Trade in services in Latin America and the Caribbean: an analysis of recent trends

Nanno Mulder
Sebastián Sáez
Claudia de Camino
Alfonso Finot

Division of International Trade and Integration

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This document was prepared by Nanno Mulder, Economic Affairs Officer, Sebastián Sáez, Expert of the International Trade and Integration Division, Claudia de Camino, Statistics Assistant of the Statistics and Economic Projections Division and Alfonso Finot, Consultant of the Economic Commission for Latin America and the Caribbean (ECLAC) of the United Nations. The authors are grateful for contributions by Rudolf Buitelaar (offshore services in the Caribbean) and Lia Valls (business services in Brazil), and comments and suggestions by Renato Baumann, José Duran, João Carlos Ferraz, René Hernandez, Felipe Jimenez, Bernardo Kosacoff, Mikio Kuwayama, José Carlos Mattos, Indira Romero, Osvaldo Rosales, Claudia Schatan, and Marcia Tavares.

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Abstract

This paper compares the dynamism of the Latin American and Caribbean region’s services trade with that of Asia, evaluates the determinants of these trade flows, and proposes measures for improving the region’s performance. The focus of this study is on “other services”, which includes all services except transport and travel services (mainly tourism). “Other services” include many modern service inputs (including communications, financial and information technology services and business services), that play an increasingly vital role in determining many businesses’ levels of competitiveness and productivity. Latin America exports of “other services” grew by less than that of the world and Asian averages between 1985 and 2005. As a result, the share of Latin America and the Caribbean in world’s “other services” trade diminished from between 1995 and 2005, although the performance varies greatly among subregions, with Argentina, Brazil, Costa Rica and Honduras being the most successful. The region’s lack of dynamism relative to that of China and India is also reflected in the drop of the region’s share in imports of the United States and European Union.

Three key determinants are analyzed to understand the region’s poor performance: national regulatory systems, human capital, and information and communication technologies (ICTs). The incidence of regulation contributes little to the understanding of the differences in export performance, as services in countries in Latin America and the Caribbean tend to be less heavily regulated than those in Asia. Together with the privatization of many state enterprises, Latin America attracted larger inflows of foreign capital as a share of GDP between 1995 and 2004. However, most of this investment was
motivated by serving local markets rather than creating an export base of services. The quality and cost of human capital provide a better explanation of the superior Asian performance. China, India and the ASEAN countries have an advantage over Latin America and the Caribbean because they have a large number of highly skilled workers (including information technology experts) who are paid competitive salaries. Another factor favoring the Asian countries is that workers have a good grasp of mathematics, an area where the region lags far behind. Third, although the quality of the ICT infrastructure is comparable between the two regions, the cost seems somewhat higher in Latin America and the Caribbean. One factor that raises the cost of access to ICTs in the region is that, by contrast with Asia, only a few countries are signatories to the WTO Information Technology Agreement.

To boost trade in these services in the region, both public and private sectors need to make an effort to produce better-quality, competitively priced services. These efforts should target the main obstacles to the sector’s development. First, a greater liberalization of services trade, combined with increased mutual recognition and gradual convergence of different countries’ regulatory frameworks. The timid approach taken to liberalization in WTO, subregional agreements (Mercosur and Andean Community), and the bilateral agreements with countries outside the region has done no more than maintain the regulatory status quo without achieving any genuine liberalization of trade in services. Second, upgrading human capital is probably the most important task for Latin America and the Caribbean. The public and private sectors should work together to establish ICT university courses and training programmes, especially for small and medium-sized enterprises. Third, an important step in opening up access to modern technologies such as telecommunications is to improve regulatory and competition policy with a view to stimulating investment and ensuring that high-quality services are provided at the lowest possible cost. Greater broadband Internet penetration makes it easier to sell more complex electronic services internationally. Broadband access can also boost companies’ competitiveness and productivity. Another measure to encourage service exports is quality certification that enhances international credibility for service delivery.
Introduction

The growing importance of services in the economy, employment and trade is a trend common to both advanced and developing countries. Services are essential inputs for many activities, and play a crucial role in increasing economic growth and productivity by improving financial intermediation, infrastructure, the use of information and communication technologies (ICT), education, health and the State apparatus. They currently represent approximately two thirds of the gross domestic product (GDP) of rich countries, and close to half that of developing countries, even though a clear difference exists between the types of services prevailing in each group. In terms of employment, the services sector accounts for 70% of workers in developed countries, but only one third of workers in emerging economies. Latin America and the Caribbean are positioned between the two groups. Cross-border trade in services has tripled since 1990, while foreign direct investment has quadrupled. Emerging economies have expanded their service exports at a rate exceeding that of developed countries (UNCTAD, 2004, 2005).

Business services play a strategic role in the overall arena of services. They are becoming increasingly knowledge-intensive (for example, advisory services, services related to information technology, engineering services and research and development services), and have become strategic inputs that increase the productivity and competitiveness of businesses. Moreover, thanks to advances in ICT, firms can now outsource many services to suppliers offering the best price-quality ratio, anywhere in the world. This process has played a key role in the explosive growth of trade in services provided to businesses, as well as the internationalization of such trade. Developing countries such as India and China, as well as
certain nuclei in Latin America, have shown a strong capacity to attract a considerable share of this dynamic component of global trade.

This study will compare the trends of trade in services (save for transportation and travel) in Latin America and the Caribbean, China, Hong Kong Special Administrative Region of China, India and the countries that comprise the Association of Southeast Asian Nations (ASEAN). It will also assess the main determining factors of such trade, and propose measures to improve international insertion in this sector. To that end, the dynamics of service exports over the last decade will be examined. The relative diversification of service exports will also be analysed and compared to the pattern of concentration found in more traditional services (transportation and tourism). The varying performance of the countries of the region in this field will then be examined—particularly with regard to the factors that have influenced trends in service exports, the progress made by regional and bilateral trade and investment agreements and the differing levels of regulation to which the sector has been subjected. Finally, policies will be proposed to improve the region’s performance in terms of service exports.

These questions will be addressed in four sections. The first section deals with the strategic role of services, and sets forth the main trends in global trade. The second section compares the performance of the region in terms of trade in services with that of a group of Asian countries, both at a global level and in the main markets of the United States and the European Union. It also discusses the success of certain Latin American transnationals in this sector. The third section analyses certain factors that play a determining role in export performance, taking into account issues such as regulation, human capital and the progress achieved by countries in the field of information and communication technologies. The fourth section analyses policies that may improve the region’s competitiveness in this regard by harmonizing regulatory frameworks among countries. This would be accomplished by establishing trade agreements, improving workforce quality and increasing the adoption of cutting-edge technologies.

This study covers all market services, with the exception of transportation and travel. The annex at the end of this paper contains a list of sectors based on balance of payments and World Trade Organisation (WTO) classifications. This paper will address not only auditing, computer, engineering and legal services provided to companies, but also construction, financial, insurance and communication services. Transportation and travel have been excluded for a variety of reasons. The term “services” will hereinafter be understood to apply to all services, except for transportation and travel.

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1 The following two minor categories were also excluded: (i) personal, cultural and recreational services; (ii) government services.

2 Firstly, travel and transportation services are usually provided directly to consumers, whereas other services are sold mainly to businesses. Since some of the determining factors of services provided to consumers differ from those offered to companies, a decision was made to focus on a single category. Secondly, while the literature on transportation and travel services is relatively abundant, trade in other services, which has become increasingly relevant in recent years, has not been extensively studied—particularly in Latin America and the Caribbean—and deserves closer attention.
I. The Strategic Role of Services

A. Theoretical Arguments

One common feature of most services is interaction between suppliers and businesses, with the general objective of increasing the productivity and competitiveness of the latter. This is true of knowledge-intensive services —advisory, auditing, computer, engineering, and research and development services, among others—as well as those which make intensive use of unskilled labour, such as cleaning and security. As production inputs, services are key to increasing competitiveness and productivity in an increasingly globalized world.

The services sector has displayed one of the highest growth levels of any sector in advanced economies and trade, primarily as a result of two phenomena (Kox and Rubalcaba, 2007).\(^3\) The first is the imperative to lower costs by delegating auxiliary tasks to third parties. By outsourcing such activities to service providers, companies can focus their resources on their core business. An increased supply of services also enables companies to achieve a greater degree of specialisation. This, in turn, reflects a “simple” shift whereby services move from one sector to another without undergoing any change in their nature. The second phenomenon is the ability of service providers to sell services that are different—superior in quality or more specialised—from those which the purchasing companies produced for themselves. This includes new services. Consequently,

\(^3\) Such services account for half the growth of employment in the European Union since 1995.
outsourcing grants companies access to inputs of greater quality than those they could have produced on their own. Services thus acquire a strategic role, as they lead to the development of other sectors, both industrial and tertiary, and attract foreign investment. Several studies of the European Union suggest that the second phenomenon is more relevant than the first in terms of explaining the massive expansion of this sector.

Another productive feature of services —particularly knowledge-intensive ones— is the key role they play in innovation in other sectors and national innovation systems (Kox, 2002; Miroudot, 2006). This occurs through three channels. Firstly, information-technology and engineering firms tend to develop technological innovations. Secondly, service companies offer their clients managerial or entrepreneurial innovations that may not be strictly technological in nature. Finally, the interaction between companies that have received innovative techniques helps disseminate best practices.

The internationalization of services is gaining importance as a result of trends supply and demand. From a demand perspective, a growing number of businesses are outsourcing or procuring their services abroad, attracted by competitive advantages. This practice, coupled with the transferral of certain internal company services overseas, is known as “off-shoring” (or “nearshoring”, when services are transferred to a nearby country). Companies require such services to improve the quality of their products and processes, sell their products abroad and coordinate the activities (inventories) of their branches in different countries, among other reasons. This trend, which is a basic feature of the globalisation of economies, has its origins in advances in information and communication technologies, strong competitive pressures to reduce costs and improve productivity and increased liberalisation of trade in the aforementioned services. Technological advances have reduced transportation costs, as well as the cost of disseminating information and ideas, leading businesses to transform their processes and production structures. ICT has made it possible to digitalize many aspects of production, and has simplified the provision of services over long distances. Services have thus become increasingly tradable, and the feasibility of outsourcing them or procuring them overseas has grown immensely. During the late 1980s and early 1990s, services shifted toward the client (particularly back office operations); in later years, however, they expanded to include professional services, software development, financial services and other activities that make intensive use of human capital (Mashayekhi, 2005). Off-shoring introduced a new form of entrepreneurial organization known as “extended organization”, in which the parent company maintains strict control of services transferred abroad. Free trade agreements have also made it possible to exchange information in real time (Aron and Singh, 2005).

