UNITED STATES COUNCIL FOUNDATION

The Benefits of U.S.-China Trade in Services

By Dr. Craig VanGrasstek

United States Council Foundation
Occasional Paper No. 1
July 2006

UNITED STATES COUNCIL FOUNDATION

The Benefits of U.S.-China Trade in Services

*By Dr. Craig VanGrasstek**

* Dr. Craig VanGrasstek is the Executive Director of the Program on Trade and Negotiations in the John F. Kennedy School of Government (Harvard University). He is the author of numerous studies on trade policy, including ***GATS: The Case for Open Services Markets*** (OECD, 2002).

United States Council Foundation

Occasional Paper No. 1

July 2006

The United States Council Foundation is a 501(c)(3) educational foundation affiliated with the United States Council for International Business.

United States Council Foundation
United States Council for International Business
1212 Avenue of the Americas
New York, NY 10036
Tel: (212) 354-4480 Fax: (212) 575-0327 Web: www.uscib.org

Executive Summary

Trade in services is a key aspect of the U.S.-China economic relationship, and one with multiple benefits for the United States. As a member of the World Trade Organization (WTO), China has reduced or removed many of its earlier barriers to trade and investment. The liberalization of China's trade regime has meant a vast increase in the opportunities for U.S. services exporters. At around $70 billion, China's market for services is already the world's sixth largest, and can be expected to grow with the expansion of the economy.

The service sector is the largest and most significant part of the American economy. Private services now account for more than two-thirds of the U.S. economy, and more than four-fifths of the workforce. Services are also an increasingly important part of U.S. trade. Over the past generation, services have gone from one-fifth to nearly one-third of exports, growing twice as fast as exports of goods.

The rules of the global trading system cover services as well as goods. The General Agreement on Trade in Services (GATS) requires, with some exceptions, that governments cannot discriminate between service suppliers from different countries, or between domestic and foreign firms. The GATS offers a framework for the negotiated reduction or elimination of barriers, while also setting limits on the imposition of any future restrictions. Like other agreements administered by the WTO, the obligations made under GATS are binding and enforceable.

China acceded to the WTO in 2001, the same year that the United States granted permanent normal trade relations to that country. A market that was once protected by high tariff walls and discriminatory restrictions on foreign investment is now in transition, and becoming much more open to business. Some of the most significant Chinese commitments, such as the final phase-ins for banking, architectural and engineering services, are scheduled to be fulfilled by December 11, 2006 (i.e., five years after accession). Exports of U.S. services to China began to grow sharply as soon as China joined the WTO. In 2004, the United States exported $11.30 in services to China for every $1 in services that it imported from that country. Some segments of the Chinese market remain protected, but new commitments might be negotiated in the Doha Round of WTO talks. Moreover, any disagreements that emerge over China's implementation of its commitments can be brought before the WTO's Dispute Settlement Body for adjudication and enforcement.

Three case studies offer concrete examples of how services trade with China is growing. The Chinese economy offers a large and rapidly expanding market to export-oriented service industries such as express delivery (the UPS case), information technology (the EDS case), and banking (the Citigroup case). Access to the China market benefits not only these firms, but also their partners in the United States. Their presence in China connects U.S. companies to producers that operate in China, and also to an emerging Chinese middle class.

Despite the benefits of trade between the United States and China, there remain many and varied sources of friction in this relationship. Those troubles sometimes lead to demands for "tough" measures such as trade sanctions. These often entail the threat to link Chinese access to the U.S. market to other issues in the relationship. It would be shortsighted, however, for the United States to take precipitous unilateral action that endangers trade relations with China. They might be aimed at Chinese goods, but they would almost certainly hit U.S. services as well.

Introduction

The Chinese market offers a huge opportunity for U.S. exporters of goods and services. As of 2004, China's 1.3 billion population accounted for one-fifth of the world's total. Its economy is now the fifth-largest in the world, and among the fastest-growing. While experts disagree on how long China can sustain growth rates of around 10% per year, it is virtually inevitable that the world's largest population will also become the world's largest market.

The relationship between the United States and China is multifaceted, covering a range of economic, social, political, and security issues. Each of these areas offer prospects for mutually beneficial cooperation, but they also produce tensions. Demands for a "get-tough" approach with China often lead to proposals that trade sanctions be threatened or imposed as a means of pursuing U.S. interests in non-trade issues.

