

The economic impact of the Services Directive: A first assessment following implementation

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Since its launch in the mid-1980's the Single Market Programme has contributed to promote integration and competition within the EU and has resulted in real benefits in terms of growth and jobs. However, while the internal market for goods has been functioning reasonably well, the Single Market for services is not equally developed and is still far from a reality.

By further liberalising cross-border provision of services and the free establishment within the EU, the Services Directive has become the largest recent reform effort in an area relatively protected and sheltered from international competition. The Directive was adopted in 2006 and its implementation deadline was December 2009. Although the majority of Member States have transposed the Directive, its full transposition is not yet completed. In addition, its mere legal transposition does not ensure that the full potential offered by the Directive would be materialised, the reason being that the Directive left some room to Member States when deciding which existing regulation was incompatible with the provisions of the Directive. Thus, from the onset a large degree of heterogeneity of implementation was expected across Member States, thus also implying remaining heterogeneity for the functioning of the internal market.

This note presents work done by the Commission services to estimate the economic impact of the actual implementation of the Services Directive across Member States (in contrast to impacts of identical and complete elimination of restrictions estimated by previous studies). The analysis is possible thanks to available information on barriers to cross-border provision and to establishment for the period before and after the Directive. The barriers dataset has been compiled by the Commission Services to a large extent on the basis of the outcomes of the "mutual evaluation" done by the Member States and of experts' knowledge. It should be acknowledged though that the analysis is still an updated prediction or extrapolation exercise, rather than a fully-blown ex-post evaluation, because the period following the implementation of the Directive is too short to yield statistically sufficient data.

In addition to the dataset used, a main characteristic of the study is the adopted analytical framework where different channels of the impact of barrier reductions are captured and consistently combined: i) impact on services sectors trade and FDI, thus the international channel of transmission; and ii) direct impact on sectoral labour productivity, which captures the domestic channel of transmission of the effects of the Directive. The estimated sectoral impacts are then translated into GDP effects for the whole economies of the Member States based on general equilibrium simulations from the QUEST model.

Although the estimates do not cover all sectors under the provisions of the Services Directive, but a selection of them, its economic significance is still considerable. The conservative estimated EU-level impact on GDP is 0.8%, with the impact varying considerably across Member States (ranging

from below 0.3% to more than 1.5%) and mainly determined by the combination of the undertaken barrier reduction and the share of the covered sectors in their economies. Although the results materialize over time, close to 80% of the gains are reaped within the first 5 years following the policy shock (barrier reduction from implementation). An important finding of the analysis refers to the importance of the domestic channel of transmission, neglected in previous studies and that however turns out to yield very significant productivity results. The GDP and productivity effects reported are a lower bound as they do not incorporate the long-term effects that the estimate increased in trade and FDI (around 7% and 4% for EU, respectively) would have on economic activity through their impact on productivity.

Given the observed heterogeneity in barriers reduction across sectors and Member States, the note also quantifies the impacts under "what-if" hypothetical scenarios of further barrier reduction. Member States may reap yet additional benefits from the Directive if they continue their reform efforts, further reducing those numerous restrictions which have been only partially reduced and a non-negligible number of those which have been kept unchanged. Under an ambitious scenario where Member States move to the level of restrictions of the five best countries in the EU per sector, which is de facto close to a full elimination of barriers, will bring additional gains amounting to 1.6% of GDP, on top of the 0.8% under the current level of implementation. Even under a moderately ambitious scenario – where each country would become an "ideal country" composed of sectors with an EU average level of barriers – the further additional gain reaches 0.4% of GDP on top of the 0.8%. An important element to highlight from this exercise is that further gains could be obtained still within the scope of the Directive both in terms of requirements and sectoral coverage.

Besides the reduction of sectoral barriers, the Directive also seeks administrative simplification through the setting up of national "Points of Single Contact" (PSC). The PSC would allow services providers to get all relevant information and to complete all procedures and formalities relating to the establishment and cross-border provision for service activities. Their creation has proven an ambitious project in terms of the innovation required to bring paper-based systems and a number of authorities and procedures under online portals. The Commission Services have thus carried out work, presented in the second part of this note, to estimate a proxy of the potential economic impact of setting up national PSC in what concerns the establishment of service activities.

The approximation is based upon the World Bank's Doing Business 2012 Database to compute procedural streamlining efforts in setting up a service provider activity. In spite of the caveats behind this approach, the current analysis can provide a comparable quantitative estimation of the potential economic impact of the MS' current development and further improvements in establishment-related conditions affected by the Services Directive's PSC.

The findings indicate that, on average, the already achieved economy-wide impact is 0.13% of GDP, and the predicted additional impact from further streamlining could reach 0.15% of GDP in the medium run and 0.21% of GDP in the long run. This suggests that the Member States could reap significant additional gains by pursuing tangible improvements in the PSC implementation, first and foremost its effective capability to benefit all the involved businesses.

This note demonstrates the importance of a swift and more ambitious implementation of the Services Directive by the Member States accompanied by enhanced governance and enforcement mechanisms at the EU level, both commensurate with the estimated high potential gains.