Another phenomenon which has become more relevant over the last few years is insourcing, which involves the participation of sub-contractors into their client companies. It differs from outsourcing in that the sub-contractor intervenes in the operations of the client company to redesign its productive and logistical processes. United Parcel Service (UPS), one of the world’s leading companies in this field, has developed systems for the management of the entire supply chain of many of its client companies (Friedman, 2005).

Services have also become internationalized from a supply standpoint. In other words, the companies offering them are operating in more and more locations around the world. Product differentiation based on point of sale and customer-oriented services are key success factors in the successful globalisation of services. This is made possible by the exchange of personal knowledge, or through information and communication technologies. Internationalisation can be achieved by means of 3 models (Toivonen, 2004): (i) the “evolutionary model”, in which companies begin by increasing their local market share, and then export their services, often by following their national clients overseas; (ii) the “born global model”, in which companies offer products to clients in different countries from the very outset, relying on intensive use of ICT; and (iii) the “think
globally, act locally” model, in which companies operate mainly in the local market but provide services to branches of foreign clients or national firms that are active in many countries. Companies in this category are often part of international networks made up of similar firms in other countries.

B. Trends

While the global trade in “other services” (total services minus transportation and travel) seems to grow faster than trade in goods, it is difficult to accurately measure its volume, given the lack of complete statistics in most countries. The only data available are estimates of cross-border trade based on the balance of payments. Such trade involves services that cross national borders while their providers and consumers do not. International phone calls and telemedicine are examples of this phenomenon. It is often the case, however, that no record is kept of operations in which a provider or client travels to provide or receive a service. In other words, many services require the physical presence of both parties, one of whom must necessarily cross a border (see box 1 and figure 1).

**BOX 1**

**SOURCES OF DATA ON INTERNATIONAL TRADE IN SERVICES**

The main difference between services and goods lies in the immediacy of the relationship between supplier and consumer. Many services are “non-transportable”, and cannot be exported like goods; the consumer must go to the supplier, or the supplier must go to the consumer. To reflect this type of trade, the Manual on Statistics of International Trade in Services extends the definition of international trade in services to include the value of services provided through foreign affiliates established abroad. Services are also provided by individuals located abroad, either as service suppliers themselves or employed by service suppliers. While a large part of this type of trade in services is covered by the balance of payments, the remainder requires additional information, as it would include transactions among residents. The Manual describes four modes through which services may be supplied:

- **Mode 1**, or cross-border supply, takes place when both the consumer and the provider of a service remain in their respective countries, while the service crosses the border. The delivery of the service can be effected by telephone, fax, Internet, mail or courier, among other means. It is similar to the traditional notion of trade in goods. Freight transport services, correspondence courses and telediagnosis are examples of this type of trade in services.

- **Mode 2**, or consumption abroad, takes place when a consumer moves outside his or her home territory and consumes services in another country. Overseas tourism is one example of this phenomenon.

- **Mode 3**, or commercial presence, entails close contact with the consumer in his or her home territory in the various stages of production and delivery, as well as after delivery. Medical services provided by a foreign-owned hospital, courses in a foreign-owned school and services provided by a domestic branch or subsidiary of a foreign bank are examples of supplies through commercial presence.

- **Mode 4**, or presence of natural persons, occurs when an individual has moved into the territory of the consumer to provide a service, whether on his or her own behalf or on behalf of his or her employer. This type of supply applies to two areas: trade in services in the Balance of Payments Manual sense (e.g., financial auditing services by an auditor sent by a foreign firm or provision of entertainment services by a professional who is temporarily in the host country), and employment, meaning physical presence of persons in the receiving country on a “non-permanent” basis. Short-term employment of foreign doctors or teachers, intra-corporate staff transfers, the presence of foreign staff in foreign affiliates or the employment of construction workers or paid domestic helpers are some examples.

This study employs data recorded in the balance of payments, and adheres to the extended definition of services. The main service categories are as follows: transportation, travel, communication services, construction services, insurance services, financial services, computer and information services, royalties and license fees, other business services, personal, cultural and recreational services and government services. During recent years, the countries of the region have improved the breakdown of their service trade in accordance with the fifth edition of the Balance of Payments Manual. These data cover trade in modes 1 and 2, and partially cover trade arising from the temporary movement of persons (mode 4).

More efforts are needed, however, to collect data on trade in services through commercial presence. Other sources cited in this paper include national data and data obtained from the World Trade Organization and the Organisation for Economic Co-operation and Development (OECD). These sources help shed light on certain issues involving the trading partners of industrialized economies in the international service trade. This makes it possible to assess the participation of Latin America and the Caribbean in the trade of those economies. The Investment Map database of the International Trade Centre was also used, as were other sources related to foreign direct investment, in order to study international trade in services from the standpoint of commercial presence.

Source: Economic Commission for Latin America and the Caribbean (ECLAC). This extended definition of international trade in services conforms with the 1993 System of National Accounts (SNA), as well as the fifth edition of the Balance of Payments Manual published by the International Monetary Fund. Its conceptual and methodological aspects are explained in United Nations (2002).
FIGURE 1
GLOBAL EXPORTS OF GOODS AND SERVICES, 1985-2006

A) Goods and services: growth (1985=100) and share

\[\text{Percentages}\]

\[\begin{array}{c}
\hline
\text{Goods (left axis)} & & & & & & & & & & \\
\text{Total services (left axis)} & & & & & & & & & & \\
\text{"Other services" a/ (OS) (left axis)} & & & & & & & & & & \\
\text{Share of OS in world trade (right axis)} & & & & & & & & & & \\
\end{array}\]

B) "Other services": growth of advanced and developing countries
(1985=100), Share of developing countries in total
(\textit{Percentages})

\[\begin{array}{c}
\hline
\text{Advanced countries (left axis)} & & & & & & & & & & \\
\text{Developing countries (left axis)} & & & & & & & & & & \\
\text{Share of developing countries in total (right axis)} & & & & & & & & & & \\
\end{array}\]


Note: "Other services" refers to total services less transportation and travel.
Available data show that, as a result of the above, global cross-border trade in “other services” has expanded at a faster rate than that of other goods and services over the past two decades (see figure 2). Its share of the global trade in goods and services has increased by three percentage points, reaching 9.0% in 2006. Between 1985 and 1995, exports of such services on the part of developing countries grew faster than those of advanced countries, although this trend was surprisingly reversed during the following decade. Developing countries lost two percentage points of their share in global trade between 1995 and 2005.

**FIGURE 2**

**STRUCTURE OF GLOBAL TRADE IN SERVICES, 1995-2005**

A) Structure of services (world)

[Diagram showing structure of global trade in services, 1995-2005.]

B) Structure of “other services” (exports of the OECD countries, 2005)

[Diagram showing structure of “other services” exports of OECD countries, 2005.]


Note: Transportation, travel, personal and government services have been excluded.
The structure of the global trade in services changed considerably between 1995 and 2005, shifting toward computer and information-technology services, as well as financial services (see figure 2). Available data on the seven main categories show that “other services” represent half of worldwide trade in those services. In the “other services” category, services related to commerce (buying and selling), legal services and research and development deserve special attention.4

Service exports from developing countries represent 23% of trade in that sector. Three fourths of this percentage are attributable to a small group of 15 countries. Developing countries in Asia have achieved a considerable increase in their share of world trade, from 9% in 1995 to around 17% in 2005. Latin America and the Caribbean export only 1.8% of services worldwide.

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4 It has only been in recent years that breakdowns of the category of “other services” in most of the advanced countries have been published; such services represent two thirds of the combined exports of OECD countries.
II. Export Trends: A Comparison Between Latin America and the Caribbean and East Asia

A. Export growth

The growth rate of service exports from Latin America and the Caribbean between 1985 and 2005 was lower than that of Asia and the world as a whole. Over the course of those two decades, service exports increased by a factor 4.5 in Latin America and the Caribbean, 6.2 worldwide, 8 in ASEAN countries and the Hong Kong Special Administrative Region (SAR) of China, 14 in India and 24 in China. Consequently, the Latin American and Caribbean share of the world service trade fell as that of Asia rose. The growth rate of the “other services” category surpassed that of transportation and travel in the two regions and the world at large. Different growth rates led to a profound change in the share of trade captured by those three categories. Transactions in the “other services” category, which are the focus of this study, increased considerably throughout the world. While the trade in this type of services increased in Latin America and the Caribbean, particularly between 1985 and 1995, its dynamism continued to lag far behind Asia and the world as a whole.

In Latin America, diverging growth trends among service export categories are reflected in their respective roles in trade and GDP (Figure 3). From the 1990s onwards, total services exports expanded at lower rates than goods exports, causing its participation in total exports to fall. The high growth rate of nominal good exports in the
2000s reflects in large part the fast rising prices of commodities, particularly oil, gas and minerals. Nevertheless, as services exports grew faster than GDP its relative share increased. Trends in the subset of “other services” were somewhat different. Except for the period after 2000, the exports of “other services” increased faster than the rest of goods and services exports. As a consequence, both its share in total exports and GDP increased steadily. However, this trend was reversed after 2000.

**FIGURE 3**

**LATIN AMERICA AND THE CARIBBEAN: SERVICES EXPORTS AS SHARE OF TOTAL EXPORTS AND SHARE OF GDP (IN %), 1980-2005**

Total services

“Other services”

Source: World Bank, World Development Indicators.

The regional average also hides large differences among sub-regions and countries in terms of the importance of services trade in GDP (Figure 4). The Caribbean is by far the sub-region where services exports play the important role, accounting for more than 25% of GDP. Services exports also expanded substantially their share in GDP in Central America.

**FIGURE 4**


Source: FMI, Estadísticas de balanza de pagos.

The lesser dynamism of Latin America between 1985 and 2005 conceals a great deal of intraregional diversity (Camino, 2003 and 2005; Ventura-Díaz and others, 2003). Guatemala, Chile and Costa Rica displayed the highest growth rates for services in general, while the Bolivarian
Republic of Venezuela, Colombia and Ecuador posted the lowest rates in this category. The greatest expansion in transportation services took place in Panama and Chile. The latter became the chief exporter of such services in the region. The strongest growth in tourism services was recorded in Guatemala, Brazil and Cuba, with annual rates exceeding 20%. Finally, Brazil, Argentina and Costa Rica posted the highest growth rates in the “other services” category. This category captured its largest share of overall exports in 2005 in Paraguay, Brazil and Argentina (see table 1).

