

## Box 7

**EURO AREA TRADE IN SERVICES: SPECIALISATION PATTERNS AND RECENT TRENDS**

This box describes the main trends in euro area cross-border trade in services in terms of economic importance and patterns of specialisation. The euro area is the largest exporter of services worldwide, accounting for almost one-quarter of total world exports of services. Trade in services tends to play a greater role in small euro area countries with large deficits in trade in goods. During the latest economic downturn trade in services was more resilient than trade in goods. Nevertheless, the effects of the recession were highly heterogeneous across different services sub-sectors.

**Extra-euro area trade in services**

Services represent the bulk of economic activity in all advanced economies. In 2010 their shares of euro area GDP and employment were 66% and 73% respectively.<sup>1</sup> Owing in particular to the non-transportability of many services, the importance of services in the domestic economy is not reflected in international trade flows. In 2010 services represented only 25% of total extra-euro area exports and 24% of total extra-euro area imports, with a positive services trade balance of 0.4% of GDP. Compared with demand for manufactured goods, and in particular

<sup>1</sup> Unless otherwise specified, all data refer to the 16-country composition of the euro area.

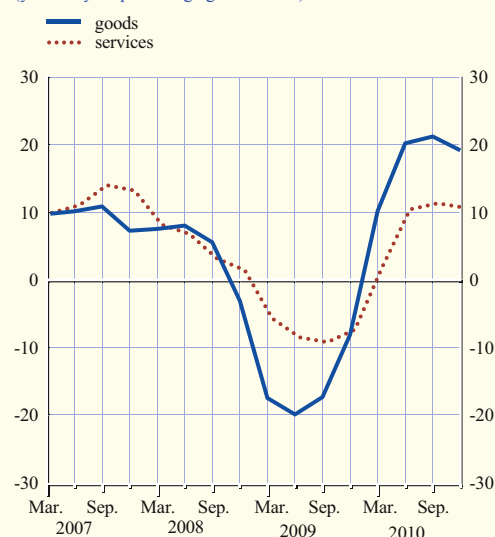
for durables, the demand for a range of traded services appears to be less cyclical; services trade and production seem to be less dependent on external finance, as suggested by developments during the recent recession episode (see Chart A). In the second quarter of 2009 total trade in goods contracted by 20% compared with the level recorded in the second quarter of 2008, while total trade in services declined by 8.7% in the same period. The developments in early 2010 when the recovery in trade in goods was much stronger than that in trade in services can be seen as unwinding those that took place in 2009.

In nominal terms, the euro area is the largest exporter of services worldwide. In 2009 extra-euro area exports accounted for 23% of global trade in services. The United States was the second largest exporter (16%), followed by the United Kingdom (8.1%), Japan (4.4%), China (4.4%) and India (3.1%). Looking at the last decade, the euro area export share increased from 20% in 2000 to 23% in 2004 and stabilised thereafter. By contrast, the United States experienced a sizeable decline in its market share. This could reflect in part valuation effects derived from the weakening of the US dollar, as well as the increasing role of emerging economies, such as China and India. Market size and cultural and linguistic ties are the main determinants of the direction of services trade flows. The euro area's main trading partners are the United Kingdom and the United States (see Table A). Both markets have become less important in the last few years, to the advantage of other European countries and the emerging economies.

The export specialisation of the euro area is quite balanced across services and manufacturing (see Chart B).<sup>2</sup> This is in sharp contrast to the specialisation patterns of the euro area's main trading partners. For instance, both the United Kingdom and the United States appear to specialise in insurance and financial services, and India exhibits a specialisation in computer, information and

**Chart A Extra-euro area trade in goods and services**

(year-on-year percentage growth rates)



Sources: ECB data and calculations.

**Table A Geographical breakdown of extra-euro area trade in services in 2010**

(percentages)

Trading partner	Exports	Imports
United Kingdom	20.3	16.5
United States	14.7	19.2
Other EU countries	10.4	10.1
Switzerland	10.1	8.5
China	3.0	2.4
Japan	2.4	1.9
Other countries	39.1	33.5

Source: ECB.

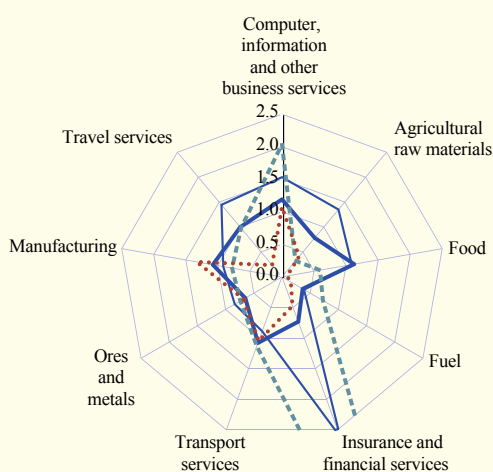
2 Chart B is based on the Balassa index, which is a measure of revealed comparative advantage. For country *c* and sector *i*, the index value is computed as:  $\frac{x_{ci}/X_c}{X_i/X}$ , where the numerator represents the share of sector *i* in the total exports of country *c*, and the denominator represents the sector's share in world exports. A value greater than 1 indicates that a country specialises in exports in a given sector, as it implies that the share of the sector in the country's exports is higher than the share of the same sector in world exports. Conversely, an index value of less than 1 indicates that a country lacks a specialisation in the given sector.

