Paper presented at

ADBI-PECC Conference

"Services Trade: New Approaches for the 21st Century"

China's Services Policy Reform:

pre- and post- Global Financial Crisis

Jun 1-3, 2011

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China’s Services Policy Reform:

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Abstract

Adverse effects of global financial crisis on international trade are as follows: falling demand, increased trade protectionism and drying up of trade finance. Much attention has focused on the impact of the global financial crisis on goods trade; literatures on its impact on services trade are limited, especially on China’s services trade. This paper will analyse the impact of global financial crisis on China’s services trade and discuss the policy responses taken by Chinese government and raise some policy suggestions. The main findings of the paper are as follows: Although global economic and financial crisis spawned a synchronized recession leading to a contraction in China’s services trade, global financial crisis has a moderate effect on China’s trade in services owning to lower internationalisation degree of services. China’s trade surplus in goods decreased and trade deficit is services increased post crisis. It is urgent to embrace structural reforms to help support the recovery of output and trade. It is a possible solution to rebalance the balance of trade (trade surplus in goods and trade deficit in services) by expanding trade in services. The openness degree of services is lower than that of goods in China. Further liberalization in services trade is the appropriate policy choice by Chinese government. Continued policy and regulatory reform in favour of services trade will be vital to supporting economic recovery. On one side, improvement of the market access and national treatment for foreign service suppliers help to enhance the productivity and competitiveness of Chinese local service firms and upgrade the industry structure of services, which is essential for China’s economy changing from mode driven by export to mode driven by domestic demand; on the other side, decreasing the trade and investment barriers helps to expand China’s Services Trade and Investment and increase the involvement of the services globalization.

Keywords: China, Services, trade, crisis

JEL Classification: F13, F14

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* Acknowledgement: the author was grateful to Professor John Whalley, Christopher Findlay and Xiaopeng Yin for their constructive comments. This paper is part of the research work under IDRC/CIGI Project “Young China Scholars Research and Policy Engagement Network”

1. Introduction: the growing importance of services and services trade Paradox in China

1.1 The Growing Importance of Services in China

Service makes a direct and significant contribution to GDP and job creation. The services sector makes an important contribution to employment growth, productivity and innovation in most economies. Services become the most dynamic sectors in China as well. According to ***National Bureau of Statistics***, the share of services in China's economy increased considerably in the past three decades (see figure 1). In 1978, China's services sector only accounted for **23.9%** of GDP. In 2010, the share of China's services sector in GDP amounted to **43.0%**. The number of employees in services sector accounted for **12.2%** in total employees in 1978 and the share amounted to **34.1%** in 2009. The Chinese government regards the accelerated development of the service sector as an important way to promote the rationalization of economic structure, transform the economic development mode and the foreign trade development mode as well as to create job opportunities. If sufficiently competitive, services have the potential in the long run to generate new jobs for surplus labour currently located in China rural areas.

China's services sector is becoming more and more important. However, compared with other economies whose services are becoming the largest sector, China is lagged behind in services sector owing to the lower share of services in GDP. The service sector accounts for a significant proportion of GDP in most countries, including low income countries, where it frequently generates over 50% of GDP. Services contributed 72% of GDP in industrialized economies and 54% of GDP in developing countries, and average level of share of services in world GDP is 69%. United States' services share is 76.5%, UK's services share in GDP is 75.6%, India's services share in GDP is 53.7%, Brazil's services share is 64.0%. China's services share in GDP is lower than both the developed and developing economies.

1.2 Services trade Paradox in China

Given the growing importance of services trade in terms of its increasing contribution to China's GDP and employment, services trade would also be of substantial importance to China's further economic development. Trade in services can improve economic performance and provide a range of traditional and new export opportunities.

Services have been the fastest growing segment of world trade between 1990 and 2010. It's the same case for China. China's annual growth rate of services export was 18% and annual growth rate of services import is 24% on year-on-year basis between 1990—2000. China's annual growth rate of services export was 17% and annual growth rate of services import is 18% on year-on-year basis between 2000—2009. The growth of China's services trade exceeded world average growth level between 1990—2009.

China's position in world services trade also increased from 12^{th} in 2001 to 5^{th} in 2009 in exports and from 10^{th} in 2001 to 4^{th} in 2009 in imports. China has become one of the top 5 trading nations so far.

Despite of the higher growth rate and increased ranking of China's services trade, there was also services trade paradox in China. In contrast to merchandise trade, China's trade in services was of a smaller scale and had long been in deficit. The paradox was showed by the extremely lower share of services trade compared with goods trade. China's share of services in total trade is lower than both the world average level and the leading trading nations' level (see figure 5 and 6). The share of services in world trade is around 20% between 1990—2009. China's share of services in total trade is below 10%. The fact of lower share of services in China's total trade complied with the fact of lower share of services in China's GDP.

China's service paradox results from the bias in favour of merchandise manufacturing and heavy industries. Services play a key role in competitiveness and trade facilitation. The potential gains from more open services trade are greater than those from liberalizing goods. China's lower share of services trade impeded the expansion of benefits of trade liberalization in services sector.

2. Impacts of the Global Financial Crisis on China's trade in services ----Stylized Facts and Main Findings

2.1 Global Financial Crisis and its impacts on China's Trade in Services —overview

2.1.1 Stylized Facts

The financial crisis impacted international trade from two aspects: On financial side, the crisis directly impaired the environment for trade financing with tougher conditions, reduced credit lines and delayed trade settlement, thus adversely affecting international trade. On physical side, the financial crisis caused substantial depreciation of the financial assets. The rapid reduction of wealth triggered off steep decline in investment and consumption, resulting in reduced demand for imports including the services. The services sector is more directly affected by the financial crisis, since financing itself falls in the category of services. And trade in services by nature is highly conditional on the operation of the physical economy. The downturn in demand for investment and consumption will not only affect merchandise imports and exports, but will directly affect the demand for services at the same time.

Under the impact of the financial crisis, China's trade in services fell notably. In 2008, China's services imports and exports (on BOP basis) amounted to USD 304.45 billion, up 21.3% as compared to 2007, while the growth margin dropped by 9.6%, of which the growth of services exports declined by 12.7%. The traditional services like transportation and tourism were more seriously inflicted by the financial crisis, while the services with high added value such as insurance, and computer and information were less affected, with the growth rate of their exports being more than twice of the services exports as a whole on a year-on-year basis, together with their export growth margin dropping at a smaller degree.

In 2009, China's services imports and exports (on BOP basis) totaled USD 286.8 billion, down 6% as compared to 2008. Of which the growth of services exports declined by 12.2% and imports increased by 0.1%. Owing to the decrease of exports, services trade deficit in 2009 increased by 150%. Transportation, Royalties and Licenses, insurance, tourism etc all run big trade deficit. In 2009, the share of transportation and tourism was 53.6%. Compared to 2008, the share of traditional services like transportation and tourism decreased. Tourism used to be the service sector which run trade surplus but it began to run deficit in 2009. Other business services run trade surplus in 2009, increased by 104.2% compared to 2008.

