THE RELATIONSHIP OF EXPORTS IN SELECTED U.S. SERVICE INDUSTRIES TO U.S. MERCHANDISE EXPORTS

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PREFACE

On September 16, 1981, in accordance with the provisions of section 332(b) of the Tariff Act of 1930 (19 U.S.C. 1332(b)), the United States International Trade Commission instituted investigation No. 332-132, "The Relationship of Exports in Selected U.S. Service Industries to U.S. Merchandise Exports." 1/ The study was undertaken to provide information on U.S. international service activities and key markets with major focus on the following areas: (1) the dollar value of foreign revenues generated by major U.S. service industries; (2) the level and type of merchandise exports which result from U.S. services provided abroad; (3) the economic effect of international barriers to U.S. services trade as measured by the increased dollar potential of U.S. exports of services and manufactured goods, assuming reduction or elimination of nontariff measures; and (4) the markets and competitive factors which the major service industries consider important in international trade.

The study was undertaken to provide a basis for the President and the Congress to better understand the U.S. service sector's importance in world markets. Further, the study was intended to provide data on new aspects of international service trade which would assist policy makers in the more complete incorporation of the service sector into the United States' future trade negotiating posture. It is believed that the investigation is important in light of the increased interest by the service sector in Government assistance to facilitate more equitable access to international markets. This assistance is hampered by the fact that data available on the service industry relating to international trade and tariff matters are limited, in spite of increased Government attention and discussion on the importance of these issues. In addition, it is believed that the Commission's commodity expertise and knowledge of trade and tariff matters could make a contribution to the provision of information required to resolve questions concerning the proper approach to integrating into the General Agreement on Tariffs and Trade those industries that are not strictly product oriented.

In its study, the Commission collected information from various published sources, from a survey questionnaire mailed to 479 known international service companies in 14 categories of services, and from discussions with service sector executives. It should be noted that the industries included in the Commission's study represent only a portion of the service industries operating domestically and internationally. In addition, the data presented in the study cover only these areas and are not comparable to the data coverage in the categories of "service transactions" in U.S. international accounts which are published in various issues of the Survey of Current Business by the Bureau of Economic Analysis, U.S. Department of Commerce. In the preparation of the questionnaire, the Commission staff met with major trade associations and selected business representatives (16 persons participated) from the 14 areas to obtain comments and suggestions on the content of the questionnaire; eight additional industry contacts were made by

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1/ The notice of investigation was given by posting copies at the Office of the Secretary, U.S. International Trade Commission, Washington, D.C., and by publication of the notice in the Federal Register of September 30, 1981 (46 F.R. 47899).

telephone or in person to field test the questionnaire prior to mailing. The following tabulation shows the breakout of firms surveyed and those responding to the Commission questionnaire, which should be considered in reviewing the information contained in each industry report that follows:

Industry	Number of firms surveyed	Number of respondents
Communication services---------	8	1
Computer and data processing services----------	19	3
Construction and engineering services---------------------	93	38
Consulting and management services	59	13
Educational services-----------	48	11
Equipment leasing and rental services---------------------	27	6
Financial services-------------	42	17
Franchising services-----------	71	15
Health services----------------	7	5
Hotel and motel services-------	7	4
Insurance services-------------	28	15
Motion picture services--------	10	4
Transportation, air------------	23	3
Transportation, maritime-------	37	8
Total----------------------	479	143

The companies or organizations surveyed in each of the 14 industries represent firms with service operations as a primary activity or those with a major services component in conducting foreign operations. Manufacturing companies which often provide what is believed to be an important trade volume in secondary service activities--frequently associated with equipment suppliers, such as maintenance service agreements, systems design, and services primarily associated with marketing of manufactured products--are not within the scope of this study.

During the study, nearly 30 representatives of more than 20 major service firms and trade associations, covering nine of the service industries studied, participated in a series of informal discussions with Commission staff to explore overall trade issues concerning U.S. services in international markets. In addition, field interviews were held with representatives of 11 service companies and trade associations, and all questionnaire recipients were contacted by letter and by telephone to facilitate a response to the questionnaire. The data in the report have been aggregated by service industries, or data have been withheld when necessary, in order not to disclose the business operations of individual firms. In cases within a service industry where few responses were provided to a specific question, data is included only by special permission granted by the respondent firms in order to avoid revealing the individual operations of the firms. Annual data presented in the report are on a calendar-year basis, and dollar amounts are in U.S. dollars, unadjusted for inflation.

Unlike most questionnaries utilized by the Commission, the service sector questionnaire was a voluntary one. In spite of the fact that respondents were advised that data provided in the questionnaires would be aggregated in the final Commission report and confidential business information protected, the response rate was low. Nevertheless, it should be recognized that the information incorporated in the report constitutes another building block in the compilation of information and data relating to U.S. service activities in international markets.

Data presented in the report, on the basis of the questionnaire and other sources, present information which to date have not been available in such areas as (1) the level and type of merchandise exports associated with U.S. service activities abroad; (2) trade generated in the host or third countries as a result of U.S. service industry activity abroad; (3) a quantification of the incidence of specific nontariff barriers which individual service industries believe to be significant barriers either to maintaining or increasing their foreign operations; (4) the percentage increase and potential dollar value in U.S. service revenue and merchandise exports assuming reduction or elimination of service-related trade barriers in selected markets; (5) a list of the number of competing firms in international service markets by geographic scope of operations; (6) an identification of the reasons for competitive firms' success in foreign service markets; and (7) an indication of reasons for the U.S. service industries' competitive position in key markets, by industries.

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OVERVIEW

It should be recognized that the various service industries do not act as a monolithic unit and do not have the same goals and objectives in international trade. The service industries vary considerably in the degree to which they want Government involvement, the degree to which they are willing to make information available, and the degree to which they believe international institutions might provide a legitimate forum for resolving various trade and tariff problems which they face in international markets. For example, one service industry, which has long been active in international markets, uses an approach which involves Government and industry negotiations relating to various international issues. It has provided an effective basis to resolve, or at least bring to the attention of major trading partners, specific areas of concern. This traditional and established system to isolate and resolve international trade and nontariff trade barriers is generally accepted by the industry as largely satisfactory. There is an underlying concern on the industry's part that being included in a larger negotiation unit covering all service industries could lead to a diminution of their particular resolution mechanism in future negotiations.

A similar situation exists for another service industry which has been able, through close working contacts with commercial representatives in the State Department, to resolve their various problems to such an extent that they do not wish to be defined as a service industry for purposes of international service sector agreements. Elements of other service groups also do not wish to be included in such agreements for various trade-competitive reasons. Many service industries, on the other hand, have aggressively sought greater government involvement in various areas of their concern in order to develop a better understanding of major problems encountered in their foreign business activities, and to facilitate action to address international trade issues which currently or potentially affect all service industry operations abroad.

On the issue of developing a service sector database, there is a reluctance on the part of some well-established service industries to provide information which would indicate anything about their competitive position, not only in terms of international competitors, but domestic competitors as well. This reluctance is complicated by the fact that the service industries, unlike the manufacturing, agriculture, and mining sectors of the economy, are unaccustomed to providing detailed information on the nature and extent of their business operations to the Government on a regular basis. These industries have been characterized by some of their spokesmen as individualistic and having an overriding concern about the proprietary nature of business information. Many are reluctant to make any significant information available to the Government on a voluntary or mandatory basis. Moreover, there is no consensus among the service industries as to the type and detail of data which would be useful and/or necessary from a Government policymaker's point of view. The concern exists in some areas that negotiations by the United States could weaken and/or provide competitors with information about their markets and be detrimental to their competitive position internationally.

In spite of data problems, it is likely that the large number of service industries, their dynamic nature, and the significant domestic and international growth of service industries may keep this sector in the forefront of international trade issues in the foreseeable future. Any Government program to develop and maintain current data on the service sector to stay abreast of trading problems and issues will require a major commitment of time and resources and close ties with the service sector itself.

The Commission surveyed 479 international service firms in the 14 service industries encompassed by investigation No. 332-132. There were 143 responses to the questionnaire. Based on information obtained during the investigation, it is estimated that foreign revenue 1/ generated by the 14 U.S. service industries operating overseas will total $135.7 billion in 1982, up from $109.6 billion in 1981 and $89.4 billion in 1980, representing an increase of approximately 52 percent over the 3-year period. 2/ In 1981, the four service industries generating the largest foreign revenues were as follows: (1) financial services ($56.4 billion), (2) equipment leasing and rental ($13.4 billion), (3) insurance ($6.5 billion), and (4) air transportation ($6.4 billion). The data for 1980 and 1981 support the upward growth of service sector foreign earnings as generally presented in other published reports by other Government agencies and private research efforts. The following tabulation indicates Commission estimates of total service activity revenues including receivables and billings for 1980-82, but excluding the value of merchandise exports (in millions of dollars): 3/

1/ Often an international service company recognized in one special area has a secondary activity in foreign markets. Based on 1981 data from respondents these secondary activities generated an additional $3.2 billion in revenues not included in the total for the 14 service industries.

2/ Estimated by the staff of the U.S. International Trade Commission based on discussions with industry representatives and Government and private sources. Data returns from the questionnaire were not expanded to the universe to estimate a total because of a low response rate.

3/ For the investment bank segment of the financial services industry, foreign and domestic revenues cannot be estimated separately, and therefore are not included. However, total consolidated investment firm revenues for 1980, 1981, and 1982 are estimated at $16.0 billion, $19.8 billion, and $18.1 billion, respectively.

Domestic receipts for the motion picture services industry also are not available for 1980 and 1982; thus no figures for the industry are included. Foreign revenues for 1980, 1981, and 1982, however, are estimated at $1.4 billion, $1.37 billion, and $1.7 billion, respectively. Domestic revenues of this industry in 1981 were valued at $7.1 billion.

Domestic revenues for the franchising services industry are not available for 1980 or 1982; thus no figures for the industry are presented in the table. Foreign revenues for 1980, 1981, and 1982, however, are estimated at $2.5 billion, $2.7 billion, and $2.7 billion, respectively. Domestic revenues of this industry in 1981 are estimated at $40.6 billion.

Year	Foreign	Domestic	Total
1980	85,498	579,787	665,285
1981	105,541	659,811	765,352
1982	131,344	748,178	879,522

In 1981, U.S. service industries operating overseas used a variety of operational structures. Many questionnaire respondents employed more than one form of foreign operations. Approximately 55 percent of foreign operations were reportedly conducted by foreign affiliates, including independent subsidiaries and foreign branch offices. Other operational structures included joint ventures (20 percent), licensing and franchising arrangements (12 percent), and various miscellaneous structures (13 percent).

Based on data supplied in response to the Commission's questionnaire, the following tabulation provides a measure of the regional activity of the U.S. service sector in terms of the number of firms operating in each major world area in 1981:

World area	Number of respondent firms operating in each area
Far East	89
Latin America	84
Europe	82
Middle East	81
Canada	69
Africa	64
Mexico	62

In terms of the regional distribution of foreign revenues generated by the respondent firms, the following tabulation indicates the percentage distribution of total foreign revenues by major world area in 1981:

World area	Percentage of total foreign revenues of respondent firms
Europe	25
Far East	24
Latin America	17
Middle East	13
Canada	7
Africa	4
Mexico	2
Other	8
Total	100

Data collected from the questionnaire seem to support the contention that U.S. international service activities lead to increased exports of U.S. merchandise. However, because of the relatively low response rate to the merchandise trade section of the questionnaire, the Commission is unable to extrapolate the total value of U.S. merchandise exports directly generated by U.S. service sector activities abroad. Industry respondents for 12 industries covered in the study estimated that their foreign service activities resulted in the total U.S. export of approximately $2.7 billion in goods in 1981. Respondent data on merchandise exports generated as a direct result of U.S. service sector activity are summarized in the following tabulation:

Year	Number of responses 1/	Exports of U.S. merchandise estimated by respondents 2/ (million dollars)
1980------------	68	2,095
1981------------	67	2,699
1982------------	67	3,403

1/ The total number of questionnaire respondents in the 14 service industries was 143 of 479 firms surveyed.
2/ Does not include communications and air transportation industries.

In addition to the actual merchandise exports reported, two-thirds of the respondents to the questionnaire indicated that they believed their activities generated merchandise exports even though they may have been unable to quantify them. Approximately half indicated that U.S. merchandise was specified or recommended in the course of providing their service.

Moreover, in a series of questions asked to identify the degree to which host- or third-country merchandise shipments 1/ are generated by U.S. service sector activities abroad, industry respondents estimated a total of $11.2 billion in shipments by these countries. Slightly over half of the respondents indicated that they believed such shipments were generated, but they could not in all cases quantify them. One-third indicated that they specified or recommended foreign or host country products in the course of providing their service. Significant examples are given in the individual service industry reports of instances in which the entry of U.S. services into a foreign market has benefited the economies of the host or third countries.

The survey results provide the first look at the incidence of specific nontariff barriers encountered by the individual service industries. Using

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1/ "Host-country merchandise shipments" refers to the shipments (within the host country) of host-country-manufactured products which are generated by U.S. service operations in the host-country market. "Third-country merchandise shipments" refers to the shipments of other foreign-manufactured products to a foreign market as a result of U.S. service operations in that market.

major categories of nontariff barriers 1/ for which the United States Trade Representative has generalized information, the questionnaire responses indicate that right of establishment, trade in services, and foreign-exchange controls were the most frequently encountered barriers in the period of the study, as shown in the following tabulation: 2/

Category of barrier	Number of responses indicating barriers	Percentage of total respondents
Right of establishment	90	63
Trade in services 1/	88	62
Foreign exchange controls	78	54
Government procurement	43	30
Technical issues	38	27
Trade in goods 2/	30	21
Subsidies/countervailing duties	30	21
Licensing	26	18
Standards/certification	24	17
Customs valuation	19	13
Commercial counterfeiting	17	12
Professional qualification restrictions	15	10

1/ "Trade in services" barriers include restrictive actions related to (1) complete prohibition on services provided by non-resident firms, (2) requirements that a fixed percentage of service must be provided by domestic resident companies, and (3) discriminatory taxation of services provided by non-resident companies. Other examples may be cited in the industry reports that follow.

2/ "Trade in goods" barriers include restrictive actions related to (1) local purchase requirements, (2) entry of equipment or supplies, and (3) burdensome regulations or administrative procedures. Other examples may be cited in the industry reports that follow.

A significant percentage of respondents expressed a belief that the barriers cited affected their operations and potential U.S. exports. Approximately half of the respondents indicated that removal of service trade barriers would increase their foreign revenues. Approximately one-quarter indicated that the removal of such barriers would have no effect on foreign revenue. Based on questionnaire responses by service companies in 11 industries, which identified an estimate of the percentage change in 1981 receivables, billings, or revenues, by regional markets (assuming major

1/ Examples of the type of barriers encountered by service industries in the major categories of nontariff barriers are provided in the questionnaire, included in the appendix, and the industry reports that follow.

2/ The total number of questionnaire respondents in the 14 service industries was 143 of 479 firms surveyed. Does not include information on communications and air transportation.

impediments to service market entry were removed), an estimated $1 billion in increased revenue could have been realized. The following tabulation showing increased dollar potential in U.S. service "exports" is based on actual revenue data reported by each company respondent within the respective service industry:

Industry	Estimated increases in exports of U.S. services absent trade barriers (1,000 dollars)
Computer and data processing services	76,536
Construction and engineering services	1/ 485,958
Consulting and management services	826
Education services	2/
Financial services	209,715
Franchising	2/
Health services	2/
Hotel and motel services	180,766
Insurance services	64,032
Motion picture services	2/
Transportation services, maritime	2/
Total	1,093,728

1/ Data may include contract awards in addition to receivables, billings, or revenues reported by construction and engineering services firms.
2/ Withheld to avoid the possibility that figures for individual companies could be derived by disclosing data.

When asked the effect of the removal of service barriers on current or potential merchandise exports, roughly one-third of the respondents indicated that removal of these barriers would increase merchandise exports, and about one-quarter said there would be no effect. Based on questionnaire responses by service companies in seven industries, which identified an estimate of the percentage change in 1981 U.S. merchandise export sales assuming major trade barriers to services were removed, an estimated $1.8 billion in merchandise export sales could have been realized. The following increased dollar potential in exports of U.S.-manufactured goods is based on actual product export data reported by each company respondent within the respective service industry:

Industry	Estimated increases in U.S. merchandise export sales absent trade barriers (1,000 dollars)
Computer and data processing services	24,940
Construction and engineering services	560,516
Consulting and management services	250,000
Financial services	909,400
Franchising services	100,815
Health services	13,260
Hotel and motel services	27,741
Total	1,886,672

A discussion of percentage shifts in these exports and revenues, and the actual service barriers are presented on an industry-by-industry basis in the individual service industry segments of the report.

U.S. service companies responding to the questionnaire cited the following reasons for their success in current and potential international markets:

Competitive factor	Number of times factor cited for--	
	Existing markets	Potential markets
Superior quality	127	127
Experience in market or service	111	88
Technology lead	99	131
Financial strength	56	52
Lower price	13	13
Other	22	29

As shown in the following tabulation, the key reasons cited by the respondents for the success of other countries' service organizations in current world markets are lower price, government support, preferential financing, and market or service experience:

Competitive factor	Number of times factor cited
Lower price	111
Government support	71
Preferential financing	62
Experience in market or service	62
Political or regional bias	56
U.S. restrictions	34
Technology expertise	18
Superior quality	5

Communication Services

Executive Summary

1. In 1981, international revenues earned from communication services amounted to about $2.7 billion.

2. U.S. exports of equipment generated by communication service activity are believed to be small given the largely corresponding nature of foreign activity and the primary involvement of telecommunications equipment manufacturers in providing system design services in foreign markets. Merchandise exports related to communication services is estimated at less than 1 percent of total U.S. exports of communication equipment. No U.S. firms supplied data on exports generated by their service activity.

3. Because most countries provide communication services and hardware from within their own national boundaries, host or third country merchandise shipments resulting from U.S. communication services are small.

4. Industry sources indicate that the principal barrier to international trade in communication services is the structure of the communication industries which are government owned or controlled in most countries.

5. The increased dollar potential of U.S. exports of communication services and manufactured goods, assuming reduction or elimination of nontariff trade barriers, is unknown but believed to be large based on the reputation of U.S. companies for quality, reliability, and advanced technology in both communications and hardware design. Developed countries, while the largest potential markets for trade in goods and services, are closed to U.S. communications systems; however, developing countries are a potential market and, at this time, are more accessible.

6. U.S. service firms, while generally leading the world in the development of international communications and services and in hardware technology, are virtually precluded from providing communications in other countries. The U.S. firms involved in international trade in communication services are those engaged in satellite, undersea cable, and point-to-point communications. Their strengths are their technology and investment capabilities.

Industry Profile

Definition and coverage

The communication services industry includes firms and establishments providing point-to-point communication service, radio and television broadcasting, and services which entail exchange or recording of messages. It includes firms and establishments providing telephone (Standard Industrial Classification (SIC) 4811) and telegraph (SIC 4821) services and establishments disseminating information by radio (SIC 4832) and television (SIC 4833) broadcasting, as well as those providing program material. Other communication services (SIC 4899), such as cablevision service, operation of missile-tracking stations, phototransmission services, and stock ticker services, are also included. These services include both domestic and international activity.

International communications services are provided from one country to another by means of submarine cables, satellites, or radio links. Sharing of these facilities is subject to an agreement between U.S. carriers and foreign entities which provide communication services in foreign countries. Service activities provided by telecommunication equipment manufacturers in foreign markets, such as systems design, are not within the scope of this study, and therefore, this report is limited to service firms providing telex, private-line, data and voice communication in foreign markets.

Of the 8 communication service firms surveyed and believed to be operating internationally in 1981, one company responded to the Commission's questionnaire. Insufficient data (without disclosing the confidential operations of an individual company) were provided to enable preparation of tables consistent with other service industry reports. This report is based largely on discussions with industry and/or association representives and secondary sources.

Highlights in 1981

- DOMESTIC SALES of communication services were estimated to be $84.3 billion.
- U.S. ESTABLISHMENTS providing communication services numbered over 10,000.
- U.S. EMPLOYMENT in these establishments was about 1.3 million persons.
- INTERNATIONAL REVENUES earned from communications services amounted to about $2.7 billion.
- FOREIGN ESTABLISHMENTS affiliated with U.S. firms engaged in providing communication services are estimated to be few.
- FOREIGN EMPLOYMENT in affiliates of U.S. firms providing communication services is estimated to be about 100.
- U.S. TRADE BALANCE in the communication services sector is probably positive, but by less than $50 million.

Industry structure

U.S. institutional structure.--The U.S. industry is divided, for the most part, into groups of companies providing the various types of communication services, i.e., television broadcasting, radio broadcasting, telephone, telegraph, and international record carriers. Overlap occurs in that some firms provide more than one of these services. Of the approximate 10,000 companies operating in the United States in 1981, including broadcasting companies and telephone and telegraph firms, about 75 percent provided radio broadcasting services.

Telephone communication services in the United States are dominated by a major system, although some 1,450 firms provide this service. These firms provide for voice and data communication utilizing telephone lines (wire) and point-to-point radio communication links, including satellites. Telegraph services are also dominated by a major system but are provided by a few other firms. Telegraph services consist principally of message transmission intended for designated persons.

Radio broadcasting stations disseminate programs by radio to the listening public. About 7,800 stations were in operation in 1981, approximately 60 percent were AM stations and the remainder were FM stations. Less than 30 percent of the firms operate both AM and FM stations. These stations sell advertising time or solicit donations.

Television broadcast stations disseminate programs by radio to the viewing public. Like radio broadcasting stations, television broadcasting stations sell advertising time or solicit donations. An increasing number of television networks are broadcast through cables and point-to-point links which restrict reception to subscribers rather than broadcasting to the entire viewing public.

Interstate transmission of telephone, telegraph, radio broadcasting, and television broadcasting is regulated by the Federal Communications Commission (FCC). The FCC also limits the electromagnetic radiation emissions from large transmitters and certain receivers and insures that communicators adhere to the frequency standard allocated them. Given the international structure of the communications industry, which necessitates an operating agreement with the communication authority in each country, foreign carriers do not operate in the United States.

International institutional structure.--International transmission of communication services is performed by a small number of firms, each composed of an international consortium of firms that connect U.S. communications systems to foreign systems. U.S. telephone companies and record carriers, by agreement with foreign governments or firms controlled by foreign governments (e.g., the various post telephone and telegraph (PTT) entities in European countries), share the costs of transmitting telephone calls whether the transmission is by satellite, submarine cable, or radio links. Calls and messages in the United States are usually separated from calls and messages in foreign countries for revenue purposes. Domestic and international revenue of $87 billion for the communication services industry accounted for over 10 percent of total U.S. service sector trade, estimated at $837 billion in 1981 for the 14 service industries covered in this study. With the exception of a U.S.-based telephone company operating in Southwest Canada next to the United States border, U.S. carriers do not operate in foreign countries.

Recent trends and outlook

Net revenues of the domestic communication services industry grew from about $49.7 billion in 1976 to an estimated $84.3 billion in 1981. Operating units increased from 9,954 to over 10,000 during 1976-81, and employment rose from 1,122,000 persons to about 1,300,000 persons. International revenues (after settlement) increased from about 2 percent in 1976 to 3 percent in 1981, and accounted for about $2.7 billion of total revenues in 1981.

Demand for domestic communication services is growing, as measured by the number of telephones in use in the United States (155 million in 1976, increasing to 190 million in 1981), as well as by the increased use of communications links for exchanging text, data, facsimile, and video information. Demand for international services has also grown rapidly; the number of international circuits has increased 20 percent since 1979 to more than 19,000 at the end of 1981. As customer demand changes rapidly toward increased data transmission, more communication channels capable of transmitting data at frequencies higher than can be carried on the voice channels are being required. These channels are being provided by microwave communications and satellite. The use of fiber optic cables will soon be implemented in transoceanic marine cables.

The domestic communication services industry is in transition owing to recent legislative and judicial actions which have led to the growth in the number of companies providing communication services. Competition among these companies, the increasing demand for communication services, and the increased use of satellites as an alternative to land and marine lines in communication services are the key economic factors affecting the industry. It is generally believed that these conditions will result in an increased flow of information at lower costs.

The U.S. communication services industry is expected to continue its growth in the near term, with added new technology improving the international communication systems. Rapid U.S. technology developments have brought a reaction from industries in foreign countries as evidenced by reported cases of nontariff barriers. 1/ At the present time, U.S. service firms believe they have the capability of providing a greater number of high-technology products to foreign communication services industries provided foreign barriers were relaxed.

U.S. Service Operations in Foreign Markets

U.S. communication services companies engage in foreign operations by providing connections to firms or other entities in foreign countries by underwater cables (about 5,000 circuits), satellites (about 9,000 circuits), and radio relays. As noted, the connection is made through an agreement with the communication authority in each foreign country covering the allocation of revenue to the U.S. carrier and the foreign carrier. Operating revenue, after

1/ For a list of restrictive measures see Trade Barriers to Telecommunications, Data and Information Services, United States Trade Representative Computer Group, Nov. 14, 1980.

settlement, from international telephone and telegraph services, which increasd from $1.2 billion in 1976 to $2.7 billion in 1981, has been about 3 percent of total domestic telephone and telegraph revenues during this period.

Based on Commission staff estimates, revenue obtained from international communications services is expected to increase nearly 19 percent to $3.2 billion in 1982, as shown in table 1. Of total revenue, telephone and telegraph services accounted for almost 82 percent in 1981, down from 84 percent in 1976; radio broadcasting maintained its share of about 4 percent; television broadcasting accounted for about 12 percent, up from 10 percent; and cable television remained at about 2 percent.

Table 1.--Indicators of activity in the foreign and domestic operations of communication service firms, 1980-82

Item	Foreign	Domestic	Total
Estimated 1/ value of total sector receivables, billings, or revenues: 2/			
1980------------------1,000 dollars--	2,300,000	73,400,000	75,700,000
1981----------------------------do---	2,700,000	84,300,000	87,000,000
1982----------------------------do----	3,200,000	95,000,000	98,200,000

1/ By the staff of the U.S. International Trade Commission based on discussions with industry and/or association representatives, and secondary sources.

2/ Excluding the value of any merchandise exports.

Source: Based on U.S. International Trade Commission staff discussions with industry and/or association representatives, and secondary sources.

The expansion of international communication services appears to have kept pace with the rapid expansion of domestic communication services. Increased world trade and a growing number of multinational firms are expected to generate increased demand for the U.S. communication services industry. However, given the restrictive international competitive structure of the PTT entities, the revenue obtained by U.S. service companies in providing these services is likely to be divided proportionally with foreign firms. As a result, revenue generated by U.S. communication service in foreign countries is expected to remain relatively small in the forseeable future, representing 2 percent of total estimated service sector foreign revenue estimated at $135.7 billion in 1982 for the 14 service industries covered in this study (table 2).

Table 2.--Estimated total foreign revenue generated by the communication service industry and estimated total foreign revenue for selected service industries, 1980-82

Year	Total foreign revenue for service industry 1/ (1)	Total foreign revenue for selected service industries 2/ (2)	Ratio of (1) to (2)
	1,000 U.S. dollars		Percent
1980	2,300,000	89,398,000	3
1981	2,700,000	109,611,000	2
1982	3,200,000	135,744,000	2

1/ Estimated based on discussion with industry and/or association representatives, and secondary sources.

2/ Based on totaling Commission-estimated foreign revenue for each of the 14 selected industries covered in the study.

Source: Estimated by the staff of the U.S. International Trade Commission.

Trade in Merchandise Generated by Trade in Services

The growth in communication services requires a large amount of equipment. For communications supplied within developed countries, the equipment is usually supplied by indigenous firms. U.S. exports of equipment generated directly by communication service activity are believed to be small given the largely correspondent nature of this sector's foreign activity and the primary involvement of telecommunication equipment manufacturers in providing system design services in foreign markets. Similarly, host- or third-country merchandise shipments 1/ most likely to be generated by U.S. communication service activity in foreign markets are small.

The largest potential markets for services-generated merchandise are developed countries, where communications systems are well developed; however, since these markets are virtually closed to U.S. exports, developing countries entering into the rapidly expanding communications age are probably the best prospects for sales of U.S. telecommunications hardware and services. In the case of both developed and developing country markets, the high-technology products of U.S. firms are utilized to a limited degree; in the former markets, because of access problems, and in the latter markets, although purchases are greater, competition is intense.