### TABLE 1

**SERVICE EXPORTS, 1985-2005: LEVELS, COMPOSITION AND ANNUAL GROWTH RATES**

<table>
<thead>
<tr>
<th></th>
<th>1985 Millions of dollars</th>
<th>Transportation (percentages)</th>
<th>Travel</th>
<th>Other</th>
<th>2005 Millions of dollars</th>
<th>Transportation (percentages)</th>
<th>Travel</th>
<th>Other</th>
<th>Average annual growth rate</th>
</tr>
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<td></td>
<td></td>
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</tr>
<tr>
<td>Total</td>
<td>16 514</td>
<td>33</td>
<td>49</td>
<td>19</td>
<td>74 152</td>
<td>22</td>
<td>52</td>
<td>26</td>
<td>7 5 8 9</td>
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<tr>
<td>Andean Community</td>
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<td>24</td>
<td>6 834</td>
<td>29</td>
<td>52</td>
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<tr>
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<td>2 388</td>
<td>31</td>
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<td><strong>Central American Common Market</strong></td>
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<td>58 638</td>
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<tr>
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<td>16</td>
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<td>59</td>
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<td>37</td>
<td>2 420</td>
<td>23</td>
<td>28</td>
<td>48</td>
<td>10 8 9 11</td>
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</tbody>
</table>

This intraregional diversity led to significant shifts in the shares of each country and subregion in the service trade between 1985 and 2005. While Mexico remains the region’s largest exporter, its share dropped by seven percentage points during the period in question (see figure 5). The Caribbean Community (CARICOM) and the Andean Community also lost ground. Conversely, service exports from “other countries” (particularly Chile) and Brazil increased considerably. The good performance of Brazil can be attributed mainly to its buoyancy in the “other services” subcategory, where its share rose from 15% to 38%. The Andean Community and Mexico were the biggest losers in this regard. The latter maintained its position only thanks to the good performance of its tourism services sector.

**FIGURE 5**

**LATIN AMERICAN SERVICE EXPORTS BY COUNTRY OR SUBREGION, 1985-2005**

(Percentages)

a) Structure of total services: Latin America and the Caribbean by country/region

b) Structure of “other services”: Latin America and the Caribbean by country/region


Note: “Other countries” refers to Chile, Panama and the Dominican Republic; “other services” refers to all services except for transportation and travel.
B. Participation in the global trade in “other services”

The rest of this study will focus exclusively on the “other services” category, also referred to simply as “services”. This category includes all services except for transportation and travel. Growth of service exports in Latin America and the Caribbean has lagged behind the world average, with the region’s share of this sector dropping from 2.4% to 1.8% between 1995 and 2005. The picture in Asia is mixed; while the ASEAN countries and the Hong Kong Special Administrative Region (SAR) of China suffered a drop in their share, the buoyancy of China and India led to an increase (see figure 6). These overall results conceal a great deal of diversity among subsectors. While the share of Latin America and the Caribbean in the communication and insurance markets fell sharply, it remained above that of Asia. The only category where growth occurred was “other business services” (see annex). India warrants special attention, as its share of the global computer services market reached 14% in 2005. This goes a long way toward explaining its superior overall position in the “other services” trade. The countries of ASEAN lost overall market share, although their share of the communications and construction sectors improved.

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**FIGURE 6**

**PARTICIPATION OF LATIN AMERICA AND THE CARIBBEAN AND THEIR ASIAN COMPETITORS IN THE GLOBAL TRADE IN “OTHER SERVICES”, 1995-2005**

(Percentages)

A) Share of Latin America and the Caribbean and its competitors in “other services”

B) Share of Latin America and the Caribbean and its competitors in communication services (5%)

C) Share of Latin America and the Caribbean and its competitors in construction services (5%)

D) Share of Latin America and the Caribbean and its competitors in computer services (8%)
Figure 6 (conclusion)

E) Share of Latin America and the Caribbean and its competitors in insurance services (5%)

F) Share of Latin America and the Caribbean and its competitors in financial services (15%)

G) Share of Latin America and the Caribbean and its competitors in licensing and royalty services (12%)

H) Share of Latin America and the Caribbean and its competitors in “other business services” (52%)


Note: Percentages in parenthesis refer to each category’s share in total “other services” trade as of 2005. “Other services” are all services except transport and travel.

Latin America and the Caribbean succeeded in maintaining their modest share of the global computer services market, which was the category that experienced the highest amount of growth over the past decade (see box 2). The relatively large volume of exports generated by Brazil, Argentina and Mexico should also be noted. When commercial performance is analysed as a percentage of overall sales, however, the leader is Uruguay, followed by Argentina.
BOX 2
LATIN AMERICAN SOFTWARE-RELATED SERVICE EXPORTS

The software-related service trade is an important component of computer and information services, and constitutes one of the most dynamic service categories. While its growth in the region has been low compared to that of India, Latin America and the Caribbean saw their share of world software sales increase from 1.9% to 2.7% between 2001 and 2005. Sales may reach 5% in a few short years. While Uruguay, Chile and Brazil are the largest producers of such services in relative terms (as a percentage of GDP), Uruguay and Argentina have produced the largest share of exports in terms of sales (see table). This is undoubtedly attributable to the fact that these two countries, together with Costa Rica, also lead the region in terms of human capital.

Software-related service sales and exports, 2004

<table>
<thead>
<tr>
<th>Country</th>
<th>Sales (millions of dollars)</th>
<th>Exports (millions of dollars)</th>
<th>Sales/GDP</th>
<th>Exports/Sales</th>
</tr>
</thead>
<tbody>
<tr>
<td>Argentina</td>
<td>1 173</td>
<td>192</td>
<td>0.77</td>
<td>16.3</td>
</tr>
<tr>
<td>Brazil</td>
<td>8 213</td>
<td>314</td>
<td>1.36</td>
<td>3.8</td>
</tr>
<tr>
<td>Chile</td>
<td>1 385</td>
<td>69</td>
<td>1.46</td>
<td>5.0</td>
</tr>
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<td>Colombia</td>
<td>340 a</td>
<td>10 b</td>
<td>0.35</td>
<td>3.0</td>
</tr>
<tr>
<td>Ecuador</td>
<td>90</td>
<td>11</td>
<td>0.28</td>
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<tr>
<td>Mexico</td>
<td>2 871</td>
<td>125</td>
<td>0.42</td>
<td>4.4</td>
</tr>
<tr>
<td>Uruguay</td>
<td>226</td>
<td>89</td>
<td>1.70</td>
<td>39.3</td>
</tr>
<tr>
<td>Total</td>
<td>14 298</td>
<td>809</td>
<td>0.85</td>
<td>5.7</td>
</tr>
</tbody>
</table>


a Does not include local service firms. Estimate based on the sales of 561 companies: 542 local software manufacturers (sales of 150 million dollars) and 19 transnationals (sales of 190 million dollars).

b Exports from 542 local software manufacturers.

Over half the region’s sales and exports proceed from the Latin American subsidiaries of only nine extraregional transnationals. These companies can be divided into three categories, depending on the type of strategy they employ. The first group of companies supplies services—particularly outsourcing—to other multinationals active in the region. The main firms in this category are EDS and Accenture, of the United States, and Tata Consultancy Services, of India. The second group is made up of equipment, software and service providers engaged in activities such as business process outsourcing (IBM, Unisys and HP). This is undoubtedly the most important group in the region in terms of sales and employment. The third group is involved in the provision of licenses, including enterprise resource planning licenses (Microsoft, Oracle and SAP).

It should be noted that, over the past few years, several computer manufacturers in the region have successfully morphed into software-related service providers. IBM in Argentina is one example of this phenomenon. In 2001, at a cost of 50 million dollars, the company transformed a printer factory into the best-equipped “technology campus” in Latin America. This transformation made IBM in Argentina a leading high-value-service supply centre, capable of competing on equal terms with centres in Brazil, China and India. Since 2002, the company has hired over 500 professionals per year for a variety of services. It currently employs 5,300 workers, and continues to expand.


Service imports in Latin America and the Caribbean grew at a higher rate than exports between 1995 and 2005, leading to an increased deficit in the balance of services. While a similar trend has been observed in ASEAN countries, the opposite is true in the other three Asian countries (see figure 7).
C. Share of imports to the United States and the European Union

Another way to compare trends in exports in the two regions is to analyse their share of service imports to the United States and the European Union. These two markets represent almost 60% of world services imports, and more detailed statistics, broken down by category and trading partner, are available for their study.

In the case of the United States, the share of services imported from the Latin American and Asian countries studied was 3% in 2005; significant differences exist, however, both between sub-categories and in terms of trends (BEA, 2007). While Latin America and the Caribbean enjoy a strong position with regard to communication, construction and, to a lesser degree, financial services, the participation of Asian countries in computer services is relatively high (see figure 8). Mexico is by far the largest Latin American exporter, followed by Brazil and the Caribbean.

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5 The bilateral service trade data of the Bureau of Economic Analysis are incomplete, as they exclude trade flows between parent companies headquartered in the United States and their branches abroad and between American subsidiaries and their foreign parent companies.
Between 1995 and 2005, exports from India and China to the United States grew more rapidly than exports from Latin America—with the exception of the Caribbean—and the ASEAN countries. This is surprising, given the proximity of Latin America to the United States. The good performance of the Caribbean is partly attributable to offshore financial centres. During the period in question, imports to the United States from India increased by a factor of 24, whereas imports from Latin America and the Caribbean merely doubled (Engman, 2006). As of 2005, Indian exports were equivalent to over half of Latin American and Caribbean exports. The share of the region—particularly Mexico—in United States service imports has, in fact, declined. When transportation and tourism are factored in, however, the volume of Latin American exports is still seven times larger than that of China and India combined.
One World Bank study (Freund, 2006) shows that India has effectively displaced the region in terms of trade in four types of services: research and development, legal services, industrial engineering and other services. The same cannot be said, however, of the other categories.\(^6\)

The share of imports to the European Union from Latin America and the Caribbean in 2005 was much lower than that of the sub-group of Asian countries. The only categories in which this percentage exceeded 1% were construction and communication services, while the share of the Asian countries studied surpassed that figure in almost every instance. It should be noted that the respective shares of China and India were larger than those of ASEAN countries. The European Union lacks detailed bilateral time-series data with which to study possible changes in the performance of both regions.

