

Policy and Regulatory Priorities for Developing Efficient Services Industries

Workshop on
Services Trade: New Approaches for the 21st Century

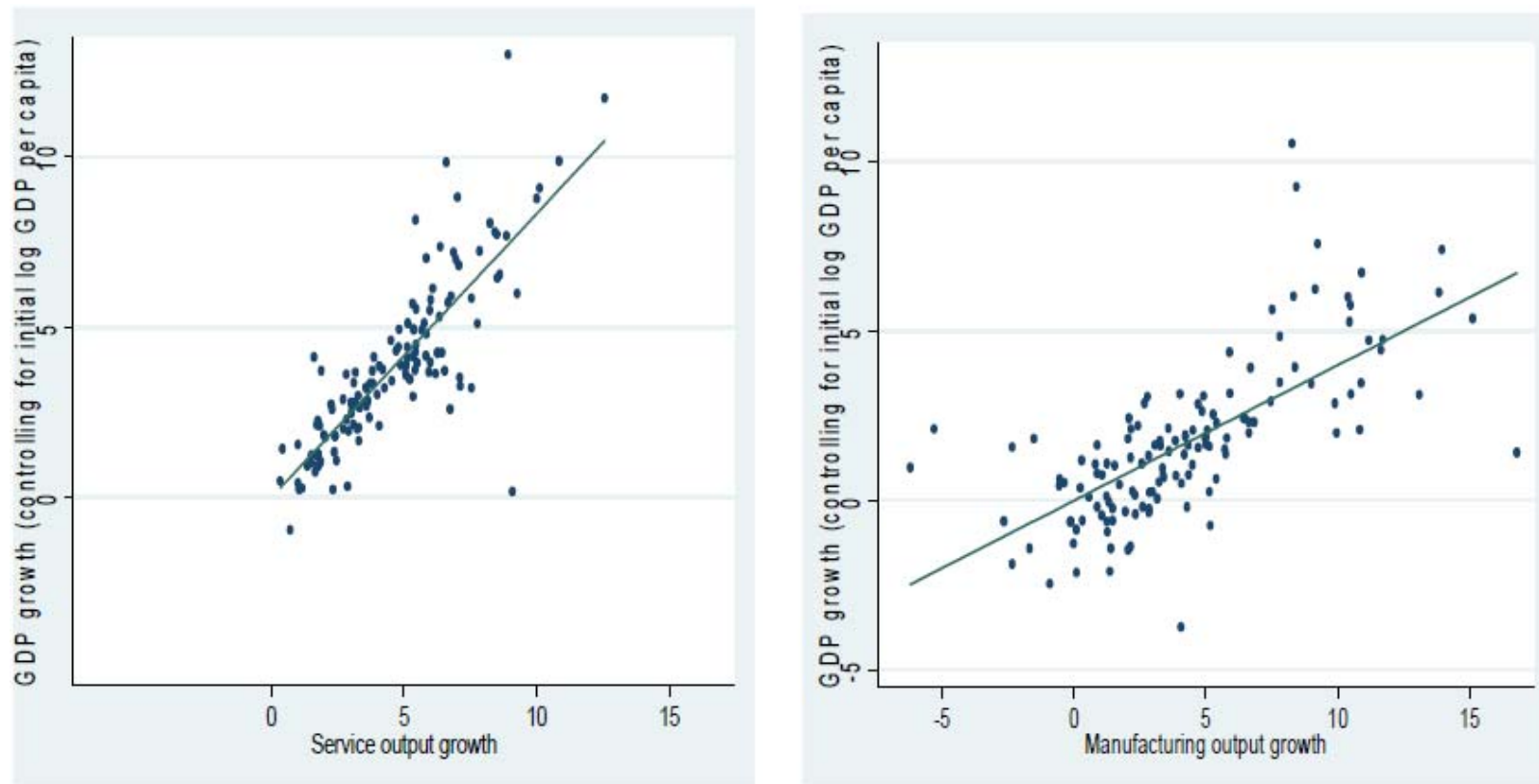
June 1-3

Soonhwa Yi
The World Bank

Roadmap

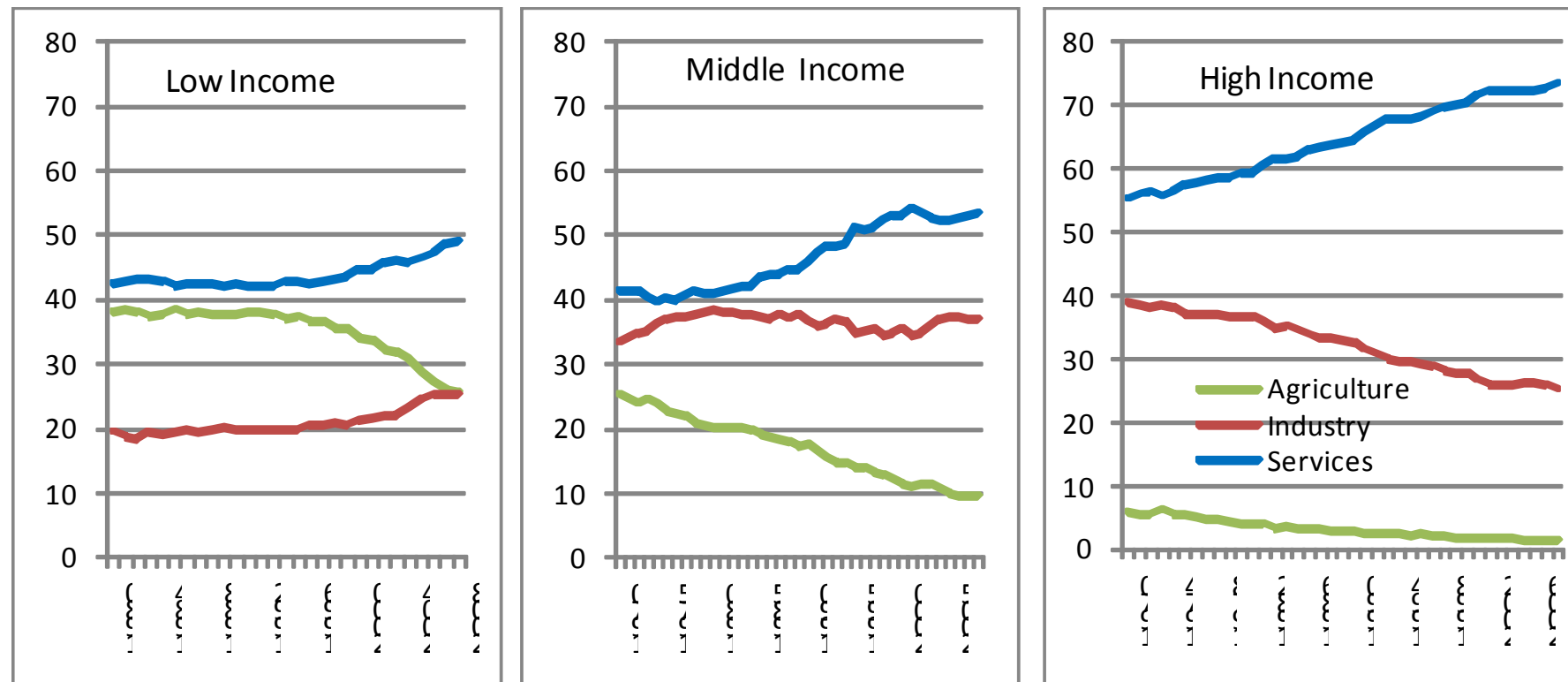
- Services: a driver for growth and poverty reduction
 - But lower productivity than in manufacturing
- Policies/regulations: an ingredient to efficiency
- Need to tailor policies and regulations to each sector, because of heterogeneity in services
 - Infrastructure
 - Domestic services
 - Business services
- Variables for policy success