While trade sanctions might be targeted at China, they are just as likely to damage U.S. economic interests. The services sector is the leading edge of the economy, accounting for large and growing shares of jobs and exports. The opening of the Chinese economy has brought great benefits not only to export-oriented service industries such as express delivery, information technology, and banking, but also to U.S. exporters of goods. It would be self-defeating for the United States to take precipitous, unilateral action that jeopardizes this relationship at the very time that it is coming to economic fruition. The World Trade Organization offers a forum in which to deal with access to the Chinese market, both through the negotiation of commitments and the adjudication of any disputes that may arise over market access; disputes outside of the trade arena can and should be handled elsewhere.

The Rising Importance of Services

Trade in services is a key aspect of the U.S.-China economic relationship, and one with multiple benefits for the United States. Services encompass such wide-ranging activities as travel and tourism, banking, insurance, entertainment, law, software, and telecommunications. Much of this so-called tertiary sector is more capital- and knowledge-intensive than either the primary sector (agriculture, mining, forestry, and fisheries) or the secondary sector (manufacturing and construction). Services are the largest and most significant section of the American economy, and account for much of the growth in U.S. exports.

Table 1:
Services in the U.S. Economy, 1980-2005

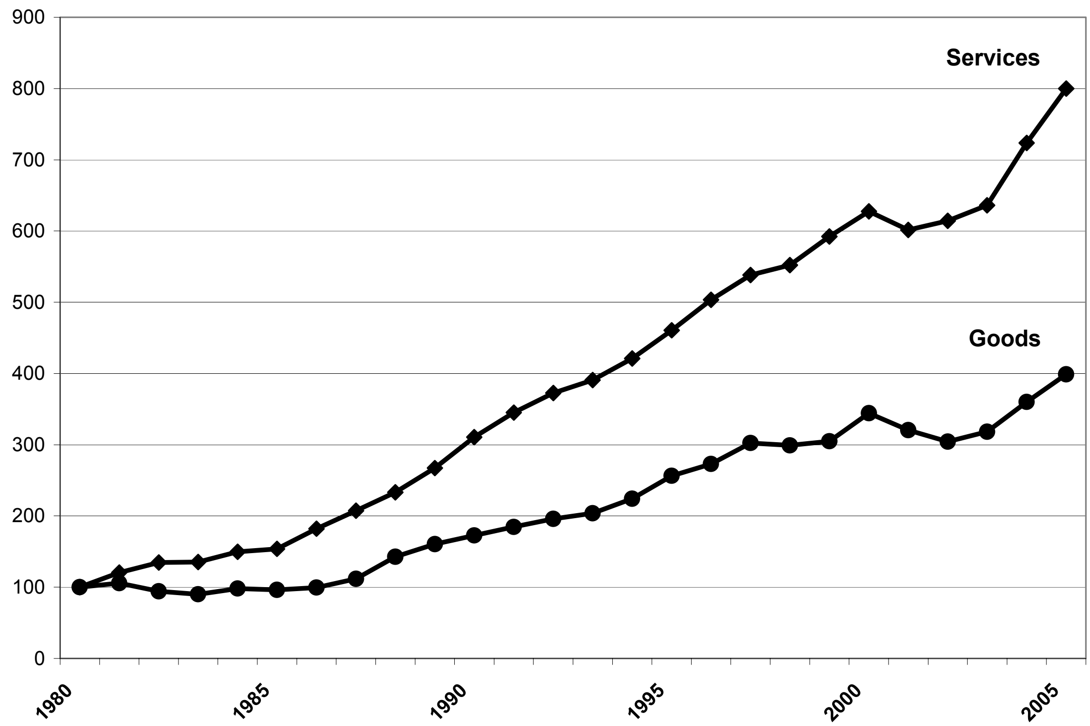
The Services Sector as a Percentage of Total

	Jobs	GDP	Exports
1980	73.2	56.1	19.6
1985	75.8	59.9	26.4
1990	78.3	62.4	28.2
1995	80.3	64.6	28.2
2000	81.3	66.5	28.5
2005	83.4	68.2	30.5

Source: Jobs and exports calculated from Council of Economic Advisors data; GDP from Bureau of Economic Analysis data.