Figure 1. China's Goods and Services Trade Growth Rate 2002—2010 (%)

Source: MOC, P.R.China; SAFE, P.R.China

In the first half of 2010, according to BOP statistics by SAFE (State Administration of Foreign Exchange), China's services trade recovered stably. The total services trade value amounted to USD 165.63 billion, increased by 31.7% on a year-on-year basis. Exports increased by 41.2% and imports increased by 24.5% on a year-on-year basis. Services trade deficit declined by 43.2% on a year-on-year basis.

2.1.2 Main Findings---- shift in the V-curve of China's services Trade and possible reasons

The Shifting V-Curve of China's Services Trade showed sharp decline in 2009 and a rapid trade recovery in 2010. The recovery of China's services trade is following the V-curve, as seen in Figure 7. China indeed faced deceleration in services trade growth rate, but the magnitude of its impact on China was felt not to be very large.

There are a number of possible explanations for the shift in the V-curve of China's services imports and exports:

- **Services trade volumes rebound symmetrically with China's economic recovery.** China's large stimulus package including vigorous and timely fiscal and monetary stimulus is a prime example, and China's growth has picked up following a large increase in unemployment from the initial shock to world trade. China's success in domestic stimulus not only helps stimulate the domestic economy but also boost Chinese demand for services imports. China is the only one whose services imports rising up instead of declining among all the world leading trading economies in 2009.

- **Service trade is more robust than goods trade because there is less cyclical demand and less dependence on external finance.** The crisis impact on China - a country less dependent on merchandise exports other than services exports for growth - is far less dramatic. The performance of the domestic market and domestic demand remained positive.
- **China's services sector is not totally integrated with global market at present.** Global financial crisis had some adverse effect on China's trade in services. But the influence of financial crisis on China's services trade was limited compared with goods trade. It was partly owing to the fact that openness degree of China's services sector is lower than goods sector. China's services trade took a small share in total trade. Services exports took only 9.34% in total exports in 2008 and 9.73% in 2009; services imports took 12.44% in total imports in 2008 and 13.81% in 2009. Compared with firms in goods trade, most Chinese services firms are not involved in services trade.

2.2 China's competitiveness in services trade

In 2008, China ranked 7P$^{\text{thP}}$ in world services exports and 5P$^{\text{thP}}$ in world services imports. In 2009, China's ranking in world services exports rose to 5P$^{\text{thP}}$ and ranking in world services imports rose to 4P$^{\text{thP}}$. In 2009, China took a share of 3.8% in world services exports (which only equal to one fourth of USA services exports) and 5.0% in world services imports. In 2009, China took 9.6% in world goods exports and 8.0% in world goods imports. The share of china in world services trade was relatively lower compared to share of goods trade.

China run big trade deficit in services both pre and post global financial services. In 2008, China's services trade deficit was USD 11.56 billion and increased by 52% compared to 2007. In 2009, China's services trade deficit amounted to USD 29.6 billion and increased by 156% compared to 2008. China's Trade Competitive Index in services trade also declined from **-0.04** in 2008 to **-0.10** in 2009.

Temporary measures alone are not sufficient to correct imbalances in China's pattern of economic growth and development, which are macroeconomic and structural in nature. The crisis has reinforced China's intention to undertake more longer-term structural reforms that are needed to strengthen its services sector and to diversify the economic and trade structure.

2.3 Trade dynamics: China’s trade in services by sectors

This section will go through the sector impacts of the global financial crisis in details and find whether the crisis changed services import and export composition in the short run.

2.3.1 Growth Rate Differed Among Different Services Sectors

The growth rate differed among twelve different services sectors in China pre and post crisis. Almost all the services sectors recovered rapidly in 2010.

For exports, seven sectors including *Transportation, Travel, Communication, Construction, Royalties and Licenses, Film & Audiovisual and Other Business Services* were affected by the global financial crisis of those the exports value declined and showed negative growth rates in 2009; while five other sectors including *Insurance, Financial Services, Computer and Information services, Consulting Services, Advertising and Public opinion polling* were less affected by the crisis and exports value increased in 2009 on a year-on-year basis. The emerging trade in services sectors with high added value such as insurance, and computer and messaging services were not so badly affected by the crisis after all, of those with the export growth margin being more than twice that of the services exports as a whole. In the first half of 2010, almost all the services sectors grew rapidly in exports except communication service.

For imports, five sectors including *Transportation, Construction, Insurance, Consulting Services and Other Business Services* were affected by the global financial crisis of those the imports value declined and showed negative growth rates in 2009; while seven other sectors including *Travel, Construction, Financial Services, Computer and Information services, Royalties and Licenses, Advertising and Public opinion polling, Film and Audiovisual* were less affected by the crisis and imports value increased in 2009 on a year-on-year basis. In the first half of 2010, almost all the services sectors grew rapidly in exports except other business services.

2.3.2 Changing Services Trade Composition post crisis

The share of China's traditional services sectors such as transport and tourism in the total services imports and exports were declining slightly, and other emerging services sectors such as insurance, computer and information services, consulting are gradually rising in proportion, although still very low. The basic composition of China's services trade changed slightly, but the traditional services sectors still took a lion's share in total services trade. The global financial crisis didn't affected China's services trade composition a lot in the short run.

For exports, the share of transportation and tourism services declined from 56.3% in 2007 to 54.1% in 2008. In 2009, the share of traditional services sectors declined to 49.2% and further to 48.1% in the first half of 2010. The emerging services sectors including insurance, financial services, computer and information services, royalties and licenses etc. took a share of 42.7% in 2007 and 44.9% in 2008. The share rose from 49.8% in 2009 to 51.2% in the first half of 2010.

For imports, the share of transportation and tourism services declined from 56.5% in 2007 to 54.8% in 2008. In 2009, the share of traditional services sectors rebounded to 57.1% and further to 60.1% in the first half of 2010. The emerging services sectors including insurance, financial services, computer and information services, royalties and licenses etc. took a share of 43.4% in 2007 and 45.4% in 2008, but the share declined to 42.9% in 2009 to further to 39.4% in the first half of 2010.

2.3.3 Different Services Sectors run trade deficit or surplus

China's services imports grew faster than exports and the trade deficit in services grew larger year by year. The total services trade deficit continues to grow post crisis, but not all the sectors run trade deficit (see Figure 13).

In 2008, four services sectors including *Transportation, Insurance, Financial Services, Royalties and Licenses* run trade deficit, while other eight services sectors run trade surplus. Among them construction services, tourism, consultancy, computer and information, and other business services are the top five, with a total surplus of

USD 21.23 billion.

In 2009, seven services sectors including *Transportation, Travel, Insurance, Financial Services, Royalties and Licenses, Film and Audiovisual* run trade deficit. Transportation services run trade deficit of 23.01 billion U.S. dollars, up 93.1% on a year-on-year basis. Tourism services shifted from trade surplus of USD 4.69 billion in 2008 to trade deficit of USD 4.0 in 2009. Construction services run trade surplus of USD 3.6 billion which was lower than 2008 level of USD 6.0 billion. China's computer and information services run trade surplus of USD 3.3 billion, increasing by 6.2%. Consulting services run surplus of USD 5.2 billion, increasing by 13%. Other business services run surplus of USD 5.92 billion, increasing by 200% on a year-on-year basis.