Services as a driver for growth



Source: World Bank (2009), *The Service Revolution in South Asia*, Figure 1.3-4, p. 41

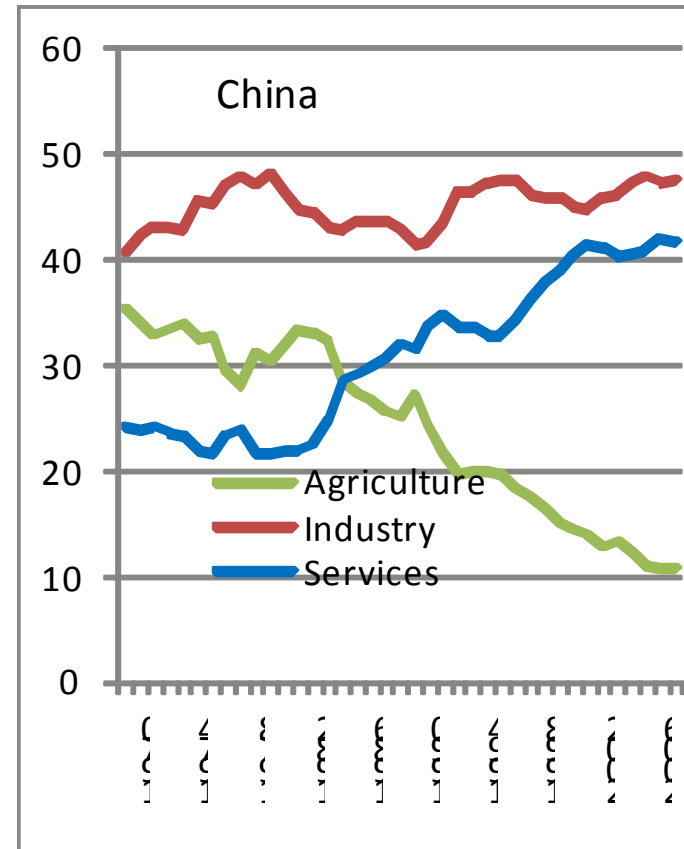
Service sector growth throughout economic evolution (% of GDP)



Source: World Bank, World Development Indicators

Sectoral development pattern: Early state of development

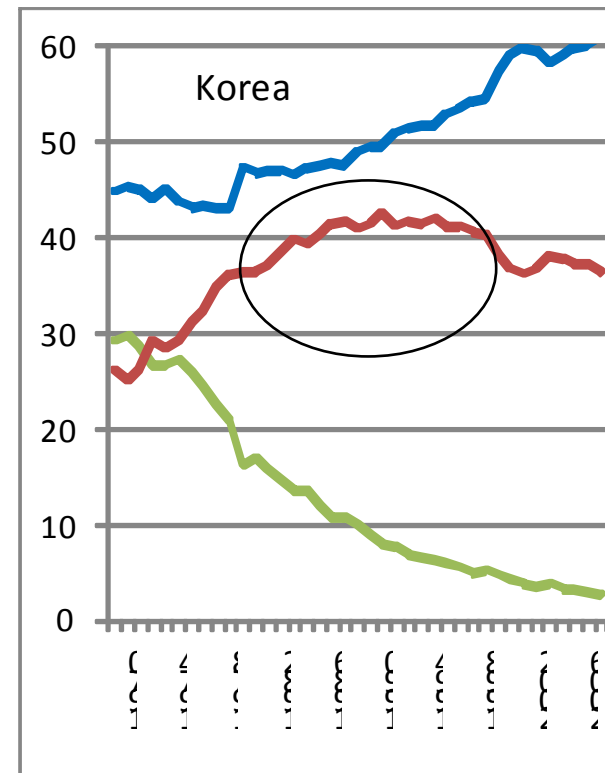
- Declining agriculture
- Fast growing industry
- Fast growing services to support industry