1/ "Host-country merchandise shipments" refers to the shipments (within the host country) of the host-country-manufactured products which are generated by U.S. service operations in the host-country market. "Third-country merchandise shipments" refers to the shipments of other foreign-manufactured products to a foreign market as a result of U.S. service operations in that market.

Further, developing countries are beginning to acquire the capability to produce their own communications equipment. With regard to equipment used in international communications linkages, the U.S. based communication service firms play a major role in concert with counterparts in other developed countries in supplying the necessary technical know-how; however, the trade generated is believed to be small in comparison with total domestic shipments of telecommunication equipment. Data on the value of the equipment used are not available. 1/

International Service Trade Barriers

According to industry sources, the principal barrier to international trade in communication services is the organization of the communication industries which are government owned or controlled in most countries. 2/ Thus, international communications traffic is a matter of the communications network of one country being hooked up with the communications network of another country. As noted previously, telephone and telegraph traffic is a prime example of this barrier. However, the barrier also extends to radio and television broadcasting, wherein nations seek to curtail or prevent incursion into their airways by broadcasts from other countries.

A particularly difficult barrier to communications services is the attempt by some governments to restrict or otherwise interrupt the flow of data between computers and computer terminals. 3/ These data, often proprietary in nature, link multinational businesses and organizations. The restriction or interruption may result in a service disruption of business activity or otherwise compromise proprietary information. The industry points out that the situation is further exacerbated by generally weak or unenforceable patent and copyright laws in many countries. Thus, compromise of proprietary information can result in a severe financial loss.

In the area of radio and television broadcasting, various countries have complained of broadcasts originating in other countries. Some agreements have been made to satisfy complaints; nonetheless, accommodation of such complaints constitute a barrier to communications services.

Conditions of Competition in Current and Potential Service Markets

U.S. service firms, while generally leading the world in the development of international communication services and in hardware technology, are virtually precluded from providing communications in other countries. Only a limited degree of services are provided in foreign countries by U.S. service

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1/ The Commission surveyed 8 firms providing international communication services. The responding firm provided no data on U.S. exports of merchandise generated by their service activity.

2/ Eight U.S. firms were requested to provide information on international service trade barriers; the responding firm did not provide information on international service trade barriers.

3/ USTR Computer Group, op. cit.

firms and a minimal amount is provided in the United States by foreign firms. However, the relatively steady international growth of the U.S. industry, primed by high demand for communication services by U.S.-owned firms and individuals, indicates its competitive advantage in technology, investment, and service capability. This advantage has been fostered by the growth of semiconductor technology in the United States and the application of such semiconductor and computer technology in the form of switches, transmitters, relays, and satellites to communication and related service industries.

Foreign countries, in an apparent effort to match the rapid technological gains made by U.S. firms, appear to be developing their own technology rather than purchasing innovative U.S. products which would speed the development of their communication services industries. Foreign-owned communications authorities in developed countries usually buy products necessary to provide services from indigenous producers rather than from outside sources. Industry states that efforts during the Tokyo round of the GATT negotiations to achieve reductions in U.S. foreign trade barriers involving foreign government purchases of U.S.-made products yielded minimal results; among the developed countries, only Japan, negotiated access for U.S. products in the Japanese communications system. To date, however, the Japanese have purchased only a small amount of U.S. products according to industry sources. Negotiations, however, are still in progress.

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Computer and Data Processing Services

Executive Summary

1. The dollar value of foreign revenues generated by the computer and data processing service sector is estimated at $3.0 billion in 1981.

2. The reported level of U.S. merchandise exports generated by the foreign market activity of firms surveyed totaled $217.6 million in 1981, with 40 to 100 percent of these service-related exports considered to be high technology products.

3. Industry respondents to the questionnaire estimated that over $480 million in host-country and third-country product shipments were generated by U.S. computer and data processing service activities abroad in 1981. The trade is believed to consist principally of data processing equipment and office machines.

4. The major restrictive measures impeding international expansion of trade in computer and data processing services reportedly are the activities by foreign governments which restrict trade in the hardware associated with the services. Respondents to the Commission's questionnaire unanimously cited trade barriers in (1) the right of establishment in foreign countries, (2) trade in goods such as local purchase requirements and restrictive entry of goods, (3) trade in services such as operating ownership restrictions, (4) government procurement practices giving preference to national firms, and (5) foreign exchange controls such as limitations on currency convertibility.

5. The economic effect of international barriers of U.S. services trade was reported to be significant by two-thirds of the industry respondents. Reducing or removing existing trade barriers could increase U.S. foreign-market service revenue and the value of service-related manufactured exports by 10 to 30 percent or more in most regions of the world.

6. Reporting U.S. firms faced significant local and foreign competition in the following important markets; the United Kingdom, France, Australia, the Netherlands, West Germany, and Italy.

7. The developed countries are the principal markets for U.S. trade in computer and data processing services, although developing countries are cited as potential markets. The technology expertise of Japanese firms was reported by all respondents as a significant competitive factor in world markets. Lower price and associated advantages of experience in the market or service and political or regional bias were cited as likely reasons for competing firms' success in world markets.

8. U.S. computer and data processing service firms are among the leaders in the United States and in many foreign markets. The competitive

strengths of the U.S. firms were reported to be (1) technological lead and (2) experience in the market or service. Financial strength and superior quality associations were also reported to be important factors for U.S. market position.

Industry Profile

Definition and coverage

The computer and data processing services industry include establishments providing computer programming, systems design and analysis, and other computer software (Standard Industrial Classification (SIC) 7372); data processing, such as time sharing, calculating, and key punching (SIC 7374); rental and leasing (except by the manufacturer or sales office of the manufacturer); and maintenance (SIC 7379). These services include both domestic and international activity.

The industry consists of a variety of firms, from very small to very large, most of which do not manufacture computers or peripherals. However, manufacturers of computers are among the leading suppliers of computer and data processing services. Many of the firms providing services either purchase, lease, or rent computers for the purpose of processing data on demand. Others specialize in writing programs to enable computers to perform specific or customized tasks. Firms which obtain computers from manufacturers for the purpose of renting or leasing and firms which specialize in maintenance are probably not large in number, but they do account for a large share of services revenue.

The computer service companies covered in this study have a major software and services component in conducting foreign operations. Secondary service activities principally provided by equipment manufacturers--such as maintenance service agreements following the sale of hardware, and service associated with marketing of manufactured computer equipment--are not within the scope of this study. The three computer and data processing service industry respondents to the Commission questionnaire represent about 15 percent of the foreign revenues of the estimated 19 major computer and data processing service firms which were surveyed and believed to be operating internationally in 1981.

Highlights in 1981

- o DOMESTIC SALES of computer and data processing services were estimated to be approximately $17.0 billion.

- o U.S. FIRMS providing some form of computer and data processing services were estimated at about 4,500.

- o U.S. EMPLOYMENT in these establishments was estimated at more than 300,000.

- o INTERNATIONAL REVENUES flowing from computer and data processing services were estimated to be about $3.0 billion.
- o FOREIGN SUBSIDIARIES of U.S. firms engaged in providing computer and data processing services are estimated to be less than 500.
- o FOREIGN EMPLOYMENT in these establishments is estimated to be about 70,000.
- o THE U.S. TRADE BALANCE in computer and data processing services is positive by $1.0 billion or more.

Industry structure

U.S. institutional structure.--The industry can be generally organized by the services provided, i.e., software, data processing, maintenance, rental, and leasing. In addition, questionnaire data discussed later in this report indicate one or more of the three respondents engage in secondary service activities. Only a few firms provide all of the computer and data processing services, and they tend to be among the largest suppliers of computers and computer peripherals. Most often, the equipment manufacturer supplies the computer and some software to the buyer; however, suppliers of software and services that do not manufacture computers are believed to exceed 4,000 firms. Users of computers frequently purchase software from sources other than the computer producer and also generate software.

A large number of service firms purchase computers, computer peripherals, and software, in addition to generating software, for the purpose of performing data processing on a contractual basis. For the most part, these firms sell time and programming on their computers and peripherals in order to perform a task required by their customers. Firms providing data processing services often lease or rent (rather than buy) equipment from manufacturers or computer equipment service companies.

In 1977, about 16,000 U.S. establishments (the number of firms is not available) provided domestic computer and data processing services, and revenues amounted to approximately $7.6 billion. By 1981, the number of U.S. establishments is estimated to have increased substantially to about 25,000 (about 4,500 firms), and the value of domestic services increased to about $17.0 billion. 1/

International institutional structure.--An estimated 500 subsidiaries of U.S. service firms were operating in foreign countries in 1981 in addition to

1/ Derived from 1980 data published by Input, Ltd., London, England. The value of computer and data processing services for 1981 is not compiled in the official statistics of the U.S. Government. Data supplied by associations and consulting firms vary. The Association of Data Processing Service Organizations valued worldwide computer services revenues of U.S. firms at $14.9 billion in 1980. An Arthur D. Little, Inc., analyst valued worldwide data processing revenues in 1981 at $75 billion. Forbes, July 6, 1981, places computer services revenues at $13 billion in 1980.

several thousand foreign firms. The major other types of operating structure identified in the Commission questionnaire are discussed in a later segment of this report. Domestic and international revenue for the computer and data processing services industry ($20 billion) accounted for over 2 percent of total U.S. service sector trade, estimated at $837 billion in 1981 for the 14 service industries covered in this study. In addition to international revenues of U.S.-based service firms, services are also provided by the foreign subsidiaries of U.S. firms; the value is unknown but is estimated to be less than the value of services provided by the parent firm in the U.S. market. Official data on the value of computer and data processing services in foreign countries and in international trade are not available; the value in foreign countries is estimated to be $17 billion, and the value of international services provided by U.S. firms, $3.0 billion in 1981.

Recent trends and outlook

The rapid increase in the value of computer and data processing services has occurred because of the increased use of computers as a commercial, industrial, and management tool. Further, the availability of small computers in the price range of small firms and individuals has lead to a vast increase in demand for data processing assistance and software. Of the total value of computer and data processing services provided in the United States in 1980, the value of software was $2.4 billion, of professional services, $3.4 billion, and of data processing services, $8.4 billion. In Western Europe, total services were valued at $8.1 billion, of which software was $1.1 billion, professional services, $2.7 billion, and processing services, $4.3 billion. 1/ Data for 1981 are not available. Each of these subsectors is reported to be increasing at a rate of 10 to 30 percent per year. Among the suppliers of these services are the manufacturers of computers and computer peripherals.

The services industry began to grow rapidly about 10 years ago when the major computer producer commenced to price computer services separate from computer hardware. This event, coupled with the availability of small low-priced computers, has, in large measure, brought about the rapid growth. The proliferation of computers brought about by their utility in solving commercial, industrial, and management problems has attracted many more people into the computer and data processing services business. This expanding activity is the key economic factor affecting short-term growth in the computer and data processing services industry.

U.S. Service Operations in Foreign Markets

Operating structure

U.S. producers of computer and computer peripherals manufacture and sell their products in many free-world countries, principally developed countries. These producers account for a large share of computer services which are provided mostly by foreign subsidiaries.

1/ Input, Ltd., London, England.

The three firms responding to the Commission's questionnaire reported that service operations in foreign markets were provided through foreign affiliates, subsidiaries or branches, and joint ventures; one of the firms reported a licensee (table 1). This small return seems to support a view prevalent in trade journals that the four types of operating structure mentioned are widely used by U.S. firms in foreign operations. In addition, the firms reported over $205 million in foreign revenue obtained from secondary activities such as service for leasing and rental, construction and engineering, consulting, health, and education.

Computer services firms, which augment the services provided by the manufacturers, have appeared in foreign countries just as in the United States. Industry sources estimate that up to a total of 500 subsidiaries of U.S. firms provide these services, and 6 of the top 10 suppliers of services in the Western European market are U.S.-owned firms. Three of those suppliers are also major manufacturers of computers and peripherals. Computer and data processing services are also provided rapidly from the United States by communications networks. While the growth in the total value of computer and data processing services provided from the United States to foreign countries is estimated to be in the range of 10 percent to 30 percent annually, the software market in Europe is estimated to have grown 39 percent from 1979 to 1980 1/.

U.S. service operations in foreign markets are linked with U.S. exports of computers and computer peripherals as well as the production and sales by foreign affiliates of such producers. Of the estimated $17 billion in foreign computer and data processing services in 1981, an unknown, but possibly significant, amount is tied to the sale of computer equipment. Beyond the initial provision for services in the sale of hardware, an unknown, but possibly substantial, amount of services is provided by the producer of the hardware or its affiliates. For example, in Europe, the top 10 suppliers of software are all producers of computers and peripherals according to Input Ltd. It is likely that the operating structure and scope of the U.S. computer services industry in all countries parallels the European example.

Growth trends and U.S. investment

The operations of three firms responding to the Commission's questionnaire indicates that their aggregate foreign revenue from service operations decreased from 30 percent of their total revenue in 1980 to 27 percent in 1981 and will remain at about 27 percent in 1982. Their combined value of foreign revenue obtained from computer and data processing services is expected to increase from $453.5 million in 1980 to a projected

1/ Input LTD., London, England.

Table 1.--Operating structures of principal service activity, and revenues associated with secondary service industry activities of computer and data processing service firms in foreign markets, 1981 1/

Item	Revenues 2/	Number of responses	Percent of total respondents
	1,000 U.S. dollars		
Operating structure:			
Foreign affiliate	-	3	100
Joint venture	-	3	100
Licensing	-	1	33
Subsidiary or branch	-	3	100
Secondary service activity:			
Construction and engineering services	3/	1	33
Consulting and management services	3/	2	67
Educational services	3/	2	67
Equipment leasing and rental services	3/	1	33
Health services	3/	1	33
Total	205,734	3	100

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 3 of 19 firms surveyed. Respondents represent about 15 percent of the foreign revenue of the estimated 19 major firms believed to be operating internationally in 1981.

2/ Calculated by the staff of the U.S. International Trade Commission from receivables, billings, or revenue data provided by respondents.

3/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

$475.2 million in 1982 (table 2). The aggregate number of operating establishments in foreign countries reported by these firms dropped from 40 percent of their total number of establishments in 1980 to a projected 30 percent in 1982. Their investment in the foreign operations was $656.5 million in 1981 and is expected to decrease to $610.6 million in 1982. For the total industry, of which the three reporting firms are a part, foreign revenues are expected to increase from $2.2 billion to $4.0 billion during 1980-82 and represent an increase in share of total industry operating revenue (from 13 percent in 1980 to 17 percent in 1982). The industry foreign revenue estimates represent about 3 percent of service sector foreign revenue for the 14 service industries selected for this study as shown in table 3.

Table 2.--Indicators of activity in the foreign and domestic operations of computer and data processing service firms, 1980-82

Item	Foreign	Domestic	Total
Estimated value of receivables, billings, or revenues: 1/ 2/			
1980------------------1,000 dollars--:	453,473	1,010,705	1,464,178
1981-----------------------------do----:	457,058	1,176,905	1,633,963
1982-----------------------------do----:	475,203	1,298,707	1,773,910
Estimate of investment in physical assets 1/ 3/ in foreign operations:			
1980------------------1,000 dollars--:	621,858	-	-
1981-----------------------------do----:	656,480	-	-
1982-----------------------------do----:	610,656	-	-
Number of establishments: 1/			
1980-----------------------------------:	201	300	501
1981-----------------------------------:	218	323	541
1982-----------------------------------:	152	364	516
Estimated 4/ value of total industry receivables, billings, or revenues:			
1980------------------1,000 dollars--:	2,200,000	14,200,000	16,400,000
1981-----------------------------do----:	3,000,000	17,000,000	20,000,000
1982-----------------------------do----:	4,000,000	20,000,000	24,000,000

1/ Data represent questionnaire respondents only. The total number of questionnaire respondents in this service industry was 3 of 19 firms surveyed. Respondents represent about 15 percent of the foreign revenue of the 19 major firms believed to be operating internationally in 1981.

2/ Excluding the value of any merchandise exports.

3/ Including the undepreciated book value of land, plant, and equipment.

4/ By the staff of the U.S. International Trade Commission based on discussions with industry and/or association representatives, and secondary sources.

Source: Compiled from data submitted in response to questionnaries of the U.S. International Trade Commission.

Table 3.--Estimated total foreign revenue generated by the computer and data processing service industry and estimated total foreign revenue for selected service industries, 1980-82

Year	Total foreign revenue for service industry 1/ (1)	Total foreign revenue for selected service industries 2/ (2)	Ratio of (1) to (2)
	1,000 U.S. dollars		Percent
1980	2,200,000	89,398,000	2
1981	3,000,000	109,611,000	3
1982	4,000,000	135,744,000	3

1/ Estimated based on discussion with industry and/or association representatives, and secondary sources.

2/ Based on totaling Commission estimated foreign revenue for each of the 14 selected industries covered in the study.

Source: Estimated by the staff of the U.S. International Trade Commission.

While nearly all sources project a rapid growth of computer and data processing services, most also project that the services market will exceed the hardware market eventually since hardware is dropping in price and the service sector is more labor intensive at the present time. U.S. firms and their foreign subsidiaries appear to be well positioned to serve the services market from the stand point of know-how, equipment, and experience.

The bulk of the revenue generated from foreign computer and data processing services is generally believed to be obtained from Europe. Data from three firms responding to the Commission's questionnaire support that estimate, although these data show decreasing revenues from Europe. Other regions, such as North America and Mexico, show increased revenues (table 4). Industry estimates are generally more optimistic for the growth rates in Western Europe. According to trade journals, an average growth rate for Western Europe is about 20 percent.

Trade in Merchandise Generated by Trade in Services

The relationship of computer and data processing service industry activity in foreign markets and U.S. merchandise exports can be characterized based on a number of insights provided by questionnaire respondents. The number of positive responses to a series of questions asked to determine

Table 4.--Regions and countries in which revenue is generated by computer and data processing service firms, 1980-82 1/

Region and country 2/	Number of responses			Percent of total respondents			Estimated revenue		
	1980	1981	1982	1980	1981	1982	1980	1981	1982
							------1,000 U.S. dollars------		
Middle East	1	1	1	33	33	33	3/	3/	3/
Israel	-	1	-						
Far East	2	2	2	67	67	67	3/	3/	3/
Australia	-	2	-						
Japan	-	2	-						
South Korea	-	1	-						
New Zealand	-	1	-						
Latin America	2	2	1	67	67	67	3/	3/	3/
Argentina	-	1	-						
Brazil	-	2	-						
Venezuela	-	2	-						
Europe	3	3	3	100	100	100	3/	3/	3/
West Germany	-	1	-						
France	-	3	-						
Italy	-	1	-						
Netherlands	-	1	-						
United Kingdom	-	3	-						
Africa	1	1	1	33	33	33	3/	3/	3/
South Africa	-	1	-						
Canada	3	3	3	100	100	100	3/	3/	3/
Mexico	2	2	2	67	67	67	3/	3/	3/
Other	1	1	1	33	33	33	3/	3/	3/

1/ Country listing is for 1981 only.
2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 3 of 19 firms surveyed. Respondents represent about 15 percent of the foreign revenue of the estimated 19 major firms believed to be operating internationally in 1981.
3/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

whether or not U.S. merchandise exports are generated by U.S. computer and data processing service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
Do you believe that U.S. merchandise might be used as a result of the services your firm provides abroad?------------------------------	3	100
Is U.S. merchandise specified or recommended in the course of providing your service?-------------	3	100
Are U.S. merchandise exports believed to be directly generated?-----------	3	100

1/ The total number of questionnaire respondents in this service industry was 3 of 19 firms surveyed. Respondents represent about 15 percent of the foreign revenue of the 19 major firms believed to be operating internationally in 1981.

Because of the relatively low response rate to the merchandise trade section of the questionnaire, the Commission is unable to extrapolate with certainty the value of U.S. merchandise exports directly generated by U.S. computer and data processing service activities abroad. However, three industry respondents estimated that their service activities overseas resulted in the total U.S. export of approximately $218 million in goods in 1981 (table 5). Based on this estimate, the number of respondents, and the number of known firms in the industry, it is estimated that $3.8 billion in U.S. merchandise exports flowed as a result of U.S. computer and data processing activities abroad in 1981. However, it should be noted that at a confidence level of 95 percent, this figure could be as low as the actual respondents' estimate of $218 million or as high as $6.8 billion. For estimates of U.S. merchandise exports for 1980 and 1982, refer to table 5.

Since large producers of computers and computer peripherals manufacture and supply equipment in developed countries and many developing countries, the movement of merchandise involved in providing computer and data processing services frequently does not enter into international trade. Although the three respondents to the Commission's survey indicated that merchandise trade is generated directly from service activity, other industry sources indicate that merchandise used in providing foreign services is usually produced in the host country. Thus, the value of merchandise generated by service activity is probably small by comparison with domestic shipments generated by computer and data processing services.

Computer and data processing service firms surveyed cited data processing (computing) equipment and office machines as the principal type of exports

Table 5.--U.S. merchandise exports generated by U.S. computer and data processing services abroad, 1980-82 1/

Year	Number of responses	Exports of U.S. merchandise estimated by respondents	Projected 2/ total: U.S. merchandise for the service industry	+ 95 percent confidence limit for projected industry exports
		1,000 U.S. dollars		
1980	3	271,649	4,766,000	4,720,000
1981	3	217,606	3,818,000	3,063,000
1982	3	202,099	3,546,000	6,496,000

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 3 of 19 firms surveyed; respondents represent about 15 percent of the foreign revenue of the estimated 19 major firms believed to be operating internationally in 1981.

2/ By the U.S. International Trade Commission.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

which are generated to support their service activities abroad (table 6). There was also an indication by respondents that a significant portion of these service-related exports are considered to be high-technology products. 1/ The percentage of high-technology items indicated by respondents for 1981 exports ranged from 40 to 100 percent.

Host-country or third-country merchandise shipments 2/ can also be stimulated by U.S. service operations abroad. The number of positive responses to a series of questions asked to determine whether or not host-country or third-country merchandise shipments are generated by U.S. computer and data processing service activities abroad was shown in the following tabulation:

1/ High-technology encompasses items of high unit value, relative to the product field, and representing the leading edge of new technology with clear and superior performance characteristics.

2/ "Host-country merchandise shipments" refers to the shipments (within the host country) of host-country-manufactured products which are generated by U.S. service operations in the host-country market. "Third-country merchandise shipments" refers to the shipments of other foreign-manufactured products to a foreign market as a result of U.S. service operations in that market.

Table 6.--Estimated U.S. merchandise exports resulting from computer and data processing services abroad, by types and by principal markets, 1981 1/

Type	U.S. exports used in providing services 2/ 3/	Number of firms indicating U.S. merchandise exports to--							
		Middle East	Far East	Central and South America (excluding Mexico)	Europe	Africa	Canada	Mexico	All other
	1,000 U.S. dollars								
Total	217,606	2	3	2	3	1	3	3	
Machinery and equipment	216,800	2	3	2	3	1	3	3	
Data processing (computing) equipment	205,600	2	3	2	3	1	3	3	
Office machines and equipment	11,200		1	1	2		1		

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 3 of 19 firms surveyed; respondents represent about 15 percent of the foreign revenue of the estimated 19 major firms believed to be operating internationally in 1981.

2/ Based on 3 responses.

3/ U.S. exports were estimated, but respondents did not identify the specific type in all cases; thus, the subcategories do not add to the total shown.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Question	Number of responses 1/	Percent of total respondents
Do you believe that foreign merchandise might be used as a result of the services your firm provides abroad?------------------------------	1	33
Are foreign or host-country products specified or recommended in the course of providing your service?----------------------------	2	67

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 3 of 19 firms surveyed; respondents represent about 15 percent of the foreign revenue of the 19 major firms believed to be operating internationally in 1981.

Estimated third-country and host-country merchandise shipments resulting from U.S. computer and data processing services abroad in 1981 were as shown in the following tabulation:

Item	Value (1,000 U.S. dollars)
Third-country shipments-----------	80,100
Host-country shipments------------	400,100

These shipments are believed to consist primarily of data processing equipment and office machines.

International Service Trade Barriers

In local markets, foreign subsidiaries of U.S. firms usually do not face the barriers which often confront efforts of U.S.-based service firms such as favoritism for local suppliers and barriers to communications. The major restrictive measures impeding international expansion of trade in computer and data processing services are the alleged activities by foreign governments which restrict trade in the hardware associated with the services. 1/ Thus, countries which subsidize or otherwise support their computer and computer peripheral industry reduce the export potential of U.S.-produced hardware and services. Further, foreign governments generally have weak or ineffective copyright and patent infringement laws which affect the U.S. computer services industry, because insufficient protection of proprietary information could result in considerable loss of revenues through piracy of programs worth large sums when retailed. Industry sources further point out that international

1/ For a list of restrictive measures, see Trade Barriers to Telecommunications, Data and Information Services, United States Trade Representative Computer Group, Nov. 14, 1980.

barriers to the flow of communications services adversely affect U.S. trade in computer services in that data processing and software are frequently transmitted by radio across national boundaries.

The three firms responding to the Commission's survey were unanimous in reporting trade barriers in (1) the right of establishment in foreign countries, (2) trade in goods such as local purchase requirements and restricted entry of goods, (3) trade in services such as operating/ownership restrictions, (4) government procurement practices giving preferences to national firms, and (5) foreign-exchange controls such as limitations on currency convertibility (table 7).

The Commission requested that firms reporting trade barriers provide an assessment of the economic effects of lifting the trade barriers. The number of responses to determine the economic effects of international barriers to U.S. services trade and associated product exports in computer and data processing service activities abroad was as follows:

Question	Number of responses 1/	Percent of total respondents
What effect, if any, would reduction or removal of service trade barriers have upon your receivables, billings, or revenues in current or potential country markets?:		
Increase	2	67
Decrease	0	0
No effect	1	33
What effect, if any, would reduction or removal of service trade barriers have upon potential U.S. products exports in current or potential country markets?:		
Increase	3	100
Decrease	0	0
No effect	0	0

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 3 of 19 firms surveyed. Respondents represent about 15 percent of the foreign revenue of the 19 major firms believed to be operating internationally in 1981.

Table 7.--Trade barriers to international services in the computer and data processing industry 1/--Continued

Category and barrier	Number of responses	Percent of total respondents
Subsidies/countervailing duties	2	67
Direct financial aid to local firm by government	2	
Preferential financing arrangements	1	
Standards/certification	2	67
Health and safety requirements	1	
Local labor or material requirements	1	
Foreign-exchange controls	3	100
Restrictions on remittances	2	
Convertibility limitations	3	
Delays in obtaining foreign-exchange permit	2	

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 3 of 19 firms surveyed. Respondents represent about 15 percent of the foreign revenue of the 19 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

The economic effects of reducing or eliminating trade barriers were estimated by one firm to be an increase in revenue in Latin America and Mexico of 80 percent or more. An increase from Canada was estimated at 50 percent and from other major markets by 10 percent or more (table 8). All respondents indicated that U.S. product exports would benefit from reduction in trade barriers, increasing by as much as 30 percent in the machinery and equipment sector (table 9). Although many firms in the computer and data processing service industries are multiproduct firms, none reported economic effects in such sectors as chemicals, minerals and metals, or miscellaneous manufactures.

Conditions of Competition in Current and Potential Service Markets

Computer and data processing services in foreign countries are similar to those provided in the United States. In many cases, the advantages in obtaining a contract for services falls to a local firm or a firm in close proximity to the customer. The ability to communicate in the language of the customer further aids in obtaining a services contract. U.S. firms have greater experience in computers and computer services and are generally considered to be the world technology leaders in designing and developing new computers and periperals. Foreign firms are not a large factor in the U.S. market at this time. Industry sources allege that many developed and developing countries have relied on nontariff measures in attempting to build internal capability to rival U.S. firms.

Table 8.--Estimated changes in revenues absent trade barriers to international business of computer and data processing service firms, by areas 1/

Area and direction of change	Number of responses	Percentage change						
		10	20	30	40	50	60	80
Middle East:								
Increase	1			1				
Decrease								
Far East:								
Increase	2	1		1				
Decrease								
Latin America:								
Increase	1							1
Decrease								
Europe:								
Increase	1	1						
Decrease								
Africa:								
Increase	1	1						
Decrease								
Canada:								
Increase	2	1				1		
Decrease								
Mexico:								
Increase	2	1						1
Decrease								

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 3 of 19 firms surveyed. Respondents represent about 15 percent of the foreign revenue of the 19 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 9.--Estimated changes in U.S. merchandise exports absent trade barriers to international business of computer and data processing service firms, by types 1/

Type and direction of change	Number of responses	Percentage change						
		10	20	30	40	50	60	80
Machinery and equipment:								
Increase	3	1		2				
Decrease								

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 3 of 19 firms surveyed. Respondents represent about 15 percent of the foreign revenue of the 19 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

The largest firms supplying computer and computer peripherals are based in the United States and are the principal source of computer and data processing services in the United States, as well as among the leading suppliers in many foreign countries. While most developed countries have established their own industries to some degree, developing countries have not achieved significant success, although many of them already have programs in effect to promote local data base and data processing service companies.