2.4 Trade dynamics: China's trade in services by modes of supply

Owing to the limitation of trade statistics on modes of supply, this sector will only go through mode 3 in details.

Change of Foreign Commercial Presence in China

The scale of services trade by Mode 3 expanded in China owing to the opening up of trade and investment in services.

In 2008, 14,582 foreign-invested enterprises were newly established in China's services sector, declining by 9.8% over 2007and accounting for **53.0%** of the total number of newly established foreign-invested enterprises in China in 2008. The actual utilization of foreign investment amounted to USD 54.94 billion, accounting for **50.7%** of the total foreign capital actually utilized by China and increasing by 3.5% over 2007.

In 2008, 262 newly approved foreign-invested construction enterprises were established and the actual use of foreign investment amounted to USD 1.09 billion, accounting for 2.0% of the total newly established foreign services enterprises and 2.9 % of the total services FDI. Foreign investment in entertainment, culture and sports services amounted to USD 230 million and 157 foreign enterprises were set up, down 40.7% on a year-on-year basis. FDI in financial services sector amounted to USD 570 million, accounting for 1.5% of total FDI in services. 25 foreign-invested enterprises in financial service sector were set up and took a share of 0.2%. 452 foreign enterprises in real estate were newly established and FDI in real estate amounted to USD 18.59 billion, taking a share of 3.4% and 48.8 % in total services respectively.

In 2009, 11,461 foreign-invested enterprises in services sector were newly established in China, down by 14.8% over 2008 and accounting for 48.9% of the total newly-established foreign enterprises. FDI in services sector (excluding banking, insurance and securities) amounted to USD 90.03 billion, declining by 2.6% on a year-on-year basis and accounting for 42.1% of the total FDI in 2009.

In 2009, commercial presence in real estate industry grew substantially. 569 foreign enterprises in the real estate industry newly established, increasing by 25.9%; FDI in real estate amounted to USD 16.8 billion, down 9.7%. Commercial presence in construction and related engineering services declined. 220 foreign-invested enterprises were newly established in construction and related engineering services sector, declining by 16%; FDI mounted to USD 690 million, declining by 36.7%. 52 foreign-invested enterprises were newly established in the financial services (excluding banking, securities, insurance) and FDI amounted to USD 460 million, declining by 20.3%. 148 foreign-invested enterprises in other social services were newly established and the FDI amounted to USD 1.57 billion, increasing by 184.9%.

FDI in service sector amounted to USD 29.74 billion in the first eight months in 2010, up 36.75% from the same period in 2009, according to the MOC.

Change of Chinese Commercial Presence abroad

In 2008, China's services sectors made outward FDI of USD 46.1 billion, up 135.6% over 2007, accounting for **82.5%** of China's total OFDI.

In 2008, OFDI in financial sector rose sharply. OFDI in financial sector amounted to USD 14.05 billion, accounting for 30.5% of the total OFDI in services, and increasing by 742.3% on a year-on-year basis. OFDI in the leasing and business services amounted to USD 21.72 billion, increasing by 287.3% and accounting for 47.1% of the total OFDI in services. OFDI in wholesale and retail amounted to USD 6.51 billion, declining by 1.4% and accounting for 14.1% of the total OFDI in services. OFDI in information transmission, computer and software industry amounted to USD 3.0 billion, declining by 1.7% and accounting for 0.6% of the total OFDI in services.

OFDI in transport, storage and postal industry amounted to USD 2.66 billion, declining by 34.7% and accounting for 5.8% of the total OFDI in services. OFDI in real estate amounted to USD 340 billion, declining by 62.7% and accounting for the total FDI in that year of 0.7%.

In 2009, the global financial crisis had adverse effects on China's commercial presence abroad. However, China's outward FDI net flows in 2009 reached USD 56.63 billion, increasing by 1.1%. China's OFDI in services sector amounted to USD 39.77 billion, declining by 13.7% than 2008 and accounting for 70.4% of the total OFDI. OFDI in financial sectors amounted to USD 8.73 billion, declining by 37.9% and accounting for 22% of the total OFDI.

In 2009, OFDI in transportation, storage and postal industry amounted to USD 2.07 billion, declining by 221.1%. OFDI in wholesale and retail amounted to USD 6.14 billion, declining by 5.8%.

In 2009, OFDI in financial sector amounted to USD 8.73 billion, declining by 37.8 %. OFDI in leasing and business services amounted to USD 20.47 billion, declining by 5.7%. OFDI in these four sectors amounted to USD 37.41 billion, accounting for 94.1% of China's total OFDI in services sector.

In 2009, OFDI in some emerging services sectors such as scientific research, technical services and geological prospecting as well as real estate, accommodation and catering industry grew rapidly. Among them, OFDI in scientific research, technical services and geological prospecting amounted to USD 780 million, increasing by 365%; OFDI in real estate amounted to USD 940 million, increasing by 176.7%; OFDI in wholesale and retail sector amounted to USD 70 million, increasing by 153.8% on a year-on-year basis.

By the end of 2009, Chinese state-owned commercial banks had set up commercial presence in the United States, Japan, UK and other 28 countries and regions, with 50 branches, 18 subsidiary bodies, 3 million employees of which 2.9 million are foreign employees.

2.5 Trade dynamics: China's trade in services by partners

Hong Kong, the United States, European Union, Japan and ASEAN are the top five services trading partners of China. Hong Kong is both the leading market for exports and source of imports for China in services trade. China's trade value with these partners decreased or fluctuated but the basic trade structure was not changed post crisis.

In 2008, China's major service trade partners concentrated in Hong Kong, U.S., EU, Japan and ASEAN, and both services import and export with major trading partners increased on a year-on-year basis.

For the sum of services imports and exports, trade value of these five partners with China accounted for 68.4% of China's total services trade in 2008. Among them, Hong Kong was the leading trading partner of China in services. China's services import and export value with Hong Kong amounted to USD 68.18 billion, accounting for 22.4% of the total services trade. USA was the 2nd largest trading partner of China in services and accounted for 15.2% of the total services trade. EU ranked 3rd and accounted for 14.7% of the total services trade. Japan ranked 4th and accounted for 8.2% of the total services trade. ASEAN ranked 5th and accounted for 7.7% of the total services trade.

For exports, Hong Kong was China's largest export market in services. In 2008, China's services exports to Hong Kong amounted to USD 41.9 billion, accounting for 28.6% of total services exports. U.S., EU, Japan and ASEAN accounting for 15.6%, 14.6%, 7.4% and 7.1% respectively of China's total services exports.

For imports, Hong Kong was China's largest source of imports in services also, accounting for 16.6% of China's total services imports. EU ranked the 2nd largest source of imports and accounted for 14.9% of China's total services imports. U.S. ranked 3rd source of imports and accounted for 14.9% of China's total services imports in 2008.