Source: World Bank, World Development Indicators

Middle income stage

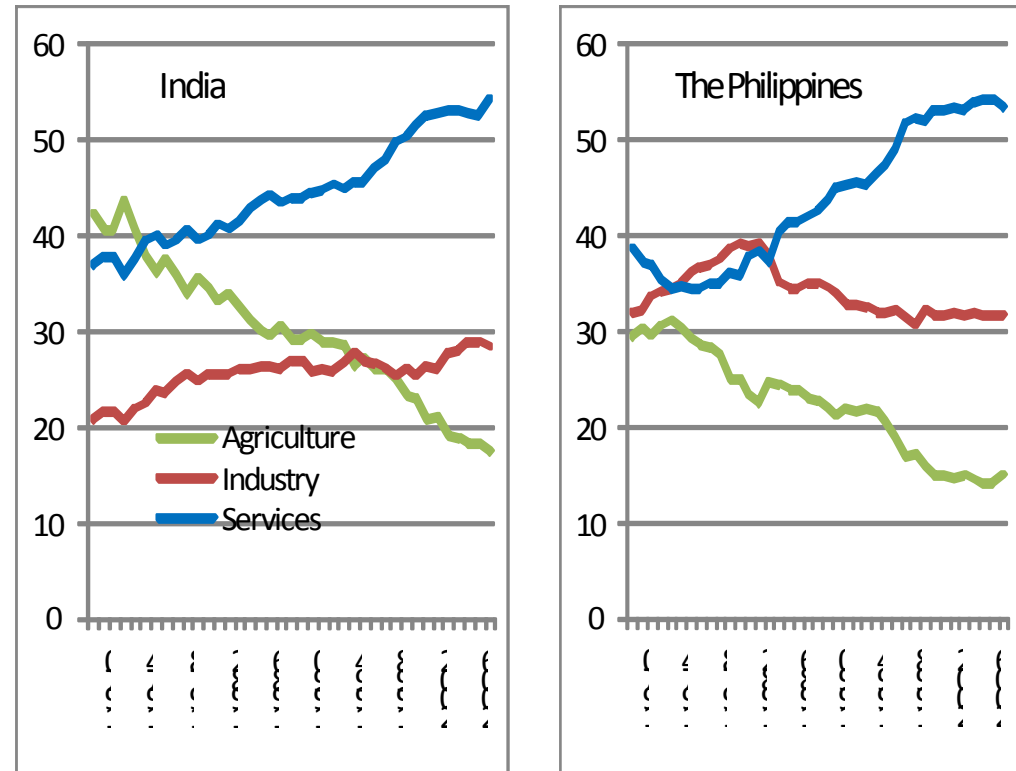
- Industry sector: A typical inverted U shape
- Continued services growth along the development curve



Source: World Bank, World Development Indicators

Services sector led growth in selected low, middle income economies

- Key business outsourcing destinations
- Built upon
 - Telecommunication liberalization
 - Talent pool
 - IT savvy and English proficient labor



Source: World Bank, World Development Indicators

Services as a driver for poverty reduction

Change in Poverty Headcount Regressed on Agriculture, Manufacturing, and Services Output Growth, for 50 Developing Countries (1990-2005)