The competitive environment of U.S. computer service operations in foreign markets can be characterized based on a number of insights provided by questionnaire respondents. Respondents appear to be facing increased competition from national firms in France and West Germany (table 10), with the Netherlands also cited as a relatively competitive market. There were no developing countries listed in major markets. The success of foreign firms competing with U.S. firms in foreign markets was attributed to (1) experience in the market or service, (2) lower price, and (3) political or regional bias, according to the three firms responding to the Commission's survey (table 11). Significantly, each of the three respondents reported technology expertise as a strength of competing Japanese firms; this factor was not reported in other markets.

Table 10.—Number of firms competing 1/ with U.S. computer and data processing service firms abroad, by principal service markets 2/ in order of revenue generated, 1981 3/

Service market	Number of competing firms				
	Total 4/	National	Regional	World-wide	Other U.S. firms
United Kingdom	50	4	2	6	
France	50	15	5	2	6
Australia	20	5	5	7	3
Italy	10	3	3	4	
West Germany	25	13	5	2	5
Netherlands	50	-	-	-	-

1/ Based on 2 responses by questionnaire respondents.

2/ Other principal service markets for the industry may not be listed here if respondents did not identify the number of competing firms.

3/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 3 of 19 firms surveyed. Respondents represent about 15 percent of the foreign revenue of the estimated 19 major firms believed to be operating internationally in 1981.

4/ The number of competing firms, by geographic scope of operation, may not equal the total shown, since the categories may not have been viewed as mutually exclusive and respondents may not have been able to identify the type of firm when providing a total.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

The competitive strengths of the U.S. firms were reported to be (1) advanced technology and (2) experience in the market or service (table 12). Financial strength and superior quality associations were also reported as important factors. Potential markets mentioned by two respondents were principally in developing countries. In these markets, respondents reported only two advantages in competitive strength (table 13). They were superior technology and quality. These strengths were noted by both respondents with regard to China and Indonesia.

Table 11.--Likely reasons 1/ for competing firms' success in world computer and data processing service markets, by base countries of firms 2/

Base country	Lower price	Technology expertise	Preferential financing	Experience in the market or service	Superior quality association	Political or regional bias	Government support	U.S. restrictions
Australia	2		1	2		1		
Japan		3		1				
West Germany	1		1	1		1		
France	1		1	1		1	1	
Italy	1			1		1	1	
United Kingdom	1			2		1	1	
Total	6	3	3	8		5	3	

1/ The importance of each reason is indicated by the number of times each was designated, based on 2 responses.
2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 3 of 19 firms surveyed. Respondents represent about 15 percent of the foreign revenue of the estimated 19 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 12.--Likely reasons 1/ for the competitive strength of U.S. computer and data processing service firms in foreign service markets 2/

Service market	Lower price	Technology lead	Financial strength	Experience in the market or service	Superior quality association	Other
Far East:						
Australia		1		1	1	
Europe:						
West Germany		1			1	
France		2	1	1	1	1
Netherlands		1	1	1		1
United Kingdom		1	1	1		
Total		6	3	4	3	2

1/ The importance of each reason is indicated by the number of times each was designated, based on 2 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 3 of 19 firms. Respondents represent about 15 percent of the foreign revenue of the estimated 19 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 13.--U.S. computer and data processing service firms' competitive strengths 1/ in potential foreign markets 2/

Potential service market	Lower price	Technology lead	Financial strength	Greater experience	Superior quality
Far East:					
People's Republic of China----------------		2			2
Indonesia--------------		2			2
Taiwan----------------		1			1
Central and S. America (excluding Mexico):					
Chile-----------------		1			1
Total----------------		6			6

1/ The importance of each reason is indicated by the number of times each was designated, based on 2 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service was 3 of 19 firms surveyed. Respondents represent about 15 percent of the foreign revenue of the 19 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

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Construction and Engineering Service

Executive Summary

1. The dollar value of foreign revenues generated by construction and engineering services amounted to $5.6 billion in 1981. This service industry is also significant as measured by an estimated $52 billion in foreign contract awards signed by U.S. firms in 1981.

2. In 1981, approximately $1.8 billion in of U.S. merchandise exports flowed as a result of international construction and engineering service activities, according to data received in response to questionnaires. The majority of the exports generated were machinery and equipment, specifically electrical-power-generating and distribution equipment and construction equipment (including material-handling equipment). Additionally, large amounts of industrial paperboard and packaging are exported as a result of construction and engineering services abroad.

3. Industry respondents to the questionnaire estimated that nearly $10.5 billion in host-country and third-country product shipments were generated by U.S. construction and engineering service activities abroad in 1981, believed to consist principally of machinery and equipment, with availability and the economies of each project affecting the mix.

4. Industry sources indicate that there are numerous barriers to international trade in the construction and engineering industry, many of which are similar to those which restrict trade in goods. These obstacles serve to hinder trade and reduce the competitiveness of the U.S. industry. The barriers can basically be grouped into three broad categories: foreign-government subsidies, foreign-market impediments, and disincentives arising from U.S. Government policies.

5. About 70 percent of industry sources indicate, in response to questionnaires, that both revenues and U.S. product exports would increase with the reduction or removal of trade barriers. The reduction of these impediments could increase construction and engineering revenues in the Middle East by more than 20 percent, according to most companies; revenues in the Far East and Latin America could gain an average 30 percent. Machinery and equipment exports were cited by questionnaire respondents as the products that could have the largest revenue increase, ranging from 10 to 50 percent, with the reduction or removal of trade barriers.

6. U.S. firms are facing increased competition from host country as well as other foreign firms in such areas as the United Kingdom, West Germany, Mexico, and Ecuador.

7. U.S. firms actively engaged in marketing their services in the international arena have lost a significant number of contracts to foreign firms in recent years. The international competition for U.S. firms comes mainly from other industrialized nations, which are

alleged to grant a wide variety of government subsidies for the export of construction and engineering services to third markets. Important markets for U.S. construction and engineering firms in the short term include Canada, Saudi Arabia, Mexico, Egypt, Venezuela, Brazil, and Australia.

8. U.S. construction and engineering firms point out that foreign firms often obtain a competitive advantage in international activity as a result of significant support by their respective embassy or consular personnel in identifying commercial opportunities and potential international projects.

9. Reasons cited for the competitive strengths of the U.S. construction and engineering firms in foreign services markets include technology lead, superior quality association, and experience in the market. These were reasons cited for strength in both current and potential markets by respondents to the Commission's questionnaire.

Industry Profile

Definition and coverage

Construction is the process of assembling and joining component parts or materials into a relatively permanent structure. The construction industry invloves the building of houses, roads, bridges, airports, dams, oil refineries, gas-gathering plants, petrochemical facilities, nuclear power plants, hydroelectric plants, pipelines, factories, and harbors. Construction operations are generally classified according to specialized fields, which include preparation of the project site, foundation treatment, steel erection, asphalt paving, and electrical and mechanical installations. Contractors are classified as highway, heavy construction, general building, and speciality (such as pipe-line, communications, and power). The industry employs those trained in nearly every technical discipline, especially architecture and engineering; those skilled in the trades, such as master plumbers and electricians; as well as other skilled and unskilled labor.

Engineering includes the planning, designing, or management of machinery, roads, bridges, buildings, fortifications, waterways, and so forth. The five main branches of engineering are civil, mechanical, mining and metallurgical, chemical, and electrical. Engineers also can be classified according to the kind of work they do. These include construction, consulting, design, planning and management, production, sales, and test engineers.

The design and engineering of a project such as a modern petroleum refinery and its equipment calls for many engineering specialists to cooperate, as well as an interdisciplinary specialist to coordinate the various engineering functions. Engineers are involved with every phase of a construction project from preliminary drawings and bid proposal through construction of the finished facility.

The U.S. Department of Commerce allocates the data which it collects concerning the engineering and construction services industry in several sections of the Standard Industrial Classification (SIC) System.

"Engineering, Architecture, and Surveying Services" are classified in SIC Category 8911, along with design services. Construction services are included in SIC categories 1541, 1542, 1611, 1622, 1623, and 1629. Construction services related to energy are included in SIC Category 162, "Heavy Construction, Except Highway and Street Construction." However, certain specific services such as electrical work, concrete work, and water-well drilling (for cooling purposes) may be classified as "Special Trade Contractors" in SIC Major Group 17 if not done as part of a larger service project.

Firms covered in this study include U.S. construction and engineering, design and design-engineering and construction management companies operating domestically and internationally in 1981. The 38 construction and engineering service industry respondents to the Commission's questionnaire (of 93 firms surveyed) represent about 30 percent of the foreign revenues of the 400 construction and engineering firms believed to be operating internationally in 1981.

Highlights in 1981

- NEW DOMESTIC CONTRACT AWARDS of the construction and engineering service industry amounted to $119.1 billion.
- U.S. ESTABLISHMENTS are estimated to number more than 75,000 dealing in all engineering and construction services.
- U.S. EMPLOYMENT in these establishments totaled approximately 4,399,000.
- INTERNATIONAL REVENUES are estimated to have amounted to $5.6 billion. Foreign revenues related to engineering and construction of energy-related projects are estimated to account for approximately $4.2 billion.
- FOREIGN ESTABLISHMENTS are estimated to number more than 250,000 firms operating worldwide.
- NEW FOREIGN CONTRACT AWARDS of construction and engineering firms totaled $52.0 billion.
- THE U.S. TRADE BALANCE in the construction and engineering services sector probably favors the United States.

Industry structure

The construction and engineering services sector consists of firms engaged in the design and construction of industrial facilities and Government-sponsored projects, as well as those firms which offer construction management services. The industry is composed of tens of thousands of companies ranging in size from 2-man partnerships to multinational firms employing upwards of 20,000 or more people, both in this country and abroad. The sector is basically organized according to services provided: design and architectural, engineering, pure construction, and construction managment. Many firms specialize in one or two particular areas; large multidiscipline firms have the capabilities to perform every facet of the business from the initial proposal and bid through the design to a facility completed 4 or more years later.

In 1977, there were over 31,000 U.S. firms providing construction and engineering services. 1/ Of this total, there are about 400 to 500 which have dominated the industry both in domestic and international contracts. An industry source indicates that these firms accounted for 80 to 90 percent of the domestic market, and 90 to 100 percent of the U.S. share of the foreign market in 1981. 2/ Within this latter group of dominant firms there are about 30 leaders, which are those firms capable of assuming the prime contractors' role on several major projects simultaneously.

U.S. construction and engineering firms provide a wide range of services from inception of a project to completion, including post-construction services. A representative list of services offered by major firms includes preparation of technical and economic feasability studies; development of architectural designs; site analysis and selection; definition and evaluation of infrastructure requirements; international financing services; bid review and analysis; development of preliminary budgets; procurement of materials and equipment; coordination of civil, structural, and mechanical engineering services; data processing; recruitment and training of supervisory personnel; field construction; and any necessary maintenance services.

Ten years ago, a U.S. firm might have provided all of the above-mentioned services for a specific project, however, in recent years, U.S. firms are increasingly being employed as "construction managers," providing their technical expertise as opposed to performing the actual project construction. 3/ Many countries have the necessary labor and capital but lack the technical knowledge to design and construct a major project. Typical construction management services provided by U.S. firms to these countries include constructability planning, cost control, purchasing and procurement of equipment, coordinating contractors' activities, and construction surveillance.

According to the 1977 Census of Service Industries, receipts of over $14 billion were generated by approximately 75,580 establishments owned by 31,682 firms supplying engineering, architectural, and surveying services in 1977 (the last year for which data are available). The most recent data available indicates that employment in these firms totaled approximately 373,150 in 1977. However, industry sources indicate that the actual size and relevance of the construction and engineering services sector is difficult to ascertain since construction firms frequently do not differentiate income by types of projects undertaken. Additionally, when computing revenues, firms do

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1/ "1982 International Construction Forecast," Constructor, January 1982, p. 61.

2/ Engineering News Record, Apr. 16. 1981, pp. 82-185; May 21, 1981, pp. 60-97; July 16, 1981, pp. 68-93; and Oct. 15, 1981, pp 30-32.

3/ Telephone conversation with a representative of the National Constructors Association, Washington, D.C., Jan. 29, 1982.

not usually specify whether income was derived from the sale of professional services or equipment. One estimate indicates that energy and energy-related projects accounted for approximately one-third of total domestic receipts in 1977. 1/

In general, most major firms are reluctant to give out information regarding their construction activities because of the intense competition they are now experiencing both abroad and domestically. According to industry figures, however, total revenues for the major firms which make up the construction and engineering, design, and construction management industries amounted to $20.7 billion in 1981, representing 2.5 percent of total service sector revenues of $837.0 billion for the 14 service sectors covered in this study. The industry, however, measures new business on the basis of yearly contract awards. The value of new contract awards among the three divisions in 1980 and 1981 is shown in the following tabulation (in billions of dollars):

	Foreign	Domestic	Total
1980 awards:			
Construction and engineering---	34.0	79.0	113.0
Design--------------------------	1.1	6.1	7.3
Construction management--------	13.0	20.0	33.0
1981 awards:			
Construction and engineering---	32.7	87.5	120.2
Design--------------------------	1.2	7.1	8.3
Construction management--------	18.1	24.5	42.6

Recent trends and outlook

The measure of growth for U.S. firms in the international construction and engineering services sector is the value of foreign contracts signed. During 1981, foreign contracts signed by U.S. firms amounted to about $52.0 billion, up from $48.1 billion in 1980. 2/

Foreign contracts signed by U.S. firms were concentrated heaviest in refineries, synfuels, marine work, and power generation. The weakest areas for foreign work by U.S. firms were forestry projects and manufacturing plants. During 1980, port construction activity reportedly increased somewhat, with significant improvement during 1981, especially for deepwater port construction

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1/ Contruction firms are covered separately in the 1977 Census of Construction Industries. The construction censuses covered here are shown in separate industry series and include the following Standard Industrial Classification (SIC) code numbers: SIC 1541, SIC 1542, SIC 1611, SIC 1622, SIC 1623, and SIC 1629. In 1977, the 58,022 establishments covered in the aggregate by these codes had 1,430,741 employees and generated total receipts of $88.2 billion. It is estimated that energy projects in 1977 from these series accounted for roughly 30 percent or less of the total receipts.

2/ "Energy Markets and Foreign Work Boost '80 Awards," Engineering News Record, Apr. 16. 1981, pp. 82-88.

to handle increased world coal trade. Construction of chemical plants reportedly improved during 1981; new refineries and synfuel projects maintained their 1980 level of investment. 1/ The strongest world markets for large-scale construction activity worldwide is in the development of oil, gas, and other energy-related fields. Minerals exploration projects reportedly have also been increasing worldwide and should continue to improve. 2/

During 1978 and 1979, U.S. construction and engineering firms experienced a decreasing share of the world construction business. This decrease was most pronounced in the Middle East where much of the new business goes to South Korean firms. During May 1978-June 1979, only 1.6 percent of the $21.8 billion in new Middle East construction contracts went to U.S. firms. 3/ In contrast, during June 1975-April 1978, U.S. firms were awarded more than 10 percent of Middle East construction contracts. 4/

Several reasons are cited for the decline in Middle East contracts signed by U.S. firms during 1978-79. Political differences have cost U.S. firms contracts in Iran, Libya, Iraq, and Syria. 5/ High-technology projects, once controlled by U.S. firms, are now being lost to a number of other competitors, especially to the South Korean, Italian, and Japanese firms, which are gaining expertise in state-of-the-art construction projects. 6/ Other factors cited by industry sources that are hindering more rapid growth for U.S. contracts signed in the Middle East and elsewhere include inequitable U.S. tax policies favoring foreign firms, lack of U.S. Government-backed project financing, and U.S. adherence to the Foreign Corrupt Practices Act. 7/

Despite market disadvantages, U.S. firms and their subsidiaries based in other highly industrialized nations are among the few companies in the world possessing the technical expertise to design and construct large refineries and petrochemical projects. The Middle East remains the largest market for U.S. construction of energy-related projects. However, in the future, the Middle East nations are expected to direct more of their development funds to building their infrastructure to facilitate futher industrialization during the early 1980's.

New projects awarded to U.S. companies in Latin America and Asia (particularly China) sparked a resurgence in U.S. firms' foreign construction activity during 1980 and 1981 by offsetting potential contracts lost in the Middle East. In Latin America, the demand for refinery and mining operations, as well as energy-processing plants, accounted for $13 billion in contracts in

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1/ Ibid.
2/ Ibid., p. 83.
3/ Curry, Bill, "U.S. Share of Mideast Contracts Declines," The Washington Post, Nov. 29, 1979, p. A-21.
4/ Ibid.
5/ "U.S. 'Arrogance' Cost Firms Billions in Lost Jobs," Engineering News Record, Nov. 29, 1979, p. 26.
6/ Ibid.
7/ Ibid., p. 28.

1980 and $10.3 billion in 1981. 1/ Most of the contracts were in the oil and gas area, although in 1981, there was a surge in demand for services in the synthetic fuels area.

The short-term outlook for U.S.-based engineering and construction firms' growth in the world market is promising, because this market is growing. 2/ The U.S.-based firms are adapting to changes in the market and have a high level of technical expertise. U.S.-based engineering and construction firms are expected to compete for most of the growing number of international contracts that are being awarded. 3/

Although the Middle East continued to be the major foreign market for U.S. firms in 1981, other important markets expanded in Latin America, the Far East, Australia, and Canada. Certain U.S. firms began to concentrate more heavily on these later markets in anticipation of slackening demand in the Middle East, caused by market saturation in addition to the economic and political difficulties in that area. Construction and design bids are also expected for the retooling and upgrading of already-existing facilities in Europe, where plants need to be modernized and refineries equipped to handle the less expensive, but more readily available, heavier petroleum feedstocks.

In order to increase their competitiveness, U.S. construction companies have altered their traditional methods of conducting business. One major change has been the initiation of joint ventures or partnerships between multidisciplinary (both engineering and construction) firms, or a design firm and a construction firm. During 1979, 35 percent of the world's top 200 engineering and construction firms were involved in joint ventures; foreign firms accounted for one-third of these projects. A recent survey of 80 U.S. contractors and 142 foreign contractors indicated that 98 percent of the foreign and 91 percent of the U.S. contractors were planning on forming this type of partnership in the near future. 4/ An example of an existing partnership is one formed between the Jacobs Engineering Group, Inc., located in Pasadena, Calif., and British contractor George Wimpey, Ltd. This association was formed in order to compete for an international hydrocarbons project. 5/ The first contract was awarded to Jacobs-Wimpey in April 1981 to replace extensive saltwater-piping systems in an Indonesian liquefied natural gas plant. 6/

According to industry sources, far more important to the overseas business success of U.S.-based engineering and construction firms than the removal of nontariff barriers in foreign countries is the existence of certain disincentives arising from U.S. Government policies. The disincentives most

1/ Engineering News Record, Apr. 16, 1981, and Apr. 22, 1982, p. 115.

2/ "1982 International Construction Forecast," Constructor, Jan. 1982, p. 48.

3/ "Foreign Work Powered by Resources Development," Engineering News Record, Apr. 16, 1981, p. 115.

4/ Engineering News Record, "Joint Ventures Win Big Contracts," Apr. 30, 1981, p. 25.

5/ Engineering News Record, "Jacob Engineering's Goal: Quintupling," Aug. 13, 1981, p. 24.

6/ Engineering News Record, "Joint Ventures Win Big Contracts," Apr. 30, 1981, p. 25.

frequently mentioned by industry sources include (1) U.S. tax treatment of foreign earned income, (2) the Foreign Corrupt Practices Act, (3) antiboycott restriction, and (4) antitrust regulations.

Another aspect of the increasing demand for all services is that one project typically breeds another. For example, once a firm has completed an oil refinery, there is usually the demand that a primary petrochemicals plant be built to take advantage of the readily available feedstocks. There is also a need for the construction of facilities for the transport of both the feedstock and whatever products are manufactured throughout the system. The demand for infrastructure to handle the social and economic needs of the host nation also leads to the construction of many projects outside of the energy field.

In recent years, the U.S.-based engineering and construction firms have faced increased international competition from their traditional European and Japanese rivals as well as from new competitors from the Republic of Korea and Taiwan. However, the U.S. industry should do well in the short term because of its acknowledged lead in certain types of engineering.

U.S. Service Operations in Foreign Markets

Operating structure

Foreign markets, particularly in developing nations, have become an integral part of the revenues of large construction and engineering firms. According to industry sources, U.S. construction firms operating abroad collectively receive from one-fifth to one-third of their billings from foreign sources. 1/ Additionally, profits from foreign work generally provide a greater return than profits from domestic work. Average profit on foreign work revenues in 1980 exceeded 10.0 percent, compared with a 3.5-percent return on domestic project revenues. 2/

U.S. Government and industry officials indicate that 8 to 10 percent of the typical new construction contract represents the value of construction/engineering services exported; 2 to 6 percent of the total value of foreign projects managed by U.S. firms constitutes the value of construction management services. In regard to design-only work, design services constitute 100 percent of the value of foreign contracts awarded to U.S. firms. 3/

U.S. construction and engineering firms operate in foreign markets in a number of ways, including joint ventures, affiliated companies, subsidiary companies, international divisions, export departments, and combinations of the above. Some firms incorporate only in the United States and generally operate through export divisions or international divisions. Firms that

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1/ U.S. Department of Commerce, Current Developments in U.S. International Service Industries, March 1980, p. 51.

2/ "List Leaders Charge With New Roles and Markets," Engineering News Record, July 16, 1981, p. 73.

3/ Economic Consulting Services, Inc., The International Operations of U.S. Service Industries: Current Data Collection and Analysis, Washington, D.C., June 1981.

derive a part of their income from foreign contracts usually have affiliates or subsidiaries which are permanently registered in one or more foreign nations--usually in those nations that either have, or are likely to generate, new projects or renovation and repair projects. A few of the larger construction and engineering firms have even gone so far as to locate the headquarters of their international divisions overseas. 1/ According to data received from 38 industry questionnaires, 82 percent of the firms responding indicated that they had subsidiaries or branches overseas, and 66 percent stated that they had foreign affiliates (table 1). Participation in joint ventures was indicated by 79 percent of the respondents, and licensing was cited by 8 percent as the operating structure utilized in international operations. In general, most U.S. firms operating abroad employ expatriate personnel, averaging around 1,300 persons per firm. 2/ Questionnaire

Table 1.--Operating structures of principal service activity, and revenues associated with secondary service industry activities of construction and engineering service firms in foreign markets, 1981 1/

Item	Revenues 2/	Number of responses	Percent of total respondents
	1,000 U.S. dollars		
Operating structure:			
Foreign affiliate	-	25	66
Joint venture	-	30	79
Licensing	-	3	8
Subsidiary or branch	-	31	82
Other	-	7	18
Secondary service activity:			
Consulting and management services	1,261,938	18	47
Equipment-leasing and rental services	3/	1	3
Other	3/	4	11
Total	1,263,705	23	60

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 38 of 93 firms surveyed; respondents represent about 30 percent of the foreign revenue of the major 400 firms believed to be operating internationally in 1981.

2/ Calculated by the staff of the U.S. International Trade Commission from receivables, billings, or revenue data provided by respondents.

3/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

1/ Annual report of Fluor Corp., 1980 and the annual report of Jacobs Engineering Group, Inc., 1980.

2/ "Overseas Rivals Gain Ground and Eye New Markets," Engineering News Record, July 17, 1980, p. 46.

respondents also indicated that they often provide other services in addition to construction and engineering services. Consulting and management and equipment leasing services were cited as secondary service activities.

Overseas construction contracts secured by American firms originate from numerous sources. While a portion of their business is obtained through the bidding process of international funding agencies, the bulk of foreign contracts obtained by American firms originate directly from successful bidding overseas. The primary markets for construction and engineering services include local governments, local private firms, multinational corporations, and services required under grant or loan from international lending agencies or financial institutions. The local government market is generally the major source of engineering contracts. Typical projects for which local governments may require the services of foreign constructors and engineers include the development of "infrastructure" such as roads, tunnels, bridges and ports, as well as schools and hospitals. Local private firms also offer opportunities in the construction of factories and office buildings. Multinational corporations and potential investors planning to establish in-country or regional operations offer a market for the design and construction of such facilities as warehouses, pipelines, industrial, and manufacturing plants, in addition to other commercial buildings. Multilateral lending agencies, such as the World Bank, offer opportunities for major projects; such opportunities are particularly important in developing countries, where financing is critical to a project. 1/

Firms operating in developing nations, where nationalism is generally high, often set up local subsidiaries or affiliated firms. A number of developing nations have enacted legislation requiring construction firms which have secured large contracts to incorporate locally. 2/ Alternatively, many countries (about 30, identified in the section on international service trade barriers) now require that foreign firms must be associated by joint venture with a local firm to obtain contracts.

There are two basic reasons for these joint-venture requirements. First, many construction projects are highly labor intensive, particularly the building of schools and roads. Developing countries have an interest in promoting local industries which are labor intensive and require a low level of skills as part of their overall development plan. Thus, through joint ventures and/or local participation requirements, countries are able to promote employment. 3/ Their second motivation is to improve their own technical expertise and develop skills and capabilities in their workforce which do not currently exist. U.S. construction and engineering firms help to train the local unskilled labor force in the techniques of the construction trade and upgrade the capability of the local construction firms by helping them to become diversified and skilled in the competition of complex projects. According to industry sources, these local firms are then able to

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1/ U.S. Department of Commerce, Recent Trends in Consulting Engineering, July 21, 1981, p. 4.

2/ Robert F. Cushman, Esq., Construction Business Handbook, 1978, pp. 5-1 to 5-7.

3/ United States Trade Representative, Trade Issues in the Engineering and Construction and Related Consultancy Service Industry, September 1981. p. 11.

undertake subsequent projects either with no help from U.S. firms or with the U.S. firm acting only in an advisory role.

There are many variations in the basic organization of a joint venture; however, four characteristics are common in most associations. These include a board of directors, that controls the overall operation and resolves any conflicts; an internal management, led by a managing director, that runs the venture as would the head of a conventional company; a managing partner, with the responsibility of providing leadership and coordinating activities between the parties; and a system of management control--the framework for conducting relations among all parties. 1/ Additionally, a joint venture is not always a 50-50 partnership. The degree to which each associate is involved differs from case to case.

Just as there are many variations in the basic organization of a joint venture, there are also numerous reasons for voluntarily entering into such an association. U.S. firms engage in joint ventures with domestic or foreign companies in order to combine technical skills to expand their own capabilities, spread the risk associated with working abroad, and to obtain preferred financing arrangements. Sharing in government subsidies offered by many foreign countries is also cited as an important reason for these partnerships. Pakistan and India are among those Governments which will give financial assistance to a joint venture that includes one of their nation's companies. However, for U.S. firms, one of the most important reasons for international joint venturing is the access to less expensive manpower. 2/ Recently, several Chinese corporations have been actively soliciting Western companies to participate in a joint venture on construction projects. They have indicated that they are primarily interested in supplying labor to large construction projects where foreign firms have won the overall contract. 3/

The scope of U.S. construction and engineering firms' involvement overseas depends on several factors, including the ability of the firm to compete successfully for large-scale projects 4/ and the willingness of firms to commit themselves to major overseas projects. Some major firms are more conservative in their orientation and thus favor domestic projects. 5/ On the other hand, some major U.S. construction and engineering firms are deeply committed to foreign projects, which provide a large share of their annual revenue, in spite of the uncertainty associated with working in developing countries. 6/

1/ "Joint Ventures Win Big Contracts," Engineering News Record, Apr. 30, 1981, p. 25.

2/ "Joint Ventures Win Big Contracts," Engineering News Record, Apr. 30, 1981, p. 25.

3/ "Chinese Companies offering Labor on Foreign Projects," Department of State Airgram, Mar. 3, 1980, p. 3.

4/ "U.S. Engineering Firms Losing Global Business," Chemical and Engineering News, Sept. 14, 1981, p. 17.

5/ "Jacobs Engineering Goal: Quintupling by '86," Engineering News Record, Aug. 13, 1981, p. 24.

6/ "Fluor's Global Energy Machine Tuned for Tomorrow," Engineering News Record, Feb. 14, 1980, p. 41.