Figure 1: Growth in U.S. Exports of Goods and Services, 1980-2005

Level of Exports in 1980 = 100



Source: Calculated from Bureau of the Census data.

Role of Services in the U.S. Economy

Services dominate the post-industrial U.S. economy. As of 2005, the United States produced $8.5 trillion worth of private services, accounting for more than two-thirds of gross domestic product (GDP). As shown in Table 1, the service sector is the most important employer in the United States. Over 111 million Americans were employed by service industries in 2005, accounting for more than four-fifths of the workforce. Services are also an increasingly important part of U.S. trade. Services have gone from one-fifth to nearly one-third of exports since 1980. The data in Figure 1 show that services exports during 1980-2005 grew exactly twice as fast as exports of goods.

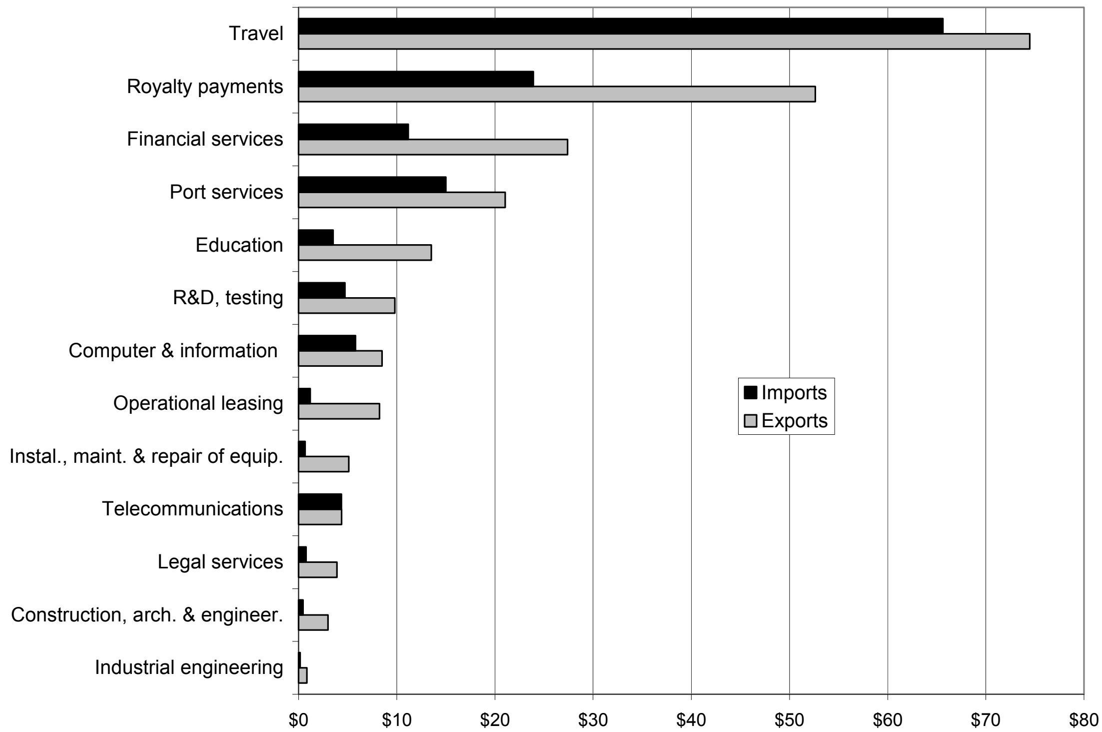
The data in Figure 2 illustrate the main service sectors in which the United States has a strong competitive advantage. While trade is roughly in balance for some important sectors, notably travel and telecom, the United States runs major surpluses in others. Multinational firms also derive significant income from the royalty payments they receive for licensing their products and processes, and from leasing their equipment.

Services in the Trading System

Services first became a major issue in trade negotiations in the early 1980s, when it was among the “new issues” that the United States brought to the negotiating table. Together with investment and intellectual property rights, this cluster of issues served the interests of competitive industries that were just then moving into mass production (e.g., computers and software), expanding international operations (e.g., financial services), or had been excluded from previous trade negotiations (e.g., motion pictures and television).

Figure 2: The Leading Sectors in U.S. Services Trade, 2004

Billions of Dollars



Source: Calculated from U.S. Department of Commerce data.

