



PACT EAC PROJECT

Promoting Agriculture, Climate and Trade linkages
in the East African Community



Promoting **Trade in Services:** Analysing Potential Sectors in the EAC

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Introduction

With the world's growth and development, the importance of services as a share of overall production and employment is increasing quickly. The EAC is no exception: for the past years, trade in services of the region has witnessed increasing importance. Both intra-EAC trade and international trade in services are contributing to the expansion of the region's economies, as well as improvement of the populations' well-being.

Enhancing trade in services exports in the EAC has great potential to further benefit the region. The purpose of this paper is to thus identify the current opportunities and challenges for the EAC to develop their exports in services, and to provide an insight of the service sectors that could be of top interest to the respective EAC member countries.

The paper argues that as a matter of policy, the EAC should identify the services sectors in which they have a comparative advantage for purposes of promoting exports within and beyond the region. Strategies for promoting the identified sectors can then be integrated into national and regional trade development plans; the outcomes from such an exercise would also inform the regions priorities in pursuing market access through bi-lateral, regional and multilateral trade agreements.

Trade in Services

- **Background**

Trade in services under the WTO is covered by the General Agreement on Trade in Services (GATS), which classifies services in the following categories: business services, communication services, construction and related engineering

services, distribution services, education services, environmental services, financial services, health related and social services, tourism and travel related services, recreational, cultural and sporting services, transport services and others.¹ Services differ from goods in a number of ways, most commonly in the immediacy of the relationship between supplier and consumer. Many services are non-transportable; i.e. they require the physical proximity of supplier and customer, for example, the provision of a hotel service requires that the hotel is where the customer wishes to stay, a cleaning service for a business must be provided at the site of the business, and a haircut requires that both hairstylist and client be present. For international trade in such non-transportable services to take place, either the consumer must go to the supplier or the supplier must go to the consumer.²

Services play a key role to developing countries, including in quest for achieving the Millennium Development Goals such as poverty alleviation and access to basic services of health, education, etc. Thanks to its linkages with other economic activities, exports of services could greatly enhance the EACs' economic capacity and performance. For developing countries and LDCs such as the EAC member states, services trade is the new frontier for enhancing their participation in international trade and, in turn, realizing development gains.³

The GATS provides for four modes of services supply, which are illustrated below from the perspective of an "importing" country A:

- Mode 1: Cross border trade. From the territory of one Member into the territory of any other

¹ WTO, Services sectoral classification list, July 1991

² <http://stats.oecd.org/glossary/detail.asp?ID=2742>

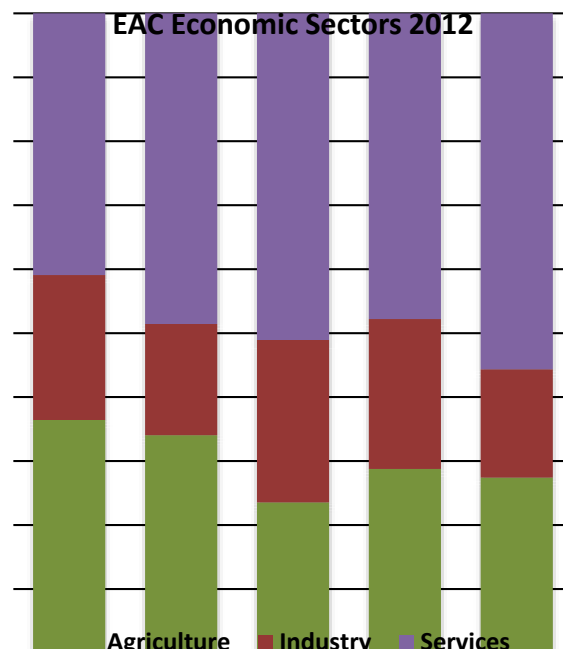
³ <http://unctad.org/en/Pages/DITC/Services/Global-importance-of-services.aspx>

Member, for instance a user in country A receives services from abroad through its telecommunications or postal infrastructure. Such supplies may include consultancy or market research reports, tele-medical advice, distance training, or architectural drawings.