Growth trends and U.S. investment

The U.S. construction and engineering industry has invested several million dollars in facilities abroad, including office space for regional offices and headquarters buildings for international divisions, as well as research and development laboratories for engineering and other scientific studies. According to data received from industry questionnaires, it is estimated that $203.8 million was invested in physical assets of foreign operations of U.S. companies in 1981. Foreign establishments are estimated to have totaled 335 in 1981 (table 2.) Many of the construction and engineering firms make the equipment used in the construction of energy facilities, and in order to sell their equipment to foreign projects, many of these firms have built manufacturing plants overseas.

A recent study 1/ reports that new foreign contracts awarded to the 400 leading U.S. construction contractors increased from $15.6 billion in 1976 to $32.7 billion in 1981, or by 109.6 percent. Construction management fees also contributed significantly to international revenues in 1981, amounting to $18.1 billion in new contracts. Design-only firms earned only $1.2 billion for foreign design work in 1981. 2/ Estimated foreign service generated by the construction and engineering services industry represents about 5 percent of total service sector trade (table 3).

1/ Economic Consulting Services, Inc., The International Operations of U.S. Service Industries: Current Data Collection and Analysis, June 1981, p. 121.
2/ Ibid.

Table 2.--Indicators of activity in the foreign and domestic operations of construction and engineering service firms, 1980-82

Item	Foreign	Domestic	Total
Estimated value of receivables, billings, or revenues: 1/ 2/			
1980------------------1,000 dollars--:	3/	3/	3/
1981---------------------------do----:	3/	3/	3/
1982---------------------------do----:	3/	3/	3/
Estimate of investment in physical assets 1/ 4/ in foreign operations:			
1980------------------1,000 dollars--:	216,507	-	-
1981---------------------------do----:	203,797	-	-
1982---------------------------do----:	204,109	-	-
Number of establishments: 1/			
1980-----------------------------------:	320	314	633
1981-----------------------------------:	335	326	660
1982-----------------------------------:	359	322	680
Estimated 5/ value of total sector receivables, billings, or revenues:			
1980------------------1,000 dollars--:	5,300,000	13,200,000	18,500,000
1981---------------------------do----:	5,600,000	15,100,000	20,700,000
1982---------------------------do----:	5,800,000	15,500,000	21,300,000

1/ Data are for questionnaire respondent only. The total number of questionnaire respondents in this service industry was 38 of 93 firms surveyed; respondents represent about 30 percent of the foreign revenue of the 400 major firms believed to be operating internationally in 1981.

2/ Excluding the value of any merchandise exports.

3/ Data submitted by respondents are not comparable and, therefore, have been deleted from this report.

4/ Including the undepreciated book value of land, plant, and equipment.

5/ By the staff of the U.S. International Trade Commission based on discussions with industry and/or association representatives, and secondary sources.

Source: Compiled from data submitted in response to questionnaries of the U.S. International Trade Commission.

Table 3.--Estimated total foreign revenue generated by the construction and engineering service industry and estimated total foreign revenue for selected service industries, 1980-82

Year	Total foreign revenue for service industry 1/ (1)	Total foreign revenue for selected service industries 2/ (2)	Ratio of (1) to (2)
	1,000 U.S. dollars		Percent
1980	5,300,000	89,398,000	6
1981	5,600,000	109,611,000	5
1982	5,800,000	135,744,000	4

1/ Estimated based on discussion with industry and/or association representatives, and secondary sources.
2/ Based on totaling Commission-estimated foreign revenue for each of the 14 selected industries covered in the study.

Source: Estimated by the staff of the U.S. International Trade Commission.

Estimated total foreign revenues for U.S. construction, engineering, and design firms amounted to $5.8 billion in 1981. 1/ Industry sources report that energy-related projects accounted for 75 percent of the value of foreign projects obtained by U.S. firms in 1981. 2/ During 1976-80, industry sources estimate that foreign energy projects as a percent of total foreign projects increased by no more than 10 percent.

There are mixed views regarding the effect of further development in foreign energy sources on the awarding of future energy-related contracts to U.S. construction and engineering firms. Some industry sources do not believe that the share of energy-related contracts awarded abroad will change significantly during the current decade. 3/ The dominance of petroleum-related projects in the future is questioned, and one source stated that U.S. contractors no longer view oil-producing countries as their best future sources of income. 4/ Other sources, however, claim that energy contracts, including refinery reconfiguration, project management, and oil and gas

1/ Economic Consulting Services, Inc., The International Operations of U.S. Service Industries: Current Data Collection and Analysis, June 1981, p. 121.
2/ Based on information developed during telephone conversations with industry sources. These sources reported that foreign estimates may not include the residential and commercial construction done by national contractors. No data is yet available for 1981.
3/ Based on information obtained during telephone conversations with representatives of construction and engineering firms.
4/ Engineering News-Record, July 16, 1981, p. 69.

recovery jobs are still important for the U.S. construction and engineering industry at home and abroad. 1/

An official of a leading construction and engineering trade association stated that the type of construction and engineering energy projects abroad will change. 2/ In the future, more emphasis will be placed on infrastructure projects which are ancillary to petroleum refineries or petrochemical plants. A number of the energy-rich nations have already finalized the contracts for many of the proposed oil refineries, gas-gathering plants, and so forth. In the future, these facilities will need maintenance and repair, much of which can be handled by local firms that will have been trained by U.S. construction and engineering firms in the sophisticated technology needed to maintain these plants.

Regional and country activity

The Middle East has traditionally been the major regional market for U.S. construction and engineering services. 3/ (See table 4 for specific country activity in 1981, as indicated by questionnaire respondents). A large portion of the fiscal years 1981 and 1982 budget for military construction is allocated to upgrade bases in the Indian Ocean/Persian Gulf region, in conjunction with an expansion of the U.S. Rapid Deployment Forces in Diego Garcia, Oman, Kenya, Eygpt, Somalia, and Lajes in the Azores. Industry officials indicate that the majority of this work will be reserved for American contractors. 4/ International contractors will thus continue to find Middle East countries an attractive market, although several major firms believe that major activity has peaked, because most major infrastructure jobs are completed or near completion.

Asia and Latin America also provided a significant amount of new contracts for U.S. firms in 1981. Asian countries, in particular, signed up numerous U.S. firms to provide contracting and management services on new projects. With vast resources in copper, diamonds, coal, and other minerals, Australia was the most lucrative market in Asia for the leading U.S. contractors. Other important Asian markets in 1981 included South Korea, Indonesia, Malaysia, and the People's Republic of China. In Latin America, Venezuela, Argentina, and Brazil were important contributors to new contract awards. Among the European countries, the United Kingdom, the Netherlands, and France were important sources of new business in 1981. Canada was also a major market for U.S. firms because of the expansion of the country's

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1/ Engineering News-Record, Apr. 16, 1981, pp. 83, 84, 114, and 115.

2/ An official of the American Consulting Engineers Council, Washington, D.C.

3/ U.S. Department of Commerce, Recent Trends in Consulting Engineering, July 21, 1981, p. 10.

4/ "International Construction in 1982," Constructor, January 1982, p. 48.

Table 4.--Regions and countries in which revenue is generated by construction and engineering service firms, 1980-82 1/

Region and country 2/	Number of responses			Percent of total respondents			Estimated revenue		
	1980	1981	1982	1980	1981	1982	1980	1981	1982
							------1,000 U.S. dollars------		
Middle East	27	33	30	71	87	79	2,759,433	207,417	8,308,040
Bahrain	-	1	-						
Iraq	-	3	-						
Israel	-	4	-						
Jordan	-	11	-						
Kuwait	-	4	-						
Oman	-	2	-						
Pakistan	-	2	-						
Saudi Arabia	-	24	-						
Syria	-	3	-						
Turkey	-	4	-						
United Arab Emirates	-	5	-						
North Yemen	-	2	-						
Far East	20	24	21	53	63	55	1,801,192	1,091,142	6,338,701
Australia	-	4	-						
Bangladesh	-	5	-						
China	-	2	-						
Taiwan	-	5	-						
India	-	2	-						
Indonesia	-	7	-						
Japan	-	2	-						
Republic of Korea	-	7	-						
Malaysia	-	4	-						
New Zealand	-	2	-						
Papria-New Guinea	-	1	-						
Philippines	-	7	-						
Thailand	-	9	-						
Latin America	17	24	23	45	63	61	93,491	359,374	680,637
Argentina	-	7	-						
Bolivia	-	2	-						
Brazil	-	9	-						
Chile	-	5	-						
Colombia	-	5	-						
Ecuador	-	4	-						
Guatemala	-	2	-						
Honduras	-	1	-						
Nicaragua	-	1	-						
Panama	-	6	-						
Paraguay	-	1	-						
Peru	-	4	-						
Venezuela	-	10	-						

See footnotes at end of table.

Table 4.--Regions and countries in which revenue is generated by construction and engineering service firms, 1980-82 1/--continued

Region and country 2/	Number of responses			Percent of total respondents			Estimated revenue		
	1980	1981	1982	1980	1981	1982	1980	1981	1982
							1,000 U.S. dollars		
Europe	10	15	12	26	39	32	66,728	94,131	350,818
Belgium	-	2	-						
West Germany	-	7	-						
France	-	1	-						
Ireland	-	3	-						
Italy	-	5	-						
Netherlands	-	6	-						
Portugal	-	2	-						
Spain	-	2	-						
United Kingdom	-	6	-						
Africa	22	29	21	58	76	55	1,953,591	374,133	1,628,939
Algeria	-	3	-						
Botswana	-	1	-						
Egypt	-	21	-						
Ethiopia	-	1	-						
Ghana	-	1	-						
Guinea	-	2	-						
Ivory Coast	-	2	-						
Kenya	-	2	-						
Liberia	-	3	-						
Libya	-	4	-						
Morocco	-	4	-						
Nigeria	-	7	-						
South Africa	-	5	-						
Sudan	-	1	-						
Tunisa	-	1	-						
Zaire	-	3	-						
Canada	9	13	9	24	34	24	1,198,547	58,349	103,487
Mexico	7	12	7	18	32	18	8,196	6,223	12,004
Other	11	12	11				5,753,388	944,444	447,467

1/ Country listing is for 1981 only.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 38 of 93 firms surveyed; respondents represent about 30 percent of the foreign revenues of the 400 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

petrochemical industry (table 4). 1/ Table 5 indicates the actual number of U.S. companies engaged in construction and engineering services and the regions they were working in during 1981: 2/

Table 5.--Number of U.S. firms engaged in construction and engineering services in foreign countries, by areas, 1981

Area	Number of firms	Area	Number of firms
Middle East:		Latin America:	
Bahrain	6	Argentina	16
Iraq	7	Bolivia	4
Israel	5	Brazil	19
Jordan	3	Chile	10
Kuwait	12	Colombia	10
Lebanon	3	Costa Rica	4
Oman	5	Equador	7
Pakistan	4	El Salvador	2
Qatar	4	Guatemala	8
Saudia Arabia	37	Guyana	1
Syria	2	Honduras	2
Turkey	9	Nicarugua	1
United Arab Emirates	10	Panama	10
North Yemen	1	Paraguay	2
		Peru	11
Asia:		Uraguay	2
Australia	18	Venezuela	25
Bangladesh	4		
Brunel	4	Caribbean Islands:	
Burma	1	Greater Antilles	14
China	7	Lesser Antilles	15
Taiwan	11		
Hong Kong	6		
India	9	North Africa:	
Indonesia	14	Algeria	9
Japan	9	Egypt	22
Republic of Korea	14	Ethiopia	1
Malaysia	12	Libya	5
New Zealand	10	Morrocio	5
Pacific Islands	9	Sudan	2
Philippines	6	Tunisia	5
Singapore	11		
Sri Lanka	7	Canada	42
Thailand	10		
		Mexico	26

1/ "Mideast Dip Slows Foreign Market," Engineering News Record, April 22, 1981, p. 115.
2/ Ibid.

Table 5.--Number of U.S. firms engaged in construction and engineering services in foreign countries, by areas, 1981--Continued

Area	Number of firms	Area	Number of firms
Africa:			
Angola	3	Europe:	
Cameroon	2	Austria	3
Cabon	1	Belgium	11
Ghana	2	Denmark	2
Guinea	1	East Europe	3
Ivory Coast	3	West Germany	11
Kenya	2	Greece	5
Liberia	2	France	14
Malawi	1	Ireland	9
Mozambique	1	Italy	10
Nigeria	10	Netherlands	15
Senegal	1	Portugal	5
South Africa	9	Scandinavia	6
Uganda	1	Spain	11
Upper Volta	1	Switzerland	4
Zaire	4	United Kingdom	27
Zambia	1	U.S.S.R	2
Zimbabwe/Rhodesia	1	Yugoslavia	6

Source: Prepared by the staff of the U.S. International Trade Commission based on data provided in the Engineering News Record, Apr. 22, 1981, p. 115.

Trade in Merchandise Generated by Trade in Services

Industry officials point out that sales of construction and engineering services in foreign markets creates U.S. exports of merchandise. This relationship is illustrated by industry response to questionnaires. The number of positive responses to a series of questions asked to determine whether or not U.S. merchandise exports are generated by U.S. construction and engineering service activities abroad was as follows:

Question	Number of responses 1/	Percent of total respondents
Do you believe that U.S. merchandise might be used as a result of the services your firm provides abroad?------------------------------	36	95
Is U.S. merchandise specified or recommended?------------------------	33	87
Are U.S. merchandise exports believed to be directly generated?-----------	32	84

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 38 of 93 firms surveyed; respondents represent about 30 percent of the foreign revenue of the 400 major firms believed to be operating internationally in 1981.

The most important U.S. merchandise export generated by construction and engineering firms, in terms of value, is the export of machinery and equipment required to construct projects. Included in this category of merchandise is construction equipment and material handling equipment. Finally, U.S. exports of services related to the construction of factories, petrochemical facilities, hydroelectric projects, and so forth creates U.S. exports of products needed to equip those facilities.

Because of the relatively low response rate to the merchandise trade section of the questionnaire, the Commission is unable to extrapolate with certainty the value of U.S. merchandise exports directly generated by U.S. construction and engineering activities abroad. However, these industry respondents estimated that their service activities overseas resulted in the total U.S. exports of approximately $1.8 billion in goods in 1981 (table 6). Based on this estimate, the number of respondents, and the number of known firms in the industry, it is estimated that about $22.4 billion in U.S. merchandise exports flowed as a result of U.S. firms' international construction and engineering service activities in 1981. However, it should be noted that at a confidence level of 95 percent, this figure could be as low as the actual respondent's estimate of $1.8 billion or as high as $37.1 billion. For estimates of U.S. merchandise exports for 1980 and 1982, refer to table 6.

Machinery generally regarded as construction machinery is produced by more than 200 U.S. manufacturers and is classified in the SIC under code

3531. The following is a list of selected construction machinery in that category.

Selected construction machinery in SIC 3531

Front-end loaders	Dredges
Off-highway tractors	Bulldozers
Backhoes	Snowblowers and throwers
Excavators (shovels)	Concrete mixers and batchers
Walking draglines	Bituminous pavers, finishers, and spreaders
Road rollers	Cranes
Scrapers	Off-highway trucks
Ditchers and trenches	Log skidders

Table 6.—U.S. merchandise exports generated by U.S. construction and engineering services abroad, 1980-82 1/

Year	Number of responses	Exports of U.S. merchandise estimated by respondents	Projected 2/ total: U.S. merchandise for the service industry	± 95-percent confidence limit for projected industry exports
		1,000 U.S. dollars		
1980	25	1,185,301	15,058,000	9,770,000
1981	25	1,824,120	22,401,000	14,736,000
1982	22	2,480,951	35,155,000	24,515,000

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 38 of 93 firms surveyed; respondents represent about 30 percent of the foreign revenue of the 400 major firms believed to be operating internationally in 1981.
2/ By the U.S. International Trade Commission.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

As illustrated in the following tabulation, both U.S. exports of construction machinery and the value of foreign contracts awarded to U.S. construction and engineering service companies have increased in recent years.

Year	Value of foreign contracts signed by U.S. companies 1/	Percentage increase from previous year	U.S. exports of construction machinery 2/	Percentage increase from previous year
	Billion dollars	Percent	Billion dollars	Percent
1979	3/	3/	4.5	-
1980	48.1	3/	5.7	26.7
1981	52.0	8.1	6.3	10.5

1/ Engineering New Record, Apr. 16, 1981.
2/ Compiled from official statistics of the U.S. Department of Commerce.
3/ Not available.

U.S. machinery manufacturers believe that the increase in foreign contracts signed by U.S. service companies helped spur increases in U.S. exports of construction machinery. Construction machinery exports (including material handling equipment) generated as a result of U.S. services provided abroad amounted to approximately $145.2 million in 1981, according to data received in response to industry questionnaires (table 7). The proportion of imported machinery on construction projects depends very much on the availability of this machinery in the host country. In the Middle East, for example, virtually all machinery must be imported because of the lack of local production of the required construction machinery. The proportion of machinery and materials on a Middle East project may be as high as 60 percent of the contract value. 1/ The percentage of procurement in the United States by all U.S. contractors working in Saudi Arabia, the largest Middle East construction market, was estimated to be about 80 percent for construction equipment. 2/ The percent of local procurement for most Western projects is much higher, because many types of construction machinery are produced in Western Europe.

Due to the generic nature of building materials, such as lumber or other wood products, cement, concrete, steel, plumbing products, fabricated steel, insulation, and so forth, country-of-origin considerations are less important; therefore, these products are most often obtained in the host country. For this reason, there is a limited foreign market for most U.S. building material. This is borne out by the data received in response to questionnaires indicating that U.S. exports of lumber, building products, and prefabricated buildings generated by construction and engineering services overseas amounted to only $2.6 million in 1981. However, a few categories of forest products are more likely than others to be exported because of their specialized nature. Industrial paperboard and packaging are examples of these products; exports of approximately $120.0 million were generated as a result of U.S. construction and engineering services abroad. Other products likely to be exported include certain lubricants and other products from petroleum, miscellaneous plastic products, fabricated steel plates, pipes, valves, pipefittings, and refrigeration equipment.

1/ "Vague Domestic Procurement Haunts Construction," Engineering News Record, Nov. 29, 1979, p. 32.
2/ Ibid.

Table 7.--Estimated U.S. merchandise exports resulting from construction and engineering services abroad, by types and by principal markets, 1981 1/

Type	U.S. exports used in providing services 2/	Number of firms indicating U.S. merchandise exports to-- Middle East	Far East	Central and South America (excluding Mexico)	Europe	Africa	Canada	Mexico	All other
	1,000 U.S. dollars								
Total	1,824,120	15	8	10	4	11	3	4	2
Machinery and equipment	935,614	11	6	6	2	7	3	3	1
Data processing (computing) equipment	9,594	3	4	3	1	3	1	1	
Office machines and equipment	428	2	3	1		2			
Electrical power generation and distribution equipment	789,203	8	2	6	2	6	3	2	1
Pulp paper machinery	72,500	1	1	1	1	1	2	1	
Metal working equipment	426	-	-	-	-	-	-	-	-
Construction machinery and equiment	62,795	4	2	4	1	3	1	1	1
Materials handling equipment	82,427	7	4	5	3	4	2	2	
Telecommunications equipment	6,346	2	1	2		2	1		
Motor vehicles and accessories	3,319	5	3						
Agricultural machinery and equipment	460	1	1	1		1			
Air conditioning and refrigeration equipment	11,298	2	1	2		3	1	1	
Machine tools and related equipment	1,357	1				2		1	
Pollution abatement equipment	33,725	4	4	5	3	4	2	2	
Machine parts	806	2	1	1		2			1
Water treatment equipment	4,535	2	2	1	1	2			
Miscelleneous machinery	1,550	2	1	1	1	1			
Forest products	192,908	3	1	2	2	2	1	1	1
Lumber and building products	866	1				1			1
Prefabricated buildings	1,732	1				1			
Paper products	70,310	2	1	2	2	1	1	1	
Industrial paperboard and packaging	120,000	1		1	1		1	1	
Textiles, apparel, and footwear	346	1							
Fabric and carpet	346	1							
Chemicals and related products	473	1	1			1			
Pneumatic tires	173	1				1			
Salt (NDG 1)	300		1						
Minerals and metals	5,849	2	1	1	1	2			1
Fabricated structural metal products	2,905	2	1	1	1	2			1
Industrial fasteners	173	1				1			
Handtools and hardware	173	1							
Ceramic tile, electrical and sanitary ware	2,598	1							

See footnotes at end of table.

Table 7.--Estimated U.S. merchandise exports resulting from construction and engineering services abroad, by types and by principal markets, 1981 1/--Continued

Type	U.S. exports used in providing services 2/	Number of firms indicating U.S. merchandise exports to--							
		Middle East	Far East	Central and South America (excluding Mexico)	Europe	Africa	Canada	Mexico	All other
	1,000 U.S. dollars								
Miscellaneous manufacturers	6,721	3	2	2	1	3	1		1
Electronic production and test equipment	2,500	1	1	1		1	1		
Medical instruments and apparatus	1,366	2							
Measuring and checking instruments and apparatus	1,550	3	2	2		2	1		
Surveying instruments or gauges	1,755	4	2	2		3	1		1
Nontextile floor coverings	250	2							
Kitchen supplies	100	1							
Electric equipment	8,200	1							

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 38 of 93 firms surveyed; respondents represent about 30 percent of the foreign revenue of the 400 major firms believed to be operating internationally in 1981.
2/ U.S. exports were estimated, but respondents could not identify the specific type in all cases; thus, the subcategories do not add to the totals shown.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

The final category of merchandise associated with exports of construction and engineering services involves merchandise used to equip factories, hydroelectric projects, nuclear power facilities, petrochemical facilities, port facilities, and other industrial projects. Products utilized in these projects will differ from year to year depending on the types of engineering and construction projects signed by U.S. companies. In large-scale industrial hydroelectrical, petrochemical, and nuclear facilities, U.S. engineering and construction firms also prefer U.S.-supplied equipment, because they have used U.S. equipment almost exclusively in the past. 1/ This is clearly illustrated in table 7, as electrical power generating and distribution equipment accounted for over 84 percent of total machinery and equipment exports generated by U.S. construction services abroad.

Bechtel Power Corp. reported the items which are likely to be exported at a rate higher than average, average, and below average as a result of U.S. construction and engineering operations overseas on an energy project. In this ranking scheme, the average export rate, calculated by Bechtel, is 30 percent; this means that 30 percent of the items thus ranked are exported. Above-average items, would be exported at a greater rate, and below-average items, at a lower rate. The following tabulation ranks some of the more commonly used energy project items: 2/

Above average	Average	Below average
Fired heaters, including furnaces, ovens, boilers, tubes, headers, stocks, and flues.	Columns, and pressure vessels, including towers, reactors, drums, trays, and liners.	Piping, including all process and utility piping, sewer and drainage piping, instrument piping and tubing, and columns and vessels.
Pumps and drivers, including all pumps and their drivers.	Tanks, including low pressure storage tanks, bins, and hoppers.	Electrical, including generators and drivers, motor controls, and transformers.
Vacuum equipment, including vacuum pumps, ejectors, and other vacuum producing apparatus.	Exchangers, including tubular exchangers, condensers, and evaporators.	Materials-handling equipment, including bucket elevators, conveyors, cranes, hoists, and weighing devices and hoppers.
	Instruments, including safety valves, indicators, and instrument panels.	
	Compressors and drivers, including expanders, blowers, and fans.	

1/ Korehi, URA, "Building Markets Overseas," The Construction Specifier, February 1981, p. 23.

2/ Based on information supplied by Bechtel Power Corp.

Above average--Con.	Average--Con.
General sawmills and planing mill products (SIC 2421).	Processing equipment, including crushers, pulverizers, and blenders.
Petroleum refining and miscellaneous products of petroleum and coal (291, 299).	Water and waste treatment, including clarifiers, chemical feeders, mixers, and agitators.
Miscellaneous plastics products (307).	Veneer and plywood (SIC 2435-6).
Fabricated plate work (3443)	Paints and allied products (285).
Pipes, valves, and pipe fittings (3494, 3498).	Nonferrous wire drawing and insulating (3357).
Refrigeration and heating equipment (3585).	Plumbing fixture fittings and trim (3432).
Switchgear and switchboard apparatus (3613).	Heating equipment, except electric (3433).
Wiring devices (3643-4).	Fabricated structural metal (3441).
	Lighting fixtures and equipment (3645-8).

The relationship between the export of U.S. construction and engineering services and shipments of foreign merchandise is more difficult to establish, because merchandise for foreign projects is not necessarily obtained in the home market of the country providing construction and engineering services. However, host-country and third-country merchandise shipments 1/ appear to be directly affected by these service activities.

The number of positive responses to a series of questions asked to determine whether or not host-country or third-country merchandise shipments are generated by U.S. construction and engineering service activities abroad was as shown in the following tabulation:

1/ "Host-country merchandise shipments" refers to the shipments (within the host country) of host-country-manufactured products which are generated by U.S. service operations in the host-country market. "Third-country merchandise shipments" refers to the shipments of other foreign-manufactured products to a foreign market as a result of U.S. service operations in that market.

Question	Number of responses 1/	Percent of total respondents
Do you believe that foreign merchandise might be used as a result of the services your firm provides abroad?------------------------------	32	84
Are foreign or host-country products specified or recommended in the course of providing your service?---	29	76

1/ Data are for questionnaire respondents only. The total number of respondents in this industry was 38 of 93 firms surveyed; respondents represent about 30 percent of the foreign revenue of the 400 major firms believed to be operating internationally in 1981.

Based on 17 questionnaire responses, estimated third-country and host-country merchandise shipments resulting from U.S. construction and engineering services abroad in 1981 were as shown in the following tabulation:

Item	Value (1,000 U.S. dollars)
Third-country shipments----------------	7,331,600
Host-country shipments-----------------	3,162,205

A U.S. construction and engineering company may specify French-made hydraulic excavators for a Middle-East project because of supply availability, price, or financing. Conversely, a French-based construction and engineering company may specify a superior quality and service package of U.S. material-handling equipment to equip a factory that the French firm is constructing in Africa. Simply stated, the export of U.S. construction and engineering services in foreign projects generates merchandise trade in both host or third countries and from the United States, with availability and the economics of each project affecting the mix.

International Service Trade Barriers

There are numerous barriers to international trade in the construction and engineering industry, many of which are similar to those that restrict trade in goods. The category and specific type of barriers identified by respondents to the Commission questionnaire are provided in table 8. Industry officials indicate that these obstacles serve to hinder trade and reduce the competitiveness of the U.S. industry. The severity of the trade-distorting effect depends greatly on the nature of the barrier and how consistently it is applied. The barriers can basically be grouped into three broad categories: government subsidies, foreign-market impediments, and disincentives arising from U.S. Government policies.

Government subsidies

Foreign governments allegedly engage in a number of practices which place U.S. construction and engineering firms at a distinct disadvantage in the world market. They include, most importantly, a wide variety of government subsidies for export of construction and engineering services to third-country markets. This subsidization takes many forms, including direct financial assistance, tax subsidies, and subsidies in the form, of government insurance of commercial and political risk for overseas contracts. 1/ According to data received in response to industry questionnaires, 39 percent of the construction and engineering firms surveyed indicated that some form of subsidization was provided to foreign competitors (table 8).

Many foreign countries provide financial assistance in the form of export credits for feasability studies and government guarantees against loss of bid. Subsidies provided for a feasability study and/or bid proposal are often a critical factor in obtaining construction contracts. 2/ It has been noted by industry officials that in most cases, the firm which performs the feasability study will be awarded the final contract. This is because firms hired to conduct feasability studies have the advantage of specifying designs, materials, and equipment which highlight their strengths.

Industry sources indicate that another type of direct financial assistance provided by many foreign countries is project financing. Many countries offer project financing for an indigenous construction and engineering firm at below prevailing market rates. According to the United States Trade Representative, over $5.5 billion was spent on interest rate subsidies by the major Organization for Economic Cooperation and Development (OECD) countries alone in 1980. New agreements were reached in October 1981 to raise the minimum interest rate levels under the OECD arrangements; however, this is expected to eliminate only 20 to 25 percent of the current interest rate subsidies. 3/

Tax subsidies are also provided by many third-world governments to assist indigenous construction and engineering firms in obtaining foreign and domestic construction contracts. The most common type is corporate tax exemptions on exported capital goods, building materials, and professional services employed on foreign projects. According to industry officials, in many developing countries, "infant" construction industries are given so much direct financial support by the government that they are increasingly able to underbid U.S. companies on foreign contracts.