For trade balance, despite of large trade deficit in services in 2008, China run trade surplus of USD 15.62 billion with Hong Kong. Australia was the largest trading partner with whom China run trade deficit in services and China's trade deficit from

Australia amounted to USD 5.52 billion. The trade deficit of China in services with Japan amounted to USD 3.86 billion. The trade deficit of China in services with South Korea amounted to USD 2.68 billion. The Trade deficit of China in services with U.S. amounted to USD 0.73 billion.

In 2009, China's services imports and exports still concentrated in Hong Kong, U.S., EU, Japan and ASEAN. Exports to these major trading partners showed a decreasing trend, and imports from these major trading partners remained the same scale as that of the previous year.

For the sum of services imports and exports, trade value of these five partners with China amounted to USD 171.47 billion, accounting for 59.8% of China’s total services trade in 2009, falling by 8.6%. Among them, Hong Kong was still the leading trading partner of China in services. China’s services import and export value with Hong Kong amounted to USD 63.5 billion, accounting for 22.1% of the total services trade, declining 7.1%. EU (25), Japan, USA and ASEAN accounted for 14.8%, 8.6%, 8.3% and 7.7% of the total services imports and exports in 2009.

For exports, Hong Kong was still China's largest export market in services. In 2009, China's services exports to Hong Kong amounted to USD 37.19 billion, accounting for 28.9% of total services exports. EU, U.S., Japan and ASEAN accounted for 13.3%、7.4%、7.3% and 6.4％ respectively of China's total services exports.

For imports, Hong Kong was still China's largest source of imports in services. China’s imports from Hong Kong amounted to USD 26.31 billion in 2009, accounting for 16.6% of China’s total services imports. EU, U.S., Japan and ASEAN accounted for 12.8%、9.6%、8% and 9.9% respectively of China's total services imports in 2009.

For trade balance, Hong Kong was the largest source of China's service trade surplus in 2009, and the surplus amounted to USD 10.88 billion. In 2009, United States became the leading source of China’s trade deficit in services. China's service trade deficit the United States rose sharply to USD 7.46 billion, increasing by 33.1% on a year-on-year basis. China’s trade deficit from Japan, Australia and South Korea's in services amounted USD 5.69 billion, USD 4.89 billion and USD 4.53 billion respectively in 2009.

For commercial presence, Hong Kong EU were China's main destination for outward foreign direct investment in services. In 2009, China's OFDI in Hong Kong's service sector was USD 28.92 billion, accounting for 72.7% of China's total OFDI in services. The OFDI flew to the services sectors such as leasing & business services, financial services, wholesale and retail, accounting for 48.2%, 25.9% and 16.8% respectively of China's total OFDI to Hong Kong's in services. China's OFDI in the EU service sector was USD 26.7 billion, accounting for 6.7% of China's total OFDI in services. The OFDI flew to the leasing & business services and financial services sector, accounting for 86.7% and 7.9% of China's total OFDI to EU in services.

3. China's pre-crisis Services Trade Policy: WTO GATS commitments and China's fulfillment

3.1 China's Services schedule

GATS differs from GATT on its approach to WTO basic principles: members may take exemptions to the obligation of MFN treatment and grant national treatment only in sectors listed in their Schedules, subject to conditions and qualifications set out there. A specific commitment in a services schedule is an undertaking to provide market access and national treatment for the service activity in question on the terms and conditions specified in the schedule. When making a commitment a government therefore binds the specified level of market access and national treatment and undertakes not to impose any new measures that would restrict entry into the market or the operation of the services.

In nearly all schedules, commitments are split into two sections: First, "horizontal" commitments which stipulate limitations that apply to all of the sectors included in the schedule; these often refer to a particular mode of supply, notably commercial presence and the presence of natural persons. Any evaluation of sector-specific commitments must therefore take the horizontal entries into account. In the second section of the schedule, commitments which apply to trade in services in a particular sector or sub-sector are listed.

China's service industry is opened to a level close to that in the developed countries, covering 10 out of the 12 major GATS service categories and 100 out of the 160 minor categories. The schedule of China has not only a high sectoral coverage but also made commitments in key sectors. China has made specific commitments on 93 service sub-sectors. Among 26 basic groups of service sectors, China made 22 commitments except R&D, postal services, health and social services and recreational services. China had made relatively broad commitments upon its accession to the WTO as a developing country.

The importance of the different modes varies from sector to sector. Sectors committed are more often "unbound" under mode 1 (cross-border supply) than under other modes, while commitments under mode 2(consumption abroad) tend to be unrestricted. A relatively number of limitations tend to be attached to commitments under mode 3(commercial presence) and mode 4(movement of natural persons). Example of limitations under mode 3 included foreign equity limits, restrictions on the type of legal entity and limitations on the number of suppliers. Mode 4 commitments are usually set out in the horizontal section of the Schedule.

China committed to the substantial opening of a broad range of services sectors through the elimination of many existing limitations on market access. China also made certain "horizontal" commitments, which are commitments that apply to all sectors listed in its Services Schedule (see table 2).

3.2 China's implementation of the GATS commitments

Since China's accession to WTO, China had been liberalizing its services sectors closely in line with its commitments under the GATS. Chinese government has recognized the importance and benefits of services liberalization for China's economic growth and continued to make its trade policy regime more transparent.

The second Trade Policy Review of China was held on 21 and 23 May 2008. The

WTO Secretariat report[1], along with a policy statement by the Government of China[2], was the basis for the second TPR of China by the Trade Policy Review Body of the WTO. According to the TPR report, China has continued to adopt measures to increase the level of transparency of its trade and trade-related policies, practices, and measures. China had been liberalizing its services sectors closely in line with its commitments under the GATS. The relevant legislations are also being operated consistent with the WTO rules. China had made efforts to comply with its WTO obligations, pursuing substantial reform programmes, in both its trade and investment regimes.

After accession to WTO, the Chinese Government has established a set of new rules and regulations to promote further opening up of its service sectors. These rules and regulations mainly included: Regulation on Administration of Commercial Franchise, Detailed Rules for the Implementation of the Regulations on the Administration of Foreign-funded Banks of the People's Republic of China, Measures for the Information Disclosure of Commercial Banks, Measures for the Administration of Trust Companies, Measures for the Administration of Finance Leasing Companies, Measures for the Overseas Investment with Insurance Funds, Administrative Measures for Insurance Licenses, Measures for the Administration of Foreign Stock Exchanges' Representative Offices in China, and etc.. These laws and regulations not only embody China's WTO commitments but also incorporate measures of autonomous liberalization, demonstrating China's positive stand towards opening up its trade in services.

China made its trade regime more transparent, by introducing the Regulation on Open Government Information, which had entered into force on 1 May 2008. As a designated publication of the Chinese Government to make public trade-related laws and regulations, China Foreign Economic and Trade Gazette has made public more than 3,300 laws, regulations and specific measures by the end of 2007.