D. Regional diversity

The regional average conceals a great deal of diversity in terms of the position and trends of subregions and countries. While average service exports as a percentage of GDP amount to only 1%, their relative importance is much greater for the Caribbean, whereas Mexico saw them drop to 0.3% in 2005 (see figure 9). The dynamism of Brazil and the rest of the Southern Common Market (MERCOSUR) deserves special attention. The balance of trade in services is negative in almost every country except for Central America, Argentina, Uruguay, Paraguay and the Caribbean.\(^7\) A larger deficit does not necessarily imply weakness, however; it may suggest an increased use of external services as a means of improving the competitiveness of the rest of the economy, particularly with regard to the export of goods.

Two other indicators also display a significant degree of diversity. Firstly, the diversification of exports within the overall context of services plays an important role in evaluating the efforts of countries to penetrate other niches that hold promise in terms of learning, productivity and reducing exposure to crises in specific markets. The progress achieved by Argentina, Uruguay and the Caribbean in this regard deserves special notice. Secondly, intrasectoral trade reflects the degree to which a country participates in international networks that encourage the differentiation of services, increase productivity and generate economies of scale with regard to production. The greatest achievers in this area are Brazil and the rest of MERCOSUR, which possess the highest percentage of intrasectoral trade. While there appears to be a marked correlation between the two variables—the most diversified countries are also those which have increased their intrasectoral trade, or vice-versa—the exact causes of this phenomenon are unknown. The performance of Argentina, Brazil, the Caribbean, Costa Rica and Uruguay should be noted in this regard. Certain aspects of the Caribbean and Brazilian experience are discussed below.

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\(^6\) Another interesting finding of this study was that database and other information service exports from the United States are shifting from the region to India. This may be a cause for concern, given the intensity of intrasectoral trade in this category. The Indian computer industry requires inputs from the United States (Freund, 2006).

\(^7\) Significant contrasts exist between the islands of the Caribbean. Barbados, Saint Vincent and the Grenadines, Grenada, and Trinidad and Tobago posted surpluses in 2005, while Suriname, Antigua and Barbuda, Jamaica and the Bahamas posted deficits.
Note: “Other services” are all services except transport and travel.
a) The Caribbean (English-speaking and Dutch-speaking)

The economies with the highest relative volume of service exports in the region are those of the Caribbean (English-speaking and Dutch-speaking). On average, services represented almost two thirds —and in some cases almost 90%— of exports of goods and services from Caribbean countries between 2000 and 2005.\(^8\) Tourism accounted for two thirds of service exports —a ratio which has remained steady over the last few decades. This category is followed by transportation, with a share of between 11% and 17%.\(^9\) Business services represent around 18% of service exports, while financial and insurance services represented only 2.5%. This last category is significantly undervalued, given the exclusion of services provided by offshore companies.\(^10\)

Several economies have been able to achieve and maintain relatively high income levels and good standards of living by focusing on the export of services. Success is neither automatic nor guaranteed, however. On the contrary, it entails a long-term process of continuous learning and feedback, in which service exports generate growth, which in turn increases productivity and the diversification of service exports. This cycle of mutually reinforcing factors requires concerted action in the public and private spheres, as well as the constant renewal of competitive strategies.

While there is no direct evidence in this regard, it is safe to say that offshore services have acquired an important role in the Caribbean in recent years. Offshoring involves the incorporation of companies on the islands without any requirements as to physical presence. The success of these services, which were pioneered by the Bahamas, can be attributed to the non-existent or very low corporate taxes to which these companies are subject. Over the last few decades —particularly in the wake of the terrorist attacks in New York and Washington, D.C., on September 11, 2001— the industry has modernized its legal framework and controls, in order to avoid abuse on the part of criminals and terrorists. In addition to low taxes, the main factor encouraging businesses to form offshore centres in the Caribbean is the confidence generated by a modern, stable legal framework.\(^11\) This enables companies exporting financial and insurance services to achieve high levels of productivity and sophistication, thanks to their enhanced efficiency and ability to assume risks. In several countries, offshoring dovetails neatly with tourism, as visitors can combine recreational activities with the purchase of financial and insurance services.

It is impossible to gauge the true importance of services exported by offshore companies, since Caribbean countries do not include them in their balances of payments. These balances include only the fees companies pay governments to become incorporated on the islands. A comparison of the declared value of Caribbean exports with data on imports brought into the United States from those countries (given that the United States is their most important trading partner) suggests that Caribbean exports are undervalued by a factor of at least two.\(^12\)

Bermuda, which according to The Economist (2007) has the highest per capita income in the world, ranks at the top of the market for insurance and extraterritorial funds. Its exports seem to have been underestimated at least by a factor of 10.\(^13\) The Bahamas, which has the highest number

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\(^8\) Guyana, Suriname, and Trinidad and Tobago are exceptions, as their chief exports proceed from the energy, agricultural and mining sectors.

\(^9\) The World Travel and Tourism Council estimates that the direct and indirect contribution of tourism to the region in 2004 was equivalent to 15% of GDP and 16% of employment. In countries more focused on tourism, these percentages exceeded 80%.

\(^10\) The data contained in the Services section of the balance of payments is deficient with regard to the coverage of certain service areas. This applies to services supplied by consultants who travel to deliver services, and is especially true of business and professional services, as well as services delivered by offshore companies (CARICOM, 2004, p. 7).

\(^11\) The flip side of low taxation in fiscal paradises is the loss of tax revenue in other parts of the world.

\(^12\) In 2005, the Caribbean islands recorded service exports (excluding transportation and travel) in the amount of 1.706 billion dollars, whereas the United States declared imports in the amount of 3.5 billion dollars (IMF and Bureau of Economic Analysis).

\(^13\) Bermuda’s exports of services (other than transport and travel) totalled US$ 1.3 billion, while the United States declared imports of US$ 12.478 billion in 2004. These data suggest that actual exports must be at least 9.5 times higher than the figures declared by Bermuda (IMF and Bureau of Economic Analysis).
of ships registered and a well-established international services sector, is specializing, among other things, in managing the assets of the wealthiest people in the world. The British Virgin Islands have the highest number of registered offshore companies.

Offshore companies have become a significant source of tax revenues and foreign exchange in several countries and non-independent territories of the Caribbean. However, the available information on their contribution to the economy and to exports is still scanty. According to a study dealing specifically with the Bahamas, the offshore sector accounts for 15% of GDP, 13% of jobs and 19% of tax revenues (Bahamas Financial Services Board, 2006). In other countries, including the British Virgin Islands, Bermuda and the Cayman Islands, it is estimated that the sector accounts for an even higher share of the economy.

b) Brazil

The service sector is one of the fastest growing categories in Brazilian exports. Exports of services more than tripled between 1995 and 2005, while exports of goods rose two and a half times. In 2006, services other than transportation and travel accounted for more than half of all services (including transportation and travel), a high percentage for the region. The subcategories that grew most in recent years were professional services and execution of technical projects. These activities are related to engineering and architecture, which still rank at the top in exports of services (one third of the total) and which constitute one of the main comparative advantages of Brazil (World Bank, 2004; Bom Angelo, 2004; Valls Pereira, 2002; Moreira, Alves and Kubota, 2006).

The success of services is partly a result of high demand from exporters of manufactured goods and commodities. Financial services support the marketing firms, whose business is growing in leaps and bounds. Different banks take different approaches: Banco do Brasil (a State bank) serves medium-sized firms, while the local branches of foreign banks (ABN-AMRO, HSBC and Santander) carry out large, complex transactions for multinational corporations. IT and information services are also quite successful: Brazilian (CPM, Datasul and Microsiga) and foreign companies (EDS, IBM and TATA) follow similar strategies in providing support for multinationals within and outside Latin America. The main functions they perform are: administrative control activities, payroll management, help-desk services and call centres. Although the growth of these sectors is higher than the average growth of exports, it is small in comparison with countries like India (Mantega, 2005).

E. The trans-Latins

To complete the analysis of exports by firms located in Latin America and the Caribbean, the preceding analysis of cross-border trade needs to be supplemented with an assessment of the volume of sales by branches set up by these companies in other countries. As noted above, around half of the world’s trade in services is accounted for by sales of branches located in foreign markets (mode 3).

Although data are still scarce, some partial figures and qualitative information suggest that over the past few years, there has been an increase in the presence in foreign markets of several Latin American multinational corporations (trans-Latins). The data on sales of Latin American transnationals are incomplete, among other things because in many cases sales by subsidiaries are not published separately. Also, many subsidiaries are relatively small and are therefore not included in classifications of large corporations. For example, in its 2004 and 2005 rankings of

14 There are several sources of partial information on foreign sales by branches in Latin America and the Caribbean and in developing countries in general: (i) some databases such as the Country Reports published by UNCTAD in its World Investment Directory and the Investment Map (based mainly on Who Owns Whom, by Dun and Bradstreet, London) published by the UNCTAD/WTO
the 500 largest corporations (branches) in Latin America by volume of sales, América Economía only included two branches of one trans-Latin outside its country of origin, namely, Empresa Brasileira de Telecomunicações (EMBRATEL) and Claro de Brasil, which belong to the Mexican firm América Móvil.

Sales of services abroad by the trans-Latins may be approximated by looking at their levels of foreign direct investment (FDI) (see box 3). The data on Brazil, Chile and Colombia show that in the last few years, services accounted for at least half of outward FDI. Service sector investment abroad grew significantly, especially in engineering and construction, telecommunications and finance, as well as transport, retailing and electricity. Except in the case of the first segment, this is a fairly recent phenomenon.

**BOX 3**

**TRANS-LATINS IN THE SERVICES SECTOR: AN OVERVIEW OF PARTIAL DATA**

The partial data that are available on outward FDI from Brazil, Chile and Colombia show that services accounted for at least half of such investment during the period studied. In Brazil, services accounted for between half and two thirds of investment abroad between 2001 and 2005 (other than investment in tax havens). The main subsectors are trade (50%), construction (25%), transportation, telecommunications and real estate (which make up the remainder). In Colombia, almost half of investment abroad in 2005 was in services. Within this sector, the main subsectors were business services (40%), transportation, storage and telecommunications (31%), public services (12%) and trade (11%). In Chile, three quarters of investments between 1990 and 2006 were in the services sector, mainly in energy, trade and financial services.

The location of the main branches of the trans-Latins gives a general idea of their geographical strategy. UNCTAD data for 2002 suggest that branches of trans-Latins are set up in a number of different countries or regions (see table below). In the case of Argentina and Chile, other countries in the region are the main destinations; for other countries, the preferred destination is the United States. There has been very little development in Asia; Panama has the greatest geographic diversification.