					Sectoral Output Growth Weighted by Initial Share of Sector in GDP	
	(1)	(2)	(3)	(4)	(5)	(6)
Log GDP per capita initial			9.99*** (3.07)	9.82*** (3.36)	14.59*** (3.84)	13.87*** (4.26)
Initial level of poverty	-0.17* (0.08)	-0.17* (0.09)				
Growth in agriculture output	0.55 (0.97)	0.58 (1.04)	0.51 (0.91)	0.55 (0.97)	0.02 (0.02)	0.02 (0.02)
Growth in manufacturing output	-0.06 (0.46)	0.08 (0.44)	-0.01 (0.54)	0.11 (0.53)	-0.03 (0.02)	0.001 (0.02)
Growth in services output	-2.30*** (0.86)	-2.11** (0.89)	-1.92** (0.88)	-1.74* (0.91)	-0.02** (0.01)	-0.04*** (0.01)
India indicator		9.44** (4.22)		8.83** (3.71)		10.63*** (3.64)
China indicator		-24.48*** (5.48)		-23.01*** (5.35)		-27.51*** (8.84)
Bangladesh indicator		-3.99 (4.19)		-4.24 (3.24)		-2.06 (3.72)
Sri Lanka indicator		4.51** (1.98)		7.76*** (2.35)		9.25*** (2.58)
Control for time period	Yes	Yes	Yes	Yes	Yes	Yes
Observations	50	50	50	50	50	50

Source: World Bank (2009), *The Service Revolution in South Asia*, Table 1, p. 19

Services productivity: Lower than industry in East and Southeast Asian countries, whose key exports are manufacturing goods