For Mode 3 – commercial presence, prior to China's WTO accession, foreign

[1] WT/TPR/S/199 China: Report by the Secretariat
[2] WT/TPR/G/199 Report by China

companies in many service sectors did not have an unqualified right to apply for a license to establish or otherwise provide services in China. They could only apply for a license if they first received an invitation from the relevant Chinese regulatory authorities, and even then the decision-making process lacked transparency and was subject to inordinate delay and discretion. In its accession agreement, China committed to licensing procedures that were streamlined, transparent and more predictable. China's Services Schedule called for the implementation of relatively minor additional commitments by December 11, 2007, in areas such as taxation services, management consulting services, travel and tourism services, and rail transport services. These commitments are the last ones scheduled to be phased in pursuant to China's scheduled commitments.

Since China's entry to WTO, China has gradually lifted the limits on the foreign investment in services sectors in aspects such as geographic regions, equity and business scope. Services sectors were more open to the outside, resulting in attraction of more foreign investment and further expansion of commercial presence in China.

China had established a set of new rules and regulations to promote further opening up of its service sectors. These laws and regulations incorporated measures of autonomous liberalization, demonstrating China's positive stance towards opening up its trade in services. At the domestic level, several new trade-related laws had been adopted, including the Property Law, Enterprise Income Tax Law, Anti-Monopoly Law and Law on Enterprise Bankruptcy. These laws contributed towards a more rule-based predictable business environment, which was particularly important for foreign investors. China had been moving recently towards establishing a more level playing field for domestic and foreign investors.

3.3 Measuring China's services policy by STRI

China's services commitments at accession had been recognized for their breadth and significance. China has been steadily implementing its commitments. China's services market is open and tries to provide fair, non-discriminatory access in line with its WTO commitments.

Eight years after China's WTO entry, there are still some areas in which China should continue to improve on, including access by foreign companies; more transparency in China's domestic regulations; smoother administrative procedures, especially licensing procedures; capital requirements for financial institutions, clearer guidelines on access to the telecommunications industry for joint ventures and rules governing domestic distribution of foreign products, etc. In China, some services sectors are still subject to certain degree of state control and lack of competition. Several services sector continued to be characterized by state involvement and the level of state interference in the economy was still noticeable, distorting market functioning. There were still some restrictions on foreign investment and private-sector activities in several of the individual sectors including banking, insurance, securities, asset management, and telecommunications services.

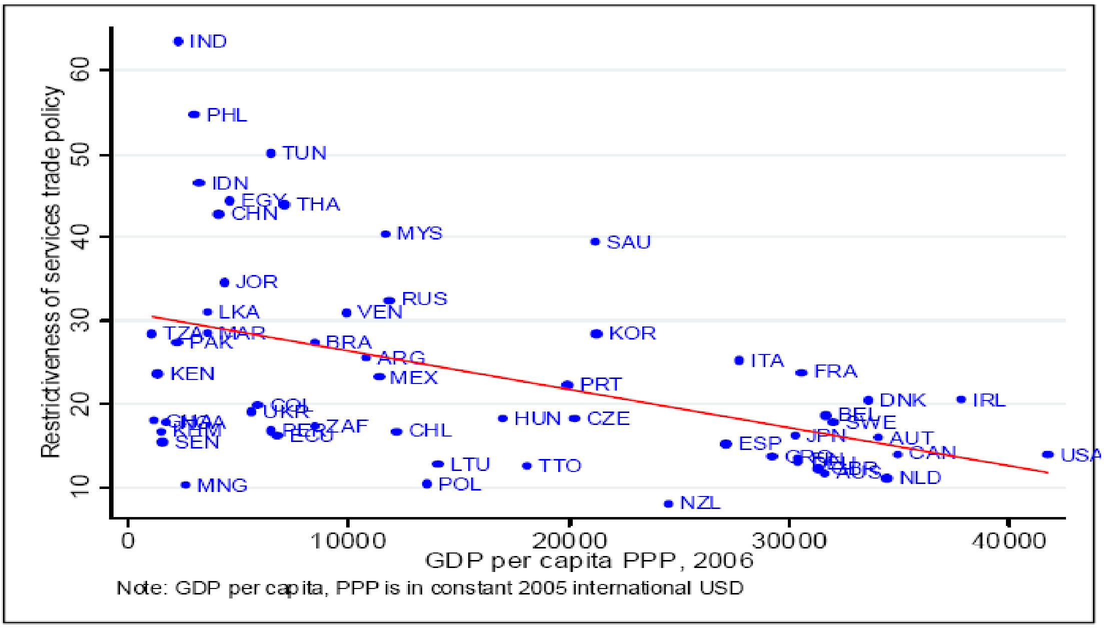
China's regulations have generated significant concerns with regard to the implementation of important commitments in the area of banking services. Excessive and often apparently discriminatory capital requirements by international norms continued to restrict market entry for foreign suppliers in many sectors, such as banking, securities, asset management, telecommunications and construction services, among others. In addition, in banking, insurance and legal services, branching restrictions and related practices limit market access for foreign suppliers. In other sectors, particularly construction services, problematic measures appear to be taking away previously acquired market access rights.

National treatment concerns remained, particularly in the banking and insurance sectors. In some sectors, particularly insurance services, the licensing process was characterized by lengthy delays. China still does not allow foreign credit card companies and other suppliers to provide electronic payments processing and related services for domestic currency transactions in China.

Restrictions on trade in services impose costs, limit domestic and international competition, decrease efficiency and permit incumbent services suppliers to charge prices above those in a competitive market. Restrictions in services trade usually take the form of government regulation. Administrative regulation includes reporting, information and application procedures and burdens on start-ups, implied by both economy-wide and sector-specific requirements which restrict domestic market mechanisms and curb international transactions. Economic regulation includes all other domestic regulatory provisions affecting product market competition such as state control and legal barriers to competition.

Gootiiz and Mattoo (2009) calculated the overall restrictiveness of services trade polices of 56 countries in 2005. Among which, China belongs to the groups whose STRI is higher and has more restrictive services policies than most developed countries and some underdeveloped countries such as Cambodia, Nigeria and Mongolia. China's STRI is lower than that of other Asian economies such as India, Indonesia, Thailand and Philippines.

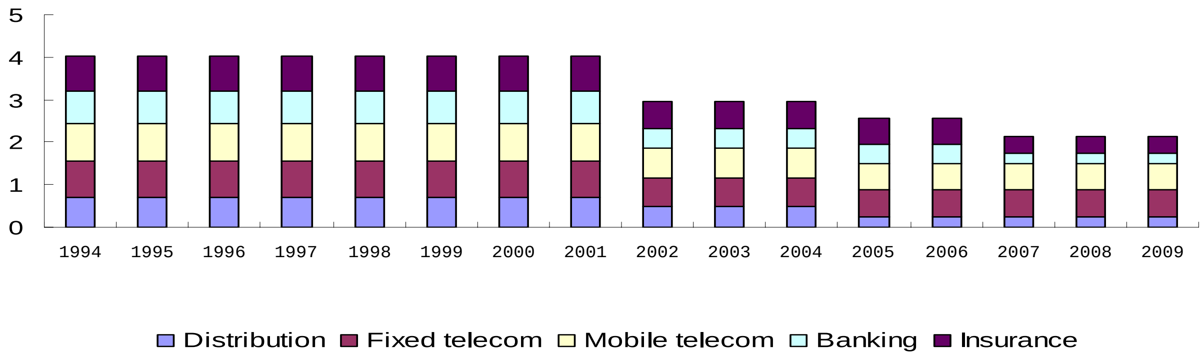
Figure 2: Restrictiveness of Services Trade Policies of 56 Countries, 2005



Source: Gootiiz and Mattoo (2009)

On the basis of time-series developments in China's regulations, Ying FAN (2009) calculated STRI of China's services sectors, mainly on specific sectors such as distribution, telecommunication and financial services. According to the services trade restrictiveness index (STRI) in China calculated by the author, the results provide evidence that the China's trade barriers in services are decreasing. Total trade barriers in service sectors are decreasing and degrees of market openness differed across sectors. Compared to other sectors, STRI for distribution services sector is the lowest and STRI for communication services sector is the highest.

