

EU-AUSTRALIA TRADE IN SERVICES PROJECT*

WORKSHOP REPORT ON TRADE IN FINANCIAL SERVICES

This Report summarises the discussions in the ‘Trade in Financial Services: exploring priorities’ session of the recent Workshop on trade in services. The session was held under Chatham House rules on the 26 July 2019 at the ANU Centre for European Studies (ANUCES). Participation was by invitation and participants came from a wide range of backgrounds. The Workshop sought to identify priority areas for the current European Union-Australia trade negotiations on financial services. Participants were provided with background material on trade in financial services and the OECD’s Services Trade Restrictiveness Index (STRI). This material will shortly be published as an ANUCES Briefing Paper.

The session commenced with participants asked to suggest two priority issues related to international trade in financial services. Participants noted that financial services trade is a particularly sensitive topic for trade negotiations, and almost always attracts a dedicated chapter in any agreement. It was suggested that a frequent barrier to effective trade agreement outcomes is a failure to focus on a select number of issues for improving access. Negotiators should therefore ask what it is they really want and seek to achieve gains in those areas.

Effective transmission of data emerged as the most discussed and agreed issue for trade in financial services. Such data include company and customer level information. The discussion suggested that requirements to hold data locally or to limit the transmission of sensitive data (such as that of customers) seriously limit trade in financial services. It was noted that data and privacy requirements are often economy wide (horizontal barriers to trade), with few sector-specific rules for financial services. But given how heavily financial services rely on the movement of data, it was generally agreed that pursuing financial services specific rules in a trade agreement would be an effective means for increasing trade in financial services. It was noted that the US Trade Representative has made data transmission a key goal in trade negotiations.

Several participants identified the United Kingdom’s exit from the European Union as a significant background issue, noting that the country is the EU’s largest centre for financial services. The UK’s exit will substantially split the market into which Australian financial services companies export. The EU is also conscious of ensuring post-Brexit access for financial services is substantially more limited than single-market rules. This is shaping the EU’s approach to third-country trade agreements that will influence both current negotiations with Australia and future negotiations with the UK. An important suggestion was that, given this, Australia should seek to incorporate a 3-year review into those parts of any trade agreement affecting financial services.

The history of financial services regulation in the aftermath of the Global Financial Crisis also weighs against increased liberalisation of market access rules. In particular, participants noted that the focus of central banks on financial stability has limited the scope for cross-border trade and commerce (mode one) except for services provided to wholesale and sophisticated investors. Some participants suggested that this reflects over-regulation and excessive caution, while others noted a trend towards increased financialisation as a significant risk to real economies and to tolerance of increased cross-border trade.

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It was generally accepted that the requirement for commercial presence (mode three) will remain the primary vehicle for market access, often driven by acquisitions of existing banks and insurers. The key explanation for this is the prudential ‘carve-out’ in all trade agreements, which protects the right of states to regulate for financial stability. This forms an important domestic policy basis underlying the requirement for commercial presence. Limited consumption abroad (mode two) and movement of natural persons (such as bankers – mode four) will continue. Here it is important to ensure arrangements for business visa and temporary residence visa work well.

Given the continued reliance on commercial presence as the primary means of market access, several participants raised limited competition in the Australian financial services market as a concern. The example of the high average cost of funds management compared to Europe was given. Some participants suggested that the significant concentration of Australia’s banking and insurance industries reflects a failure of competition policy that can only be addressed through domestic microeconomic reform. In the absence of such reform, foreign companies will struggle to establish a presence in the Australian market except through mergers and acquisition (a spate of foreign acquisitions is currently occurring in the Australian insurance industry). The workshop noted the 2018 Productivity Commission report on Competition in the Australian Financial System.

Towards the end of the session, discussion turned towards identifying restrictions that can be subject to negotiation in the proposed EU-Australia trade agreement. It was generally accepted that the OECD’s Services Trade Restrictiveness Index (STRI) offers a useful means to identify priority barriers to trade in commercial banking and insurance. It was, however, noted that many of the barriers identified in the STRI are difficult to reduce given the context discussed above. The value of alternatives to the STRI appeared mixed.

Several participants noted significant data limitations in assessing services trade barriers and in valuing existing services trade, particularly due to the commercially sensitive nature of the data and the impact of currency fluctuations.

There was strong agreement that foreign direct investment data are very important in measuring trade in financial services given the degree to which such services are delivered through commercial presence in the country.

It was noted that data for Global Trade Analysis Project (GTAP) models are collected infrequently and were initially intended for use in developing countries, so can be fairly poor measures of the underlying variables (e.g. they are quite ‘noisy’). There was significant debate over the use of computable general equilibrium (CGE) models, with several participants noting that such modelling is challenging for services trade, since it notably doesn’t take full consideration of foreign direct investment. It was suggested that one needs to be sceptical of the models and wary of the data used, and that these models can significantly underestimate imports and exports of services.