The construction and engineering industry feels that firms operating abroad do so in an environment with potential risk of expropriation, nationalization, and changing political conditions. These risks must be valued, and their costs and the cost of insurance against them must be added into a contract bid. Official export credit agencies of many foreign

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1/ United States Trade Representative, Trade Issues in the Engineering and Construction and Related Consultancy Service Industry, September 1981, p. 4.

2/ Interview with a representative of the American Consulting Engineers Council, Washingtion, D.C., Feb. 5, 1982.

3/ David B. Perini, "International Construction in 1982," Constructor, January 1982, p. 49.

Table 8.--Trade barriers to international services in the construction and engineering industry 1/

Category and barrier	Number of responses	Percent of total respondents
Right of establishment	26	68
Restrictive employment regulations (e.g. local labor requirement)	17	
Credit, investment or financial activity restrictions	9	
Administrative/ownership restrictions	13	
Entry of service personnel and specialized tools	8	
Citizenship/residency requirements	14	
Restrictive government/business regulations	13	
Grandfather clause requiring practice before specified date	3	
Reinsurance based on local assets	2	
Special deposit requirement for foreign companies	3	
Commission terms less favorable than national companies	4	
Trade in goods	8	21
Restrictive regulations or administrative procedure	6	
Local purchase requirements	7	
Restricting entry of equipment or supply	3	
Trade in services	28	74
Restrictive government/business regulations and administrative procedures	15	
Restriction related to resident firm preference (fixed percent of service must be provided by domestic resident companies)	22	
Employment related restrictions on nonnationals	14	
Operating/ownership restrictions	12	
Discriminatory taxation	8	
Prohibition on services offered by nonresident companies	11	
Taxation of U.S. employees	1	
Technical issues	13	33
Lack of security control	1	
Privacy restrictions	2	
Contract enforcement problems	8	
Time limitations on franchise agreements	1	
Discriminatory bilateral agreements	4	
Governmental paper requirement	4	
Discriminatory standards requirements	1	

See footnote at end of table.

Table 8.--Trade barriers to international services in the construction and engineering industry 1/--Continued

Category and barrier	Number of responses	Percent of total respondents
Licensing	5	13
Licensing procedures	5	
Licensing restrictions (e.g., quotas)	3	
Refusal to license or renew	1	
Commercial counterfeiting	2	5
Inadequate patent or trademark enforcement	2	
Unclear definitions of trademark, patent, imported goods, or counterfeit goods	1	
Government procurement	19	50
Preference given to national firms	17	
Governmental import or distribution monopoly	3	
Prohibition of foreign services contracts (bilateral or multilateral)	5	
Shipment restricted to national flag carriers partially or completely	6	
Customs valuation	2	5
Discrimination in customs valuation between computer and data processing services transmitted through a telecommunications system of transferred through physical software products	1	
Discriminatory tariffs and customs procedures	2	
Subsidies/countervailing duties	15	39
Tax benefits (e.g., rebate or tax breaks)	8	
Insurance paid by government for local firm (e.g., inflation insurance)	3	
Direct financial aid to local firm by government	9	
Preferential financing arrangements	9	
Standards/certification	9	24
Origin declaration	4	
Local labor or material requirements	8	
Professional qualification restrictions	12	32
Professional license required to practice	11	
Foreign-exchange controls	24	63
Restrictions on remittances	21	
Convertibility limitations	18	
Delays in obtaining foreign-exchange permit	13	

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 38 of 93 firms surveyed; respondents represent about 30 percent of the foreign revenue of the 400 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

governments provide government insurance or reinsurance of commercial and political risks for overseas contracts. These guarantees, or government backing on exported services, often provide foreign firms with an unfair advantage over their competitors. 1/

Foreign market impediments

International trade in services is allegedly becoming increasingly enmeshed in a network of barriers in nearly every country. Many of the less developed countries in particular have instituted more and more nontariff barriers against foreign service companies including licensing requirements, currency restrictions, discriminatory taxation, joint-venture requirements, wide variations in national bidding procedures, and barriers to trade directly affecting provision of construction/engineering services. These types of protectionism are both a way of retaliating against U.S. protectionism in some labor-intensive goods and of insuring the survival of domestically run infant service industries. 2/ Although these problems do not normally preclude operations in overseas markets, they impose obstacles which restrict the potential for expanding trade in services.

Licensing and registration requirements occur in both developing and developed countries, ranging from time-consuming registration procedures to special language and education requirements for licensing. 3/ Intricate "red tape" in a country's bureaucracy may force companies to struggle with long delays in receiving government sanction and approval licenses or permits for their work. For example, foreign contractors wanting to do public work projects in Hong Kong must submit prequalification papers to the Public Works Department and await their approval. 4/ Additionally, Argentina, Brazil, Ceylon, Chile, Colombia, Cyprus, the Dominican Republic, Ethiopia, Finland, Gabon, Ghana, Iceland, Jamaica, Liberia, Malaui, Malaysia, Malta, Mexico, Nigeria, Spain, and Venezuela require that foreign engineers have work permits and/or licenses, which are often difficult to obtain. 5/ Arbitrary decisions by local officials and general lack of consistency in granting licenses often discourage foreign construction and engineering firms from applying for licenses. Approximately 13 percent of the firms responding to industry questionnaires indicated that they had encountered licensing and registrating requirements abroad.

Currency restrictions are generally imposed for balance-of-payments purposes by countries with foreign-exchange shortages. Restrictions on capital transfer and profit repatriation include denial of foreign exchange, and processing delays by local authorities in granting permission for

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1/ United States Trade Representative, Trade Issues in the Engineering and Construction and Related Consultancy Service Industry, September 1981, p. 5.

2/ "The U.S. Lead in Service Exports is Under Seige," Business Week, Sept. 15, 1980, p. 70.

3/ U.S. Department of Commerce, Recent Trends in Consulting Engineering, July 21, 1981, p. 9.

4/ "1982 International Construction-Hong Kong," Constructor, January 1982, p. 55.

5/ World Bank, Trade in Non-Factor Services-Past Trends and Current Issues, December 1980, p. 51; and data supplied by United States Trade Representative.

conversion of currency, and ceilings on the amount of money that can be removed from the country. 1/ When limits are placed on remittance of earnings, there is little incentive for foreign firms to consider the project. However, in cases of delays in processing authorizations for currency transfer, these restrictions are often considered minor irritants to trade in the field. Currency restrictions and foreign-exchange controls were cited by 63 percent of the firms responding to industry questionnaires. U.S. construction and engineering firms have indicated currency restrictions and difficulties in remitting earnings from Ceylon, Colombia, the Dominican Republic, Ethiopia, Guinea, Iceland, Kenya, Nepal, Nigeria, Senegal, Tunisia, and Tanzania. 2/

Discriminatory taxation of foreign firms has the effect of restricting trade and limiting competition in international markets. Many of the construction and engineering firms which responded to industry questionnaires indicated that they have encountered discriminatory taxation in their overseas service activities. This taxation, whether it is higher levies on profits of foreign firms or subjecting nonindigenous labor to unfair income tax rates, has a significant impact on construction and engineering costs. Foreign firms must then absorb these costs into their contract bids. Algeria, Brazil, and Guinea are examples of countries where foreign construction and engineering workers are subject to higher income tax rates than local personnel. 3/

A growing number of countries are insisting that construction firms bidding on domestic construction projects form joint ventures with a local company. 4/ In some cases, these partnerships are not required by law; however, administrative procedures may be difficult to accomplish unless the U.S. firm establishes a local office staffed by domestic representatives. 5/ These joint venture requirements are sometimes burdensome, especially when they exceed the technical resources of the local industry. Countries which require or strongly encourage partnerships or local representatives include Afghanistan, Austria, Bolivia, Brazil, Canada (Quebec), Chile, China, Costa Rica, Ecuador, Egypt, Guatemala, Honduras, Hong Kong, Indonesia, Iran, the Ivory Coast, Japan, Jordan, Lebanon, Malaysia, Pakistan, Panama, Paraguay, Portugal, Sierra Leone, Taiwan, Tunisia, Uganda, Venezuela, and Yugoslavia. 6/

1/ United States Trade Representatives, Trade Issues in the Engineering and Construction and Related Consulting Services Industry, September 1981, p. 6.

2/ World Bank, Trade in Non-Factor Services-Past Trends and Current Issues, December 1980, p. 51; and data supplied by the United States Trade Representative.

3/ Data supplied by the United States Trade Representative.

4/ Some joint ventures are formed by the free choice of the volunteer partners. These "contract marriages" are formed because it is mutually beneficial for the parties involved and gives them access to benefits not otherwise available.

5/ U.S. Department of Commerce, Recent Trends in Consulting Engineering, July 21, 1981, p. 10.

6/ "Joint Ventures Win Big Contracts," Engineering News Record, Apr. 30, 1981, p. 25; "International Construction Forecast," Constructor, January 1982, p. 53; "Building Markets Overseas," Construction Specifier, February 1981, p. 24; and data supplied by the United States Trade Representative.

Industry officials state that while not a barrier in the true sense, wide variation in bidding procedures can make trade in construction and engineering services very difficult. There is no allegation of discrimination in countries where national procedures are clearly specified. However, many countries do not publish their rules and procedures for bidding in official publications. There are also no sanctions against unreasonably short time frames in which firms can bid on a contract. Additionally, there may be no guidelines for international bid specifications. These practices tend to discriminate against foreigners who are not as well versed in local administrative practices, and may require a longer lead time in which to prepare a bid. 1/

There are also numerous barriers to trade directly affecting provision of construction and engineering services. Approximately 21 percent of the U.S. firms surveyed in industry questionnaires indicated that they had encountered restrictions in this area. Construction firms often require special tools or equipment to complete projects in foreign countries. In many cases, customs delays hamper the ability of foreign contractors to complete projects within a reasonable time period. These delays can place foreign firms at a disadvantage compared with local contractors, depending on the volume of equipment involved. Additionally, many host countries impose stringent "mixing" restrictions on the proportion of foreign to domestic goods used on a project. 2/ Foreign contractors may be forced to withdraw orders from their regular supplier and purchase materials from local manufacturers, despite problems such as variations from standard sizes, delivery time requirements, and quality of workmanship. Argentina, India, Mexico, and Nigeria utilize these types of government practices. 3/

Some countries have labor requirements which specify that a certain percentage (often the majority) of the personnel on a project be locals. Similarly, some developing countries specify that a certain percentage of the payroll go to local employees. Expatriate quotas for professional personnel are common in developing countries and often represent a difficult problem because of the scarcity of qualified local personnel. 4/ (See table 8 for specific examples of labor restrictions.) Afghanistan, Bolivia, Brazil, Chile, Colombia, the Dominican Republic, Ecuador, El Salvador, Ghana, Guatemala, India, Libya, New Zealand, Pakistan, Panama, Paraguay, Peru, Saudi

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1/ United States Trade Representatives, Trade Issues in the Engineering and Construction and Related Consultancy Services Industry, September 1981, p. 7.
2/ United States Trade Representative, Trade Issues in the Engineering and Construction and Related Consultancy Services Industry, September 1981, p. 7.
3/ World Bank, Trade in Non-Factor Services-Past Trends and Current Issues, December 1980, p. 51.
4/ U.S. Department of Commerce, Recent Trends in Consulting Engineering, Jul. 21, 1981, p. 10.

Arabia, Tunisia, Venezuela, and Zambia strongly encourage or have regulations specifying that a certain percentage of employees must be nationals. 1/ In Hong Kong, no outside labor is allowed to be brought in. 2/ In other countries, quotas may not be established by law, but the employment of local personnel is sometimes a requirement for certain contracts. 3/

Disincentives of U.S. Government policy

All of the above-mentioned barriers apply to all foreign construction and engineering firms working abroad. However, the U.S. industry cites many disincentives unique to American firms, arising from U.S. Government policies. These special difficulties include a lack of sufficient export financing from the Government, burdensome Federal regulations, and the U.S. tax system.

In comparison with the favorable financial assistance many competitors receive, current export financing for U.S. firms is very limited. 4/ Obtaining financing at competitive rates is also a critical problem for American firms attempting to win contracts abroad. Domestic budget cuts have significantly reduced the amount of credit available from the U.S. Export-Import Bank, and U.S. firms must seek funds elsewhere. The resulting increased cost for financing must be figured into a contract bid. Industry officials indicate that this is a significant factor, causing many Americans firms to lose potential projects.

In addition to the actual financing problem, U.S. firms cite a lack of Government support in identifying potential international projects. The industry contends that little information regarding host-country projects is provided to firms from the U.S. commercial consulates. In contrast, the Governments of Western Europe and Japan allegedly provide much more support to their construction and engineering firms operating abroad.

Trade experts indicate that Federal regulations such as the antibribery, antitrust, and antiboycott laws damage the competitiveness of U.S. construction and engineering firms abroad and pose obstacles to exports of materials and equipment. As to bribery, the Foreign Corrupt Practices Act has been criticized by industry spokesmen as a significant hindrance to expansion of trade in this sector. The act raises questions about the legality of financial contributions which may be an accepted practice in the host country, but would be illegal in the United States. The extent to which laws and social and business customs of other countries are taken into account in determining whether a contribution is "corrupt" is uncertain. Faced with the risk of prosecution, many U.S. firms have been reluctant to enter certain foreign markets. U.S. antitrust laws are also perceived to be an important

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1/ Op. cit., World Bank; and data supplied by the United States Trade Representative.

2/ "International Construction Forecast," Constructor, January 1982, p. 55.

3/ U.S. Department of Commerce, Recent Trends in Consulting Engineering, Jul. 21, 1981, p. 10.

4/ "Building Markets Overseas," The Construction Specifier, February 1981, p. 19.

disincentive to overseas construction projects. These laws may deter firms from forming bidding consortia and other cooperative organizations. Such short-term arrangements are often useful on projects where complimentary skills are required, thus allowing U.S. construction and engineering firms to be more competitive in world markets. 1/ Two separate antiboycott statutes are now in effect prohibiting U.S. persons from complying with foreign boycotts of friendly nations. 2/ These laws were a direct result of Arab pressure on U.S. firms to support the Arab League boycott of Israel and of blacklisted countries. Because the Middle East represents an important market for construction and engineering services, these antiboycott laws hinder U.S. firms. Invitations to bid on projects in virtually all Arab countries may contain prohibited boycott terms. Competitors, however, do not face any effective antiboycott laws. Although it is difficult to assess the impact of this regulation, antiboycott restrictions have been specifically cited as major problems in Iraq, Kuwait, and Saudi Arabia. 3/

The disincentive that is most frequently mentioned by industry officials is the U.S. taxation of expatriate personal income. Construction and engineering firms operating abroad consider this to be a serious handicap to the expansion of trade. None of the other major competitor nations tax their nationals working abroad; therefore, U.S. firms indicate that this tax contributes to making them noncompetitive in foreign markets. 4/ Additionally, since Americans working overseas are also subject to the tax laws of the country in which they are working, they are often doubly taxed. Consequently, employing U.S. workers costs much more than hiring other nationals. 5/ However, starting in fiscal year 1982, Americans employed overseas will receive exclusion from U.S. income taxes on the first $75,000 of foreign income, and that amount will increase to $95,000 by 1986. 6/ This is expected to allow U.S. firms to offer more competitive bid prices, in which costs of maintaining U.S. supervisory personnel abroad are included. 7/

The overall effect of these impediments and disincentives is to reduce the international competitiveness of the U.S. industry and hinder trade. Additionally, these obstacles have a significant impact on followup trade in maintenance services and product exports. This is clearly illustrated by response to the industry questionnaires. All questionnaire respondents reported that their service activities overseas would increase as a result of reducing or eliminating existing barriers. The number of responses to a

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1/ U.S. Department of Commerce, Recent Trends in Consulting Engineering, July 21, 1981, p. 8.

2/The Anti-Boycott Amendments to the Export Adminstration Act, passed in 1977, and the Ribicoff Amendment to the Tax Reform Act of 1976.

3/ U.S. Department of Commerce, Recent Trends in Consulting Engineering, July 21, 1981, p. 8.

4/ Albert N. Alexander, "Service Exports: Brightening the '80'," Business America, Oct. 20, 1980, p. 25.

5/ "Building Markets Overseas," The Construction Specifier, February 1981, p. 19.

6/ "Economic Recovery Tax Act of 1981, P.L. 97-34.

7/ David B. Perini, "International Construction in 1982," Constructor, January 1982, p. 49.

question to determine the economic effects of international barriers to U.S. services trade and associated product exports in construction and engineering service activities abroad, was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
What effect, if any, would reduction or removal of service trade barriers have upon your receivables, billings, or revenues in current or potential country markets?:		
Increase	29	76
Decrease	0	0
No effect	7	18
What effect, if any, would reduction or removal of service trade barriers have upon potential U.S. products exports in current or potential country markets?:		
Increase	26	68
Decrease	0	0
No effect	4	11

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 38 of 93 firms surveyed; respondents represent about 30 percent of the foreign revenue of the 400 major firms believed to be operating internationally in 1981.

The reduction of trade barriers would increase construction and engineering revenues in the Middle East by 10 to 20 percent according to most companies; revenues in the Far East, Africa, and Latin America would mostly increase 30 to 40 percent in 1981 (table 9). Merchandise exports would also increase with the removal of trade barriers. Machinery and equipment exports were cited by questionnaire respondents as the category that would have the largest revenue increase, ranging from 10 to 50 percent (table 10).

Conditions of Competition in Current and Potential Service Markets

The foreign work for U.S. firms largely comes from price construction contracts and design contracts for high-technology projects, especially processing plants and hydroelectric and nuclear power plants. Labor-intensive foreign projects are more frequently handled by firms from low-range countries, especially the Republic of Korea (Korea), Taiwan, Yugoslavia, Italy, and Mexico. 1/ Often, some portion of such foreign projects must be

1/ "Non-U.S. Firms Grabs Big Share of Global Market," Engineering News Record, Dec. 6, 1979, p. 27.

Table 9.--Estimated changes in revenues absent trade barriers to international business of construction and engineering service firms, by areas 1/

Area and direction of change	Number of responses	Percentage change						
		10	20	30	40	50	60	80
Middle East:								
Increase	20	8	7	2	1	1		1
Decrease								
Far East:								
Increase	17	7	4	4	1			1
Decrease								
Latin America:								
Increase	16	1	5	6	2	2		
Decrease								
Europe:								
Increase	4	3				1		
Decrease								
Africa:								
Increase	14	1	2	5	4	1	1	
Decrease								
Canada:								
Increase	7	2	4					1
Decrease								
Mexico:								
Increase	10		3	3	1	2	1	
Decrease								
Other:								
Increase	-							
Decrease								

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 38 of 93 firms surveyed; respondents represent about 30 percent of the foreign revenue of the 400 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 10.--Estimated changes in U.S. merchandise exports absent trade barriers to international business of construction and engineering service firms, by types 1/

Type and direction of change	Number of responses	Percentage change						
		10	20	30	40	50	60	80
Machinery and equipment:								
Increase	17	6	3	3	1	4		
Decrease								
Agricultural, animal, and vegetable products:								
Increase	-							
Decrease								
Forest products:								
Increase	2		1		1			
Decrease								
Textiles, apparel, and footwear:								
Increase	1		1					
Decrease								
Chemicals and related products:								
Increase	1		1					
Decrease								
Minerals and metal products:								
Increase	2		1			1		
Decrease								
Miscellaneous manufactures:								
Increase	4		3			1		
Decrease								

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 38 of 93 firms surveyed; respondents represent about 30 percent of the foreign revenue of the 400 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

subcontracted to local construction firms to comply with local government requirements. 1/

While the competitive advantage held by U.S. firms remains in the high-techonology projects, this advantage is diminishing as more firms from Japan and Western Europe are gaining expertise in the high-tech area. In response to the increased competition from foreign contracting and design firms, U.S. companies have entered into joint ventures with other U.S. companies to bid on massive projects for the purpose of offering a more impressive and complete package of services. 2/ U.S. firms do remain ahead of their foreign competition in the computer technology area known as computer-aided-design (CAD), and this expertise has greatly increased both the efficiency and capability of U.S. firms relative to foreign-based multinationals. However, despite the CAD advantage, it is in the limited marketing support of this and other services by the U.S. commercial offices overseas that American firms lag competitively far behind the firms located in other industrialized nations.

According to industry reports, the major competitive disadvantages to U.S. firms winning international contracts include the lack of sufficient U.S.-Government-backed, low-interest financing, the almost unilateral adherence to the Foreign Corrupt Practices Act required of U.S. firms, the lack of tax credits for foreign projects similar to those provided to domestic firms by the Governments of France, Italy, and Japan, and the U.S. Government's taxation of earnings of U.S. citizens working abroad. Industry sources state that the latter disincentive for U.S. firms has been minimized starting with fiscal year 1982, with the signing of Economic Recovery Tax Act of 1981, P.L. 97-34. Industry sources also point out that no newly developed service industries in lesser developed countries, such as South Korea and Taiwan, allegedly receive enough financial support from their governments that they are sometimes able to outbid established, technologically advanced U.S. firms for key awards.

The U.S. construction and engineering firms actively engaged in marketing services in the international arena have lost a significant number of contracts to other international firms during the past 5 years. As indicated in table 11, U.S. firms are facing increased competition from host-country as well as other foreign firms in such areas as the United Kingdom, West Germany, Mexico, and Ecuador. Although U.S. firms remain ahead of their international competition in terms of technical expertise, they often locate subsidiaries in other developed nations in order to take advantage of local tax benefits. 3/ Certain governments actively promote their construction and engineering services industries abroad; industrialized nations such as France, Great Britain, Germany, and Japan also allegedly grant their industries considerable financial incentives, including tax allowances and direct subsidies, in order to encourage the export of energy-related construction and engineering

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1/ Ibid., p. 36.

2/ "American Firms Hold 42 Percent of World's Design Market," Engineering News Record, Dec. 13, 1979, p. 31.

3/ Washington Post, Jan. 22, 1982, pp. D-1 and D-2, and information obtained during conversation with representative of the American Consulting Engineers Council.

Table 11.—Number of firms competing 1/ with U.S. construction and engineering service firms abroad, by principal service markets 2/ in order of revenue generated, 1981 3/

Service market	Number of competing firms				
	Total 4/	National	Regional	World-wide	Other U.S. firms
Pakistan	15	2	2	8	3
Egypt	72	5	8	50	20
Argentina	25	2	1	12	10
Canada	29	5		6	20
United Arab Eminates	100			13	7
Australia	25	5	5	10	5
New Zealand	35			20	15
United Kingdom	80	50	10		20
Kuwait	30			12	18
Indonesia	120	2		13	15
Thailand	21	6	1	10	5
Venezuela	32	1		25	1
Nigeria	23	1	2	12	8
South Africa	10		2	4	4
Panama	34	4	5	15	10
Republic of Korea	10			3	7
Ecuador	30	10		10	10
Liberia	4			2	2
Italy	25	5	5	10	5
Malaysia	10	3	2	5	
Brazil	11	8		1	2
Mexico	22	10		3	9
Turkey	2			2	
India	10	3		7	
Spain	8	2	3	2	1
Portugal	15	2	5	6	2
Israel	1	1			
Zaire	3			1	2
Colombia	7			6	1
Iraq	3			3	
Philippines	40	5		35	10
China	10			10	

See footnotes at end of table.

Table 11.—Number of firms competing 1/ with U.S. construction and engineering service firms abroad, by principal service markets 2/ in order of revenue generated, 1981 3/--Continued

Service market	Number of competing firms				
	Total 4/	National	Regional	World-wide	Other U.S. firms
Jordan	31			2	4
Bangladesh	6			3	3
West Germany	45	20		5	20

1/ Based on 25 responses by questionnaire respondents.
2/ Other principal service markets for the industry may not be listed here if respondents did not identify the number of competing firms.
3/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 38 of 93 firms surveyed; respondents represent about 30 percent of the foreign revenue of the 400 major firms believed to be operating internationally in 1981.
4/ The number of competing firms, by geographic scope of operation, may not equal the total shown, since the categories may not have been viewed as mutually exclusive and respondents may not have been able to identify the type of firm when providing a total.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

services. 1/ Lower price, often as a result of preferential financing and government support, was cited by numerous questionnaire respondents as the most likely reason for competing firms successes in world markets (table 12).

The international competition for these U.S. firms comes mainly from other industrialized nations. Table 13 provides information on the likely reasons for the competitive strengths of U.S. construction and engineering firms in foreign service markets. Reasons most often cited include advanced technology, superior quality association, and experience in the market. Several firms located in developing nations are also extremely active in the bidding for most energy-related projects, regardless of their location. Phillipp Holzman AG, Bilfinger & Berger, and Hochtief, all located in West Germany; Davy Corp. of the United Kingdom; and Dumez of France provide the major European competition for the U.S. firms. 2/ Industry sources indicate that Korean contractors, such as Hyandai, Daelim, or DaeWoo, are able to underbid many firms headquartered in developed nations principally because of the extremely low-skilled and unskilled labor cost in Korea. None of the other concerns ranked among the 50 top international firms have as significant a cost advantage involving labor as the Korean firms.

1/ Construction Business Handbook, "Foreign Subsidiary or International Division," pp. 5-1 to 5-4, and Business Week, Sept. 15, 1980, p. 70.
2/ Engineering News-Record, July 16, 1981, pp. 68-93.

Table 12.--Likely reasons 1/ for competing firms' success in world construction and engineering service markets, by base countries of firms 2/

Base country	Lower price	Technology expertise	Preferential financing	Experience in the market or service	Superior quality association	Political or regional bias	Government support	U.S. restrictions
Australia	1					1		1
India	1						1	
Indonesia						1		
Japan	9	1	8	2	1	3	7	2
Republic of Korea	3	1	1	1		1	3	3
Brazil			1			1		
Mexico	1							
Panama						1		
West Germany	6	1	6	3	1	2	6	3
France	8	3	16	12		4	17	7
Italy	5		1	2		1	3	2
Netherlands	2	1	1	1			1	
Spain	1			1				
United Kingdom	13	2	7	10		7	12	9
Egypt	1			1		1		1
Canada	7	1	5	2	1		3	2
Other	3		2	1		2	2	
Total	61	10	48	36	3	25	55	30

1/ The importance of each reason is indicated by the number of times each was designated, based on 30 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 38 of 93 firms surveyed; respondents represent about 30 percent of the foreign revenue of the 400 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 13.--Likely reasons 1/ for the competitive strength of U.S. construction and engineering service firms in foreign service markets 2/

Service market	Lower price	Technology lead	Financial strength	Experience in the market or service	Superior quality association	Other
Middle East:						
Israel		1			1	
Jordan		3		1	3	
Kuwait		1		1	1	1
Pakistan				1		
Saudi Arabia	2	10	4	8	9	1
United Arab Emirates		1		1		
North Yemen		1			1	
Far East:						
Australia		1		1	1	
Bangladesh		1	1	2	1	
China		1				
India		1		1	1	
Indonesia	2	2	2	3	2	2
Japan		1		1	1	
Republic of Korea		1	1	1	1	
Malaysia		1		1	1	
Philippines	1	1		1	1	
Central and South America (excluding Mexico):						
Argentina		2			2	
Brazil		1	1			
Ecuador			1	1	1	
Guatemala				1	1	
Panama		1		1	1	
Venezuela		3		2	2	1
Europe:						
West Germany		1		1	1	
France		1		1	1	
Italy		2		2	2	
Portugal					1	
Spain		1		1	1	
United Kingdom		1		1	1	
Africa:						
Egypt		7		9	8	
Liberia					1	
Nigeria		1		1	1	
South Africa		2	1	1	2	1
Zaire		1				
North America and Mexico:						
Canada		3	2		2	
Mexico		1	1		1	
Other	1	2	2	1	3	
Total	5	58	16	48	57	7

1/ The importance of each reason is indicated by the number of times each was designated, based on 28 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 38 of 93 firms; respondents represent about 30 percen of the foreign revenue of the 400 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Several Korean firms are no longer relying only upon their labor-cost advantage and are seeking to develop the capability to compete for the high-technology projects. Among these Korean firms are SamWham Corp. and the Dongsan Construction Co. In order to develop the sought-after expertise, these firms are pursuing joint ventures and partnerships with foreign firms. 1/ Especially favored are design-construct partnerships which can offer a client additional technical expertise.

As indicated earlier in this report, it is generally expected by the industry that the rapid growth in design-construct type contracts in the Middle East has come to an end. The marketing strategy now is to diversify in countries outside the Middle East by creating new affiliates in other third-world oil-producing countries such as Nigeria, Venezuela, and Indonesia. Other firms agree that Africa will remain a major market for the large energy-related projects, and some still feel that North America holds possibilities, particularly in Mexico and Canada. Table 14 provides information on the competitive strengths of U.S. construction and engineering firms in potential foreign markets, with superior technology and quality most frequently cited by questionnaire respondents.