Figure 3. China's Service Trade Restrictiveness Index—by sectors



Source: Ying Fan (2009).

Decreasing of China's services barriers is essential to China's integration into the global economy and continued economic development. China's implementation of its WTO commitments in services already benefits China. But there are still a range of impediments to the growth of China's service sector, as well as service trade and foreign investment. China should remove these constraints in the future to realize the full potential economic benefits of trade and investment in services.

China was in a position to be more transparent about its regulating and trading regime. Greater transparency was in China's own interest, since this would preclude any unnecessary misunderstanding of its trade practices and measures, and foster better decision-making in China. China will also accelerate its liberalization of services to boost the development of economy.

4. China's post-crisis Services Trade Policy: Challenges, Opportunities and Possible Direction

4.1 Policies adopted by Chinese Government in services sectors to respond to global financial crisis

In order to fight against the negative impact of the global financial crisis on the economy, Chinese government adopted proactive fiscal policy and moderately loose monetary policy to expand the domestic demand and successfully alleviated the impact of the crisis on the goods export sector. The goods trade policies adopted by Chinese government to dealing with downward trend included: Changing the policy of restricting export and restore tax rebates; Strengthening export credit insurance service; Adopting loose monetary policy and alleviate enterprises' financing problems; improving processing trade policy; and stabilizing the RMB exchange rate etc.

Compared to policies adopted in goods trade sectors, the policies adopted in services trade by Chinese government was limited. Most of the policies aiming at stimulating the domestic economy are not specific to services. China has implemented a number of policies to stimulate and rebalance the economy, to increase consumer spending, to restructure and subsidize certain industries, and to boost incomes for farmers and rural poor.

Limited policies were carried out by Chinese government in services sectors to respond to the global financial crisis as following:

(1) China's two-year 4 trillion RMB ($586 billion) stimulus package (equivalent to 13.3% of China's 2008 GDP) provided stimulus to services sectors including public transport infrastructure, rural infrastructure;, environmental projects, technological innovation, health and education.

(2) In order to rely less on manufacturing sector, the Chinese government has relaxed FDI restrictions on some services sectors, notably in telecommunication and tourism, and the Central Government has been delegating to local governments licensing authority for the establishment and modification of operations of "encouraged" foreign-invested enterprises (FIEs) and certain selected sectors, as well as certain types of FIEs, such as foreign invested joint-stock companies.

(3) China's central bank took loose monetary policy and provided directives to commercial banks for provide financing and funding to help firms invest overseas, including OFDI in services sectors.

(4) China has continued to review, revise, or amend its trade and related laws including the Anti-Monopoly Law (effective 1 August 2008), China's first comprehensive competition law and the Patent Law (effective 1 October 2009), which strengthened patent protection by increasing penalties against infringement. China

has also reformed its tax system to render it more neutral; in particular, this involved the unification of enterprise income tax rates for all companies (domestic and foreign), and the transformation of VAT from a production-based tax to a consumption-based one.

4.2 Where China's services policies should be headed: challenges and opportunities

How would China, adjust to the new economic circumstances post global crisis? Global crisis generates challenges yet also opportunities for China policy.

4.2.1 Opportunities of Services Trade with China post crisis

Being a major beneficiary of world trade in services: World trade in services has recovered during 2010. The weaker downturn in services trade during the global crisis could reflect a lesser dependence on intermediate inputs as much as a lesser reliance on trade finance of certain services sectors like communications. With the continued rise of world services trade, new trading opportunities, as well as new services, were being created by the rapid improvement in communications and large reductions in costs. Distance-related barriers that had previously disadvantaged suppliers and users in remote locations were becoming less relevant. Attitudes of governments and expectations of citizens were also changing. In many parts of the world, more services were being opened-up to private commercial participation. The combination of technological and regulatory innovations enhanced the "tradability" of services and, thus, and created new opportunities for all the economies including China.

Transformation from "manufacturing industry-oriented economy" to "service – oriented economy" needs to further expand trade in services: Global financial crisis was a blow to foreign trade. It was also a push to altering trade modes. The crisis has prompted China to rethink its development strategies. China is facing the choice between growth driven by goods exports and growth driven by domestic demand. The need to find new and sustainable sources of growth in China is becoming crucial. China's transformation of economic growth pattern needs to further expand trade in services. For the welfare of the majority of people, China need to resist protectionism and become more, not less, integrated into to the global economy to continue to reap the benefits of global knowledge, technologies and innovation. Trade in services plays a special role in knowledge transfer and exchange. It can enable China to benefit from international research, contracts, use of new equipment that incorporates newer technology, and exchange of knowledge and experience. Knowledge transfers have been helped through trade in services in telecommunication, retailing, banking, and IT training.

Large domestic services market in China generated by China's urbanization and industrialization: China's industrialization and urbanization will generate huge market demand. Urbanization has become an important driving force to China's economic growth and social development. In the future 10 years, China will meet the great historical turning point where urban population exceeds that in the rural area. Emerging manufacturing and service industries will spread from coastal area to the inland, and thousand of cities will prosper, which will continuously generate huge market demands for both goods and services and drive the long-term rapid development of China's economy. With the acceleration of China's industrialization and urbanization process, the market demand for services import will rapidly grow.

Big Potential of Services in China: China can sustain service-led growth because there is a great deal of room for catch-up and convergence. The globalization of services provides opportunities for China to find niches—beyond manufacturing—where China can specialize, scale-up, and grow. Comparative advantage can just as easily be in services as in manufacturing or agriculture. In the case of China, value added in services accounts for 40 percent of GDP, and services only account for 11 percent in China's external trade. Taking advantage of this potential includes two sets of actions: one is a more neutral policy and incentives environment; another is supportive investments in services sector.

Goal of becoming services trading power: In April 2010, the MOC released its "China's Foreign Trade Development Strategy in the Post-Crisis Era" report, which stated clearly the goal of making the country a strong trading power by 2030. Specific targets for the year 2020 were a total trade value of 5.3 trillion U.S. dollars, breaking down to 4.3 trillion U.S. dollars in goods and 1 trillion U.S. dollars in services. China is expected to play a leading role in setting up international trade rules.