Putting this issue on the table required that negotiators get past a series of myths, as summarized in Box 1, that led many to underestimate the potential economic gains. Analysts and policymakers eventually caught up with the real world, where computers and other advances were revolutionizing how business is done and what is traded.

One of the main U.S. accomplishments in the Uruguay Round (1986-1994) of multilateral trade negotiations was to incorporate services fully into the rules of the trading system. This was done through the General Agreement on Trade in Services (GATS), which was largely modeled on the goods-oriented General Agreement on Tariffs and Trade (GATT). Like GATT, the GATS requires that signatories extend universal and unconditional most favored nation (MFN)[1] treatment to one another, as well as national treatment. These rules of nondiscrimination provide, albeit with some significant exceptions, that governments cannot discriminate between service suppliers from different countries, or between domestic and foreign firms. The GATS offers a framework in which countries can negotiate commitments, and thus reduce or eliminate existing barriers while also setting limits on the imposition of any future barriers. Both GATT and GATS, together with rules in many other areas, are now part of the World Trade Organization (WTO). All of the obligations and commitments under these agreements are binding and enforceable.

Box 1:
Debunking Myths About Trade in Services

Myth #1: Services Jobs Are Low-Paying

While it was once common to dismiss service jobs as low-wage, entry level occupations, that is an outdated and oversimplified view. This sector is found at both the top and the bottom of the wage scale, and everywhere in-between. It is true that, by comparison with the average national wage of $19.14 per hour for fulltime work, pay is relatively low for purely domestic occupations such as waiters and waitresses ($4.61), housekeepers ($8.34), and cashiers ($9.49). Many service-sector occupations receive far better compensation and benefits, including several that are prominent among traded services. Some of the best-paid American workers are computer programmers ($29.05), engineers ($36.59), college teachers ($41.96), lawyers ($48.63), and airline pilots ($118.58).[2]

Myth #2: Services Are Not Traded

A generation ago, economists would commonly refer to services as the "untraded" sector of the economy. Textbooks would typically point to haircuts as the ideal example of an untradeable service. That misconception stemmed from the idea that trade consists solely of cross-border sales, in which the tradeable moves while the buyer and seller remain in place. While haircuts cannot literally be shipped across a border, there are three other "modes of supply" by which they can be traded: via consumption abroad (e.g., a traveler gets her hair cut while in another country), commercial presence (e.g., the Hair Cuttery establishes a foreign franchise), or the movement of persons (e.g., a barber plies his trade in another country). And haircuts are by no means the only services that are exported. Today, there are virtually no service sectors that are entirely outside the global marketplace, whether they are performed in the country of consumption, delivered from the company's home base, or through electronic commerce (i.e., over the telephone and Internet).

Myth #3: Services Compete with the Other Sectors

It is true, but quite misleading, to note that the relative growth of one sector means that other sectors experience a proportionate reduction in their share of GDP. The fact that the share of the economy held by agriculture, manufacturing, etc., is declining does not mean that services work to their detriment. To the contrary, a vibrant services sector contributes greatly to the increasing sophistication and specialization of primary and secondary industries. America's farms and factories need innovative services to maintain and improve their own competitive edge. Manufacturers, for example, not only rely upon a strong research and development base, but also depend upon such services as advertising, express delivery, and communications to expand sales, speed transactions, and reduce costs. These benefits redound to both businesses and their employees.

U.S. Trade Relations with China

The attractions of selling to the world's most populous country are obvious, but the actual magnitude of bilateral trade has long been hobbled by political restraints. War, revolution, and other frictions acted to slow bilateral trade for generations. It was not until China completed its accession to the WTO in 2001, and Congress agreed to extend permanent normal trade relations, that the two countries established a truly normal commercial relationship. The years since China's accession have been the first time that trade relations have been relatively free from political constraint, and conducted on the basis of multilaterally agreed rules.

While trade relations are now normal, they are not free from conflict. The year 2001 was also the first time that China surpassed Japan as the leading source of the U.S. trade deficit, a distinction that has attracted considerable attention to the relationship. That deficit is on only one side of the ledger: While the United States continues to run a deficit with China on trade in goods, the balance on services is in the U.S. favor.

