar services; hospital services, other human health services, and other health-related and social services; sporting and other recreational services; and space, rail, and pipeline transportation services, services auxiliary to all modes of transportation, and other transportation services. It is also noteworthy that Chile has expanded its commitments in all services sectors (except for the professional services subsector).

The GATS schedules for Colombia partially cover six sectors.48 Under the Additional Protocol, Colombia has fully liberalized the construction and related engineering services sectors and the following subsectors: real estate services, computer and related services, rental/leasing services without operators, other communication services, commission agents’ services, franchising, and other distribution services, and hotels and restaurants, tourist guides services and other tourism services. Although it has expanded its commitments in many other subsectors, it maintains certain reservations for business, communications, financial, and transportation services, although its commitments under the Additional Protocol do expand on those under the GATS. Finally, Colombia has not undertaken commitments in health-related and social services.

Mexico has GATS schedules for all sectors except for environmental and recreational, cultural, and sporting services. Under the Additional Protocol, it has fully liberalized the following subsectors: computer and related services and real estate services; commission agents’ services, wholesale trade services, and franchising; hotels and restaurants; and entertainment services, news agency services, and libraries, archives, museums, and other cultural services. In contrast, like Colombia, Mexico has made no commitments on health-related and social services. Moreover, it maintains reservations at the federal and state level that mainly affect retail, legal, architect, engineering, and land transportation services.

GATS schedules for Peru partially cover seven sectors.49 Under the Additional Protocol, the country has fully liberalized the tourism and travel-related services sectors, along with the following subsectors: computer and related services, real estate services, commission agents’ services, franchising and other related distribution services, entertainment services, news agency services, and libraries, archives, museums, and other cultural services. A further set of subsectors have been liberalized, albeit with the possibility of quantitative restrictions being imposed in the future. These are postal and courier services, construction and related engineering services, refuse disposal services, health-related services, and space, pipeline, and other transportation services. New or improved commitments have been undertaken in all subsectors.

Technological change has brought new ways of trading services and has also boosted innovation and the creation of new services, such as software development or media streaming. For such trade to occur seamlessly, sound e-commerce regulations are needed.50 The Additional Protocol includes a chapter on

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48 Colombia has schedules for business, communication, and construction and related engineering services, as well as environmental, financial, and tourism and travel-related services.
49 Peru has schedules for business, communication, distribution, financial, tourism and travel-related services, recreational, cultural and sporting services, and transport services.
50 E-commerce is defined in the Protocol as “commerce conducted through telecommunications, alone or in conjunction with other information and communication technologies.”
e-commerce that applies to both goods and services. It conveys that electronically transmitted digital products are exempt from customs duties for import.exports but might be subject to internal taxes. The Additional Protocol includes advances in the area of privacy as it protects the personal information of users and also provides rights to users of electronic authentication and digital certificates. It imposes a nondiscrimination obligation for digital products with no sectoral exceptions and prohibits parties from requiring that computing facilities be located in their territory as a condition for conducting businesses there. Notably, the Additional Protocol also includes commitments to work toward ensuring online consumer protections, while promoting paperless trade.

Although there is still room for improvement on the path to liberalization, the Pacific Alliance has taken sound steps in the right direction and provides a template for the negotiation of other trade agreements within LAC.

*Preferential Trade Agreements with Non-LAC countries*

In addition to the agreements LAC countries have with each other, there is an ample network of treaties with countries outside the region. Specifically, there are 24 multicountry and 37 bilateral agreements, of which 17 and 28 cover services, respectively. The United States-Mexico-Canada Agreement (USMCA) and the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) are particularly noteworthy regarding trade in services and, as reported below, digital trade.

The CPTPP is a trade agreement between 11 countries (Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, and Vietnam) that entered into force on December 30, 2018. It is the successor of the Trans-Pacific Partnership (TPP), which included the same countries plus the US, but never entered into force in the latter country, as it withdrew.\(^51\) In fact, the two agreements are very similar, as two-thirds of the provisions remained unchanged, and the provisions that were modified or eliminated were those that were particularly supported by the US. The CPTPP includes chapters on investment, cross-border trade in services, temporary entry for businesspersons, and e-commerce, as well as chapters on specific services sectors (financial services and telecommunications).

The USMCA is a free trade agreement between the US, Mexico, and Canada, and is the successor of the North American Free Trade Agreement (NAFTA). It entered into force on July 1, 2020. It contains separate chapters for cross-border trade in services, investment, temporary entry, and digital trade, as well as chapters on financial services and telecommunications. The USMCA heavily draws on the original TPP—57% of the former’s text comes from the latter.\(^52\)

Beyond the sectoral openness that the CPTPP and the USMCA entail, which is not explicitly covered in this report, one aspect that sets them apart from other agreements is their chapters on digital trade. As mentioned before, e-commerce is a key enabler for trade in nontraditional services like computer and business services. The CPTPP and the USMCA are noteworthy in that they contain the most advanced provisions on such matters.

Both prohibit the imposition of customs duties on digital products and electronic transmissions of digital products, which facilitates trade by reducing costs. Nondiscriminatory treatment of digital products is also provided, although the CPTPP excludes broadcasting. This provision ensures competition and, therefore,

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\(^{51}\) All countries have ratified the CPTPP except for Chile, where ratification by the Senate is still pending.

\(^{52}\) See Alschner and Panford-Walsh (2019).
more choices and better prices for consumers. Regarding the domestic electronic transactions framework, parties agree to maintain a legal framework for electronic transactions that is consistent with the principles of the UNCITRAL Model Law on Electronic Commerce (1996). Moreover, they agree to avoid unnecessary regulatory burdens and facilitate the participation of stakeholders in the development of the domestic legal framework.