**LOCATION OF THE 50 MAIN BRANCHES OF TRANS-LATINS IN THE SERVICES SECTOR, 2002**

<table>
<thead>
<tr>
<th>Investor</th>
<th>Argentina</th>
<th>Brazil</th>
<th>Chile</th>
<th>Colombia</th>
<th>Mexico</th>
<th>Panama</th>
<th>Venezuela (Bol. Rep. of)</th>
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</thead>
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<td>Latin America</td>
<td>70</td>
<td>6</td>
<td>81</td>
<td>21</td>
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<td>74</td>
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<td><strong>100</strong></td>
<td><strong>100</strong></td>
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<td><strong>100</strong></td>
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</tbody>
</table>


International Trade Centre; (ii) América Economía magazine, which every year publishes a database showing the characteristics (including sales) of the 500 largest companies in the region, including several in the business services sector (the main findings of this database are reported every year in Foreign Investment in Latin America and the Caribbean, published by ECLAC), and (iii) data on FDI abroad. Only a few countries in the region, including Brazil, Chile and Colombia, publish sectoral breakdowns of these data. Considerable caution must be exercised in comparing these data, given the multiplicity of sources and the different accounting methods used. Indeed, the main purpose of this discussion is to illustrate trends rather than make assertions about absolute levels.

These three countries, along with Argentina, Mexico and Panama, are the largest investors in the region in absolute terms. In relative terms, the countries with the highest levels of FDI abroad in terms of GDP are Panama, Chile, Argentina, Brazil and the Bolivarian Republic of Venezuela (UNCTAD, 2007).

The growth of trans-Latins in other services sectors, including transport, distribution and electricity, is also noteworthy. In electricity, Chilean companies were the pioneers. From 1992 to 1999 they gained presence in several countries in the region. However, in 1999 they were absorbed by ENDESA from Spain. Another example is the company ISA of Colombia, which spread to the other members of the Andean Community and bought Sao Paulo’s communications company in 2006. In retail trade, the Chilean group Cencosud pioneered with several projects of its own. In 2003, it acquired part of the Latin American assets of Royal Ahold. Other Chilean examples include the department stores Falabella and Ripley, which expanded to several Latin American countries. In air transport, LAN Chile is also expanding rapidly its operations to various of its neighbors.
Engineering and construction

Engineering and construction companies, mostly from Brazil, Mexico and Argentina, already started their internationalization process in the late eighties, due to a decline in (public) infrastructure projects in their home markets. The competitive advantages of these companies include their technological capacity, operational flexibility and low costs. Their ability to operate in complex environments characterized by stringent regulations, legal and economic constraints and uncertainties has given them an advantage over many competitors, especially in developing countries.\textsuperscript{17} Two Brazilian companies (i.e. Odebrecht and Andrade Gutiérrez) are among the 100 largest international contractors. These are followed by Techint and Impsa from Argentina and ICA from Mexico. Techint is a key player in oil and gas pipeline construction world wide. According to (incomplete) data of Investmentmap,\textsuperscript{18} most foreign affiliates already existed before 2000 (26 out of a total of 29). Brazil is the dominant country, both in sales and amount of employees abroad (Table 2).

\begin{table}[h]
\centering
\begin{tabular}{|l|c|c|c|c|c|c|c|}
\hline
\textbf{Country} & \textbf{Number of trans-latins} & \textbf{Sales (million US$)} & \textbf{Employees (number)} & \textbf{Established after 2000} \\
& & \textbf{Value} & \textbf{Reporters} & \textbf{Number} & \textbf{Reporters} & \\
\hline
Brazil & 8 & 12 & 2,344 & 8 & 41,227 & 8 & \\
Mexico & 6 & 9 & 1,299 & 4 & 3,334 & 5 & 1 & \\
Colombia & 2 & 2 & 306 & 1 & 890 & 2 & 1 & \\
Panama & 4 & 4 & 316 & 1 & 120 & 1 & \\
Chile & 3 & 3 & 193 & 2 & 530 & 3 & 1 & \\
Total & 29 & 19 & 22 & 3 & \\
\hline
\end{tabular}
\caption{TRANSLATINS IN ENGINEERING AND CONSTRUCTION IN DEVELOPING COUNTRIES, 2004}
\end{table}

Source: International Trade Centre, Investmentmap.

Telecommunications

The internationalization of some national telecom companies occurred after structural reforms (privatizations, deregulation and market opening) at the end of the eighties and nineties. When they had consolidated their position in local markets, some companies saw the expansion in the region as an opportunity for growth, illustrated by the increase of mobile phone users from 3.5 to 177 million between 1995 and 2004. Subsequently, several companies merged or were bought by others. By the early 2000s, Latin America was dominated by mainly two companies: Telefonica (Spain) and America Movil/Telmex (Mexico).

América Móvil and Telmex (Grupo Carso) are among the largest corporations in the region and part of the five largest telecom companies worldwide in terms of subscribers. Their overseas activities started in 1990 with the privatization of Teléfonos de México (TELMEX). The Mexican Government’s intention was to sell a vertically integrated corporation to create a “national champion” able to compete with foreign firms (see Box 1).\textsuperscript{19}

\footnotesize
\textsuperscript{17} For more information on trans-Latins, see ECLAC (2006 and 2007). Other successful trans-Latins operate in retail and air transport services, see ECLAC (2006).

\textsuperscript{18} The data reported by this source are incomplete and should therefore be interpreted with great caution. For example, data on Argentina are largely missing.

\textsuperscript{19} After consolidating the position in their home market, TELMEX started its foreign operations in the United States in alliance with Sprint in 1995. However, as this experience turned out difficult and another endeavor in Guatemala more successful, the company decided to concentrate its expansion on the mobile phone market in Latin America. For this purpose, it created América Movil in September 2000 and set up business in Brazil, Colombia, then expanded to Argentina and Central America (El Salvador, Guatemala, Nicaragua and Honduras) and more recently to Chile, Paraguay and Peru. In less than five years, America Movil became a major company, sharing regional leadership with Telefónica. With excellent results in the mobile phone business, TELMEX entered the market of the fixed-lines, long-distance calls and data transmission in several Latin American countries through acquisitions of several companies. By 2007, America Movil had operations in 16 countries, including the United States, with 137 million mobile customers and 3.8 million fixed lines in Central America. One of their technological advantages has been the construction of a homogeneous wireless net with GMS technology, which gave them an advantage over their rivals in the region (CEPAL, 2006 and company websites).
**Financial services**

Foreign presence in financial services in South America has been dominated by banks outside the region, whereas in Central America Panamanian banks were very active until recently. In South America, inward foreign direct investment in financial services has been dominated by extraregional banks, mostly from Spain and the United States. However, recently the Brazilian Bank Itaú purchased assets from Bank of America in Brazil, Chile and Uruguay. With this acquisition Itaú, already present in Argentina, strengthened its regional presence. In Central America, on the contrary, translatin banks lost presence. Through its purchase of Banistmo (Panama), HSBC (United Kingdom) acquired positions in Colombia, Costa Rica, El Salvador, Honduras, Nicaragua and Panama and the United States. At the same time, Citigroup took control of Grupo Financiero Uno (El Salvador) and Grupo Cuscatlán (Panama). Along with the purchase of the Central American operations of Lloyds TSB (United Kingdom) in 2004, Citigroup now is also present in Costa Rica, Guatemala, Honduras Nicaragua and Panama. Finally, some Mexican banks are also expanding to the United States to serve the Hispanic community. For example, Banorte (Mexico) bought a majority share in bank INB and acquired the money transfers company UniTeller.
II. Factors Determining Performance Abroad

A. What are they?

Several recent empirical studies suggest that performance in export of services depends on several factors.\(^{20}\) The first one consists of the classic gravitational variables, such as size of markets of origin and destination, distance or proximity of markets and the effects of clustering. The second are the so-called natural barriers (differences in language, culture or institutions). Third, the rise of information and communications technologies (ICT), a key factor because it helps determine whether a service is tradable and at what cost, partly cancelling out the repercussions of distance in trade. The fourth factor is the presence, cost and productivity of skilled labour, bearing in mind that many services are labour-intensive. These last two factors have a considerable influence on operational risks (capacity to provide a steady supply of high-quality services) and structural risks (probability of customer relations not living up to expectations) (Aron and Singh, 2005). Finally, it is also important to bear in mind the

\(^{20}\) Dihel, Eschenbach and Shepherd (2006), Kox and Nordas (2007), Markusen and Strand (2007) and Piña (2005). These recent studies were undertaken with available data on bilateral trade in European Union countries and then extended to all OECD countries (Kox and Nordas, 2007). A standard model found in the literature was used, namely, a gravitational model which includes several indicators of regulation developed by OECD on the basis of the methodology used by the Australian Productivity Commission (Golub, 2003; Dihel and Shepherd, 2005) with respect to services in general and other business services and indicators developed by the International Monetary Fund and the World Bank for financial services. For a business point of view concerning the key factors for success in exporting services (e.g., subcontracting and purchase of services abroad), see Aron and Singh (2005).
impact of the regulatory systems in the different countries, including intellectual property regimes and legislation on migration.

To allow for a better understanding of the differences in the performance of Asia and of Latin America and the Caribbean with respect to the export of services, this analysis focuses on three issues: regulation, human capital and ICT.

B. Impact of regulation on trade and investment

National regulatory systems affect at least three dimensions of international trade in services (Kox and Nordas, 2007). The first has to do with the ability to engage in trade. On this point, regulation itself and the differences between regulatory systems in different countries represent a barrier or a fixed cost for trade that affects not so much the price of services provided as the level of exports needed to begin operations, and this in turn determines the average size of the export firm (Melitz, 2003). The second is the direct impact of regulations on the volume of flows of trade in services, and the third has to do with the repercussions of regulatory schemes on flows of foreign direct investment in the services sector.

1. Impact on the ability to engage in trade

Econometric models confirm that regulatory intensity has a negative impact on the ability to start operations in trade in services. This result underlines the critical role that domestic regulatory reform plays in initiating and developing services exports. In particular, countries must improve the regulatory environment, including the role of regulatory authorities. However, the differences between regulatory systems in different countries do not seem to affect the potential for trading in services. The size of the importing market is also important. Hence, service companies in countries with little domestic regulation and large trading partners will have a greater likelihood of becoming exporters.