Chart B Export specialisation in goods and services sectors in 2007-09

(Balassa index of revealed comparative advantage; relative to the rest of the world)

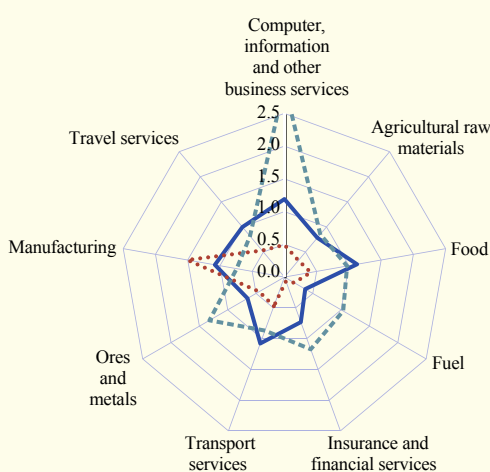
**Euro area and other developed economies**

- euro area
- ..... Japan
- - - United Kingdom
- United States



**Euro area and emerging economies**

- euro area
- ..... China
- - - India



Sources: Eurostat, World Development Indicators database and ECB calculations.

Notes: Data are averages for the period 2007-09. The United Kingdom and United States Balassa index values for insurance and financial services are 6.7 and 2.6 respectively. The India Balassa index value for computer, information and other business services is 2.9.

other business services, while China has a marked specialisation in manufacturing.<sup>3</sup> A closer look at the services sector trade balance reveals that the euro area surplus is mainly driven by computer, information and other business services, financial services and transport services. By contrast, the euro area is a net importer of royalties and licence fees and of personal, cultural and recreational services. Over the period 2004-09 only imports of insurance services fell. Conversely, during the same period exports of travel, personal and cultural services contracted slightly. These declines were in part driven by the effects of the crisis; over the period 2008-09 imports and exports of travel, transport and financial services recorded the sharpest contractions.

**Euro area countries' trade in services**

The patterns of specialisation within the services sector are quite heterogeneous across euro area countries. Some exhibit a clear specialisation in one or a few sectors: Cyprus and Luxembourg in financial services; Finland in computer and information services; Greece in transport services; and Ireland in insurance services and computer and information services. Other countries have a more balanced pattern of trade in services, with a slight dominance in one sub-sector: travel services in Austria, France, Italy, Portugal, Slovenia and Spain; communication services in Belgium and the Netherlands; construction services in Germany; and personal and cultural services in Slovakia.

<sup>3</sup> Other business services include merchanting and trade-related services, operational leasing services and miscellaneous business, professional and technical services, for instance legal, accounting, research and development, and advertising services.

**Table B Euro area trade in goods and services in 2009**

(percentages of GDP)

	Goods			Services		
	Exports	Imports	Net	Exports	Imports	Net
Belgium	78.9	74.8	4.1	16.9	15.7	1.2
Germany	33.4	27.8	5.6	6.8	7.6	-0.8
Ireland	50.7	27.3	23.4	42.6	45.4	-2.8
Greece	6.0	18.0	-12.0	11.4	5.9	5.5
Spain	14.9	19.9	-4.9	8.4	5.9	2.4
France	17.9	20.8	-2.9	5.4	4.8	0.6
Italy	19.2	19.4	-0.2	4.8	5.5	-0.7
Cyprus <sup>1)</sup>	6.6	42.7	-36.2	47.3	19.5	27.8
Luxembourg	39.8	46.3	-6.5	115.9	68.7	47.2
Malta <sup>2)</sup>	43.7	67.4	-23.6	41.2	27.4	13.8
Netherlands	63.0	56.3	6.7	11.5	10.7	0.8
Austria	35.6	37.4	-1.8	13.7	9.6	4.0
Portugal	18.9	30.4	-11.4	9.9	6.2	3.7
Slovenia	54.1	54.2	-0.2	12.4	9.3	3.2
Finland	26.3	25.2	1.1	10.8	9.9	0.9
Euro area <sup>3)</sup>	28.6	27.9	0.6	9.0	8.2	0.8

Sources: World Development Indicators database and ECB calculations.

1) The latest available data are for 2008.

2) The latest available data are for 2007.

3) The euro area data have been calculated on the basis of total euro area imports and exports (the sum of intra and extra-euro area trade for the countries listed in the table).

Trade in services plays a greater role in small economies, such as Cyprus, Luxembourg and Malta, owing possibly to the tendency of small economies to specialise in financial services or tourism (see Table B). Looking at net trade, big surpluses in trade in services tend to counterbalance large deficits in the goods balance. This is the case for Greece, Cyprus, Luxembourg, Malta and Portugal.

The importance of services in the domestic economy is only partially reflected in international trade flows. Nevertheless, over the last decade the relative importance of services trade with respect to total trade has increased for the euro area as a whole and for all the euro area countries except the Netherlands. This is also reflected in the increasing weight of services trade in GDP. The contribution of trade in services to GDP is particularly important for small economies with large negative deficits in trade in goods. This underlines the importance of taking into account the role of trade in services when assessing international competitiveness.