1/ Ibid., p. 73.

Table 14.--U.S. construction and engineering service firms' competitive strengths 1/ in potential foreign markets 2/

Potential service market	Lower price	Technology lead	Financial strength	Greater experience	Superior quality	Other
Middle East:						
Bahrian		1		1	1	
Iraq				1	1	
Jordan		2		1		
Saudi Arabia	1	7		3	7	1
Turkey		1		1	1	
United Arab Emirates		2			1	
Far East:						
Australia	2	5		4	4	1
Bangladesh		1	1	1	1	
China		4		2	3	
Taiwan		2		1	2	1
India		1			1	
Indonesia		6	2	4	5	2
Republic of Korea		2			1	
Malaysia		3	1		3	
Philippines		2	1	1	2	
Thailand		2			2	
Central and South America (excluding Mexico):						
Argentina		1				
Brazil		1		1	1	
Chile		1		1	1	
Colombia		1				
Ecuador	1	3		1	2	
Panama		1		1		1
Venezuela		4		2	3	1
Europe:						
Belgium		1			1	
Africa:						
Cameroon	1	2		1	2	
Egypt		4	1		4	1
Ivory Coast		1			1	
Kenya	1	1		1	1	
Liberia		1	1	1	1	
Morocco		1		1		1
South Africa		1				
Sudan		1			1	1
Tunisa		1			1	
Zambia				1		
Zimbabwe		1				1
North America and Mexico:						
Mexico		4	2		3	
Other		3	2	1	3	
Total	6	75	11	32	60	11

1/ The importance of each reason is indicated by the number of times each was designated, based on 29 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service was 38 of 93 firms surveyed; respondents represent about 30 percent of the foreign revenue of the 400 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

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Consulting and Management Services

Executive Summary

1. International revenues of the consulting and management services industry were estimated to have been at least $1 billion in 1981.

2. U.S. consulting and management firms responding to the Commission questionnaire generated an estimated $5.5 million in U.S. merchandise exports in 1981 as a direct result of exporting their services abroad. The consulting industry stimulates U.S. exports of office equipment, construction machinery/equipment, measuring and checking instruments, and telecommunications equipment.

3. Industry respondents to the questionnaire estimated that over $1 million in host-country and third-country product shipments were generated by U.S. consulting and management service activities abroad in 1981, believed to consist primarily of equipment used in conjunction with project implementation.

4. Despite the existence of numerous alleged nontariff barriers affecting the U.S. consulting and management services, the industry has captured the leading position in the world management and consulting market. Barriers most commonly cited included right of establishment, trade in services, and foreign-exchange controls. These have generally proved to be of a limited impact, but they could be of significance in the success of U.S. firms beginning to establish foreign offices.

5. Nearly half of the questionnaire respondents reported that their service activities overseas would increase as a result of reducing or eliminating existing barriers, in the range of 20 to 80 percent in increased revenue in Latin America and 10 to 80 percent in Europe. However, nearly two-thirds of the questionnaire respondents indicated that reduction or removal of service trade barriers would have no effect on potential U.S. product exports.

6. U.S. consulting and management service firms face competition from host and third country firms in important markets such as the United Kingdom, West Germany, Saudi Arabia, Japan, and Chile.

7. U.S. management and consulting firms point out that foreign firms often obtain a competitive advantage in international activity as a result of the significant support by their respective embassy or consular personnel in identifying commercial opportunities and leads on potential international projects. They further cite lower prices and political bias or government support as reasons for competitive strengths of foreign firms in host or third country markets.

8. Three major competitive strengths were cited for U.S. management and consulting firms in current and potential foreign markets: (1) technology lead, (2) superior quality association, and (3) experience in the market or service. These are cited as especially significant in Europe, Africa, Canada, and Mexico.

Industry Profile

Definition and coverage

Management and consulting is a service provided for a fee by independent and objective professional persons who counsel and assist various establishments and institutions in analyzing the management and operating problems associated with the goals, objectives, policies, and principal functional operating areas of the organization. Management consultants recommend solutions to the problem and may assist in implementation.

This industry is a part of Standard Industrial Classification (SIC) 7392, which includes establishments primarily engaged in furnishing general or specialized management, consulting, or public relations services. For this study, public relations services are excluded.

The majority of the management and consulting firms included in this survey had annual revenues of over $1 million and supplied most consulting services to a wide variety of industries throughout the world. Included in the survey were major accounting firms with significant management advisory services.

The 13 management and consulting service industry respondents to the Commission questionnaire (of 59 firms surveyed) represent about 8 percent of the estimated foreign revenues of the estimated 120 major firms believed to be operating internationally in 1981.

Highlights in 1981

- DOMESTIC RECEIPTS of management and consulting establishments were estimated to be $14.8 billion.
- U.S. ESTABLISHMENTS providing management and consulting services numbered over 22,000.
- U.S. EMPLOYMENT in these establishments exceeded 200,000.
- INTERNATIONAL REVENUES were estimated to be at least $1 billion.
- FOREIGN ESTABLISHMENTS of U.S. management and consulting firms are located worldwide; at least 75 to 80 U.S. firms have offices overseas.
- FOREIGN EMPLOYMENT of these overseas management and consulting offices is unknown.
- THE U.S. TRADE BALANCE in the management and consulting service sector is believed to be a trade surplus.

Industry structure

There are four basic types of management and consulting firms. Independent consultants are unrelated to other business services and range in size from individual consultants to large companies. Some consultants operate with Certified Public Accounting (CPA) firms and are accounting firm consultants. These professionals are organized within CPA firms into Management Advisory Services. Another type of consultant is the college or university professor who works as a consultant on a part-time basis. The fourth type of consultant is an internal consultant who works in a management and consulting department within an organization or company.

The two most significant consulting bodies are independent consulting firms and CPA-related consulting firms. These firms can be specialists or generalists. Specialists concentrate on a limited range of services--general management; manufacturing; personnel; marketing; finance and accounting; procurement; research and development; packaging; administration; international operations; and other miscellaneous specialized services. These principal areas can be further refined into more specialized services. Management and consulting specialists can also concentrate in certain industries--agriculture, forestry, and fishing; mining; construction; manufacturing; transportation; communications; electric, gas, and sanitary services; wholesale and retail trade; finance, insurance, and real estate services; public administration; and other nonclassifiable establishments, all of which have further subcategories for specialization purposes. Other management and consulting firms are generalists, those that offer expertise in many of the services and/or industries listed above. 1/

This service industry is dominated by the larger firms (100 or more employees), which employ the greatest number of people and capture the largest share of the industry's market volume. Domestic and international revenue for the management and consulting service industry accounts for nearly 2 percent ($15.8 billion) of total U.S. services trade, estimated at $837 billion in 1981 for the 14 service industries covered in this study. Due to U.S. management and consulting firms' prominence in the international market and the scarcity of foreign competition in the U.S. market, the United States is believed to have a trade surplus in the management and consulting service industry.

Recent trends and outlook

The management and consulting portion of the services sector is expected to experience an annual growth of 3.5 to 4 percent during this decade, 2/ although some firms are expected to continue growing at an annual rate of about 20 percent due to increased business in their specialties. 3/ This growth will probably result from the industry's principal advantages in the market--the use of high technology, such as computers, telecommunications and laboratory equipment, and the superior education and experience background offered by this industry's personnel.

1/ Directory of Management Consultants, 1980.
2/ "The Service Sector Will Explode", Business Week, June 1, 1981, p. 95.
3/ "The New Shape of Management Consulting", Business Week, May 21, 1979, p. 98.

The demand for management and consulting services is directly influenced by changes in technology, economic conditions, market competition, government regulations, and other forces. The current recession may have reduced the demand for these services. Reportedly, companies seeking ways to cut back on expenses may often terminate outside consultants and utilize in-house advisors. This is especially true of those industries seriously affected by the recession, such as the automobile and forestry industries and associated companies. Some industry sources, however, believe that consulting firms may be more successful during economic downturns. As an industry or a firm suffers increasing problems, it may seek outside advice and solutions to its problems. During periods of economic growth, when an industry or a firm may be satisfied with its position and potential in the market place, the industry or firm may not see a need to seek external advice. 1/

Increasing fuel and energy costs during the past decade created demand for energy managers and energy management firms. There are currently over 3,500 energy managers who are members of the Association of Energy Engineers. Another trend in the industry is towards investment counseling, which provides analysis and information in the areas of capital investment, financial position, and financial planning necessary to assist companies in financing and merger decisions.

In addition, according to industry sources, management and consulting firms are emphasizing specialization and internationalization in their operations. Specialization results from the desire to distinguish a consulting firm from other general management and consulting firms in order to get a share of a particular market. With increased competition occurring in the United States due to the economic situation, many firms have developed an area of specialization in which to excel and concentrate their resources. Specialization has led to increased foreign and domestic business for many consulting firms and a heightened awareness of the importance of marketing. Consulting firms have increasingly recognized the important effect of promotional materials and other advertising measures to keep clients informed about their firms' services and specialties. Management and consulting firms are also internationalizing, availing themselves of the opportunities and fast growth rates found in some overseas markets, such as the textiles/apparel market and the Third-World market.

Future growth in the consulting sector will largely depend on U.S. firms' ability to attract more business from abroad, where growth potential is considered by some industry sources to be greater than in the United States. To maintain its status as the primary source of this service in the world market, according to industry sources, U.S. consulting firms will find it necessary to overcome negativism towards the United States and to adapt to changes in business and industry operations and theories, and fluctuations in the economy. This will require flexibility of, and continual learning by, the staffs and an increased awareness of cultural differences and their importance in foreign business operations. One U.S. firm, for example, stresses the international aspect of the firm instead of its U.S. relationship. This emphasis has proved more agreeable to foreign clients and has been a contributing factor to the success of the firm.

1/ "Consulting Firms Lure Top MBA Graduates," Industry Week, Oct. 13, 1980, p. 46.

Another external factor affecting the growth of U.S. management and consulting firms is funding of projects by international organizations and governments. For the most part, total resources for most international funding organizations have increased during the past decade, providing for a larger number of potential projects for management and consulting firms.

U.S. Service Operations in Foreign Markets

U.S. consulting and management firms have generally established business operations overseas after gaining a significant number of foreign projects and clients that justified the expansion of the firm into those foreign markets. Initial growth of these firms abroad coincided with the expansion of U.S. manufacturing and other service companies into overseas markets, with services supplied to U.S.-related companies as well as their foreign clients. 1/

U.S. management and consulting firms conduct overseas projects through U.S.-based offices or foreign business operations established through foreign affiliates, subsidiaries or branches, joint ventures, franchising, and licensing. Many of these operations are staffed by nationals trained in the United States. As shown in table 1, the most common forms of overseas operations for the questionnaire respondents are subsidiaries or branches and foreign affiliates. These firms can also be active in secondary service industries, such as computer and data processing and educational services.

U.S. consultants typically obtain foreign projects through (1) international organization funding, (2) the Government, and (3) the private sector. These U.S. firms and their foreign operations develop their client relationships through referrals by former and current clients (both U.S. and foreign), referrals of trade opportunities by U.S. commercial offices overseas (seen as lacking by industry sources), and more recently, through trade-show participation, seminars, published materials, and other advertisements of their projects and services.

Contracts obtained by U.S. firms through international sources--such as those for the World Bank and the U.S. Agency for International Development, largely depend upon the service or industry specialization of the firm and, to a lesser extent, the project locale. Internationally-funded projects are most common in the Third-World countries, where management and consulting services are highly important due to the lack of a strong service industry and a relative lack of industrial and financial development. One industry source indicated that the management and consulting service can result in the development of the Third-World economy and thereby increase its exports to the United States and other developed countries. Private sourcing is most common in the developed countries.

The United States is generally a major supplier of management and consulting services to the Third World. It is estimated, for example, that U.S. consulting firms obtain up to 20 percent of the Asian Development Bank's

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1/ "The International Operations of U.S. Service Industries: Current Data Collection and Analysis", Economic Consulting Services, 1979.

Table 1.--Operating structures of principal service activity, and revenues associated with secondary service industry activities of consulting and management service firms in foreign markets, 1981 1/

Item	Revenues 2/	Number of responses	Percent of total respondents
	1,000 U.S. dollars		
Operating structure:			
Foreign affiliate	-	6	46
Joint venture	-	3	23
Licensing	-	1	8
Subsidiary or branch	-	9	69
Other	-	3	23
Secondary service activity:			
Computer and data processing services	3/	5	38
Educational services	3/	1	8
Total	2,755	6	46

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 13 of 59 firms surveyed; respondents represent about 8 percent of the foreign revenue of the estimated 120 major firms believed to be operating internationally in 1981.

2/ Calculated by the staff of the U.S. International Trade Commission from receivables, billings, or revenue data provided by respondents.

3/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

consulting business. 1/ These projects include agriculture and energy/conservation development. One industry source indicated that the competitive environment in the Third World is very intense. The multiplier effect of gaining future contracts in this area through obtaining initial contracts is significant, such as at the World Bank, where an estimated 60 percent of procurement is sole source contracting.

Private sourcing of projects is most common in developed countries, where a strong financial base has developed. These projects are generally not of a developmental nature (such as developing a country's basic industries or infrastructure), but are involved in strategy, planning, and other business operations of like manner. Referral and return clients are especially significant in areas of the world saturated with competent consulting firms competing for the same contracts.

1/ "Asian Development Bank Charts Some New Directions," Business America, Apr. 5, 1982, pp. 6-8.

Respondents to the Commission's questionnaire indicated that their total foreign revenues will increase 32 percent to $91 million during 1980-82, and their estimated total domestic and international revenues will reach $254 million (table 2). While foreign and domestic revenues gradually increased during the period covered by this study, the number of foreign and domestic establishments during the past 3 years has remained stable. The international revenues earned by U.S. management and consulting firms were believed to be at least $1 billion in 1981, about 6 percent of this industry's total revenues of approximately $15.8 billion. Foreign-market project commitments by the United States will continue to be extremely important to U.S. consulting and management firms due to the growth potential abroad and the sluggishness of certain U.S. industry sectors. As a result, overall growth in foreign revenue generated by the consulting and management industry is expected to be moderate. In 1982, foreign revenue is estimated to increase

Table 2.--Indicators of activity in the foreign and domestic operations of consulting and management service firms, 1980-82

Item	Foreign	Domestic	Total
Estimated value of receivables, billings, or revenues: 1/ 2/			
1980-------------------1,000 dollars--:	68,559	121,366	189,925
1981-----------------------------do----:	75,195	142,179	217,374
1982-----------------------------do----:	90,600	163,650	254,250
Estimate of investment in physical assets 1/ 3/ in foreign operations:			
1980-------------------1,000 dollars--:	40	-	-
1981-----------------------------do----:	50	-	-
1982-----------------------------do----:	160	-	-
Number of establishments: 1/			
1980-------------------------------------:	55	75	130
1981-------------------------------------:	55	76	131
1982-------------------------------------:	57	81	138
Estimated 4/ value of total industry receivables, billings, or revenues:			
1980-------------------1,000 dollars--:	900,000	14,200,000	15,100,000
1981-----------------------------do----:	1,000,000	14,800,000	15,800,000
1982-----------------------------do----:	1,200,000	15,500,000	16,700,000

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 13 of 59 firms surveyed; respondents represent about 8 percent of the foreign revenue of the estimated 120 firms believed to be operating internationally in 1981.

2/ Excluding the value of any merchandise exports.

3/ Including the undepreciated book value of land, plant, and equipment.

4/ By the staff of the U.S. International Trade Commission based on discussions with industry and/or association representatives, and secondary sources.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

about 20 percent to $1.2 billion, which will account for about 1 percent of total service sector foreign revenue of $135.7 billion estimated for the 14 selected service industries covered in the Commission's study (table 3).

Table 3.--Estimated total foreign revenue generated by the consulting and management service industry and estimated total foreign revenue for selected service industries, 1980-82

Year	Total foreign revenue for service industry 1/ (1)	Total foreign revenue for selected service industries 2/ (2)	Ratio of (1) to (2)
	1,000 U.S. dollars		Percent
1980	900,000	89,398,000	1
1981	1,000,000	109,611,000	1
1982	1,200,000	135,744,000	1

1/ Estimated based on discussion with industry and/or association representatives, and secondary sources.

2/ Based on totaling USITC estimated foreign revenue for each of the 14 selected industries covered in the study.

Source: Estimated by the staff of the U.S. International Trade Commission.

U.S. management and consulting operating structures overseas are concentrated in Europe due to its economic and political similarities to the United States, with generally fewer offices in Latin America and the Third World due, to some extent, to nontariff barriers and lack of advanced facilities and infrastructure. U.S. consultant project commitments overseas, however, are widely scattered throughout the world and are coordinated by a U.S.-based office or a U.S.-related foreign operation, depending upon the operational structure of the management and consulting firm hired for the project. As indicated in table 4, Latin America and Europe were the largest markets in 1981 for questionnaire respondents, with Canada and the Far East being secondary markets. Estimated revenues in Europe amounted to $114 million in 1981; revenues in Latin America totaled $37 million in the same year.

Although international operations do not account for a substantial portion of all consulting and management firms' total revenues, this service industry is important in providing the basis for the development of primary industries and facilities and the means to adapt to changes occurring in technology, government, the economy, and other business factors. The international market is likely to continue to play a significant role in the operation of U.S. firms due to the growth potential of Third World countries and stagnation of certain U.S. industry sectors.

Table 4.--Regions and countries in which revenue is generated by consulting and management service firms, 1980-82 1/

Region and country 2/	Number of responses 1980	Number of responses 1981	Number of responses 1982	Percent of total respondents 1980	Percent of total respondents 1981	Percent of total respondents 1982	Estimated revenue 1980	Estimated revenue 1981	Estimated revenue 1982
							------1,000 U.S. dollars------		
Middle East	5	5	4	38	38	31	7,051	8,100	8,350
Kuwait	-	1	-						
Pakistan	-	1	-						
Saudi Arabia	-	3	-						
Far East	5	8	7	38	62	54	21,538	31,900	35,956
Australia	-	4	-						
Taiwan	-	2	-						
Japan	-	3	-						
South Korea	-	2	-						
Malaysia	-	5	-						
New Zealand	-	2	-						
Philippines	-	1	-						
Thailand	-	1	-						
Latin America	6	7	4	46	54	31	36,325	37,064	39,537
Argentina	-	3	-						
Brazil	-	4	-						
Chile	-	2	-						
Columbia	-	1	-						
Nicaragua	-	1	-						
Peru	-	1	-						
Venezuela	-	3	-						
Europe	6	8	6	46	62	46	91,335	114,027	133,537
Belgium	-	2	-						
West Germany	-	4	-						
France	-	2	-						
Italy	-	4	-						
Spain	-	1	-						
United Kingdom	-	8	-						
Africa	0	3	2	0	23	15	3/	3/	3/
Egypt	-	1	-						
South Korea	-	2	-						
Zimbabwe	-	1	-						
Canada	5	7	5	38	54	38	32,036	36,712	43,854
Mexico	5	6	5	38	46	38	991	340	1,840
Other	0	3	0	0	20	0	-	3/	-

1/ Country listing is for 1981 only.
2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 13 of 59 firms surveyed; respondents represent about 8 percent of the foreign revenue of the estimated 120 major firms believed to be operating internationally in 1981.
3/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Trade in Merchandise Generated by Trade in Services

While discussions with industry sources suggested that product exports generated by consulting and management services were fewer than in other service industries, a certain relationship exists, as indicated by questionnaire results. The number of positive responses to a series of questions asked to determine whether or not U.S. merchandise exports are generated by U.S. consulting and management service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
Do you believe that U.S. merchandise might be used as a result of the services your firm provides abroad?--	8	62
Is U.S. merchandise specified or recommended in the course of providing your service?----------------	6	46
Are U.S. merchandise exports believed to be directly generated?------------	5	38

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 13 of 59 firms surveyed; respondents represent about 8 percent of the foreign revenue of the estimated 120 major firms believed to be operating internationally in 1981.

Because of the relatively low response rate to the merchandise trade section of the questionnaire, the Commission is unable to extrapolate with certainty the value of U.S. merchandise exports directly generated by U.S. consulting and management activities abroad. However, these industry respondents estimated that their service activities overseas resulted in the total U.S. export of approximately $5.5 million in goods in 1981 (see table 5). Based on this estimate, the number of respondents, and the number of known firms in the industry, it is estimated that nearly $46 million in U.S. merchandise exports flowed as a result of U.S. international consulting and management activities in 1981. However, it should be noted that a confidence level of 95 percent this figure could be as low as the actual respondents' estimate of $5.5 million or as high as $100 million. For estimates of U.S. merchandise exports for 1980 and 1982, refer to table 5.

Table 5.--U.S. merchandise exports generated by U.S. consulting and management services abroad, 1980-82 1/

Year	Number of responses	Exports of U.S. merchandise estimated by respondents	Projected 2/ total: U.S. merchandise for the service industry	± 95 percent confidence limit for projected industry exports
		-----------------1,000 U.S. dollars-----------------		
1980-------	4	5,030	42,000	48,000
1981-------	4	5,500	46,000	54,000
1982-------	4	6,075	51,000	60,000

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 13 of 59 firms surveyed; respondents represent about 8 percent of the foreign revenue of the estimated 120 major firms believed to be operating internationally in 1981.

2/ By the U.S. International Trade Commission.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Merchandise trade can be directly generated by U.S. consulting and management firms involved in overseas projects, principally computers and office furniture, construction machinery/equipment, measuring and checking instruments, and telecommunications equipment for overseas operations. An example of merchandise exports directly associated with a management and consulting project is a $500 million telecommunications project in Egypt funded by the U.S. Agency for International Development, according to an industry source. Merchandise trade is also indirectly related to this service area through project proposals as discussed earlier. According to an industry source, there is no guarantee that any merchandise, U.S. or foreign, recommended in a proposal will be purchased; in fact, merchandise purchases may not be included in the proposal. If the consulting firm is asked to recommend equipment manufacturers, U.S. firms are preferred, but the recommendation also depends upon the quality and availability of goods and services in the area. Transportation costs and tariffs can be a determining factor in recommending U.S. goods.

Host-country and third-country products can also be used as a result of U.S. management and consulting services, especially if the products are unavailable in the United States, as indicated by some industry sources. The number of positive responses to a series of questions asked to determine whether or not host-country or third-country merchandise shipments 1/ are generated by U.S. consulting and management service activities abroad was as shown in the following tabulation:

1/ "Host-country merchandise shipments" refers to the shipments (within the host country) of host-country-manufactured products which are generated by U.S. service operations in the host-country market. "Third-country merchandise shipments" refers to the shipments of other foreign-manufactured products to a foreign market as a result of U.S. service operations in that market.

Question	Number of responses 1/	Percent of total respondents
Do you believe that foreign merchandise might be used as a result of the services your firm provides abroad?--	6	46
Are foreign or host-country products specified or recommended in the course of providing your service?----	4	31

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 13 of 59 firms surveyed; respondents represent about 8 percent of the foreign revenue of the estimated 120 major firms believed to be operating internationally in 1981.

Estimated third-country and host-country merchandise shipments resulting from two respondents' consulting and management services abroad in 1981 were as follows:

Item	Value (1,000 U.S. dollars)
Third-country shipments----------------	500
Host-country shipments-----------------	600

An example of where the entry of U.S. consulting and management services into foreign markets has benefited the economies of the host country or a third country is an airport planning project by one U.S. firm which resulted in purchases of airport-related equipment from Mexico ($100,000), the Philippines ($100,000), and Malaysia ($100,000).

International Service Trade Barriers

U.S. management and consulting firms have been successful in establishing and expanding their foreign operations and in coordinating overseas projects from U.S.-based offices. Industry sources cite alleged trade barriers in certain parts of the world, however, that could be cause to dismantle an existing operation or discourage the establishment of proposed overseas operations. The types of barriers experienced most frequently by questionnaire respondents are identified in table 6. Trade barriers that affect only specific aspects of a foreign operation, such as visas, create aggravations and delays in efficient performance of overseas operations.

There are allegedly certain barriers to trade in services that inhibit the establishment and growth of U.S. consulting and management firms abroad. These restrictions fall into several major categories, including discriminatory taxation, such as tax withholding that places U.S. firms at a cost disadvantage; discriminatory foreign-exchange and remittance

Table 6.--Trade barriers to international services in the consulting and management industry 1/

Category and barrier	Number of responses	Percent of total respondents
Right of establishment	9	69
Restrictive employment regulations (e.g. local labor requirement)	6	
Credit, investment, or financial activity restrictions	5	
Administrative/ownership restrictions	5	
Entry of service personnel and specialized tools	1	
Citizenship/residency requirements	1	
Restrictive government/business regulations	2	
Special deposit requirement for foreign companies	1	
Trade in services	10	77
Restrictive government/business regulations and administrative procedures	2	
Restriction related to resident firm preference (fixed percentage of service must be provided by domestic resident companies)	4	
Employment related restrictions on nonnationals	4	
Operating/ownership restrictions	4	
Discriminatory taxation	2	
Prohibition on services offered by nonresident companies	1	
Technical issues	2	15
Contract enforcement problems	2	
Licensing	2	15
Licensing procedures	1	
Refusal to license or renew	1	
Commercial counterfeiting	1	8
Inadequate patent or trademark enforcement	1	
Government procurement	4	31
Preference given to national firms	4	
Foreign-exchange controls	8	62
Restrictions on remittances	7	
Convertibility limitations	3	
Delays in obtaining foreign-exchange permit	2	

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 13 of 59 firms surveyed; respondents represent about 8 percent of the foreign revenue of the estimated 120 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

requirements, which inhibit foreign currency removal from the host country and limit repatriation of profits; personnel restrictions, which create delays in hiring personnel; and policies, such as majority ownership by the host country and contract registration, which place U.S.-owned foreign operations at a competitive disadvantage when compared with the position of national firms. Examples of these restrictions and their consequences, obtained from industry sources, follow.

In Latin America, tax withholding at the source often puts U.S.-owned foreign operations at a cost disadvantage. To compensate for this taxation, the client's fees are increased or the client pays the withholding on the understanding that the tax will be remitted if the U.S. company is allowed tax credits in the United States. In the Netherlands, tax arrangements include treaties that stipulate a time period after which both U.S. and Dutch taxes must be paid. Foreign currency and remittance restrictions exist in some countries, such as Spain. These practices inhibit removal of foreign currencies from the host country and limit repatriation of earnings by U.S.-owned foreign operations to the parent company.

Personnel restrictions present additional problems and, frequently, barriers to entry for U.S.-owned foreign operations. Long-term visas and work permits for U.S. personnel working in certain foreign countries are difficult to obtain, causing unnecessary delays and additional costs in project completion. The same holds true for foreign nationals working with U.S. firms; green cards are required in many countries for these nationals. These barriers generally have limited impact on established overseas operations, but may be significant for U.S. firms beginning to establish foreign offices.

Industry representatives also indicate that there is a tendency by many countries to prefer national firms for management and consulting projects, whether for reasons of national pride, desire to develop their own management and consulting service industry, or confidence in their consultants. This tendency often leads to restrictive policies that put U.S. and other foreign consulting firms at a competitive disadvantage with national firms. In some countries, majority ownership of foreign-owned companies must be held by nationals, such as Mexico, which requires at least 51 percent ownership by Mexicans. Other clients of U.S. firms or their foreign operations must prove that the U.S. operation selected for the project is the only company that can fulfill the required services and that no national company can provide comparable services effectively.

U.S. firms or their foreign operations are also required to register their contracts with some foreign governments, especially those in Latin America, where a strong preference for national firms exists. In less developed countries, such as the Philippines and Indonesia, national firms maintain very flexible negotiating positions on contract proposals, and favored treatment for local firms is often exhibited by placing ceilings on earnings by a foreign (U.S.) consulting firm.

Some industry sources claim that a restrictive measure in gaining internationally funded projects is project solicitations that are budgeted for low-cost consulting services when the actual costs for those services by a U.S. firm are much higher. Therefore, the labor-intensive nature of the business provides an advantage to any low-cost firms. The opportunity for gaining future contracts rests with gaining market entry through initial contracts. Unreasonable rate structure ceilings, sources claim, limit projects on which U.S. firms can bid; this affects foreign business growth potential by as much as 20 percent over current levels, according to one company estimate.