2. Impact on Trade Flows

As regards the volume of trade flows, the evidence shows that business services are much more sensitive to regulatory restrictions than services in general. This sensitivity is higher in the exporting country. While a more stringent regulatory context in the exporting country has a negative impact on trade, the regulatory intensity in the importing country does not seem to have a significant impact. The diversity of regulatory systems between countries also has a marked negative impact on flows of trade. Accordingly, policies designed to encourage regulatory cooperation among trading partners could be key to increasing bilateral trade in services. In fact, there are different means that could be explored. One of them is the convergence or harmonization of regulatory schemes. Harmonization can be achieved through negotiations or adoption of

\[\text{\ref{21}}\]

The purpose of regulation is to correct market failures that lead to an inefficient allocation of services. These failures occur more frequently in the services sector because of its innate characteristics. Depending on their intensity and heterogeneity, regulations — although legitimate — can considerably restrict international trade in services by preventing one market from taking advantage of the economies of scale achieved in another.

\[\text{\ref{22}}\]

In this case, the model used was a Probit model based on regulation indexes and the existence of trade in services between countries.

\[\text{\ref{23}}\]

In this case, a Probit model based on indices of regulation and the existence of bilateral trade in services between countries was used. As suggested by gravitational models, the impact of regulation is greater in trade in services than in trade in goods. With regard to the other determining factors, the models suggest that trade in services depends on the same variables as trade in goods, although there are differences in the relative importance of each variable in trade flows. While cultural differences have a greater impact on trade in services, geographic variables have a greater impact on trade in goods. In addition, the quality of regulation and the efficiency of governments are much more important in the case of trade in services.

\[\text{\ref{24}}\]

In this case, a Poisson gravitational model of maximum verisimilitude was developed.

\[\text{\ref{25}}\]

For example, the document shows that the adoption of a fully harmonized system would bring about a 60% increase in trade in services with respect to 2003. Although this exercise tends to magnify the impact, it is nevertheless relevant.
international standards and regulation, when these are available. If harmonization is not possible or feasible, mutual recognition of regulations and regulatory frameworks is an efficient alternative countries could explore. This recognition could be achieved through negotiations or accorded autonomously. In practice, a combination of harmonization and mutual recognition will allow countries to narrow the difference in regulatory framework and the possibility to reach agreements will depend on the regulatory differences (Mattoo & Fink, 2002).

The differences in the incidence of the regulatory framework between Latin America and the Caribbean and Asia are not big enough to explain the differences in performance of exports (see table 3). Aggregate indices of regulation of different service sectors are consistently lower in the region than in Asia. However, as indicated in the preceding section, the dynamism of the Asian countries, especially China and India, in exports of services is much greater. This would appear to indicate the existence of other factors that affect this type of trade, including the availability of qualified personnel and of information and communications technologies (ICT).

3. Impact on foreign direct investment

The regulatory system not only affects cross-border trade in services, it also affects exports of services through the direct sales of branches abroad. Given the lack of data, the volume of such trade is estimated on the basis of flows of foreign direct investment. As shown in the study of OECD countries by Kox and Nordas (2007), regulation affects both the inflow of investment to the services sector in the receiving country and the country’s outward investment. Indeed, except for legal barriers, regulatory restrictions have a greater impact on investment abroad than on foreign direct investment received. As far as the other variables are concerned, there is a positive correlation between market size and FDI within the country and abroad.
**TABLE 3**

**AGGREGATE INDEX OF REGULATORY INTENSITY**

<table>
<thead>
<tr>
<th>Sector</th>
<th>Banking</th>
<th>Insurance</th>
<th>Fixed Telephone</th>
<th>Mobile Telephone</th>
<th>Engineering</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Latin America</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Argentina</td>
<td>0.76</td>
<td>0.86</td>
<td>0.28</td>
<td>0.35</td>
<td>0.51</td>
</tr>
<tr>
<td>Bolivia</td>
<td>0.88</td>
<td>1.41</td>
<td>1.36</td>
<td>0.89</td>
<td>N/A</td>
</tr>
<tr>
<td>Brazil</td>
<td>1.09</td>
<td>1.36</td>
<td>0.4</td>
<td>0.94</td>
<td>1.42</td>
</tr>
<tr>
<td>Chile</td>
<td>0.85</td>
<td>0.85</td>
<td>0.37</td>
<td>0.36</td>
<td>1.04</td>
</tr>
<tr>
<td>Colombia</td>
<td>1.44</td>
<td>0.90</td>
<td>1.19</td>
<td>0.50</td>
<td>N/A</td>
</tr>
<tr>
<td>Ecuador</td>
<td>0.66</td>
<td>1.62</td>
<td>1.38</td>
<td>0.64</td>
<td>N/A</td>
</tr>
<tr>
<td>Peru</td>
<td>0.61</td>
<td>0.61</td>
<td>0.34</td>
<td>0.17</td>
<td>N/A</td>
</tr>
<tr>
<td>Uruguay</td>
<td>0.46</td>
<td>1.24</td>
<td>1.30</td>
<td>0.15</td>
<td>N/A</td>
</tr>
<tr>
<td>Venezuela (Bolivarian Republic of)</td>
<td>1.36</td>
<td>1.26</td>
<td>0.40</td>
<td>0.81</td>
<td>N/A</td>
</tr>
<tr>
<td>Average</td>
<td>0.90</td>
<td>1.12</td>
<td>0.78</td>
<td>0.53</td>
<td>0.99</td>
</tr>
<tr>
<td><strong>Asia</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>China</td>
<td>1.73</td>
<td>1.95</td>
<td>1.66</td>
<td>2.01</td>
<td>1.71</td>
</tr>
<tr>
<td>Philippines</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>0.73</td>
</tr>
<tr>
<td>Hong Kong SAR (China)</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>India</td>
<td>2.11</td>
<td>2.81</td>
<td>1.41</td>
<td>2.00</td>
<td>N/A</td>
</tr>
<tr>
<td>Indonesia</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>1.57</td>
</tr>
<tr>
<td>Malaysia</td>
<td>2.6</td>
<td>2.48</td>
<td>1.22</td>
<td>1.86</td>
<td>2.01</td>
</tr>
<tr>
<td>Singapore</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>0.56</td>
</tr>
<tr>
<td>Thailand</td>
<td>1.46</td>
<td>1.78</td>
<td>1.63</td>
<td>2.50</td>
<td>1.39</td>
</tr>
<tr>
<td>Average</td>
<td>1.97</td>
<td>2.25</td>
<td>1.48</td>
<td>2.09</td>
<td>1.33</td>
</tr>
</tbody>
</table>


*This index was constructed on the basis of weighted aggregation using a method of factorial analysis of qualitative indicators taken from surveys of different governments conducted by the Organisation for Economic Co-operation and Development (OECD) (Regulatory Indicators Questionnaire). This indicator increases in intensity, where 0 corresponds to a hypothetical country that is completely liberalized, i.e., it replies 0 to all questions on the questionnaire. Regional aggregation is obtained by calculating the simple average of countries in which information on foreign direct investment is available.*

Given the lack of data on foreign direct investment by sector, it is only possible to illustrate the hypotheses on incoming FDI in Latin America and Asia, which seem to confirm the overall results for OECD countries (see figure 10). The fact that there are fewer restrictions on foreign direct investment (mode 3) in Latin America than in Asia was reflected in larger flows of foreign direct investment with respect to GDP during the period 1995-2004 in almost every sector of financial services, telecommunications and construction. These flows to Latin America also reflect, to a large extent, the greater role played by privatization of state enterprises in those sectors in the region, especially during the 1990s.

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26 Unlike other regions, Asia managed to attract more investment in “other services” in business, for which there is no indicator of regulatory intensity.
FIGURE 10
FOREIGN DIRECT INVESTMENT AND REGULATION IN LATIN AMERICA AND ASIA, 2004

![Graph showing foreign direct investment and regulatory intensity in Latin America and Asia, 2004.](image)


a The FDI pool represents the cumulative flows between 1995 and 2004 as a percentage of GDP in 2004.

4. Other factors: human capital and information and communications technologies

Other fundamental factors in trade in services are the quality and cost of human capital and information and communications technologies (ICT). Several private consulting firms produce annual and biannual reports measuring the competitive level of a group of advanced and emerging countries for the purpose of hiring or establishing offshoring, nearshoring or outsourcing services.27 The measurements shown in these specific reports are more useful than general indicators for measuring true competitiveness, especially that of the large countries. For example, even though at the national level China and India are behind the Latin American average with respect to the penetration of ICT and levels of human capital, the consultancies always classify them as being more competitive than the countries in the region. In fact, the national averages may mask a considerable degree of heterogeneity within a given country. Although India is still a poor country in general terms, it has managed to attract a significant share of world trade in terms of outsourcing and subcontracting abroad for information technology (IT) services, thanks to the advanced development of certain cities and regions.

In this context, the competitiveness of different countries was assessed on the basis of indicators provided in the Global Services Location Index 2007 (GSLI) by AT Kearney and of qualitative information. The Global Services Location Index consists of three categories and 13 subindexes: costs (labour, infrastructure, and taxes and regulation), business environment (country risk, quality of infrastructure, cultural adaptability and security of intellectual property) and human capital (availability of labour, training and language, experience/skills in negotiation processes and retention of employees). The final index is a weighting of the three subcategories. The type of indexes considered and the weighting were arrived at after multiple interviews with major

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27 These include CIO (2006), AT Kearney (2007a) and Diamond Cluster (2006).
stakeholders in the offshoring industry and in outsourcing. The indicators are “objectives” and are comparable between countries. The information is taken from different sources and hence was not obtained from surveys.

The countries that stand out most in the classification are India and China, while the others are similar to each other (see figure 11). Each country has certain advantages that make it interesting as a destination for investment and trade. The classifications used by other consultancies also show India and China in first and second place, but the order of the Latin American countries and ASEAN countries varies from one ranking to another because they are relatively close to each other. Both groups of countries are mixed in the final classification. Thus, some Latin American countries are ranked higher than Singapore, which has a better business environment but very high costs.

**Figure 11**

**ATTRACTIVENESS OF COUNTRIES FOR LOCATION AND EXPORT OF SERVICES IN 2007**


ARG = Argentina  
BRA = Brazil  
CHL = Chile  
CHN = China  
CRI = Costa Rica  
IDN = Indonesia  
IND = India  
MEX = Mexico  
MYS = Malaysia  
PHL = Philippines  
PAN = Panama  
SGP = Singapore  
THA = Thailand  
URY = Uruguay  
VNM = Viet Nam
Human Capital

The greatest competitive advantage that India and China have over Latin America and the Caribbean and the ASEAN countries is the large number of highly skilled workers who receive very competitive wages, despite the fact that the general population has a lower level of schooling than the average in Latin America. China and India have a huge economic critical mass which enables them to create niches of excellence despite their poverty levels. Several excellent universities and technology institutes have been set up in India which turn out some 200,000 graduates per year, including 75,000 information technology engineers. China is in a similar position, with some 50,000 IT graduates per year. India has the additional advantage of a common language with the United States, its main trading partner, and this has contributed to the establishment of a large number of call centres.