The provisions on electronic authentication and electronic signatures and on paperless trading also aim to facilitate the trade process by making transactions easier. Under the former, parties mutually recognize the process of validating electronic signatures. Under the latter, parties endeavor to accept documents submitted electronically as the legal equivalent of the paper version.

Online consumer protection is fundamental to establishing a relationship of trust between firms and consumers. This provision establishes that the parties agree to adopt or maintain consumer protection laws to proscribe fraudulent and deceptive commercial activities that could jeopardize consumers engaged in online commercial activities. Personal data protection is also key: parties agree to adopt or maintain a legal framework that protects personal information and prevents the misuse of individual information on consumers engaged in e-commerce. Moreover, parties agree to adopt or maintain measures to limit unsolicited commercial electronic communications.

To build and develop effective international electronic trade, the free cross-border transfer of information is essential. As such, parties agree to not prohibit or restrict information exchanged by electronic means. Along similar lines, they also agree to not require a covered person to use or locate computing facilities in the party’s territory as a condition for conducting business in that territory. This provision reduces costs as firms do not need to store and replicate data locally.

The provision on source code states that parties shall not require the transfer of or access to software source code as a condition for trade. Software source code often contains information and trade secrets that give the owner an advantage that might be lost if they were required to disclose the code in question. This provision therefore ensures a safer trade environment. However, the language of the respective provisions on this matter in the CPTPP and the USMCA varies slightly: the former excludes software used for critical infrastructure, whereas the latter also includes source code-related algorithms.

Cybersecurity concerns pose a constant threat to electronic transactions and undermine confidence in digital trade. As such, parties agree to build cybersecurity incident response capabilities and strengthen collaboration to identify and mitigate malicious intrusions. Another provision concerns cooperation in other areas, such as personal information protection, online consumer protection, security in electronic communications, authentication, and e-government.

In addition to the provisions described above, which are common to both treaties, the USMCA includes one on interactive computer services and one on open government data. The first of these refers to suppliers of a service that provides or enables electronic access to a computer server by multiple users and thus is not a content creator. The provision prevents intermediary services providers from being held liable for harm relating to the information stored, processed, transmitted, distributed, or made available by such services. Finally, open government data is a provision that recommends that parties make government information available to the public.

In summary, although the region has made inroads into building a network of trade agreements covering trade in services, most of these are outdated. Beyond expanding sectoral coverage, efforts to modernize
agreements to include provisions on digital trade are key to enhancing productivity and efficiency in nontraditional services exports, such as exports of business or computer services. Such provisions would help by lowering or even lifting barriers, facilitating transactions, and creating more competitive markets.
Conclusions

The relevance of trade in services has increased over time. This was due, among other factors, to technological change, which has enabled international trade in services that were once considered nontradable, while fostering the development of new services, such as software. Trade in services has opened up a window of opportunity for diversifying the export basket and increasing resilience to trade shocks.

Analyzing trade in services is challenging due to the lack of consistent, reliable data with broad country coverage. Collecting and generating sound statistics should be the foremost priority for governments, since reliable information will enable policymakers to formulate and implement better policies to address barriers to trade in services and boost competitiveness.

In the aftermath of the COVID-19 pandemic, to successfully navigate the waves of uncertainty and prepare itself for the future, LAC needs to increase its competitiveness and insert itself in the most dynamic segments of global markets, leveraging its factor endowments and comparative advantages. Traditional services, such as those relating to tourism, continue to play a major role in LAC. Although some green shoots have started to appear in certain countries, in nontraditional sectors like computer and information services or business services, their weight is still small. In the current global landscape, moving toward trade in digitally-enabled sectors is fundamental if countries want to make the most of emerging opportunities. Moreover, such sectors have proved more resilient during the economic crisis caused by the pandemic because they do not entail physical contact between buyer and seller.

The costs of trading services are substantially higher than those for trading goods, which implies that services face higher barriers and there is ample room for improvement. In LAC, these costs are higher than those estimated for the other regions of the world and are above world averages in all sectors analyzed, making the region less competitive. Although the grounds for certain trade-restricting policies may be legitimate, such as ensuring market stability and quality standards, many have the effect of increasing the cost of providing services and lowering competition and quality. Efforts to facilitate trade and lower barriers, like allowing for international payments, for example, will go a long way toward positioning LAC as a competitive player in global markets.

The regulatory framework governing trade in services in LAC is still limited. Although a large network of trade agreements is in place in the region, most of these do not go beyond the disciplines of the GATS, and some do not even cover trade in services at all. However, three agreements do include modern provisions and could serve as a benchmark for the negotiation of new ones. These are the Pacific Alliance, the sectoral openness of which makes it stand out among intraregional agreements, and the USMCA and the CPTPP, which contain comprehensive modern provisions on digital trade. Clear regulations are the basis for building a relationship of trust between buyers, sellers, and institutions and serve as a tool for promoting trade. Policymakers should revisit their regulatory framework and negotiate new agreements or update current ones by increasing sectoral openness and including provisions that address current trends, such as e-commerce.

In sum, LAC needs to position itself to take advantage of the opportunities that trade in services may bring. To do so, it needs to boost competitiveness by lowering trading costs, removing barriers, and developing...
the capabilities needed to offer high-quality modern services. The region also needs to gravitate toward dynamic sectors such as digitally-enabled services, since that is the direction the world has been moving in, and the post-COVID-19 recovery is likely to accelerate this trend. In this light, efforts to modernize trade agreements will bring high returns. Meanwhile, improving trade data collection and statistics will help policymakers design and implement sound public policies that support the development and diversification of the services sector.
References