Growth and Liberalization of China's Economy

China's economy is much more integrated in the world market than it was just a few years ago. As of 1990, exports of goods and services accounted for 19% of China's GDP, and imports for 16%. By 2004, the external sector's share rose to 34% for exports and 31% for imports. This has meant a vast increase in the opportunities for U.S. services exporters. China's imports of commercial services in 2005 were valued at $71.6 billion, or more than seventeen times larger than they were in 1990.[3] China is already the world's sixth-largest market for services, and can be expected to grow with the expansion and liberalization of the economy.

From the perspective of U.S. services exporters, the most significant development is the emergence of China's middle class (sometimes called "Chuppies"). With average annual incomes well above those of the $1,500 average for China, members of this burgeoning group enjoy incomes that are closer to the $26,660 average for Hong Kong residents.[4] The middle class already constitutes about one-fifth of the Chinese population, and is expected to double by 2020.[5] Those consumers are eager purchasers of U.S. exports, whether in the form of services (e.g., travel) or goods that depend upon services for their sales (e.g., consumer products that are ordered on the Internet and shipped to China by express delivery).

China made substantial commitments in its WTO accession, especially in the areas of investment and services. A market that was once protected by high tariff walls and discriminatory restrictions on foreign investment is now in transition, and becoming much more open to business. Some of the most significant Chinese commitments are scheduled to be fulfilled by December 11, 2006 (i.e., five years after accession). For example, all geographic and customer restrictions on the local currency businesses of foreign-invested banks will be removed, and China is to allow wholly foreign-owned enterprises in architectural, engineering, and integrated engineering services. The last of China's WTO commitments in insurance will allow wholly foreign-owned insurers to engage in a wide range of transactions, and China will lift all geographic restrictions on mobile voice and data telecom services for joint ventures.

While China's market is much more open now than it was pre-WTO, a number of restrictions remain in place affecting specific sectors. The Doha Round of multilateral trade negotiations offers an opportunity to obtain further GATS commitments from China. Moreover, any disagreements that might break out over China's implementation of its commitments can be brought before the WTO's Dispute Settlement Body, an institution that has much sharper "teeth" than did the old GATT regime.

U.S. Services Exports to China

American exports of services to China began to grow as soon as China initiated the phase-in of these commitments in late 2001. Exports here come in two forms: Those services that are sent directly to China from the United States, and those that are sold in China by the non-bank, majority-owned foreign affiliates (MOFAs) of U.S. firms.[6] While cross-border exports of U.S. services have increased, MOFAs account for the most significant growth in services exports to China . These include branches, franchises, and other affiliates. Chinese laws and regulations had prohibited or discouraged the establishment of such branches in many industries, but those rules were significantly liberalized in the WTO-accession commitments. As can be seen from the data in Figure 3, MOFA sales have quickly grown to around one-third of U.S. services exports to China. As of 2003 (the last year for which both cross-border and MOFA data are available), the United States exported $6.0 billion worth of services to China on a cross-border basis, and exported another $3.8 billion in services by way of MOFAs. Both types of service exports can be expected to expand as the final phases in the WTO commitments take effect. Cross-border exports alone increased by 20.5% in 2004.

The data in Table 2 offer more detail on trade in specific sectors. It must be stressed that these numbers count only the transactions that are conducted on a cross-border basis; the U.S. Department of Commerce does not provide industry-level data on sales of services by MOFAs. Because these numbers are not capturing the transactions that are being conducted in the fastest-growing segment of U.S. exports of services, they tend to underestimate the level of U.S. exports, and hence the magnitude of the U.S. surplus, in many of these sectors. The available data nonetheless underline the point that in most private services, the level of U.S. exports to China is far in excess of U.S. imports from China. Even when MOFA sales are excluded, the United States exported $11.30 in services to China for every $1 in services that it imported from that country in 2004.

China is an especially important consumer of U.S. education services, being second only to India as a source of foreign students. Cross-border exports in this sector are 70 times larger than imports. In some important sectors the United States imports virtually no services from China (e.g., insurance and operational leasing), while in several others the level of exports are far higher than the imports (e.g., construction, architectural, and engineering services).