The potential benefits of further services liberalization for China: Trade liberalization in services helps generate economic growth by creating bigger markets, which stimulates technology and encourages lower cost. Services liberalization is strategically important for technology transfer and development. Producer services such as telecommunications, banking, insurance, construction and transport help to shape overall economic performance. FDI in services sectors typically brings with it new skills and technologies that spill over into the wider economy in various ways. Trade liberalization can help increase the supply of services by offering an environment conducive to attracting foreign investment and by lowering cost through competition in China. The gains from more investment and greater domestic competition also go with building greater export competitiveness in both goods and services.

4.2.2 Challenges of Services Trade with China post crisis

There still remain very substantial barriers to trade and investment in services and regulations impeding both domestic and foreign services suppliers in China. Not all of these are discriminatory but may stem from barriers to entry that apply to domestic and foreign suppliers equally. Integration for services has remained slow outside a few specific sectors including telecommunications, road and air transport, financial services. Nonetheless, there are still significant restrictions, such as foreign participation limits, on foreign investment and private-sector activities in some services sectors. In banking, stringent qualification requirements remain, including high minimum asset requirements on sole or controlling shareholders and high minimum paid-up capital amounts, restrictions on the supply of credit-card services, and restrictions on the business scope of foreign banks branches. The stock market in China has continued to develop during the period under review, and the process of converting shares of state-owned enterprises (SOEs) to be traded in the market has progressed.

Opening services markets lead to long term gains but it is neither

adjustment nor risk free in the short term. Moving towards a more competitive environment may take time and may impose significant burdens as the adjustment takes place. Services sectors that previously enjoyed heavy protection will against the further trade liberalization strongly. Badly designed reforms may unnecessarily complicate the adjustment process, or even more seriously, lead to monopoly rents being transferred to private, perhaps foreign, owners.

Incentives for Chinese governments may be weak when the relevant policies are under its own control. Instability might ensue if liberalization of the services sector is not accompanied by adequate prudential supervision and regulation. The absence of well-designed universal service requirements on new services actors, especially private actors in the market could also result in reduced access to services for vulnerable groups or geographically remote regions. How to avoid unnecessary frictions and ensure the efficiency and viability of more open, market-oriented service regimes is a big problem facing the Chinese government. How to design an institutional framework that will favour structural reform, while enhancing social dialogue and public understanding and acceptance of reform measures is a big challenge.

The reform to pursue benefits across different policy areas in a complementary way and to foster synergies between policies in services is burdensome. How to integrate the regulators in sub services sectors and harmonize the services trade – related policies by different regulators is a very difficult problem facing China. Ministry of Commerce (MOC) regulates both domestic and foreign trade and works to attract foreign investment and is also the supervisory body of all distribution services in China. **MOC** set up ***Department of Trade in Services*** in 2006 which is responsible for the trade promotion in services. However, in China, there are many administrations responsible for the regulation of different sub services sectors. For communication services, in China, national telecommunication regulatory authority is **Ministry of Industry and Information Technology (MIIT)** and it has nation-wide regulatory system composed of provincial branches called “Provincial Telecommunication Administration” (PTA), which have regulatory functions in their respective provinces. The other two regulatory agencies in telecoms are the State Administration of Radio, Film and TV (SARFT) and the National Development and Reform Commission (NDRC). The former is responsible for awarding licenses for broadcasting and managing censorship of content. The latter is responsible for regulating basic telecommunication prices and interconnection charges. For financial services, **China Banking Regulatory Commission (CBRC)** is the main regulator of the banking sector along with **People's Bank of China (PBC)** and **State Administration of Foreign Exchange (SAFE)**. China's insurance regulator, the **China Insurance Regulatory Commission (CIRC)** was responsible for the approval of operating licenses. **China Securities Regulatory Commission (CSRI)** is responsible for the regulation of securities sector. How to harmonize the policies made by these regulators involved in services is very difficult.

How to harmonize the interest conflict in making services policies between the central government and local government is also puzzling. Tension often arises between local and central government over policy making in China. China is a country of multiple jurisdictions and each jurisdiction is more interested in its local development than the overall development of the country. Such a situation has led to the problem of contradictory decision-making and local protectionism. Each region having its own unique trade and investment barriers, and interpretation of regulations differs. It is not easy to balance the relationship between local community outcomes and the national long term strategy. The future services policy reforms should encourage local authorities to focus on promoting the services sectors, consistent with the principles of sustainable development.

It is difficult for Chinese government to make appropriate policy mix in expanding services trade while achieving regulatory objectives efficiently. Chinese regulators' knowledge on regulation is sector-specific. Focus of regulators often is not on international trade/investment or on competition support development of national services trade strategies. The policy adjustment challenge faced by China differs both in nature and extent from that faced by the advanced industrialised economies. So therefore does the required policy mix and the ability to implement policies. It is difficult for Chinese regulators to make an efficient framework of regulation that achieves regulatory objectives while keeping regulatory burdens on enterprises to the necessary minimum, fosters competition and helps ensure genuine market openness in services.

4.3. Possible Directions for China's Services Policy Reform

4.3.1 Effective Policy system linkage in services should be established

Within the system of trade in services, the role played by the cross-sector liaison mechanism in policy coordination is to be strengthened. Under the general framework of the liaison mechanism, more effective working mechanisms are to be developed for the key sectors according to their respective natures. These are to offer coordinated solutions to problems of overall significance for trade in services. A liaison mechanism between the Government and the enterprises is to be established. Industrial associations for trade in services are encouraged throughout the country. A coordinating mechanism and a working system for promotion of trade in services shall be formed by way of close cooperation between different sectors and tight liaison between the Government and the enterprises.

4.3.2Trade Promotion Policy Reform to Expand Exports of Services by Key Sectors

Efforts will be concentrated on further increase in exports of the Key sectors by offering sector-specific Exports Guidance Catalogue. Independent services export brands are encouraged. A number of enterprises with core competencies in the trade in services will be created. Producer services including transportation, telecommunications, logistics, distribution and financial services, is a prerequisite to ensure and sustain economic growth. Trade in services has the advantage of being high in added value, and low in energy consumption and pollution. By developing trade in producer services, the quality for growth of trade in goods will be upgraded. The aim is to achieve coordinated development between trade in goods and trade in services through the mutual complementary effects between the two.

Develop trade promotion organizations in services to serve the enterprises' trade and investment strategy.

4.3.3 Reducing Trade/Investment Barriers in services by Policy Mix

Trade/investment barriers include both discriminatory barriers against foreign services providers and domestic regulation that applies to all firms whatever their nationality. Restrictions on inward FDI, entry (ownership) limitation and operating requirements would have effects on foreign services providers. There is a positive relationship between FDI in services and the performance of domestic firms in services. Reducing barriers to trade and investment in services helps improve the productivity and competitiveness of services firms. China should take policy mix to further open services markets. On one side, open services markets by improving services regulation and ensuring that regulations do not impede market access. On the other side, remove the discriminatory policies to increase both export and import opportunities form services providers.