- Mode 2: Consumption abroad. In the territory of one Member to the service consumer of any other Member. Nationals of A have moved abroad as tourists, students, or patients to consume the respective services.
- Mode 3: Commercial presence. By a service supplier of one Member, through commercial presence, in the territory of any other Member. The service is provided within A by a locally established affiliate, subsidiary, or representative office of a foreign-owned and — controlled company (bank, hotel group, construction company, etc.).
- Mode 4: Movement of natural persons. By a service supplier of one Member, through the presence of natural persons of a Member in the territory of any other Member, for instance a foreign national provides a service within country A as an independent supplier (e.g., consultant, health worker) or employee of a service supplier (e.g. consultancy firm, hospital, construction company).

- **Economic Context**

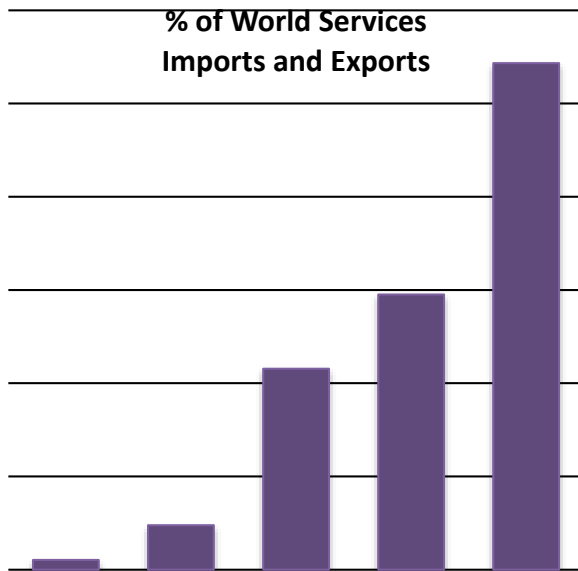
In recent years, the service sector has become more important in the economies of the EAC countries and is contributing significantly to their respective GDP. In 2012 it contributed 40% to Burundi's GDP, 45% of Rwanda's, 45.5 % of Uganda's, 44.6% of Tanzania's and 55% of Kenya's. Therefore, on average, the service sector covers nearly half of the EAC economies.



Source: UNCTADSTAT

Despite the growing importance of domestic services sector, trade in services at the international level remains quite limited. The main reason is the lack of competitiveness and also because most of services exports occurs within the EAC. In fact, without Kenya, the percentage of total world imports and exports of services varies between 0.002% (Burundi) and 0.05% (Tanzania). However, as shown in the graph below, from 1999 to 2011, the trend of the services exports by the EAC/LDCs is upward.

Irrespective of slight declines and different paces of growth among countries, the region's overall exports of services are continuously increasing in quantity. Tanzania and Uganda show steeper rising trends, while compared to them, Rwanda and Burundi didn't have as much growth in exports of services. Yet all of the four EAC-LDCs experienced expansion of their services exports.

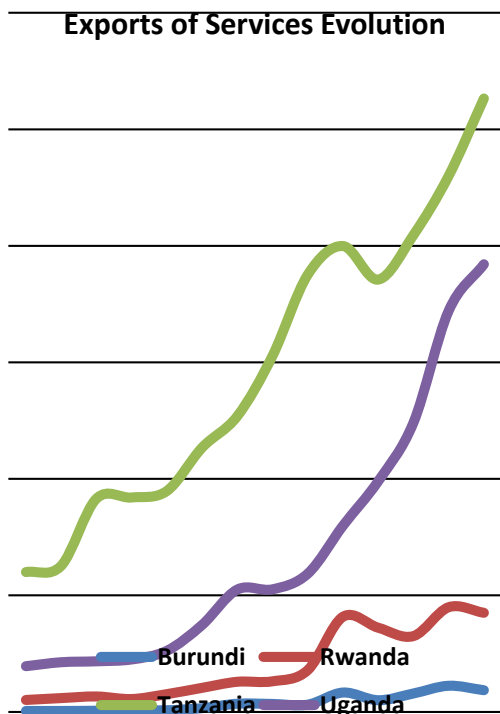


➤ Significance of trade in services important

From a broad point of view, the services sector contributes significantly to steady and healthy economic growth. The 2011 World Development Indicators show that the services sector accounted for almost 71% of global GDP in 2010. And it is expanding at a quicker rate than the agriculture and the manufacturing sectors.⁴

Development of trade in services of the EAC has great potential to benefit the region in several ways. First of all, services play a key role in enhancing the welfare of the population; they assume an important social function by directly providing access to basics. Services provisions in, for example, health, education, telecommunication and transportation directly improve people's quality of life. Services are also central in offering personal development opportunities to individuals through employment creation and better social environment.