As shown in table 6, the three most significant trade barriers for questionnaire respondents were the right of establishment, such as restrictive employment regulations; trade in services, such as restrictions related to resident firm preference; and foreign-exchange controls, such as restrictions on remittances.

Nearly half of the questionnaire respondents reported that their service activities overseas would increase as a result of reducing or eliminating existing barriers. The number of responses to a question to determine the economic effects of international barriers to U.S. services trade and associated product exports in consulting and management service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
What effect, if any, would reduction or removal of service trade barriers have upon your receivable billings, or revenues in current or potential country markets?:		
Increase	6	46
Decrease	0	0
No effect	3	23
What effect, if any, would reduction or removal of service trade barriers have upon potential U.S. product exports in current or potential country markets?:		
Increase	3	23
Decrease	0	0
No effect	8	62

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 13 of 59 firms surveyed; respondents represent 8 percent of the foreign revenue of the estimated 120 major firms believed to be operating internationally in 1981.

Respondents indicating that reduction or removal of trade barriers would have a positive effect on foreign revenues indicated that trade would increase from 20 to 80 percent in Latin America and from 10 to 80 percent in Europe (table 7).

Table 7.--Estimated changes in revenues absent trade barriers to international business of consulting and management service firms, by areas 1/

Area and direction of change	Number of responses	Percentage change: 10	20	30	40	50	60	80
Middle East:								
Increase	1	1						
Decrease								
Far East:								
Increase	2		2					
Decrease								
Latin America:								
Increase	4		3					1
Decrease								
Europe:								
Increase	4	2				1		1
Decrease								
Africa:								
Increase	-							
Decrease								
Canada:								
Increase	2	1	1					
Decrease								
Mexico:								
Increase	2		1					1
Decrease								
Other:								
Increase	-							
Decrease								

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 13 of 59 firms surveyed; respondents represent about 8 percent of the foreign revenue of the estimated 120 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Conditions of Competition in Current and Potential Service Markets

U.S. management and consulting firms are generally the primary suppliers of this service to the international market. This leadership is due to two principal factors, commonly referred to as American know-how--extensive experience and expertise in their field(s) and highly qualified and well-educated personnel. The most significant disadvantage cited by industry sources for U.S. firms is the cultural difference, to which U.S. personnel and policies must adapt. U.S. firms must also overcome a negative attitude towards the United States that exists in many countries.

This "American know-how" is now challenged, however, by other international consultants, such as the Japanese, who have developed a highly publicized theory of management desired by some European clients. Outside competition, such as this, is a major motivating factor for U.S. firms to develop greater expertise and knowledge of their service sector. A potential competitive disadvantage for U.S. firms is the cultural factor, according to industry sources. U.S. firms and personnel must be able to adapt to cultural differences and overcome a growing negative attitude towards the United States.

In addition, industry spokesmen claim that U.S. Government commercial attaches generally do not provide leads or insights on potential international projects for U.S. management and consulting firms to the significant degree that business leads are provided to other foreign management and consulting firms by their respective embassy or consular personnel.

The competitive environment of U.S. consulting and management companies in foreign markets can be characterized based on a number of insights provided by questionnaire respondents. As shown in table 8, among the top foreign markets identified by U.S. consulting firms as their leading revenue generators in 1981, the United Kingdom and West Germany provide relatively significant competition in these markets, with 20 and 14 national firms competing, respectively. The likely reasons for competing firms' success in bidding for service contracts, as indicated in table 9, were lower prices and political bias or government support. Questionnaire respondents indicated that the three major competitive strengths of U.S. firms in current foreign service markets were (1) technology lead, (2) superior quality association, and (3) experience in the market or service (table 10). These same reasons were given as competitive strengths for U.S. management and consulting firms in potential foreign markets (table 11). These are especially significant in Europe, Africa, Canada, and Mexico. Lower price is a secondary competitive strength in certain countries, such as Saudi Arabia and West Germany.

Table 8.--Number of firms competing 1/ with U.S. consulting and management service firms abroad, by principal service markets 2/ in order of revenue generated, 1981 3/

Service market	Number of competing firms				
	Total	National	Regional	World-wide	Other U.S. firms
United Kingdom	30	20		5	5
Yugoslavia	15	5		5	5
West Germany	25	14		5	6
Saudi Arabia	23	5		10	8
Venezuela	6			6	
Malaysia	8			6	2
Philippines	10	2		8	
Spain	8			8	
Argentina	8			8	
Japan	20	10		5	5
Chile	10	2		4	4
Mexico	8	3			5
Brazil	6	3			3

1/ Based on 6 responses by questionnaire respondents.
2/ Other principal service markets for the industry may not be listed here if respondents did not identify the number of competing firms.
3/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 13 of 59 firms surveyed; respondents represent about 8 percent of the foreign revenue of the estimated 120 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 9.--Likely reasons 1/ for competing firms' success in world consulting and management service markets, by base countries of firms 2/

Base country	Lower price	Technology expertise	Preferential financing	Experience in the market or service	Superior quality association	Political or regional bias	Government support	U.S. restrictions
Bahrain	1					1		
Iraq	2					2		
United Kingdom	1						1	
Total	4					3	1	

1/ The importance of each reason is indicated by the number of times each was designated, based on 5 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 13 of 59 firms surveyed; respondents represent about 8 percent of foreign revenue of the estimated 120 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 10.--Likely reasons 1/ for the competitive strength of U.S. consulting and management service firms in foreign service markets 2/

Service market	Lower price	Technology lead	Financial strength	Experience in the market or service	Superior quality association
Middle East:					
Pakistan		1		1	1
Saudi Arabia		1			
Far East:					
Japan		1		1	1
Malaysia		1			
Philippines		1			
Central and South America (excluding Mexico):					
Argentina		1		1	1
Brazil		1		1	
Venezuela		1		1	1
Europe:					
West Germany		1		2	3
United Kingdom		1		1	2
Mexico		1		1	2
Other		1		1	1
Total		12		10	12

1/ The importance of each reason is indicated by the number of times each was designated, based on 4 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 13 of 59 firms; respondents represent about 8 percent of foreign revenue of the estimated 120 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 11.--U.S. consulting and management service firms' competitive strengths 1/ in potential foreign markets 2/

Potential service market	Lower price	Technology lead	Financial strength	Greater experience	Superior quality
Middle East:					
Saudi Arabia	1	1			
Far East:					
People's Republic of China		1			
Central and South America: (excluding Mexico):					
Brazil		1		2	2
Europe:					
West Germany	1	1		1	
Italy				1	1
United Kingdom		1			
Africa:					
Egypt		1			
Morocco	1	1		1	1
Nigeria	1	2		1	
Canada		1		2	2
Mexico		1		1	1
Total	4	11		9	7

1/ The importance of each reason is indicated by the number of times each was designated, based on 4 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service was 13 of 59 firms surveyed; respondents represent about 8 percent of foreign revenue of the estimated 120 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

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Educational Services

Executive Summary

1. International revenues of the U.S. educational services industry are estimated at $1.9 billion in 1981, most of which was derived from foreign students studying in the United States, and from foreign operations of universities, colleges, proprietary trade schools, and consultants.

2. The relationship of U.S. educational services activity abroad to U.S. exports of merchandise is complex and difficult to measure. Two-thirds of the respondents to the Commission questionnaire indicated that there was no positive relationship between the two. One of the respondents, who did indicate that educational activities abroad increased sales of U.S. merchandise exports, estimated that such merchandise exports were increased by $14 million in 1981.

3. Trade barriers to increasing educational services going to foreign markets include such things as excessive foreign government regulations and problems with commercial counterfeiting or "pirating" of U.S. educational materials or technology. Firms also mentioned exchange controls as limiting their service activities in education abroad.

4. Three-fourths of the questionnaire respondents reported that reduction of existing barriers would have no effect on foreign revenues. The remainder reported that revenues could increase from 10 to 50 percent in Europe, Latin America, the Far East and Africa.

5. U.S. educational services face growing competition from host- and third-country firms in Japan and Canada and lesser competition from host country firms in Saudi Arabia and Taiwan.

6. Lower prices and political or regional bias appear to be the major competitive strengths of foreign competition in world markets.

7. U.S. educational services strengths in world markets are its greater experience and superior quality.

Industry Profile

Definition and coverage

The educational services industry includes public and private nonprofit schools, colleges, universities, and other institutions of higher learning, libraries, and proprietary technical, trade, and commercial schools, as well as those management/consulting proprietary firms (some of which may be composed of a single person) specializing in education or vocational training. The educational services industry's primary foreign business operations involve attracting foreign students to reside in the United States for study at universities, colleges, or other educational establishments. Secondarily, the industry's foreign operations include the provision abroad of training, development assistance, language instruction, and teaching. The U.S. Department of Commerce includes the private educational industry primarily under Standard Industrial Classification (SIC) Group 82 (Private Educational Services), SIC Group 7392 (Management and Public Relations), and SIC Group 8331 (Job Training and Related Services).

The educational services organizations surveyed in this study include 48 selected major colleges and universities, vocational and junior colleges, and private firms active in education. The 11 educational service industry respondents to the Commission's questionnaire (mostly private firms) represent about 3 percent of the foreign revenues of the 200 educational service organizations believed to be operating internationally in 1981.

Highlights in 1981

- DOMESTIC SALES of the educational services industry are estimated to have totaled $140.3 billion.
- U.S. ESTABLISHMENTS in 1981 amounted to 18,300 private schools, colleges and universities and 42,000 public schools, colleges, and universities, and an unknown number of private firms providing training and other educational services.
- U.S. EMPLOYMENT amounted to 3.3 million teachers and 2.7 million other employees in 1981 (a total of 6 million employees).
- INTERNATIONAL REVENUES of the U.S. educational services industry are estimated at $1.9 billion in 1981, most of which was derived from foreign students studying in the United States, and from foreign operations of universities, colleges, proprietary trade schools, and consultants.
- FOREIGN ESTABLISHMENTS (which mainly consist of trade schools) owned or operated by U.S. firms numbered less than 200.
- FOREIGN EMPLOYMENT of U.S. citizens (who are mostly engaged in teaching) in educational services in 1981 is estimated to have totaled 10,000. An estimated 40,000 Americans are also employed in the United States providing services to foreign university students.
- U.S. TRADE BALANCE of the educational services industry is a positive $1.7 billion with the value of imported services being an estimated $200 million.

Industry structure

Domestically, the U.S. educational services industry provides the bulk of its services through public schools and secondarily through private, mostly nonprofit schools, colleges, and universities. Government provided about four-fifths of the $140 billion expended on U.S. education in 1981 with the private sector supplying the rest. 1/ The private sector includes not only privately owned elementary and secondary schools, and colleges, but also the proprietary trade or vocational schools.

It is the higher levels of education (colleges, universities, and the proprietary trade schools) that are primarily involved in international trade transactions. Typical services offered internationally by the higher levels of the U.S. education service sector consist of educating foreign students within the United States at colleges, universities, and English-language or other vocational trade schools. The foreign student, in essence, comes to the United States and purchases (consumes) services from universities, colleges and proprietary schools. 2/ U.S. educational establishments are thereby competing internationally and attracting foreign students who could alternatively purchase these educational services either from their own country or from a third country. 3/

Several examples of the large amounts of money currently being spent by foreign governments within the United States for educating their own students, mainly at U.S. universities and colleges, were provided by an individual consultant. Norway spends about $1.5 million on its 1,500 students who are studying mostly engineering or science in the United States. Malaysia is now doubling the amount it spends annually on its students in the United States, from $30 million to about $60 million (for 15,000 students). The People's Republic of China now has 6,000 students in the United States, compared with none in 1977. Venezuela has slightly less than 6,000 students in the United States, and the Venezuelan Government spends $100 to $150 million annually in the United States and maintains an administrative office in New York City to manage these educational activities.

U.S. educational services offered abroad include the teaching of English or other academic subjects, and technical consulting by U.S. professors or educational specialists aimed at vocational instruction or general development assistance. A small number of U.S. universities or colleges directly operate branches abroad either for U.S. Armed Forces personnel or American college students 4/ studying overseas for one or two semesters. Private U.S. firms operate a number of trade schools abroad, most of these being language schools. Domestic and international revenue for the educational services industry amounted to about $142.2 billion, or 17 percent, of total U.S. service sector trade, valued at $837 billion in 1981 for the 14 service sectors covered in this study.

1/ U.S. Department of Commerce, U.S. Industrial Outlook, p. 415. Data are for school year 1980/81.

2/ It should also be noted that foreign students spend in the United States considerable amounts of money on consumer goods and services outside the eductional sector. See for example, E. Boyd Wennergren and M. L. Rosario, The Economic Importance of International Assistance Activities at Utah State University, January 1981.

3/ An "import" of an educational service involves U.S. students going abroad, studying and paying a foreign educational institution. This often involves an American college student in a "semester abroad" program with a fair amount of tourism as well.

4/ The Institute of International Eduction in its Open Doors reported that there were 26,000 American students in these programs in 1980/81.

During the 1980-81 school year, expenditures for all types of education in the United States reached about $140 billion (in constant 1978-79 dollars), which is an increase of about 1.1 percent annually from the $131 billion spent in 1974-75. 1/ Expenditures solely for higher education rose from $45 billion to $50 billion in this same period.

Student enrollment in all school levels in the United States peaked in 1975 at about 61 million students, and since then it has declined every year, reaching about 58 million students in 1981. 1/ For students enrolled in higher education, enrollments have increased from 11.2 million in 1975 to an alltime high of 11.6 million in 1981.

Foreign activities of U.S. educational establishments.--Foreign revenues are particularly important to the higher levels of education (largely nonprofit colleges and universities) in the United States. The 310,000 foreign students studying at U.S. colleges and universities spent an estimated $2.5 billion for living costs and educational expenses in the United States during 1981, and constituted about 2.5 percent of total enrollments of all students according to an estimate by the American Council on Education. 2/ Of the $50 billion in revenues received by U.S. institutions of higher learning in 1981, an estimated $1.5 billion came from fees paid by the enrolled foreign students. These students also spent $1.0 billion in the United States for other living costs and expenses outside these educational institutions. The foreign students' family or personal resources provided about two-thirds of the total $2.5 billion spent; foreign governments or foreign private sources one-sixth; and U.S. public and private sources the remainder.

U.S. colleges and universities provide educational services internationally by directly contracting with a foreign institution, by allowing their faculty to do consulting work on their own, and by indirectly contracting with foreign institutions through a development assistance agency such as the U.S. Agency for International Development (AID). Combined with special skills training and development of technical facilities and schools by private firms, such activities abroad are estimated by an industry source to generate revenues of $400 million to $500 million annually.

Proprietary trade schools (also called technical schools) number about 10,000 within the United States according to the U.S. Department of Education, and include a wide diversity of schools teaching such subjects as electronics, typing, the English language, Bible studies, barber and cosmetology, auto mechanics, carpentry, computer processing, and aviation. 3/ These proprietary trade schools enroll an estimated 3 million students of whom probably 1 to 2 percent are foreign. Overseas operations by the proprietary trade schools amount to less than an estimated 200 schools operated abroad, and to correspondence courses offered by these schools. Total estimated net foreign revenues of these trade schools is less than $100 million annually.

1/ U.S. Department of Commerce, U.S. Industrial Outlook, p. 415.

2/ American Council on Education, Foreign Students and Institutional Policy, Washington, D.C., 1982, p. 37.

3/ Marci Kenney, Current Developments and Trends in International Educational Services, Washington, D.C., June 1981, p. 19.

Another segment of the U.S. educational services industry is composed of private firms which do not operate trade schools, but do provide a wide variety of professional services for education abroad or for training foreigners overseas. Among these firms are management consultants specializing in training or development assistance; noninstitutional affiliated teachers of English as a second language (TESL) or other academic subjects working abroad; and domestic companies supplying a variety of educational inputs to foreign educators such as textbooks published abroad, computer-based coursework, and educational testing services. Income from these services include repatriated royalties, and licenses or fees from textbooks published or copyrighted educational materials used abroad. A number of U.S. management/consulting firms specialize in the training of foreign students in a vocational skill, generally on a contractual basis to a foreign government and often in a developing country.

Also included among these private firms are U.S. citizens who are teachers of English and other academic subjects who are working abroad. Other types of services offered abroad for education include training of foreigners in data processing, language instruction, correspondence courses, and educational testing for admittance into U.S. universities or schools. Total foreign revenues for all of these private educational service firms, according to several educational consultants, amounted to an estimated $100 million to $200 million in 1981.

Recent trends and outlook

The U.S. Department of Education expects the number of students enrolled in all domestic educational institutions to decline through the late 1980's. The record high enrollments in U.S. colleges and universities in 1980-81 are expected to decrease as well, but the outlook for proprietary training schools and programs is optimistic. Curtailments in public expenditures on education have sharply reduced the number of college instructors and professors in many colleges and universities. As a result, a number of these college instructors are considering foreign employment opportunities, and U.S. universities and colleges are looking to foreign students to maintain their enrollments in light of the declining number of available domestic students.

A considerable number of U.S. colleges and universities have developed exchange agreements with foreign universities and governments to provide services abroad in recent years. Universities are thus better able to "spread their overhead costs" in certain faculties or departments facing a downturn in enrolled students or research funding.

Trained university faculty and other teachers from the primary or secondary levels, unemployed as a result of the domestic budgetary reductions, are increasingly attracted to employment by foreign universities and institutions. 1/ Foreign institutions thus are directly recruiting and

1/ International Education Department, University of Maryland, College Park, Md. The University of Maryland has been heavily involved in international educational activities over the years. There have been numerous periodical articles in recent months on the current "surplus" of university (often Ph.D.-trained) instructors. See, for example, Lawrence Feinberg, "The Retrofitting of the Ph.D.," The Washington Post, July 19, 1982.

employing U.S. educators who might have become "surplus" because of U.S. educational reductions.

The United States has a comparative advantage since U.S. educational facilities are perceived in foreign countries as the best in the world. Many educational leaders believe that as a result, scientific and technical training in the United States will continue to provide a significant multiplier effect for exports of science and engineering technology, systems, and products developed by the U.S. manufacturing sector. In addition to the economic benefits accruing to U.S. exporters of merchandise exports, an individual consultant indicates that political and development benefits accrue to the host country which sends students to the United States or has U.S. educators involved abroad.

The U.S. Department of Education projects that U.S. expenditures on education will grow to $163 billion (in constant 1978-79 dollars) by the 1988-89 school year, or by 1.7 percent annually, from the 1980-81 school year. 1/ The Department also projects that school enrollments will decline to slightly below 56 million students by 1988-89 from the 1979-80 level of about 57.4 million.

U.S. educational experts predict that many foreign countries, over the next 20 years, will desire to send even larger numbers of students to U.S. institutions. The number of foreign students studying in the United States is expected to increase at a rate of about 10 percent annually through the end of the 1980's, with the ratio of foreign to U.S. students enrolled in higher education rising from 1:50 in 1980 to about 1:12 by 1990. 1/ An individual consultant sees prospects for expanding U.S. exports of educational services as excellent with the number of foreign students studying in the United States projected to rise to 1 million students by 1990 from the present number of about 30,000. This will occur due to the growing need for technical engineers and computer science expertise to coincide with industrial development in both developed and developing nations.

A majority of U.S. educators providing services abroad have likely received direct or indirect financing for foreign development assistance from both U.S. Government and multilateral development groups (such as the World Bank) to finance these services. Educational sources indicate that, given the likelihood of reduced foreign development assistance, U.S. educators will likely have to diversify the services offered in order to grow or even maintain current project levels. Already a number of middle-income developing countries have been excluded from receiving such development assistance and, therefore, are looking to their own resources to purchase U.S. educational services.

The outlook for foreign sales of U.S. educational expertise is good, especially for the larger private firms or larger universities and colleges which are involved in consortia which can provide a variety of educational services to potential customers such as foreign institutions or governments. Moreover, it is likely that the middle-income developing countries, such as South Korea or Brazil, or petroleum exporting (OPEC) countries will continue to remain excellent markets for U.S. educational expertise.

1/ U.S. Department of Education, National Center for Education Statistics, Projections of Education Statistics to 1988-89, 1980.

Future business in foreign markets is likely to involve "blue collar" technical training and an acceleration of revenue generating educational programs, according to one industry source. For example, ad hoc informal structures exist where most major U.S. universities will contract to establish an educational program abroad (e.g., a major university completed a $7.5 million project of this nature in Portugal). In addition, teaching English as a second language is a major growth market which is likely to account for nearly half of the increased growth in foreign students projected for 1990, and to create about 15,000 to 20,000 jobs.

U.S. Service Operations in Foreign Markets

Operating structure

Because of the strong demand by foreign students for a U.S. college education, U.S. colleges and universities do not normally need to recruit or advertise abroad to attract foreign students, although some proprietary trade schools apparently do so. U.S. embassies abroad normally provide catalogues and brochures on U.S. educational institutions, and assist the foreign student in obtaining a U.S. visa.

Privately owned vocational, business or trade schools are active in the international area and market their services internationally by (1) establishing branch schools in the foreign country, (2) direct enrollment of foreign students in their U.S. schools, and (3) correspondence courses. A number of U.S. firms own and operate trade schools abroad: these include Berlitz (language instruction schools in numerous countries), Control Data (data processing schools in Canada, France, West Germany and the United Kingdom), and International Telephone and Telegraph (several business schools in Western Europe and North Africa). 1/ However, the total foreign trade schools owned by U.S. firms probably amount to less than 200 schools or less than 2 percent of total domestic trade schools. About one-half dozen U.S. trade schools also offer correspondence courses to foreigners in such subjects as English and electronics. These firms operate by sending course material directly by mail to foreign students living mainly in Canada, Western Europe, and Latin America (Mexico). Some U.S. trade schools have begun in recent years advertising to and recruiting foreign students to attend their U.S. branches.

The other private educational services firms are very diverse in the types of services they provide and in their reliance on foreign sales. A large number of U.S. teachers of English as a second language work abroad. A number of U.S. consulting firms and private sector firms provide special skills training and development of technical facilities and schools abroad and rely to a larger extent on foreign sales. For the remaining U.S. private firms operating abroad and providing other educational services (such as educational testing, book publishing, correspondence courses), foreign revenues are insignificant (less than 1 percent of their total net revenues).

1/ Marci Kenney, op. cit.

Total foreign revenues of all levels of educational services came to an estimated $1.9 billion in 1981, which is about 1.4 percent of the total domestic expenditures of $140 billion on education, and accounts for about 2 percent of the total service sector foreign revenue of $109.6 billion estimated for the 14 selected service industries covered in the Commission's study. Overall, at least 40,000 jobs are created domestically by the presence of 310,000 foreign students in U.S. universities and colleges; and at least 10,000 Americans are employed abroad in educational activities. 1/ Foreign students constituted about 2.5 percent of all enrolled students in U.S. universities and colleges. 2/

Although about 26,000 U.S. college students study abroad in foreign study programs administered by U.S. institutions of higher learning 3/, the principal activity abroad of these U.S. institutions consists of providing contracted educational or consulting services to foreign governments, universities, and other institutions located mainly in developing countries. 4/ There are an estimated 6,500 U.S. college faculty members working or engaged in study abroad. 5/ The U.S. Agency for International Development employs, on a consulting basis, some 500 U.S. university faculty members abroad for a variety of projects. 6/

According to the Institute of International Education, foreign countries interested in recruiting Americans for foreign teaching or university jobs requested the following types of educators: Engineers (25 percent), physical or life scientists (18 percent), English or education instructors (16 percent), business or management professors (12 percent), social scientists (10 percent), and teachers of other subjects (19 percent). 7/ Foreign governments or institutions hire some of these Americans directly, and in other cases, they contract with a U.S. educational institution or private firm which then provides its own employees for short-term assignments abroad.

There are also a substantial number of noninstitutional affiliated U.S. teachers of English or other academic subjects abroad. 8/ In 1981, there were at least 3,000 Americans estimated to have been privately employed abroad teaching English as a second language TESL. Some of these TESL teachers are employed by U.S. firms whose primary business is the selling of aeronautical

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1/ Estimation of the number of domestic jobs (some of which are outside the educational sector) is by Frederick Centanni, Sylvania Systems Group/GTE Inc., Waltham, Mass. Foreign employment is estimated by the Commission's staff, based upon conversation with various education experts.

2/ Institute of International Education, op. cit.

3/ Institute of International Education, op. cit.

4/ Professors provide their services both by "free-lancing" on their own, and by university-to-foreign institution contract.

5/ Carnegie Council on Policy Studies in Higher Education, (Barbara Burn, ed.), Expanding the International Dimension of Higher Education, New York, 1980, p. 101-104.

6/ Agency for International Development.

7/ Unpublished program summary for April-October 1981, Institute of International Education, New York.

8/ Teachers of English as a Second Language Association (TESLA), Washington, D.C.

equipment, computers or other high-technology products, requiring English language proficiency.

Firms responding to the Commission's questionnaire identified several operating structures used abroad (table 1). The dominant operating structure indicated was the subsidiary or branch structure. Secondary service activities carried out abroad included mainly consulting and management, a function related to the technical training and development assistance that a number of these educational service firms perform.

Table 1.--Operating structures of principal service activity, and revenues associated with secondary service industry activities of educational services firms in foreign markets, 1981 1/

Item	Revenues 2/	Number of responses	Percent of total respondents
	1,000 U.S. dollars		
Operating structure:			
Foreign affiliate	-	1	9
Licensing	-	1	9
Subsidiary or branch	-	4	36
Franchising	-	1	9
Other	-	4	36
Secondary service activity:			
Computer and data processing services	3/	1	9
Consulting and management services	3/	1	9
Health services	3/	1	9
Total	531	3	27

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 11 of 48 firms surveyed; respondents represented about 3 percent of the foreign revenue of the 200 major firms believed to be operating internationally in 1981.
2/ Calculated by the staff of the U.S. International Trade Commission from receivables, billings, or revenue data provided by respondents.
3/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Growth trends and U.S. investment

The total foreign revenues of U.S. educational service establishments (table 2) are derived mainly from foreign students studying at U.S. universities or colleges (80 percent of the $1.9 billion in estimated foreign revenues of the entire services industry), services abroad of American university professors and teachers (15 percent), and net foreign earnings of proprietary trade schools, repatriated foreign royalties of educational materials or book-publishing firms, and other private firms (5 percent). The basis for estimated foreign revenues for all U.S. educational services in 1981 is shown in the following tabulation (in millions of dollars):

Type of education service	Value
1. Payments of foreign students to U.S. universities, colleges, and trade schools 1/-----	1,500
2. Services of U.S. college faculty, and teachers working abroad 2/-----------------------	300
3. Repatriated profits, royalties, and miscellaneous foreign earnings of private U.S. firms operating trade schools abroad, or receiving fees from foreign use of educational materials such as books or correspondence course materials--	100
Total--	1,900

1/ Based on the assumption that 60 percent of the reported expenditures of foreign students in the United States go to colleges, universities, and trade schools; and that these expenditures are derived solely from foreign funds. American Council on Education is the source of the total foreign students expenditure level of $2.5 billion. The $1.0 billion expended outside education by foreign students presumably is spent on consumer goods, housing not controlled by universities, and other services, except education.

2/ These services are mainly the value of U.S. university contracted services, assisted by the Agency for International Development, and by the World Bank; the Saudia Arabian University project; and the earnings of TESL teachers working abroad.

Table 2.—Indicators of activity in the foreign and domestic operations of educational service firms, 1980-82

Item	Foreign	Domestic	Total
Estimated value of receivables, billings, or revenues: 1/ 2/			
1980------------------1,000 dollars--:	49,442	97,533	146,975
1981----------------------------do----:	46,988	108,605	155,593
1982----------------------------do----:	54,113	122,220	176,333
Estimate of investment in physical assets 3/ in foreign operations:			
1980------------------1,000 dollars--:	5,897	-	-
1981----------------------------do----:	18,067	-	-
1982----------------------------do----:	29,928	-	-
Number of establishments:			
1980----------------------------------:	81	27	105
1981----------------------------------:	97	27	122
1982----------------------------------:	114	28	140
Estimated 4/ value of total industry receivables, billings, or revenues:			
1980------------------1,000 dollars--:	1,900,000	140,700,000	142,600,000
1981----------------------------do----:	1,900,000	140,300,000	142,200,000
1982----------------------------do----:	2,100,000	140,900,000	143,100,000

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 11 of 48 firms surveyed; respondents represented about 3 percent of the foreign revenue of the 200 major firms believed to be operating internationally in 1981.

2/ Excluding the value of any merchandise exports.

3/ Including the undepreciated book value of land, plant, and equipment.

4/ By the staff of the U.S. International Trade Commission based on discussions with industry and/or association representatives, and secondary sources.