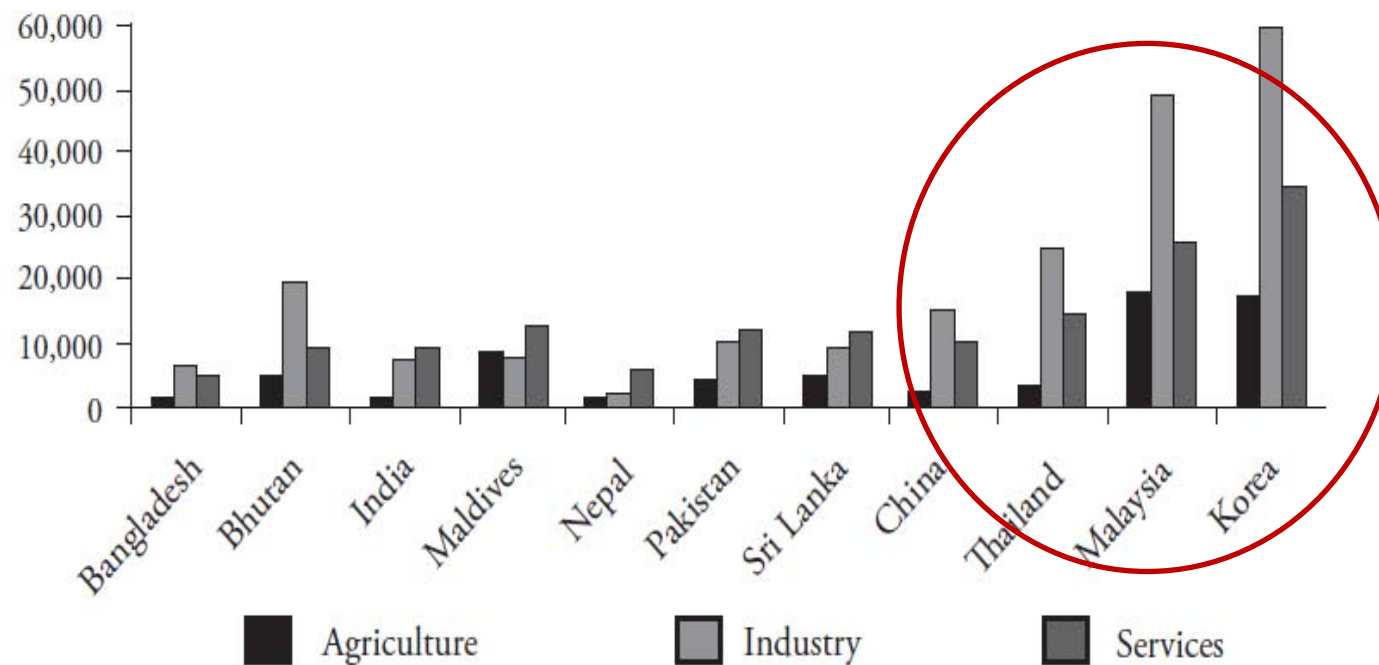


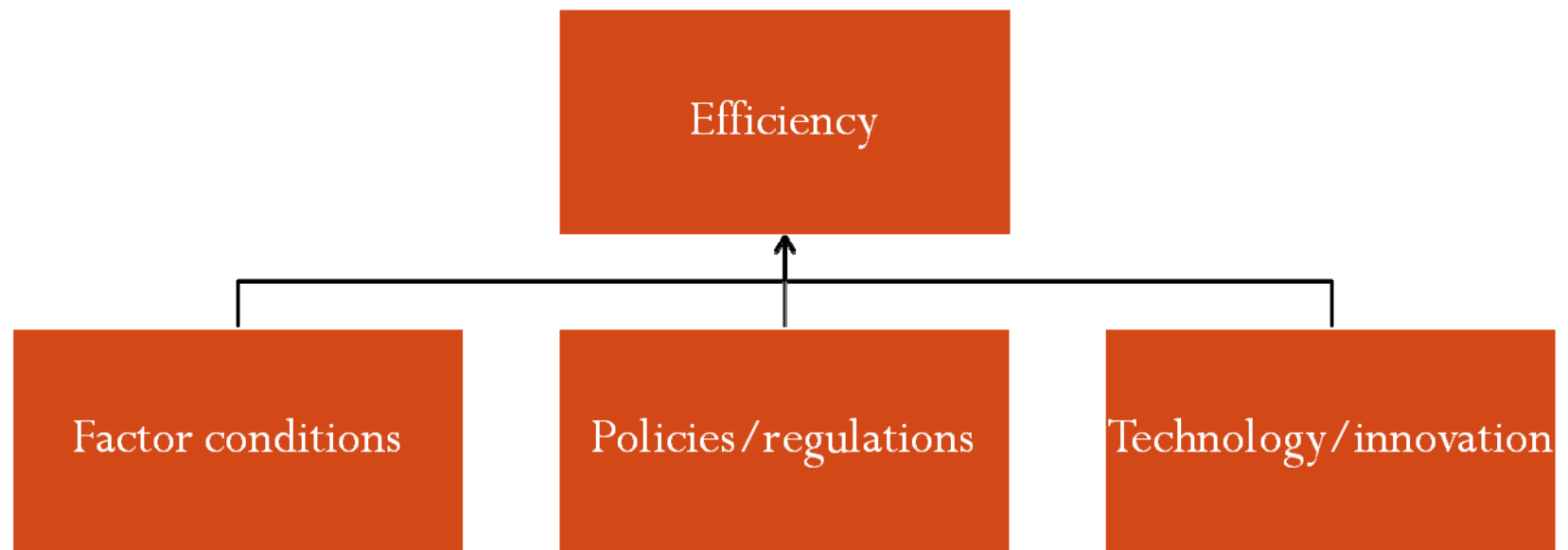
FIGURE 6 Labour Productivity Levels by Sector (2005)
(PPP international dollars per worker)

Source: World Bank (2009), *The Service Revolution in South Asia*, Figure 6.