4.3.4 Tax system reform aimed at strengthening services sector

China should accelerate the reform of its tax system to shore up the transition of its economic growth pattern from goods-orientation to services-orientation. The Chinese government will replace sales tax with value-added tax (VAT) for the service sector to unify tax implementation on goods and services in five years. According to Ministry of Finance, beginning from 2011, the Chinese government will start with a pilot program to impose VAT on some producer services, while reducing the sales tax on them at the same time. The gradual unification of taxes on goods and services will boost development of the services sector. Before 2011, VAT is levied only on manufacturing in China, while services are subject to a business tax that raises a much smaller amount. Given the heavy dependency of local governments on VAT revenue, they have a strong incentive to promote manufacturing, rather than services. The current frame of China's finance and tax system which was set up in 1994 can no longer adjust to rapid economic growth and solve emerging problems. Uniform VAT implementation on goods and services will offer incentive for the local government to promote services sector. China will make better use of taxes' role in accelerating the transition of the development pattern. In addition, a preferential tax policy should also be implemented to help some small and medium-sized services enterprises, and the policy will aid sub services sectors involved in protecting the environment and creating new jobs. Some sub services sectors can add not only fiscal revenue for local governments but also help create job opportunities for citizens and migrant workers and improve people's standard of living. Tax break should be offered to the enterprises in these sectors. More favorable tax policies should be implemented to support the efforts of qualified services enterprises to list on the stock markets. China will also give provincial-level governments the power to adjust local tax categories, rates, and cuts in the next five years to ensure their fiscal revenues in accord with administrative responsibilities.

4.3.5 Competition Policy reform to provide equal opportunity for all services providers

There is still a dominant presence of State-owned enterprises (SOEs) in the services sector, which constrains competitiveness and productivity. The high market concentration limits the entrance of both new domestic and new foreign players, thus reducing the benefits of enhanced competition and liberalization. Against this background, wide-ranging reforms are needed to turn services into an efficient and competitive sector. That would strengthen domestic sources of growth and support government efforts to rebalance the economy. Competition Policy should be reformed by reducing market concentration in the sector, the resulting liberalization and improved competitiveness would lower production costs and prices, and increase the quality of the services provided to consumers and producers both. Recent efforts by the Chinese government to better enforce the **Antitrust Law** are steps in the right direction by avoiding abuses of dominant position in post-deregulation services marekts. More openness toward foreign participation in sectors, including banking, telecommunications and professional services, will foster liberalization efforts. In this regard, a reliable intellectual property rights regime, which is crucial for the development of services, where copyrights and trademarks are important, would help attract more overseas direct investment into the sector, and encourage domestic firms to innovate.

4.3.6 Financial Policy Reform for private and small & medium enterprises in services sector

Services exports should be encouraged by a combination of ways including discount interest loans, financial allowances and rewards. The inefficient allocation of financial resources enhances the dominance of SOEs in the provision of services. While significant progress in financial sector liberalization has been achieved, the current system remains biased toward large SOEs, which absorb about two-thirds of total lending. In contrast, private enterprises, which tend to be more efficient and innovative, receive only one fourth of the available credit. Notwithstanding their significantly smaller allocation, private firms generate about 50 percent of GDP and are the primary source of employment generation in China. It is important to deepen financial sector reform for the improvement of capital allocation to move toward an innovation-based economy and grant wider access to finance. Given the superior performance of private companies in China, more efficient capital allocation would translate into higher GDP growth. Furthermore, more sophisticated capital markets will bring benefits to self-employed entrepreneurs, and small- and medium-sized enterprises, which are critical players in a vibrant services sector-based economy.

4.3.7 Negotiate Market Access for China services exports under GATS and GATS+ commitments

Both the WTO and the regional or bilateral trade agreements provide mechanisms for liberalizing access to services markets. Commitments by WTO members on services take the form of a partial listing of sectors that are subject to market access and national treatment obligations. Trade agreements can potentially help Chinese government implement policy reforms that enhance the contestability of services markets that are opposed by domestic interests groups. By committing to certain multilateral or bilateral trading rules, the Chinese government can make domestic policy reforms more credible. The trade agreements act as a domestic policy reform anchors. China will make progressive liberalisation under the bilateral and regional FTAs framework through binding GATS + commitments and make progressive liberalisation under WTO framework GATS through binding GATS commitments. China should also stimulate services exports by improving market access through multilateral and regional negotiation channels.

4.3.8 Diminish the negative effects of trade liberalization in services by complementary policies reform

Specific benefits are likely to result from the liberalization of trade in services. However, services liberalisation also carries risks. Making appropriate regulation and other complementary policies reform help to ensure that liberalisation delivers the expected benefits. The trade related policy reform challenges facing China are preference erosion and revenue loss. Policy to provide adequate income support and make certain compensation to those suffer from the losses is necessary. Undertaking reforms across different policy areas in a complementary way can reduce the adjustment cost of policy reform. In one world, comprehensive policy reform is more effective than piecemeal strategies in China.

5. Conclusion

- China's services exports sector suffered the impact of global financial crisis. But the crisis did not change the overall pattern of China's trade in services both by sectors and by partners in the short run.
- The share of services in GDP and services-related employment in total employment are relatively lower in China. The relative underdevelopment of the services sector is a direct consequence of the economic development model adopted by China, which favours manufacturing with focus on manufactured exports. As a result, policy incentives have directed investment into the production and export of goods, discouraging investment in services.
- China's economy has come at a turning point because of the global crisis but also because of the domestic tensions engendered by the export-led model. To have a sustainable growth China has to rebalance its economy towards the domestic market and services sector.
- A well-developed services sector plays a major role in improving production efficiency and promoting technical progress and innovation. More favorable policies aimed at boosting the services sector's development should be implemented, which found the basis of China's trade in services.
- While manufacturing greatly benefited from liberalization brought about by the

successful opening-up policy, progress of openness has been limited in the services sector. The restricted exposure of the services sector to overseas direct investment, and its implicit technological transfer, has limited the expansion of the sector and the quality of the services provided. It has constrained the potential of trading services, too, which explains the persistent deficit observed in the services account of the balance of payments.

- Despite the ambitious services liberalization commitments that China agreed to when it joined the WTO, the implementation and enforcement remain not perfect in some fields. There is still a dominant presence of State-owned enterprises (SOEs) in the services sector, which constrains competitiveness an productivity. The high market concentration limits the entrance of new domestic and foreign players, thus reducing the benefits of enhanced competition and liberalization.
- The possible direction for China's policy reform in services should focus on strengthening the contribution of services trade to China's economic growth and removing the trade/investment barriers in services. Liberal trade and investment policies contribute to growth, innovation and competitiveness and avoid policy reversal. Because of downstream linkages, particular benefits are likely to arise from the liberalisation of trade in services. Services barriers contribute to effective taxation, rather than protection. Liberalize China's services sectors further by building sound institutions, fostering an appropriate services policy framework and removing any anti-export bias, improving firms' access to international services market and reducing other domestic barriers to services trade and investment.
- Trade liberalization policy should be backed by other supportive action in other policy areas to complement the reform process. A comprehensive policy response is crucial for China.
- Trade liberalisation in services also carries risks. Making appropriate regulation and other complementary policies reform help to ensure that liberalisation delivers the expected benefits.

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