Although in general terms, Latin America and the Caribbean do not match the number of university and IT graduates in India and China, some centres of excellence have been created, especially in the major cities. As a result, the services industry in those countries has grown considerably. Brazil, for example, has 15,000 IT graduates per year (CIO, 2006). In addition to having gained experience in the domestic market, the region’s service industry has a highly qualified work force that could increase exports. According to AT Kearney (2007b), among the eight Latin American countries that are most attractive to international business in the remote services sector, the availability of skilled labour is adequate in Argentina, Brazil and Mexico; intermediate in Chile and Costa Rica; and is inadequate in Colombia. In terms of language skills, while some countries such as Argentina, Costa Rica and Mexico have a significant number of bilingual people (Spanish-English) who can serve the United States market, language skills are scarce in other countries including Brazil, Chile and Colombia. The governments of these and other countries are paying more attention to the teaching of English. Spanish is also becoming increasingly important in cross-border services with the United States, given the growing Spanish-speaking population of that country. Mathematics is another important skill for trade in services, but in that regard, the region is way behind the Asian countries. In fact, the results of standardized mathematics tests (Trends in International Mathematics and Science Study (TIMSS 2003) and OECD Programme for International Student Assessment (PISA)) that were administered in several countries showed that Asian students (especially in Singapore, Republic of Korea, Hong Kong SAR (China) and Malaysia) scored higher than students in Argentina, Chile and Brazil.

Another problem that arises in competing with the Asian countries is the wage level, although worker productivity must also be considered. For example, wages for IT programmers or call centre operators in India and the Philippines range between one third and one half the average of the top eight Latin American countries. Taking into account differences in productivity and nominal exchange rates, Argentina and Uruguay are the most competitive countries in the region and can compete with India in certain services. Considering that wages in India are rising by two digits per year (15% in 2006), Latin America is becoming a more appealing destination, as shown by the investments made in the region by Indian companies such as TATA.

Access and quality of information and communications technologies

Other variables that affect the performance of exporters of services are the quality and cost of telecommunications, internet access and other information technologies. A study by Freund and Weinhold (2002) showed that improving Internet access can enable a trading partner of the United States to increase its exports of services to the United States market by 1.7%. Different classifications suggest that the quality of infrastructure in Latin America and Asia is similar, but

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28 Buenos Aires and Córdoba in Argentina; Rio de Janeiro, São Paulo and other cities in southern Brazil; Santiago in Chile; Bogotá in Colombia; San José in Costa Rica; and Ciudad Juárez, Mexico City, Monterrey and Tijuana in Mexico, among others (AT Kearney, 2007b).
costs are somewhat higher in the Latin American countries. Within the region, Chile stands out for the quality of its infrastructure and Argentina for its low costs in 2007.

One factor that has had a negative effect on the cost of access to information and communications technologies (ICT) in Latin America and the Caribbean is the fact that, unlike Asia, only a few countries (Costa Rica, El Salvador, Guatemala, Nicaragua, Panama and the Dominican Republic) have signed the WTO Information Technology Agreement (ITA). The 70 countries that signed the Agreement in 2007 account for 97% of world trade in IT products. These countries have undertaken to import those products duty free on the basis of most-favoured-nation treatment. However, no South American country has signed the Agreement, although some, such as Chile, apply a most-favoured-nation (MFN) zero tariff. Consequently, enterprises in several South American countries are at a disadvantage because of the added cost of acquiring foreign technologies compared with companies in the signatory countries. Brazil, for example, applies a 13% MFN tariff on ICT products in order to protect its national industry.

Another key factor in competition is the ability to guarantee high standards of quality of the services provided by means of international certification. This is essential in overcoming cultural barriers and prejudices in advanced countries regarding standards of services provided by developing countries. Quality standards for industrial products (ISO 9000) and the Capability Maturity Model (CMM) are two certifications that are fundamental. The Capability Maturity Model, which has five levels, is a model for evaluating and improving software processes. Level 5 is the highest and refers to the most important processes that must be complied with by the company concerned (Prieto, 2003).

29 Chile eliminated tariffs on all information and communications technology products after signing the free trade agreement with Canada in 1997.
IV. Promoting the Sector

In brief, although Latin America and the Caribbean have been less successful than India and China in attracting the growing international demand for services, there is a great potential for changing this trend. The region has several advantages that make it an increasingly appealing alternative for outsourcing and nearshoring: a growing contingent of skilled labour at fairly competitive wages, a sound technological infrastructure and the same culture as other Western countries. Moreover, interest in the Spanish language has increased internationally, as have the English language skills of Latin Americans. The region is geographically close to the large importers of services—the United States and Canada—and is in the same time zones. The increasing political and macroeconomic stability of most Latin American countries is another positive trend.

Although the conditions for taking better advantage of opportunities for trade in services are relatively good, the change will not be automatic and will require a considerable effort on the part of the public and private sectors, as they must continue to improve the quality of services at competitive prices. In promoting services, the focus should be on the main obstacles hindering the sector’s development. The following is a discussion of two important issues that are relevant to the preceding section: liberalization and recognition of regulatory frameworks among countries under bilateral and regional treaties, and the effort of the public and private sectors to improve the supply of skilled labour and create a legal framework that will encourage production and the use of information and communications technologies (ICT). In addition to these, there are many other ways to encourage trade in services, including by
improving access to financing, granting tax incentives, promoting innovation and improving the logistical apparatus (see ECLAC, 2003 and Prieto, 2003).

**A. Services in intra and extraregional integration**

Since the creation of the WTO in 1995, the number of regional trade agreements (RTAs) notified by members has increased dramatically, reaching 375 in October 2007, of which 194 are “active” (Figure 12).

**FIGURE 12**

REGIONAL TRADE AGREEMENTS NOTIFIED TO THE WTO: 1995-2007 (NUMBER)

![Graph showing regional trade agreements notified to the WTO: 1995-2007 (number)]

Source: Elaborated on the basis of WTO data.

Note: Data exclude 22 agreements notified under the “Enabling Clause”.

Until 1995 RTAs covered basically trade in goods, except for the EC Treaty (1958), US-Canada FTA (1989) and the Closer Economic Relation Trade Agreement between Australia and New Zealand (1989), which also included trade in services provisions. After the conclusion of Uruguay Round Negotiations and the entry into force of NAFTA in 1994, trade in services provisions have been included in 49 active agreements notified to the WTO (see table 4).32

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30 For a review of trade in services in the context of agreements signed in Latin America and the Caribbean, see Marconini (2005 and 2006), Sáez (2005) and Stephenson (2002).

31 The term RTAs is used broadly including regional agreements signed by countries in a region or subregions, plurilateral agreements signed by two or more countries and bilateral trade agreements.

32 The total number of services agreements notified to the WTO is 59.
TABLE 4

NOTIFIED AND ACTIVE TRADE AGREEMENTS: ACCUMULATED AS OF OCTOBER 2007 (NUMBER)

<table>
<thead>
<tr>
<th>TYPE OF AGREEMENTS</th>
<th>Enabling Clause</th>
<th>GATS Art. V</th>
<th>GATT Art. XXIV</th>
<th>TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
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<td><em>LACs EIA</em></td>
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<td>2</td>
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<tr>
<td>Free Trade Agreements (FTAs)</td>
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<td>Partial Scope Agreements (PSA)</td>
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<tr>
<td><em>LACs PSA</em></td>
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<td>1</td>
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<td>1</td>
<td></td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>21</strong></td>
<td><strong>49</strong></td>
<td><strong>124</strong></td>
<td><strong>194</strong></td>
</tr>
</tbody>
</table>

Source: WTO.

The economic literature has addressed extensively the theoretical and empirical economic analysis of trade agreements in goods (both free trade agreements and custom unions). But much less attention has been devoted to the economic effects of trade in services agreements. \(^{33}\) Recently, new analyses have emerged regarding the increasing number of RTAs covering trade in services disciplines and commitments. These studies focus on the relationship between RTAs and Article V of the General Agreements on Trade in Services (GATS), and their structure. They also assess to what extent RTAs have been more effective in promoting liberalisation than the WTO. \(^{34}\)

Latin America and the Caribbean have not been immune to these developments. On the contrary, the region has negotiated various trade agreements that include services provisions, although this trend is recent. In fact, Latin American countries have notified 53 agreements, of which 27 under Article XXIV of GATT (22% of total); 23 under Article V of GATS (almost half), and 3 under the Enabling Clause. \(^{35}\) Chile and Mexico have been the most active countries in the region pursuing both trade in goods free trade agreements and trade in services economic integration agreements.

Mexico was the first country of the region to negotiate liberalization of trade in services in the context of a trade agreement, namely, the North American Free Trade Agreement (NAFTA). These negotiations took a new approach to liberalization in that cross-border trade in services was separated from the sale of services through foreign direct investment (mode 3) and accordingly, the

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\(^{33}\) Mattoo & Fink (2002).


\(^{35}\) The number of agreements under the enabling clause is underestimated, for example a number of trade agreements signed under the LAIA framework are not counted in these figures.
relevant rules and disciplines were established. The General Agreement on Trade in Services (GATS) entry into force in 1995 as part of the result of the GATT’s Uruguay Round negotiations.\(^{36}\) The first generation of free trade agreements (Complementary Trade Agreements) between Latin American countries, especially in the framework of the Latin American Integration Association (LAIA), included a clause allowing further negotiations on services. However, it was not until the late 1990s that this dimension of trade began to be included in agreements in the region.

The three incentives that led to the definitive inclusion of services on the trade agenda of the region during the 1990s were the entry into force of NAFTA, GATS and the decision of the countries in the region to begin negotiations on the creation of the Free Trade Area of the Americas (FTAA); that decision was taken in April 1998. Prior to that, for almost four years, a collective analysis had been made of the implications of negotiations on services in the context of free trade agreements, and it was decided that the latter should be included in the results of negotiations on FTAA.

After Mexico, Chile was the second country of the region to actively include this dimension in its trade negotiations. Following the NAFTA model, services were included in the agreement with Canada that was signed in mid-1997.

On 11 June 1998, the Andean Community adopted Decision 439, on a General Framework of Principles and Rules and for Liberalizing Trade in Services in the Andean Community, in fulfilment of the provisions of articles 79 and 80 of the Cartagena Agreement. On 30 October 2001, the Commission of the Andean Community adopted Decision 510, which contained an inventory of measures in force at the time that restricted trade in services, and provided that such measures should be eliminated by 1 January 2006. This was achieved on 14 December 2006 with the adoption of Decision 659, on services sectors where rules would be liberalized or harmonized.\(^{37}\) The Andean Community follows a liberalization framework for the services sector which is similar to that of GATS but lays down a procedure for countries to list those measures that are incompatible with the agreed rules (negative list) and undertook to eliminate them and not to introduce new restrictions (Andean Community, 2007).