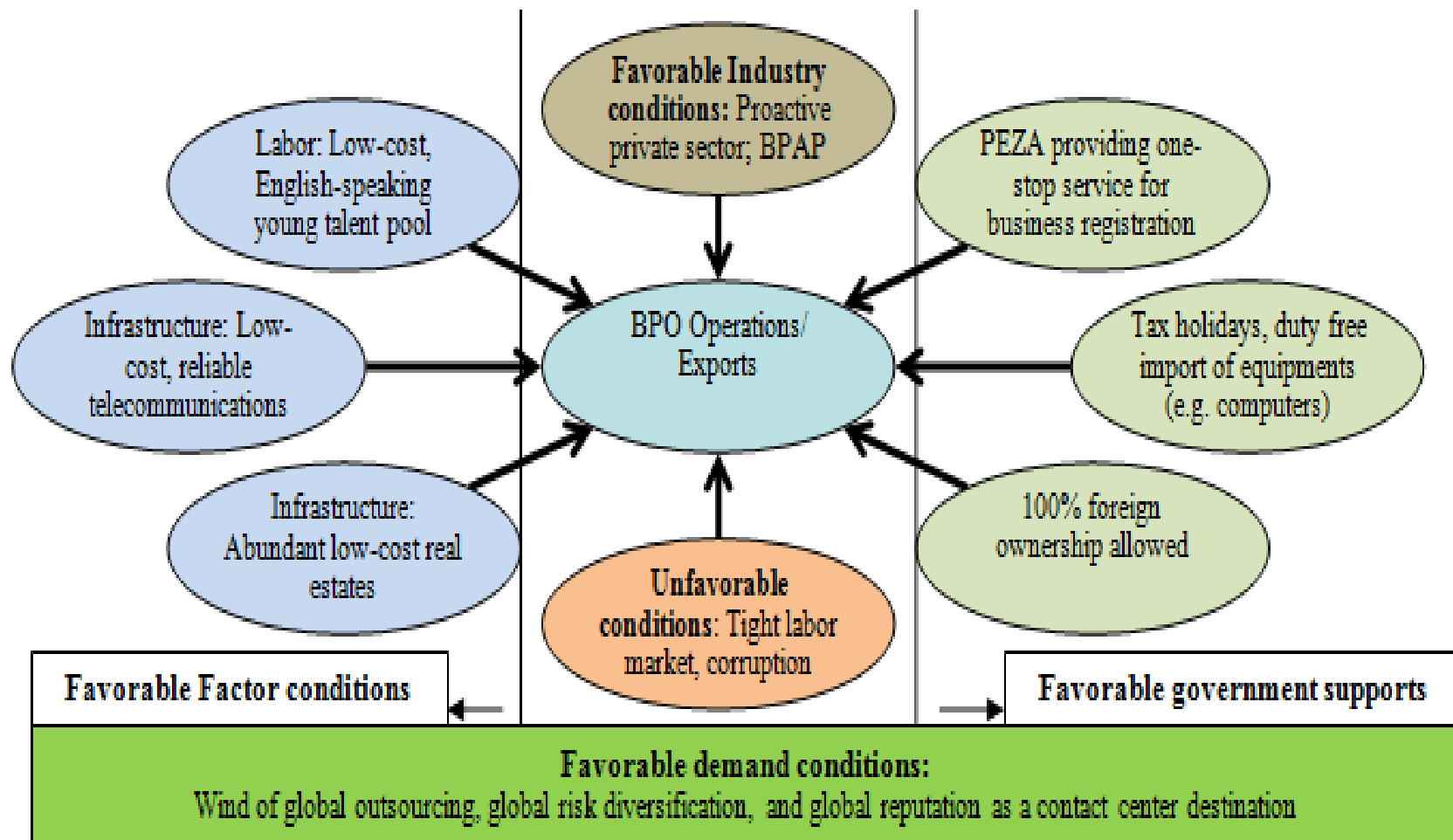
Roadmap

- Services: a driver for growth and poverty reduction
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Sources of efficiency



Example: Success of the Philippine BPO



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 - This categorization is borrowed from McKinsey Global Institute (2010)
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Policies and regulations for services

- Need to tailor policy and regulations to each sector because of
 - Heterogeneity
 - Intangible nature -> difficult to measure
 - Presence of market failures
 - High rates of firm entry and exit
 - Firms smaller than in manufacturing

Infrastructure services

- Sector: Telecommunications, Transport, Utilities (energy and water)
- Feature: Large economies of scale
- Key: to strike right balance between cost savings from large single operators and incentives to offer new, affordable services packages

