Mike Moore: Financial services and the WTO

Remarks by Mr Mike Moore, Director-General of the World Trade Organization, at a Working Dinner of Central Bank Governors held at the Bank for International Settlements in Basel on 11 September 2000 (prepared speech; not a verbatim transcription).

* * *

I am grateful for the opportunity to talk to you today. The timing is good because we have started new negotiations on trade in services in the WTO that will certainly include talks on the liberalization of trade in financial services, an area of great importance to you and to all WTO Members.

Financial services has always been seen, from the start of the discussions about whether the GATT should deal with services at all, as a special and controversial sector in terms of its strategic importance and political sensitivity: not only is it the largest of all internationally traded services, and the backbone of all other economic activity, but it is also a key tool for the control of national economies. For some governments the achievement of greater freedom and security to offer banking, securities and insurance services in foreign markets was the pre-eminent objective of the Uruguay Round. Without the insistence of the banking and insurance industries of the US and other countries on bringing trade in services, and financial services especially, under the framework of multilateral law, there would have been no services agreement in the WTO.

In the early stages of services negotiations, many developing countries were hesitant. They feared that competition and increased participation and influence of foreign financial institutions would threaten their control of the key levers of the national economy, as well as their national financial institutions. But even in the developed world there were some underlying systemic doubts: finance ministries in a number of countries were initially doubtful about the value of a multilateral approach to financial services. They had been comfortable with bilateral negotiation of banking licenses and other rights - based mostly on reciprocity - and were not convinced of the virtues of granting most favoured treatment, nor comfortable with the prospect of decisions being subject to dispute settlement in the multilateral framework. The relative openness of financial markets at the time, at least in the developed world, made the need for change less obvious. It seemed worthwhile to embark on multilateral negotiations only if the results promised something better than what was already there. And a key element in the calculus was how far developing countries would join in the negotiations.

Two conflicting approaches - the high ambitions of some developed countries and the nervous caution of developing countries - are reflected in the long history of the negotiations and in the GATS itself. The Agreement's design - a framework of rules coupled with national schedules of commitments - allows governments to decide which sectors they will open to competition by guaranteeing the rights of foreign suppliers and also the extent of those rights. The GATS commitments of many WTO Members do not offer unrestricted access to their markets. But significant progress has been made, and the groundwork completed for moving ahead with liberalization in future negotiations.

Despite the tension and sensitivities surrounding the early discussions, today 106 WTO Members have commitments in the sector - more than in any other sector except tourism. Not all of those commitments involve liberalization - often they are bindings of the existing level of access and regulation. Let us not forget that in trade negotiations liberalization is always incremental; in the case of services this is more so since the principle of progressive liberalization has been expressly recognized.

We sometimes forget that the financial services negotiations that successfully concluded in December 1997 coincided with the financial crisis in Asia. Contrary to what some might have feared, the crisis had no impact on the negotiations: no country withdrew or wrote down the commitments it had negotiated. Even the Asian countries most seriously affected made commitments to improve access to their markets for foreign financial institutions. They did so in the belief that stronger competition and greater openness would make their national financial infrastructure stronger, not weaker. In fact, the crisis seems to have strengthened the conviction that competitive financial markets are essential to restore confidence and induce the long-term investment needed for growth and development.

Several factors made it easier for crisis-ridden countries to embrace the WTO negotiations. First, the negotiations were not concerned with the liberalization of the capital account, but purely with the terms on which foreign suppliers would be allowed to do business, subject to whatever capital controls were in force. While it is true that a government is required to allow capital flows when the country has a commitment liberalizing the supply of a service requiring such capital movement, the capital account liberalization involved is limited in extent.

Second, the liberalization of financial services trade takes place inside a system of rules and procedures with the necessary flexibility and safeguard clauses to address prudential concerns. Governments are free to take any measure necessary to preserve the stability of the financial system and also temporary, non-discriminatory restrictions on trade in services in the event of serious balance-of-payments and external financial difficulties. In fact, nothing in the services agreement curtails governments' ability to pursue sound macroeconomic and regulatory policies.

Third, these particular negotiations were mostly about allowing foreign institutions to establish in the market - entailing foreign direct investment - to provide services and bring technology, capital and expertise with them. This was seen not as an additional threat, but as part of the answer to the crisis. Commitments in the WTO provide a guarantee that the terms and conditions on which investment decisions are made, and trade is carried on, are not going to change overnight. Since nothing chills investment more than uncertainty about the direction of government policy, such guarantees are valuable to traders and investors, as well as to governments wanting to attract foreign investment.

The financial industry in the US, Europe and Japan has been active in formulating positions for the negotiations that began this year. The liberalization of the rights of establishment and operation for suppliers remains essential for the provision of most financial services, and there will be calls for further liberalization on this front. At the same time, technological advances in telecommunications and informatics are radically changing the manner in which financial services are traded, making cross-border trade increasingly important. The negotiations will certainly seek improved access and greater security for this type of trade. This issue is also relevant to the ongoing work on electronic commerce.

Now, what can we do to ensure successful conclusion of these negotiations? There is much that can be done, especially in creating conditions favourable to further liberalization. Many countries, particularly developing countries, lack the necessary institutions, regulatory structures and legal frameworks needed to support a fast-changing, modern economy. In a sense we find ourselves between two worlds - between an economic system which is increasingly global and a patchwork of institutions and structures which remains largely national in scope.

More generally, there is a continuing need for vigorous international dialogue and cooperation. The efforts being made by the *BIS* and other international fora are critical for confidence and stability in the financial systems of the world, which in turn is a key requirement for keeping the trading system open.

We need to make the markets work. Adequate prudential regulation and supervision, enhanced transparency and corporate governance, strengthened competition policy, provision of safety nets and proper legal and accounting systems are all preconditions for countries to be able to take advantage of the sizeable benefits of liberalization. Your contribution on these fronts is crucial to our efforts.

Thank you.