The MERCOSUR countries also followed the GATS model in liberalizing trade in services on the intraregional market, but only in the sectors specified in the schedules of commitments (positive list). The Montevideo Protocol, which lays down the regulatory framework for trade in services, was adopted in December 1997. The first commitments were annexed in July 1998, but the agreement only entered into force in December 2005, once the process of ratification by the legislatures of Member States was finalized. One of the main objectives of the Montevideo Protocol on Trade in Services in MERCOSUR is to complete, no later than ten years from the date of entry into force of the Protocol, the programme of liberalization of trade in services of MERCOSUR (article XIX). Annual negotiations are to be held to that end.

Although the Protocol entered into force in December 2005, six rounds of negotiations have been held since 1997, at which new sectors have been added to the commitments undertaken.\(^{38}\) These negotiations have made it possible to move forward in consolidating the existing restrictions,
but they have not led to any significant liberalization of the market within the free trade zone (Grupo de Servicios del MERCOSUR (no date)).

Progress has been made in the drafting of common regulatory instruments, especially those aimed at facilitating the temporary movement of persons. In particular, the Agreement on the creation of the MERCOSUR visa; the Mechanism for the exercise of temporary professional services and the Agreement on the facilitation of business activities. Ratification of these instruments by the legislatures of Member States is still pending.

In 1997, CARICOM adopted an approach to services integration that enshrined the right of establishment, namely, the right to carry out any commercial, industrial, agricultural, professional or artisanal activities and to create and administer any type of organization. This agreement also grants persons in Member States the freedom to provide services. In addition, there is a commitment not to establish new restrictions and to remove existing ones. The latter goal was to have been reached by 31 December 2005.

In negotiations conducted by the United States with Chile, Central America, Colombia and Peru, the NAFTA model was adopted, while European Union negotiations with Mexico and Chile used the GATS model, as will probably be the case with the Andean Community, Central America and MERCOSUR (Fereira Portela, 2001). One might ask how and to what extent these negotiations between certain countries of the region and the United States and Europe have progressed further than multilateral negotiations and negotiations within the region.

Marconini (2006) conducted a comparative study of the provisions of the World Trade Organization, NAFTA and the agreements recently negotiated by the United States with Latin American countries, the European Union and Japan. Both the GATS model, followed by the European Union, and NAFTA, used by the United States, are similar in scope with respect to the measures that affect services, and they make a distinction between trade in services and modes of supply. However, they differ in regard to the depth with which each of these issues is treated.

In the GATS model, the same disciplines are applicable to all the modes of supply. In the case of NAFTA, the disciplines are developed separately, with a distinction being made between those that apply to “cross-border trade” (including modes of supply 1, 2 and 4 of GATS), investment (mode 3 of GATS) and procedures applicable for access of businesspersons in the destination market (mode 4). However, this criterion has not been uniform, especially in the agreements signed by the United States subsequent to the agreements with Chile and Singapore, which contain no provisions on “businesspersons”.

According to Marconini (2006), it is not possible to determine a priori if the agreements signed by the United States, the European Union and Japan have created more liberalization than the results of WTO negotiations. In some cases, certain sectors have been excluded, such as air transport and audiovisual services, while in others the scope of application in certain areas has been limited. For example, movement of natural persons has been limited to “businesspersons”, while GATS includes all categories of service suppliers. Finally, in other cases, certain sectors or activities have been excluded by way of negotiated reservations (maritime transport and subfederal and municipal measures). Fink and Molinuevo (2007) reach similar conclusions with regard to services agreements signed by Asian countries.

In other regards, however, some agreements have gone beyond the WTO provisions, including in financial services or telecommunications and even some disciplines of the maritime transport sector (in the context of agreements negotiated by the European Union) (Pereira

39 Modes of supply are defined as: (i) cross border; (ii) consumption abroad; (iii) commercial presence; and (iv) presence of natural persons.
Gonçalves and Stephanou, 2007; Sáez, 2005b). Also, rules of origin applicable to service suppliers appear to be more flexible than those agreed in GATS.\(^\text{40}\) Furthermore, agreements negotiated by the United States and Japan in the area of investment (applicable to services established through commercial presence) include stricter disciplines in terms of performance requirements and the prohibition to establish local-presence requirements as a condition for providing a service.

One of the main elements supplementing the disciplines regulating trade in services are the schedules of commitments whereby the countries define those sectors and terms that will be subject to the provisions on trade in services. The agreements negotiated by the United States and Japan include a larger number of disciplines, follow a negative-list approach (everything is included except that which is expressly excluded), and adapt the level of commitments to the regulatory status quo (consolidation); these agreements are considered more transparent and liberalizing than the GATS model followed by the European Union. As noted above, however, the actual level of liberalization is determined by the content of the schedules of commitment. In WTO, in the subregional agreements like NAFTA, and in the aforementioned bilateral agreements, liberalization has been approached from a standpoint that has simply maintained the prevailing regulatory situation without achieving true liberalization of trade in services (Marconini, 2006; Sáez, 2005b). This has also been the objective achieved in the case of MERCOSUR, whereas the Andean Community has tried to freeze the current situation, assuming a commitment to liberalization supplemented by specific disciplines in certain sectors. Since this is a very recent development, it is difficult to assess its effects.\(^\text{41}\)

Marconini (2006) discusses four aspects of the provisions on domestic regulation that are applicable to trade in services: transparency, good governance, requirements and recognition. The agreements negotiated by the United States and Japan seem to move towards transparency and good governance, as they establish requirements relating to the drafting and the procedure for adopting and applying rules, issues which are not addressed in the agreements signed by the European Union. As Sáez (2005) points out, however, none of the agreements show progress specifically in terms of reducing the costs involved in rules and regulations that service suppliers must comply with in order to be able to carry out their activities. Nor do they clarify the conditions under which domestic regulations might be considered “unnecessary barriers to trade”, an issue that is at the centre of the debate on trade in services and trade agreements.

The difficulties involved in addressing liberalization of trade in services are closely related to the regulatory changes that must be made, economic policy and the practical implications for managing economic and development policies (Marconini, 2006; Sáez, 2005). It is therefore advisable to keep open the possibility of creating new regulations should the existing ones prove inadequate and provided they are not challenged under the dispute settlement system as being contrary to the commitments assumed or as being unnecessary barriers to trade. Another aspect that should be considered is the degree to which the desired policies are aimed at discriminating against foreign suppliers or to give the State an advantage as a service provider. Consequently, the most direct repercussions may be seen in the type of policy instruments applied and their effect (discrimination in favour of national suppliers) and the degree of State participation in the provision of services, either as a regulator or as a direct supplier (Sáez, 2005).

Both GATS and the aforementioned agreements, including those negotiated by the United States, contain a number of mechanisms that enable countries to define a priori the policy options they wish to keep open. In other words, sovereign decisions concerning policies and instruments are preserved, and the sectors affected, including the type of State participation in the activity, are

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\(^{40}\) Although these might be relevant only for those countries that are not members of GATS, given that the most-favoured-nation clause requires all WTO members to receive equal treatment.

\(^{41}\) For an analysis of the situation of trade agreements signed in Asia see Fink & Molinuevo (2007).
policy decisions that can be adequately addressed in the context of international negotiations. What is important is that governments should be able to clearly identify their policy objectives and the tools to be used in achieving them.

B. Human capital, technology and quality

Other areas in which exports can be promoted are the training of skilled workers and the creation of an environment in which investment and information technologies are encouraged. Cooperation between the public and private sectors is key to identifying problems and formulating policy proposals.

1. Human capital

The improvement of human capital, a key factor in India’s success, is probably the most important challenge facing Latin America and the Caribbean. Priority should be assigned to three areas. In the first place, since many services require highly skilled personnel, the public and private sectors should offer incentives for university-level ICT programmes, as well as training programmes, especially for small and medium-sized enterprises. Furthermore, governments should ensure the quality of technical education by requiring accreditation at regular intervals. And finally, citizens should be encouraged to learn English, the main language of international trade, and the teaching of mathematics and information technologies in secondary schools should be improved.

2. Development of (information) technology and certification

An important step in promoting access to modern (information) technologies —including in the telecommunications sector— is to improve regulatory policies and competition so as to encourage investment and guarantee high-quality services at the lowest possible cost. The increased availability of broadband internet connections facilitates the sale of more complex electronic services at the international level. Broadband goes a long way towards promoting competitiveness and productivity. Public policies should encourage both the supply of and the demand for broadband, with special emphasis on small and medium-sized enterprises (Ueki, Tsuji and Cárcamo, 2005). This can be done by eliminating or reducing import taxes and value added taxes on IT equipment and related services. Another key measure will be to encourage (micro) entrepreneurs to use ICT by stepping up the development of e-government in the areas of registration and transactions with the business sector. Also, governments should strengthen programmes aimed at raising awareness and training businesses in ICT-related subjects and demonstrating the potential of ICTs for promoting innovation and competitiveness. It must be pointed out, however, that ICTs should not be considered a goal in themselves but rather a means of improving efficiency.

Exports of services can also be encouraged by promoting different types of certification, including quality standards for industrial products (ISO 9000). Such certification —which applies to the processes by which services are provided— enhances quality and international credibility. However, considerable resources are needed in order to obtain and maintain certification. Governments and trade organizations in the private sector have an important role to play in encouraging certification. Governments could set priorities for certain types of certification, maintain their requirements and prevent them from becoming a barrier to trade. Certification should be voluntary and only for a limited time. Private trade associations could carry out special activities for certifying the quality of different services and help entrepreneurs comply with the international quality standards that are applied to management techniques, rationalization of costs and quality control.
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United Nations publication, Sales No. E.04.II.D.36


Annexes
### Annex 1

**TABLE A.1**

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<td>Operating leasing services</td>
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<td>Transportation</td>
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<tr>
<td>Travel (including tourism)</td>
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<td>Personal, cultural and recreational services</td>
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FIGURE A.1
THE FOUR MODES OF SUPPLY FOR SERVICES IN INTERNATIONAL TRADE

Mode 1: Cross-border supply

Mode 2: Consumption abroad

Mode 3: Commercial presence

Mode 4: Presence of natural persons

Source: Economic Commission for Latin America and the Caribbean (ECLAC), based on information from the Organisation for Economic Co-operation and Development (OCDE).
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