Case Studies

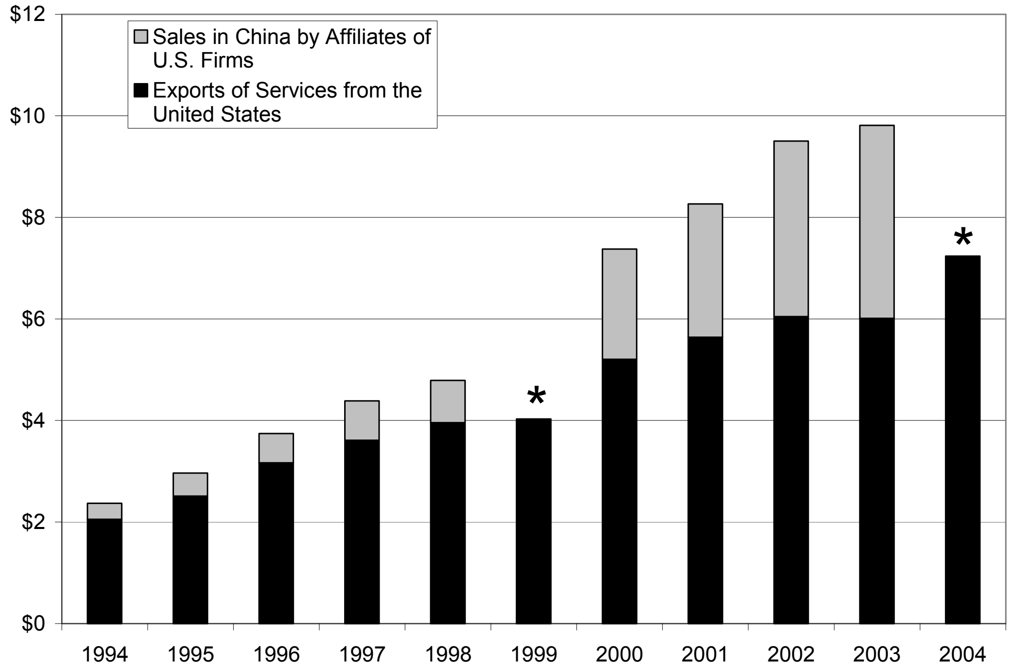
The three cases below offer concrete examples of how services trade with China works to the advantage not only of the services providers themselves, but also to other U.S. firms that export goods and services. While every company’s experience will be unique in some respects, the stories for UPS, EDS, and Citigroup are broadly representative of the opportunities that China now offers for competitive U.S. firms. The companies profiled here provide services that facilitate the exports of other American companies.

Shipping and Supply-Chain Management: UPS

In the century since it was founded, the former United Parcel Service has moved from horse-drawn carts and intra-city operations to a high-tech, worldwide presence. The company is the third-largest private employer in the United States, and around 60% of its 407,000 employees are union members. Known primarily for its express shipping and cargo services, as well as for those ubiquitous brown trucks, UPS also offers a much wider array of business solutions to its over one million customers worldwide.

Figure 3: Growth in U.S. Exports of Services to China, 1994-2004

Billions of Dollars



** : MOFA data are not available for 1999 and have not yet been published for 2004.*
Source: Calculated from U.S. Department of Commerce data.

Table 2:
U.S. Cross-Border Trade in Private Services with China, 2004

Millions of Current Dollars

	Exports	**Imports**	**Balance**
Total	**2,882**	**255**	**2,627**
Education	1,260	18	1,243
Financial services	165	20	145
Telecommunications	90	54	36
Insurance	23	0	23
Business, professional, and technical	1,216	154	1,062
Operational leasing	415	0	415
Construction, architect. & engineering	328	7	321
Installation, maintenance & repair of equip.	199	19	180
Legal Services	60	16	44
Management, consulting & public relations	53	8	45
Computer and information services	48	7	41
Research, development, and testing	14	17	-3
Advertising	6	18	-12
Industrial engineering	(D)	2	(D)
Other	(D)	60	(D)
Other private services	127	9	118

Source: Calculated from U.S. Department of Commerce data.
(D) = Suppressed by the Department of Commerce to avoid disclosure of data of individual companies.
Note that "0" can mean more than zero but less than $500,000.

China is one of the 200 countries and territories in which UPS now operates. It first entered the Chinese express shipping market in 1988, working through an agency agreement with a government agency called Sinotrans. A Closer Economic Partnership Agreement (i.e., free trade agreement) between China and Hong Kong opened up new investment opportunities for UPS in 2004; other international shipping companies established similar operations the next year, taking advantage of the commitments that China made in its accession to the WTO. UPS's main areas of operation in China are in the regions surrounding Beijing, Hong Kong, and its hub in Shanghai. This has been a wholly-owned venture since 2005.