Infrastructure services: Policies and Regulations

- Rules on competition
 - Reflecting the nature of higher entry and exit constraints
 - Positive relationship between easier entry and competition (e.g. the Philippines' deregulation in telecommunication and in domestic air transport market, Cebu Pacific, Zest Air)
 - Competition improved the allocative efficiency of the incumbent firms (Oum and Zhang, 1995)
 - Establish an effective universal access scheme
- Incentives for efficient private operators
 - Incentives to energy providers who promote higher energy efficiency among their customers (e.g. demand-side management –shifting energy demand from peak time to night-time, McKinsey, 2010)

Domestic services

- Sectors: Construction, Personal, Banking, Hotel and restaurant, Wholesale and retail services.
- Feature: Labor intensive, fast growing sectors and therefore needs to boost competition
- Key: Productivity through innovation and adaptation of best practices (e.g. adapting POS in Korea distribution services)
 - Use of ICT leads to efficiency increase

Domestic services: Policies/ Regulations

- Promote entry and exit
 - Liberalization
 - Knowledge spillover in merchandising and inventory management
- Flexible, low-minimum wage labor regulation
 - Labor rigidity is associated with informal employment
- Rationalize industry-specific regulations
 - Liberal zoning and the size of stores in retail services (e.g. Korea)
 - Flexible regulations on land
- Promote the use of ICT
- Foster entrepreneurship
 - Emphasis on SMEs as most services firms are in the form of SME
 - Improve access to finance to level the playing field

Business services

- Sectors: Professional, medical, IT-related services
- Feature: Skilled labor force
- Government intervention on building talent pool:
 - Support local research capabilities through government contracts
 - R & D subsidies or incentives to the private sector (McKinsey, 2010)
 - Promote the use of ICT and diffusion of innovations

Business services: Policies/ Regulations

- To enable effective competition
 - FDI in business service sector stimulates specialization and raises the productivity of the industry that uses them (Rivera-Batiz, 1992)
- So far, very little change in area of professional services restrictions (e.g. licensing)
 - Conducting mutual recognition agreements
 - Rationalizing quotas
- Creation of a business corridor (or a cluster) to take advantage of network and knowledge spillovers.

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Policy success is a function of

- Good data
- Streamlining regulatory system
 - Through interchange between the government and the private sector,
 - Government: tap private sector expertise
 - Private sector: effective engagement with the government, including SMEs
 - Alert the government changes and challenges they confront
 - Literature: Reductions in regulations are related to increases in productivity
- Utilizing growth diagnostics, business environment assessments, competitiveness studies, innovation audits, and product space analyses

Streamline Regulatory System

- Create database on regulations by sector
 - A starting point for regulatory reform
 - Useful for trade in services negotiations
- Constant update of regulations to reflect changes in business environment
 - e.g. Australia's "one in, one out" rule
- Regulatory reform based on sound analysis
 - Regulatory impact analysis (assessment)
 - Conduct both ex-ante and ex-post
 - Examine regulations vis-à-vis policy objectives
 - Measure changes in regulatory burden
 - Evidence- and data-based
 - Quantitative and qualitative analyses on costs and benefits
 - Propose cost-effective alternatives
 - Coordinate among different line agencies and Include stakeholders in the consultation process

Regulatory Governance

- Independent regulatory body
- Mechanism to resolve disputes between regulators and operators
- Clarity on the role of regulators
 - Set tariffs, penalize operators
- Transparency and participation of stakeholders in regulatory process

Conclusion

- Services is an engine for growth
- Need to improve efficiency
- Through sector-specific policies/regulations
- For success
 - Have a system in place to collect data
 - Streamline regulatory system using regulatory impact assessment for both ex-ante and ex-post regulations
 - Utilize growth diagnostics and other analysis
 - Have regulatory governance framework in place

Thank you

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