Secondly, trade in services not only brings in more earning for the region, which contributes to the economic growth, but also promotes the upgrading of the economy. Services by their nature are more value oriented, globally, 46% of the value added that is embodied in exports is contributed by service activities. Trade in services is particularly important for maintaining the competitiveness of landlocked countries. Its development pushes an upgrade in the whole economy due to its critical inputs for other economic activities.



⁴ <http://unctad.org/en/conferences/publicsymposium/2013/Pages/importance-of-services.aspx>

Thirdly, the development of trade in services sector helps to orient the EAC's economy towards sustainable development. The increased share of services with much less carbon footprint in the economy implies that greener economy could be achieved. Furthermore, for the important economic sector of agriculture, environmental, testing and R&D services may support more sustainable agricultural practices. Compared to the manufacturing industry or extractive industry, services sector generates much less GHG such as CO₂ and SO₂, less pollutants into the water or the soil, which largely contribute to the reduction of negative impacts of human activities on the ecological world.

Fourthly, trade in services provides an alternative for diversification. The EAC's exports have long been concentrated on primary goods exports such as coffee, tea, etc. These products are less commercially meaningful compared to services provisions, and are not beneficial to a diversified economic structure. For example, equipped with rich natural endowments, the EAC/LDCs could orient their economy more to the tourism sector by enhancing the regions image as a tourist's destination. Further, with the progress in information technologies, telecommunication is also a sector that the EAC/LDCs could diversity to, through training and providing incentives for promoting virtual tele-ICT services. Reliance on agricultural exports in a sector affected by weather vagaries makes the region's economic stability unpredictable, while exports of services helps diversify the exports and decrease vulnerability and dependence on foreign financing.

Potential opportunities for the EAC's services exports

- **The WTO services waiver offered to LDCs**

At the Eighth WTO Ministerial Conference in 2011, trade ministers adopted a services waiver for the LDCs. This waiver releases developing and developed-country Members from their legal obligation to provide non-discriminatory treatment to all trading partners (under GATS Article II: Most-Favored-Nation Treatment).⁵ The waiver will last for 15 years from the date of adoption. Of the 153 WTO Members, 31 are LDCs who stand to benefit from the preferential treatment. The waiver is available to all LDCs, not only WTO members and is aimed at enhancing their international trade in services.

Given that four of the EAC member countries are LDCs, the WTO waiver creates an opportunity for them to better penetrate into the global services market, by improving their access to service distribution channels and global information networks. It would bridge the gap between LDC suppliers and the recipients in developed or developing countries, via the opportunity for preferential market access of LDC service suppliers. However this would also require the LDC to negotiate for the preferential treatment of their service suppliers in markets of their interest, as well as enhancing their capacity and efficiency in tapping such opportunities, once they arise.

⁵ http://www.wto.org/english/news_e/news11_e/serv_17dec11_e.htm

- **The EAC Common Market Protocol**

Apart from international market opportunities, advantageous policies also encourage intra-region trade in services. The EAC Common Market Protocol was signed on 20 November 2009 by the EAC Heads of State, and entered into force on 1 July 2010. It provides for the free movement of goods, persons, services and capital to be progressively implemented.⁶ Article 1 of Part F of the EAC Common Market Protocol states that:

The Partner States hereby guarantee the free movement of services supplied by nationals of Partner States and the free movement of service suppliers who are nationals of the Partner States within the Community. This means the free movement of all service suppliers in all sectors in all Partner States of the EAC.

It should be noted a great portion of trade in services is conducted within EAC. Intra-EAC trade can lead to lower prices and better services quality for consumers and create more jobs for EAC citizens. It also introduces more competition among service providers in the same sub-sector, thus increasing the overall efficiency of that sub-sector. Thus, intra-EAC policies like the EAC Common Market Protocol serve as an impetus for the regional economy to move forward in terms of efficiency and in services' quality, to be more dynamic and competitive in the international services trade.

⁶EAC, Protocol on the establishment of the East African Community Common Market, 2009

Analysis: Top Services Export Sectors of Interest to the EAC/LDCs

Taking into account the opportunities and challenges that the EAC face in terms of trade in services, it's important to identify by country their capacities and comparative advantages, as well as what regulatory and institutional measures will best support the development of their trade in services. Going by literature review, some of the potential sectors are discussed by country.