The Chinese market is proving lucrative for UPS, but what can "brown" do for other American businesses? The most obvious point is that large volumes and a local presence translate into low-cost, high-speed shipping for U.S. exporters, allowing even small and medium enterprises to thrive in a just-in-time, low-inventory, build-to-order world. UPS also provides a full array of services and solutions that are tailored for small and medium-sized enterprises (SMEs) that are often new to international business. The subsidiaries of UPS provide aid in logistics (UPS Supply Chain Solutions), leasing (UPS Capital), as well as insurance and other financial services (Glenlake Financial Corporation). Six years ago UPS changed its focus from satisfying customer's small package needs to enabling global commerce. Global commerce requires customized solutions and more logistics and supply chain management. Any firm with goods in the United States and customers in China can use these services to bring them together at low cost and low risk.

The growing volume of traffic between the United States and China has ancillary benefits for other U.S. industries. UPS estimates that for every 40 new packages it ships, a new job is created in the U.S. The UPS fleet of 276 planes is now the 11th-largest airline in the world, and 90% of those aircraft are manufactured by Boeing.

Information Technology: EDS

Founded in 1962 as Electronic Data Systems, EDS is now active in more than 60 countries. Over half of its annual $20 billion in revenue comes from outside the United States. EDS performs a variety of data-processing and systems operations for its clients. It is a leader in the outsourcing[7] of information technology (IT) services such as systems management, systems integration, and centralized transaction processing, and also operates the world's largest private digital voice, data, and video network.

EDS has been in China since the late 1980s, when it made one of the first IT services deals with the government. As more of its global clients invested in China, the firm responded by designating China as a strategic growth market and locating its regional headquarters in Shanghai. The Chinese market for IT services is growing rapidly. It is anticipated that by 2015 China will be the world's second-largest purchaser of these services. That market is still at an early stage of development, and is highly fragmented among numerous players. EDS is building its presence there, and anticipates that in a decade China may account for around one-tenth of the company's revenue.

China's accession to the WTO was a major step forward for EDS, both by creating new opportunities and by easing up regulations on its own operations. Those opportunities arose when the actual and potential clients of EDS were allowed to establish or expand operations that had previously been restricted. EDS also benefited directly from a Chinese commitment allowing firms to process data for other multinational corporations. EDS now has three types of clients in China: companies with which it has long-standing relationships that are now investing in or exporting to China; other multinationals that are in the Chinese market; and Chinese firms that are going global (including some former state-owned enterprises that have opened up to partial foreign ownership and joint ventures).

What does this mean for a U.S. company that wants to invest in or sell to China? Global companies come to EDS so that they have a consistent framework. EDS services include the development, management, and maintenance of enterprise system software; managing networks; and processing the payrolls, payments, and personnel management systems of a firm.

China also serves as a platform for U.S. entry into other Asian markets. Firms in Japan, for example, are becoming more open to offshoring some of their data services to China, as are companies in Hong Kong, Taiwan, and Korea. The EDS presence in China helps this U.S. company land business that might otherwise go to Chinese or third-country competitors.

Financial Services: Citibank

Citibank's Chinese operations include international and foreign currency transactions, comprehensive account services via different channels, and foreign currency investment products. Citibank's clients in China include multinational companies, joint ventures, local enterprises, and individuals.

Citibank has had a number of important "firsts" in China, starting in 1995 when it opened the first full-service branch in China in 45 years. Citibank became in 2002 the first foreign bank to enter the Chinese retail banking business, and the next year it was the first foreign bank in China to launch a personal investment product. Starting in 2005, a first-of-its-kind alliance with China UnionPay (CUP) has allowed reciprocal use of bankcards: CUP cardholders can use their cards in Citibank's worldwide ATM network, and Citibank international cardholders can use their cards at foreign-enabled CUP ATMs in China. In partnership with Shanghai Pudong Development Bank, Citibank also offers a dual-currency credit card.