- **Tanzania**

Actually, for the whole EAC area, tourism industry is rivalled only by the agricultural sector which is the main economic backbone for most countries in the region.⁷ For Tanzania, tourism is growing in importance and ranks as the second highest foreign exchange earner after agriculture. As could be seen in the chart below, the tourism sector contributed \$1564 million to the nation's exports in 2012, which means that tourism takes up 16% of the national GDP. Compared to other sub-sectors of services, it is evident that the tourism sector represents Tanzania's comparative advantage in services. In fact, Tanzania ranked third globally in the Travel and Tourism Competitiveness Index (TTCI). This indicates that Tanzania has prevailing natural and cultural resources to be used to enhance the country's destination competitiveness. Significant linkages exist between tourism in LDCs' and poverty alleviation as well as economic development. It is worth noting that, tourism is not a single activity, but an

⁷ UNECA, Towards a Sustainable Tourism Industry in Eastern Africa- A study on challenges and opportunities for tourism development, 2011

agglomeration of many separate and related activities that include transport, accommodation, food and beverage services, cultural entertainment, conventions and trade fairs, sports and recreation.⁸ It thus could be assumed that, thanks to its linkage with other economic sectors, the development of tourism leads to the economic multiplier effects and a better overall economic growth. Moreover, Tanzanian growth in employment has so far largely come from domestically-oriented industries with the exception of tourism.⁹ This implies that tourism's function of job creation could assist with releasing the country's stress of employment. The potential of the tourism industry is big in Tanzania and needs to be explored further. Tanzanian government should clearly identify strategic development plans for the sector while implementing guidelines and policies that support and encourage its development. More capacity-building activities such as thematic workshops, training sessions should be systematically organized. The establishment of tourism schools to educate skilled workers in the industry is also a good way to enhance the competitiveness of Tanzania's tourism sector.

Financial	1	1	0	27
Computer	0	0	7	57
Royalties & license fees	0	0	0	20
Other business	1	0	303	197
Cultural and recreational	0	0	5	9

Source: IMF database

● Uganda

Uganda's service sector is one of the fastest growing sectors of the economy. In 2012, Uganda's services exports amounted to 1.9 billion USD, expressing high potential to grow and become a source of external revenue. Uganda's main services' exports sectors include travel, transport, and ICT among others. Uganda still needs to exploit the potential of these activities in order to achieve high and sustainable export growth.

Tourism is also an important services sector for Uganda given its abundant stock of natural resources; however these need to be complemented with the requisite infrastructures, technologies and information.

While transportation plays a major role in facilitating other economic activities just as the tourism sector, thus has great potential to boost the economy. As shown in the chart, transportation sector in Uganda ranks just after the tourism sector, contributing \$129 million- a substantial proportion to the services exports. The EAC countries are connected by a fairly extensive rail, road, lake, and pipeline network. Well-developed transport policies, along with modernized transportation infrastructures can reduce the costs of travelling, attract greater traffic, expand consumer choice and increase

Exports in millions of dollars – Year:2012				
Service sector	Burundi	Rwanda	Tanzania	Uganda
Transportation	3	59	632	129
Travel	1	282	1564	1084
Communications	0	16	39	23
Telecommunication	0	16	39	17
Construction	3	0	38	245
Insurance	2	1	11	28

⁸Ibid

⁹ World Bank: Tanzania's Economic Overview: Performance and Outlook, <http://www.worldbank.org/en/country/tanzania/overview>

competition. The capacity of transportation is also crucial in attracting foreign investments and in capturing more manufacturing opportunity. While inefficient transport and logistics chains act like a tax on production and undermine the ability of Uganda to compete effectively in external markets. Despite the rail, road and water connectivity in the EAC, most of these infrastructures are dilapidated leading to high cost of transportation that makes Uganda's products very expensive by the time they reach the international market.¹⁰ Therefore, if transportation infrastructures are renovated and extended, the transportation costs would be reduced and the competitiveness of the country's products could be improved. In a word, transportation plays an important role in Uganda trade in services and in creating new opportunities for the region's economic growth.