Another first is Citigroup's Small and Medium Enterprises (SME) program, which it launched in 2004. Among the services that Citigroup offers to SMEs are vendor and supplier financing, export negotiation products, working capital, trade finance, equipment finance, and other credit facilities. Trade finance is an important component of Citigroup's operations in China, in which it provides exporters and importers as well as domestic firms with a full range of services.

As part of its WTO accession agreement, China pledged to phase in national treatment for foreign banking services over a five-year period, and to reform its domestic banking system. Geographic and client restrictions are scheduled to be lifted on December 11, 2006. The Citigroup Private Bank is already in place, having opened its Shanghai office in early 2006. It currently offers approved foreign currency products to Chinese and foreign residents, as well as approved local currency products to foreign residents. As restrictions are relaxed or eliminated, the services offered to Chinese individuals will include student loans, mortgages, personal finance and wealth management services, insurance, and retirement accounts.

These consumer services are emblematic of changes now taking place in Chinese society. As China becomes more fully integrated in the global economy, and as its citizens acquire more disposable income, there will be ever more opportunities for U.S. producers of goods and services. Bankcards already facilitate travel to the United States, to the benefit of the U.S. travel and tourism industry. When Citibank begins to finance student loans in China, many of those students may be headed to American schools. Chinese individuals may eventually be investors in the U.S. stock and bond markets. Such transactions are currently prohibited, but China is developing a qualified domestic institutional investor initiative that will allow individuals to invest overseas. This undertaking, which goes beyond what China committed to in its WTO accession, is one response to the capital that has been flowing into China.

Conclusion

These three cases serve to illustrate how the evolving trade relationship between the United States and China has worked to the advantage of American economic interests. Now that U.S.-China commerce is conducted on the basis of normal trade relations, and China is a member of the WTO, the world's fastest-growing market has been opened to the fastest-growing part of the U.S. economy. The services sector accounts for most of the jobs and economic activity in the United States, and offers the best prospects for growth in U.S. exports.

Despite the benefits of trade between the United States and China, there remain many and varied sources of friction in this relationship. On the trade side, the WTO offers the best forum in which to negotiate further commitments with China, and to settle any disputes that may arise over the implementation of these commitments. When justified, the WTO's Dispute-Settlement Body can authorize the use of trade sanctions to enforce a country's rights. But while WTO-authorized trade sanctions may sometimes be an appropriate response to trade disputes, unilateral restrictions are not the way to deal with disputes in other areas of the relationship. The wide-ranging and sometimes troubled relations between the United States and China sometimes lead to demands for "tough" measures, but it would be shortsighted and self-defeating for the United States to take precipitous, unilateral action that endangers trade relations with China. Sanctions might be aimed at Chinese goods, but they would almost certainly hit U.S. services as well.

Notes

[1] Since 1998, in the United States MFN treatment has been called "normal trade relations" (NTR).

[2] All data in this paragraph are from U.S. Department of Labor, Bureau of Labor Statistics, *National Compensation Survey: Occupational Wages in the United States, July 2004* (August, 2005).

[3] All data in this paragraph from http://devdata.worldbank.org/wdi2006/contents/Section4.htm.

[4] http://devdata.worldbank.org/wdi2006/contents/Section2.htm.

[5] Chinese Academy of Social Sciences, as quoted by UPS.

[6] In GATS terms, cross-border sales are known as Mode 1, and MOFA sales are Mode 3. There are also two other modes that account for smaller shares of sales in most sectors: Mode 2 consists of consumption abroad (i.e., services sold to Chinese customers who come to the United States), and Mode 4 services are provided through the presence of natural persons (i.e., U.S. nationals travel to China and provide services there).

[7] It is important to distinguish between *outsourcing* and *offshoring*. In outsourcing, one firm contracts with another to perform specific services that might otherwise be done in-house. This practice allows companies to reduce costs, concentrate on their core businesses, and take advantage of the economies of scale and expertise of a partner firm. Companies now outsource everything from janitorial services to the advanced IT and supply-chain management services performed by EDS and UPS, respectively. Offshoring means more specifically the outsourcing of these services to a provider in a foreign country. Whereas off-shoring often entails increased U.S. imports of services, the type of outsourcing that is described here is on the export side of the ledger.

United States Council Foundation
United States Council for International Business
1212 Avenue of the Americas
New York, NY 10036
Tel: (212) 354-4480 Fax: (212) 575-0327
www.uscib.org