- **Rwanda**

Despite its status as a LDC, Rwanda is undergoing a high speed of economic growth. Rwanda's economy has remained on a strong growth path with real GDP growth increasing to 8.8% in 2011 from 7.6% in 2010. The rate of GDP growth in 2012 is 7%. This growth applies to the services sector which contributed 46% of GDP in 2011 and 45% in 2012.

Within the service sector, tourism is the biggest contributor as shown in the chart above. In 2011, Rwanda was qualified by WEF, World Bank and African Development Bank as one of the countries with the biggest potential in tourism. At the same time, telecommunication also plays a key role in Rwanda's trade in services. Actually Rwanda has become Africa's fastest growing telecom market, which has great potential to benefit the whole nation's economic growth. In

recent years, there is growing enthusiasm about the increasing number of mobile phones in Africa and the potential of the mobile platform in helping to address the needs of small businesses. Rwanda is no exception: the increasing adoption of information and communication technologies (ICTs) facilitates business both within and beyond the borders. Mobile commerce at large is gaining importance in many developing countries. From the perspective of small businesses, mobile solutions can be applied to facilitate money transfers as well as merchant, bill and salary payments. More sophisticated financial services, such as credit, savings and insurance schemes, are also likely to expand in the coming years.¹¹ Rwanda has enterprises such as MTN, TIGO and AIRTEL.

Rwanda's ICT sector has already surpassed other EAC countries in some ICT indicators. Especially in the case of number of Internet subscriptions per inhabitants Rwanda has become the leading EAC country. Rwanda's achievements in terms of the diffusion of ICTs have been spurred by a range of innovative 'pro-development' applications such as e-banking, e-agriculture, and e-trade from the ICT sector spread across the development agenda within agriculture, health, manufacturing, infrastructure, etc. Moreover, jobs in the ICT sector are often perceived as attractive, because of upward mobility, job security, and the availability of training opportunities.¹² The government of Rwanda could seize this opportunity to tackle the challenge of inadequate or insufficient ICT skills by training more skilled workers serving the telecommunication sector. Through Mode 1, the latter could supply and export their services to foreigners within or outside the EAC. The

¹⁰ African development Fund, East Africa Trade and Transport Facilitation Project, 2006

¹¹ UNCTAD, Mobile money for business development in the EAC, 2012

¹² UNCTAD, Services Policy Review for Rwanda, 2013

development of this sector not only directly contributes to the economic growth of the region, but also facilitates other industrial sectors' contribution, including tourism, education, financial services, etc.

- **Burundi**

Burundi's services sector has not been aggressively export-oriented, partly due to the country's poor infrastructure and low pace of technological advancement. Many firms in the sector are not competitive beyond the Burundi border. Never the less the tourism and travel sectors are promising sources of export revenue and economic growth. The adverse effects of the political tensions along with the resultant negative image the country experienced in the recent past are hindering growth in the services trade.

Challenges for the EAC to develop the exports of services

Despite the abundant potential for promoting trade in services in the EAC, the region is still faced with a number of challenges.

First, there need for requisite policies, regulations, and other institutional arrangements that would create incentives for growth and promotion of the services sector. Such regulations are important in creating an enabling environment for trade in services.

The other challenge is underdevelopment of infrastructures in the region which hampers development of the trade in services, given that

infrastructure such as roads, rail, air and others are vital for various sectors of trade in services.

Market access on the international scene is another challenge, given the less competitiveness of EAC service suppliers and barriers they are faced with in attempting to access international markets.

The third element meriting attention is the lack of systematic studies, assessment and clear plans for identifying the potential and comparative advantages in global services market. There is need for more knowledge about exporting opportunities, markets, and processes. Lack of awareness is a key factor that constrains service providers from exploiting new business opportunities beyond the borders.

Conclusion

This policy note analyzed briefly the significance of trade in services to the EAC, the opportunities and challenges to develop it, as well as the top sectors that could be of interest to the region. It should be pointed out that the WTO services waiver for the LDCs does not *oblige* members to grant preferences. Therefore, EAC/LDCs themselves should take the initiative to propose concrete demands to WTO members. To achieve this, they should firstly identify the sectors with export potential and markets of interest amongst the WTO membership. In other words, the EAC should analyze the key services to export, for example tourism, transportation and telecommunication, and to integrate the development of these economic activities into national and regional strategies.

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