Source: Compiled from data submitted in response to questionnaries of the U.S. International Trade Commission.

The 11 firms (including universities) that responded to the Commission's questionnaire indicated that their total revenues reached $156 million in 1981, and that it would rise by about 13 percent to $176 million in 1982 (table 2). The firms indicated that their foreign revenues provided about 30 percent of their total receipts in 1981. The 11 firms also reported that their foreign investments totaled about $18 million in 1981 and was spread out among 97 foreign establishments. Most of their foreign establishments consist of small schools, each with an average investment of $186,000 in 1981. Total foreign revenues for the educational services industry are expected to continue growing, but will account for only a small portion of the total service sector foreign revenue estimated at $135.7 billion in 1982 (table 3).

Table 3.--Estimated total foreign revenue generated by the educational service industry and estimated total foreign revenue for selected service industries, 1980-82

Year	Total foreign revenue for service industry 1/ (1)	Total foreign revenue for selected service industries 2/ (2)	Ratio of (1) to (2)
	1,000 U.S. dollars		Percent
1980	1,900,000	89,398,000	2
1981	1,900,000	109,611,000	2
1982	2,100,000	135,744,000	2

1/ Estimated, based on discussion with industry and/or association representatives, and secondary sources.
2/ Based on totaling Commission-estimated foreign revenue for each of the 14 selected industries covered in this study.

Source: Estimated by the staff of the U.S. International Trade Commission.

One of the largest projects abroad, undertaken by a group of U.S. universities, involved contracting with the Saudi Arabian Government to assist its university system expansion, a project to ultimately cost over $3.5 billion. 1/ The project entails the setting up of an entire university--course work, research skill development, teaching, construction of classrooms, and purchase of laboratory and scientific equipment. 2/ Another recent typical example of university involvement overseas occurred with a consortium of Midwestern land-grant universities signing a development assistance agreement with an Indonesian university worth a reported $12 million to $20 million. 3/

The estimated 3,000 TESL teachers working abroad receive an estimated $50 million annually for their services. Many of these teachers of TESL or other subjects are instructing foreigners who intend to use English or other skills to utilize U.S. machinery or technology or possibly to travel or study at a later time in the United States. Industry discussions, reveal that U.S. private firms receive an estimated $100 million annually in foreign royalties from educational materials published abroad, repatriated profits from their foreign subsidiaries, copublishing fees from foreign publishers, translation rights fees for educational coursework or materials from foreign publishers, and other miscellaneous foreign receipts.

Regional and country activity

The worldwide demand for U.S. educational services has previously been noted by the large expenditures by foreign governments for educational

1/ According to the U.S. Department of Labor.
2/ See "Universities Get Out and Sell," The Economist, Sept. 24, 1981.
3/ According to the Michigan State University.

purposes in the United States, and the establishment of U.S. technical facilities and educational programs abroad. Foreign market activity reported by respondents to the Commission's questionnaire confirms the broad involvement of this industry in international trade (table 4).

The Middle East, Far East, and Latin America are identified as the most significant market regions for the U.S. educational industry in 1981, based on revenues generated. The Far East appears to be an important growth region with the Japanese market cited most frequently. The European region is equally mentioned by respondents as an area of activity but it has not generated the revenue of other important markets.

Trade in Merchandise Generated by Trade in Services

Some U.S. merchandise exports of educational materials are directly generated by educational service activities, although the more significant relationship is an indirect one, according to an industry source. The direct and short-term effect of educational services offered abroad may involve the purchase of U.S. textbooks, and learning or audiovisual equipment. The indirect, long-run effect occurs when a foreign student returns to his/her own country and then purchases U.S. merchandise and equipment other than strictly educational materials. One industry source estimates that annual U.S. merchandise exports of machinery, high-technology equipment, and general consumer goods have been increasing by $500 million to $1 billion as a result of U.S. educational services to foreigners. The Michigan State University has a program, for example, in which foreign students visit and become familiar with a variety of Michigan industries and their products. As a result, some of these Michigan industries have increased their exports to the countries of these students. Foreign students are thus likely to eventually stimulate foreign demand for U.S. exports, although this has not been quantitatively analyzed.

Consistent with the often indirect relationship between U.S. educational services abroad and U.S. merchandise exports, most firms responding to the Commission's questionnaire did not indicate that there was a positive relationship between the two. Only 4 of the 11 firms responding indicated that educational services activity might influence the purchase of U.S. merchandise exports. The number of positive responses to a series of questions asked to determine whether or not U.S. merchandise exports are

Table 4.--Regions and countries in which revenue is generated by educational service firms, 1980-82 1/

Region and country 2/	Number of responses			Percent of total respondents			Estimated revenue		
	1980	1981	1982	1980	1981	1982	1980	1981	1982
							------1,000 U.S. dollars------		
Middle East	4	7	4	36	64	36	13,923	12,248	11,528
Iran	-	3	-						
Israel	-	2	-						
Jordan	-	1	-						
Kuwait	-	3	-						
Lebanon	-	1	-						
Saudi Arabia	-	4	-						
Turkey	-	1	-						
Far East	4	8	4	36	73	36	14,004	13,546	20,074
Australia	-	2	-						
Taiwan	-	3	-						
Japan	-	8	-						
Republic of Korea	-	2	-						
Malaysia	-	1	-						
New Zealand	-	1	-						
Thailand	-	1	-						
Latin America	3	6	4	27	54	36	3/	11,436	14,438
Argentina	-	1	-						
Brazil	-	4	-						
Chile	-	1	-						
Colombia	-	2	-						
El Salvador	-	1	-						
Peru	-	1	-						
Uruguay	-	1	-						
Venezuela	-	4	-						
Europe	6	8	6	54	73	54	2,555	2,511	2,325
West Germany	-	4	-						
Greece	-	2	-						
France	-	3	-						
Italy	-	3	-						
Netherlands	-	1	-						
Spain	-	2	-						
United Kingdom	-	4	-						
Africa	3	4	3	27	36	27	3/	2,033	3/
Algeria	-	3	-						
Egypt	-	2	-						
Libya	-	2	-						
Morocco	-	1	-						
Nigeria	-	3	-						
Africa South	-	1	-						
Canada	2	4	2	18	36	18	3/	648	3/
Mexico	4	5	3	36	45	27	4,380	3,780	3,469
Other	2	3	2	18	27	18	3/	3/	3/

1/ Country listing is for 1981 only.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 11 of 48 firms surveyed; respondents represented about 3 percent of the foreign revenue of the 200 major firms believed to be operating internationally in 1981.

3/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

generated by U.S. educational service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
Do your believe that U.S. merchandise might be used as a result of the services your firm provides abroad?------------------------------	4	36
Is U.S. merchandise specified or recommended in the course of providing your service?-------------	1	9
Are U.S. merchandise exports believed to be directly generated?-----------	1	9

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 11 of 48 firms surveyed; respondents represented about 3 percent of the foreign revenue of the 200 major firms believed to be operating internationally in 1981.

One firm estimated that their educational service activities abroad generated $14 million in U.S. merchandise purchases in 1981 and projected an increase of about 25 percent in service-related merchandise exports in 1982.

The service activities of U.S. educators operating abroad directly stimulate foreign demand for some U.S. products such as textbooks, scientific instruments or high-technology products such as computers or computer software. 1/ The outlook for increased exports of U.S. textbooks and of U.S. publishers services to formal education in other countries is excellent, according to some U.S. publishers, 2/ particularly in developing countries, where there is often only one textbook for every 10 students.

Foreign demand for technical training by U.S. educators usually is a direct consequence of the sale of technologically advanced equipment made in the United States. The U.S. Department of Commerce expects the rapidly expanding markets for U.S. high-technology products in Latin America, Africa, and especially the Middle East to present increasing demands for technical training offered by U.S. companies abroad. The Department expects the volume of such training of foreign nationals to increase in the 1980's and be more and more directed to sales in the developing countries mentioned above. It is likely that this training enhances U.S. exports of the high-technology products, although the relationship of training to equipment is a mutually supportive consideration.

1/ The Economist, op. cit., for the example of the case of the Saudi Arabian university expansion on later purchases of educational materials from the United Kingdom and the United States.

2/ Leo Albert, "Widening Horizons for International Publishing," Publishers Weekly Sept. 17, 1979.

Firms responding to the questionnaire also indicated that their educational service activities could stimulate the purchase of foreign merchandise abroad. The number of positive responses to a series of questions asked to determine whether or not host-country or third-country merchandise shipments 1/ are generated by U.S. educational service activities abroad was as follows:

Question	Number of responses 1/	Percent of total respondents
Do your believe that foreign merchandise might be used as a result of the services your firm provides abroad?----------------------------	3	27
Are foreign or host-country products specified or recommended in the course of providing your service?---	0	0

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 11 of 48 firms surveyed, respondents represented about 3 percent of the foreign revenue of the 200 major firms believed to be operating internationally in 1981.

No further insights were provided by respondents as to specific instances where the entry of U.S. educational services in a foreign market has benefited the host country, accept as noted in other segments of this report.

International Service Trade Barriers

Since the bulk of the educational services provided abroad by U.S. universities and colleges are heavily influenced by either U.S. or foreign government funds, a U.S. university, college or a private firm seeking to provide educational services abroad must thus be able to meet the requirements of government contracting. However, excessive or burdensome contracting requirements of either foreign governments or of multilateral organizations have not been reported widely as a barrier to firms or universities seeking to provide services abroad. Generally, once the decision is made by a foreign government or institution to seek out and purchase U.S. educational services, there are few trade barriers--particularly for U.S. universities and colleges.

1/ "Host-country merchandise shipments" refers to the shipments (within the host country) of host-country-manufactured products which are generated by U.S. service operations in the host-country market. "Third-country merchandise shipments" refers to the shipments of other foreign-manufactured products to a foreign market as a result of U.S. service operations in that market.

There are, however, some trade barriers which do affect private firms; Many of these are identified by questionnaire respondents in table 5. For U.S. firms operating trade schools in foreign countries, each country has its own set of regulations and procedures for businesses operating such a school. Thus, most of the U.S.-owned trade schools located abroad are subject to some foreign government restrictions. Response to the Commission's questionnaire indicates that government regulations and restrictive rights of business establishments were a problem.

There have been some complaints from firms operating trade schools abroad (and also reported by Commission's questionnaire respondents) of "pirating" or commercial counterfeiting of their curriculum or correspondence course material in some foreign countries. This complaint is related to the general problem of preventing copyrights held by U.S. citizens and firms of books, academic research, or other "intellectual property" from being abused in foreign countries. 1/

There have been efforts by the United Nations Educational, Scientific, and Cultural Organization and by the International Publishers Association to encourage authors of textbooks or other educational material to share their products internationally by having countries respect foreign authors' legal (copyright) and intellectual rights. However, some foreign governments (and this was reflected in questionnaire responses) have delayed payments for direct purchase of U.S. manufactured books or payment of royalties to U.S. publishers or authors. The net effect being that some authors or publishers are reluctant to allow any use of their works abroad.

In responses to the Commission's questionnaire, the most frequently cited trade barriers to educational service exports were foreign exchange controls (particularly restrictions on remittances), restrictive rights of establishment, restrictive government/business regulations, and commercial counterfeiting (table 5). Because of the nature of education, it is obvious that such government regulations and the forementioned "pirating" or counterfeiting problems have served as impediments to expanding international trade in educational services.

However, while such barriers are associated with the operation of educational service activities overseas, their overall quantitative effect, according to the respondents, still appears to be relatively minimal. The number of responses to a question to determine the economic effects of international barriers to U.S. services trade and associated product exports in educational service activities abroad was as shown in the following tabulation:

1/ Albert, ibid.

Table 5.--Trade barriers to international services in the educational services industry 1/

Category and barrier	Number of responses	Percent of total respondents
Right of establishment	2	18
Restrictive employment regulations (e.g., local labor requirement)	2	
Credit, investment, or financial activity restrictions	1	
Administrative/ownership restrictions	2	
Restrictive government/business regulations	1	
Special deposit requirement for foreign companies	1	
Trade in goods	1	9
Restrictive regulations or administrative procedure	1	
Local purchase requirements	1	
Restricting entry of equipment or supply	1	
Trade in services	3	27
Restrictive government/business regulations and administrative procedures	2	
Technical issues	1	9
Contract enforcement problems	1	
Licensing	1	9
Licensing restrictions (e.g., quotas)	1	
Commercial counterfeiting	2	18
Inadequate patent or trademark enforcement	2	
Unclear definitions of trademark, patent, imported goods, or counterfeit goods	1	
Government procurement	1	9
Preference given to national firms	1	
Governmental import or distribution monopoly	1	
Prohibition of foreign services contracts (bilateral or multilateral)	1	
Foreign exchange controls	4	36
Restrictions on remittances	4	
Convertibility limitations	3	
Delays in obtaining foreign exchange permit	1	

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 11 of 48 firms surveyed; respondents represented about 3 percent of the foreign revenue of the 200 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Question	Number of responses 1/	Percent of total respondents
What effect, if any, would reduction or removal of service trade barriers have upon your receivables, billings, or revenues in current or potential country markets?:		
Increase	3	27
Decrease	0	0
No effect	8	73
What effect, if any, would reduction or removal of service trade barriers have upon potential U.S. products exports in current or potential country markets?:		
Increase	0	0
Decrease	0	0
No effect	8	73

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in thes service industry was 11 of 48 firms surveyed; respondents represented about 3 percent of the foreign revenue of the 200 major firms believed to be operating internationally in 1981.

The few respondents, indicating that reduction or removal of trade barriers would have a positive affect on foreign revenues, reported that trade would increase from 10 to 20 percent in Europe and Latin America; and from 40 to 50 percent in the Far East and Africa (table 6). Respondents did not feel that U.S. product exports associated with educational services would be affected by a reduction in existing barriers.

Conditions of Competition in Current and Potential Service Markets

Although some developed countries such as Japan, the European Community (EC), and Canada send significant numbers of students to the United States, the primary markets for U.S. educational services are the developing countries 1/, with a significant portion of the funding for these services derived, directly or indirectly, from government funds or in some cases multilateral organizations such as the World Bank. The United States competes with other countries such as Japan and the EC in offering its educational services. For the most part, because of U.S. technological expertise, foreign demand for U.S. education is high and competition with other countries for foreign students is limited. An industry source cited the example of Venezuela, which furnishes scholarships to its qualified university students desiring to study anywhere abroad. Out of some 6,000 Venezuelan university students studying abroad and receiving full government scholarships, all but 200 or 300 study in the United States.

1/ Institute of International Education, op cit., reports the nationality of foreign students in the United States for each school year.

Table 6.--Estimated changes in revenues absent trade barriers to international business of educational service firms, by areas 1/

Area and direction of change	Number of responses	Percentage change						
		10	20	30	40	50	60	80
Middle East:								
Increase	-							
Decrease								
Far East:								
Increase	1				1			
Decrease								
Latin America:								
Increase	1		1					
Decrease								
Europe:								
Increase	1	1						
Decrease								
Africa:								
Increase	1					1		
Decrease								
Canada:								
Increase	-							
Decrease								
Mexico:								
Increase	-							
Decrease								
Other:								
Increase	-							
Decrease								

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 11 of 48 firms surveyed; respondents represented about 3 percent of the foreign revenue of the 200 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

With the cost of maintaining branches of U.S. colleges and universities overseas almost prohibitive, most U.S. nonprofit institutions of higher learning rely on bringing foreign students to this country rather than attempting to carry out education abroad. The demand by foreign students for a U.S. college education is very strong. In 1980, for example, some 600,000 foreign students overseas took an English-language proficiency test needed for admission to many U.S. colleges or universities. 1/ Industry experts cite several factors which may limit the increase in the number of foreign students studying in the United States as mainly (1) cost, (2) cultural or language

1/ National Association for Foreign Student Affairs, Washington, D.C.

problems, (3) U.S. immigration controls, and (4) restrictions relating to the public subsidy issue because of U.S. and State Governments' fiscal reductions. 1/

For U.S. proprietary schools attempting to attract foreign students, there have been some problems with unsubstantiated advertising claims about their programs. In some cases, foreign students have come to the United States and not received the services promised, leading to problems of "quality assurance" in which all U.S. educational programs are then made to suffer. Several educational associations have proposed voluntary standards for their member institutions to use in recruiting foreign students. 2/

With regard to direct overseas involvement, U.S. colleges and universities provide mainly services to developing countries which have received funds for this purpose from U.S. development agencies such as AID or from foreign governments. In 1980, AID provided over $2.5 billion in development assistance out of which about $109 million went specifically for rural education in developing countries, and $50 million went for contracted services provided by about 70 U.S. colleges and universities. The World Bank as well as other multilateral organizations such as the Asian Development Bank, the Inter-American Development Bank, and United Nations are other sources for financing international educational services. The largest of these organizations, the World Bank, loaned about $700 million in 1980 for education, such as the construction of school facilities, purchase of books or scientific equipment for teaching, and development of curricula and staff training (so-called "institution-building").

It appears that U.S. institutions of higher learning will have little difficulty, over the next decade, in attracting foreign students desiring to study in the United States, according to many education observers. Indeed, it may well turn out that, because of domestic policy considerations, U.S. institutions may have to limit their foreign student enrollments. 3/

Institutions in some foreign countries offer educational services that compete with those offered by U.S. universities and colleges operating abroad, although U.S. educational services, because of the preeminence of U.S. technology, have a strong demand in many developing and OPEC countries. A number of developed countries have well-known and established university systems and offer these educational services internationally: these countries include, for example, the United Kingdom, Japan, West Germany, Australia, and Canada among the market economy countries, and East Germany among the nonmarket economy countries.

1/ The complex policy question of to what degree a foreign student receives a subsidy by studying at a U.S. university or college receiving government funds is addressed in the American Council on Education, Foreign Students and Institutional Policy, Washington, D.C., 1982.

2/ American Council on Education, op. cit.

3/ American Council on Education, Ibid., p. 50-54. See also Marci Kenney, op. cit.

For the most part, however, competition with foreign universities or firms is weak, as identified by questionnaire respondents in table 7. The U.S. educational services compete largely among themselves for certain key markets, whereas the apparent strength of the service organizations in Canada and the United Kingdom have apparently limited participation of U.S. service activity there. Some additional insight is shown in the likely reasons for competing firms' success in world educational service markets which were cited by three firms for the United Kingdom (table 8). All three indicated that lower price was the dominant reason for the United Kingdom's success.

Certain competitive disadvantages of U.S. educational services were cited earlier in this report. A major problem, emphasized by industry sources, results when U.S. institutions charge a 70-percent "overhead" fee in addition to the actual cost of any services or materials furnished in completing a contracted educational project. This "overhead" charge can make U.S. institutions less cost competitive internationally. Although the Agency for International Development has begun a program matching potential foreign purchasers of U.S. educational services with available U.S. private firms, universities, and colleges, there is often a lack of marketing information for foreign customers concerning U.S. educational institutions.

Table 7.--Number of firms competing 1/ with U.S. educational services firms abroad, by principal service markets 2/ in order of revenue generated, 1981 3/

Service market	Number of competing firms				
	Total	National	Regional	World-wide	Other U.S. firms
Saudi Arabia	105	5			100
Taiwan	105	5			100
Japan	130	20	5	5	100
United Kingdom	3	2		1	
Canada	6	3		1	2

1/ Based on 2 responses by questionnaire respondents.
2/ Other principal service markets for the industry may not be listed here if respondents did not identify the number of competing firms.
3/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 3 of 23 firms surveyed; respondents represented about 3 percent of the foreign revenue of the 200 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 8.--Likely reasons 1/ for competing firms' success in world educational service markets, by base countries of firms 2/

Base country	Lower price	Technology expertise	Preferential financing	Experience in the market or service
United Kingdom	3			
Total	3			

Base country	Superior quality association	Political or regional bias	Government support	U.S. restrictions
United Kingdom		1		
Total		1		

1/ The importance of each reason is indicated by the number of times each was designated, based on one response.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 11 of 48 firms surveyed; respondents represent almost 3 percent of the foreign revenue of the 200 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Conditions of competition abroad for proprietary trade schools and other private firms offering educational services vary considerably depending on the type of services offered. The overall competitive strengths of U.S. educational organizations appears to center in the areas of greater experience and superior quality as cited by three questionnaire respondents (table 9). A few domestic companies have experienced success in offering correspondence courses overseas in advanced electronic, computer or high-technology instruction in Western Europe, whereas others are now entering the international market by selling or leasing rights to foreign companies which administer the programs locally. In 1981 for example, McGraw Hill Continuing Education Center, Inc., entered into an agreement with a Swedish firm to sell correspondence courses throughout Scandinavia. 1/ A number of U.S. firms have been successful in operating English-language schools abroad as well. However, other trade schools operating abroad are reported to have been only marginally successful in offering instruction in auto repair, heating, air-conditioning, and electronics. The curriculum areas reported as likely to be especially in demand in Western Europe include clerical, management, computer science, and certain technical skills.

U.S. firms offering other educational services abroad tend to be very competitive in their respective business fields with their foreign

1/ Cited by Marci Kenney, op. cit., pp. 26-27.

Table 9.--U.S. educational service firms' competitive strengths 1/ in potential foreign markets 2/

Potential service market	Lower price	Technology lead	Financial strength	Greater experience	Superior quality
Far East:					
Republic of Korea------				1	1
Malaysia---------------				1	1
North America and Mexico:					
Mexico-----------------				1	1
Total----------------				3	3

1/ The importance of each reason is indicated by the number of times each was designated, based on 1 response.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service was 11 of 48 firms surveyed; respondents represented about 3 percent of the foreign revenue of the 200 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

competitors. There is a large number of U.S. management consulting firms operating internationally and offering educational services; these U.S. firms tend to dominate the international market for these specialized educational as well as the general management consulting services field. The larger firms tend to be multinational, and emphasize marketing of U.S. technology and educational techniques.

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Equipment Leasing and Rental Services

Executive Summary

1. Foreign revenues generated by U.S. equipment leasing and rental service firms were $13.4 billion in 1981.

2. At least $56.7 million in U.S. merchandise exports were directly generated by U.S. leasing activities overseas in 1981. U.S. firms report they do not specify U.S.-made equipment in their leasing contracts. However, major items exported as a result of the equipment leasing and rental service activity include machinery and industrial equipment, business machines, and medical equipment. Industry sources point out that a greater share of U.S. merchandise is expected to be exported as a direct result of U.S. international leasing activities if the U.S. Eximbank develops a financing program for lease-generated exports and OPIC implements its export credit risk insurance program.

3. Third-country and host-country merchandise shipments resulting from U.S. equipment leasing and rental services abroad in 1981 were estimated at $120 million, largely dry cargo containers.

4. Based on questionnaire responses and industry discussions, there seem to be few specific barriers to trade in leasing services in foreign markets. However, each country has its own requirements, regulations, and tax laws which must be dealt with. Different types of leasing contracts may be subject to different laws and requirements in these countries, which makes it difficult for U.S. firms to enter the market. These include such issues as (1) whether a country has statutory provision for leasing services, (2) funding and currency exchange regulations, (3) licensing and registration requirements, (4) tax laws applicable to leasing transactions, and (5) restrictions limiting access to imported equipment and/or personnel.

5. U.S. firms face host-country and/or third-country competition in important markets such as Mexico, the United Kingdom, Canada, West Germany, Japan and Argentina.

6. U.S. firms are generally competitive in foreign markets. However, when competitive disadvantages occur they relate to the host nation's requirements for varying degrees of domestic participation in leasing projects, discriminatory taxation, foreign exchange regulations, capital requirements, and foreign government procedures which favor domestic firms.

7. Industry representatives indicate that the U.S. has a technological lead in certain product areas such as computers, aircraft, and energy equipment which facilities its competitive posture in world markets. Reporting firms also cited U.S. company financial strength, market experience and superior quality associated with U.S. products as reasons for this position in world markets.

Industry Profile

Definition and coverage

A lease is a contractual arrangement under which the owner of an asset, the lessor, permits another party, the lessee, to use the asset for a specified period of time in return for a specified payment. The type of lease determines whether or not the lessee has the option to purchase the asset.

This study covers two broad leasing categories, finance (Standard Industrial Classification (SIC) 6159) and operating (SIC 7394). Not included in these two SIC groups are establishments which lease the equipment they manufacture and those which provide personnel to operate or maintain the equipment during the lease period, more often called a contract. However, certain affiliates or branches of these establishments may be included if their sole function is to provide leasing services.

It should be noted that the term "lease" is a legal term in the United States and carries with it certain implications. For example, revenues generated domestically by the equipment leasing service industry are totally independent of revenues generated by service "contracts." However, in other nations, these terms may be either interchangeable (all revenues generated are reported in one category or the other) or at least not mutually exclusive.

Approximately one-third of the firms covered in this study are independent leasing firms and the majority are financial firms or their subsidiaries. The increase in leasing activity over the past decade has resulted in a number of financial firms entering the leasing field and only a few new independent leasing companies.

The 6 equipment leasing and rental service industry respondents to the Commission's questionnaire (of 27 firms surveyed) represent about 43 percent of the estimated $13.4 billion in foreign revenue generated by the 60 equipment leasing and rental service firms believed to be operating internationally in 1981.

Highlights in 1981

- DOMESTIC REVENUES of the U.S. equipment leasing and rental services industry totaled $47.5 billion, 10 to 25 percent of which are energy related.

- U.S. ESTABLISHMENTS which lease or rent equipment numbered more than 32,000, approximately one third of which dealt with energy-related equipment.

- U.S. EMPLOYMENT in these establishments totaled approximately 95,000.

- FOREIGN REVENUES of U.S. firms were estimated at $13.4 billion; less than 10 percent were energy related.

- o FOREIGN ESTABLISHMENTS are operational for an estimated 60 U.S. equipment leasing and rental firms with international operations.

- o THE TRADE BALANCE of the equipment leasing services industry favored the United States by over $10 billion due to the relative insignificance of foreign leasing operations in the United States.

Industry structure

Equipment-leasing firms include major banks, finance houses, credit subsidiaries of multinational firms, and independent leasing firms. They operate in the financial arena of business and employ personnel skilled in accounting, finance, and the application of tax laws to leasing activities. Based on the 1977 Census of Service Industries and discussions with industry representatives, it is estimated that 32,000 U.S. establishments are providing leasing services both in this country and abroad.

Lessees include industrial corporations, transport companies, other service businesses, and government agencies. The common factor among these lessees is that they make lease payments at monthly, quarterly, semi- annual, or annual intervals.

The original lease contract is known as the primary term. If the value of the equipment is not amortized over the period of the primary term, it may be leased again, for a secondary term, either to the same or a different lessee. Equipment that is subject to rapidly changing technology, such as computers, is frequently leased for primary and secondary terms; the primary term is usually to a firm which requires state of the art equipment and the secondary term to a firm which either does not require or cannot afford state of the art equipment.

The value of the asset at the end of the lease is known as the residual. The cost of the lease transaction depends a great deal on whether the lessee will realize all or some of the residual value at the end of the lease. The duration of the lease, the exact amount and frequency of payments, and the treatment of the residual value of the equipment are normally stated in the lease contract. This fundamental document also delineates the relationship between lessor and lessee. There may be other documentation pertaining to the lease including sales agency letters, agency appointments, assignments, and novation agreements. The extent and scope of documentation will reflect the complexity of the lease contract.

The differences between the finance lease and the operating lease may have a major effect on accounting treatments, legal rights, the amount and frequency of payments.

Finance lease.--Under this type lease, the lessor acts simply as a financing institution. The lessor raises the capital, accepts the invoice from the equipment supplier, and pays accordingly. The lessor is the legal owner of the asset, to which he has recourse if the lessee fails to make the necessary payments. Over the primary term, the lease payments cover the full cost of the asset, plus the interest and the lessor's profit. The lessee specifies the equipment needed, orders it, inspects it, and maintains it throughout the term of the contract.

Operating lease.--The lessor purchases the equipment, and is usually responsible for the maintenance, insurance, and property taxes on it. The lessee's payment rate and term do not cover the cost of the equipment, the interest, or the profit of the lessor, so one or more secondary lease terms must be written. The lessor bears the risk of technological obsolescence of the asset.

Domestic and international revenues for the equipment leasing and rental services industry ($60.9 billion) accounted for about 7.5 percent of total U.S. service trade, valued at $837 billion in 1981 for the 14 service industries covered in this study.

Recent trends and outlook

The value of U.S. equipment leased has increased at an annual growth rate of 12 to 15 percent since 1977, and during the same period, the value of foreign equipment leased has increased at an annual growth rate of 20 to 25 percent. 1/ Industry officials attribute the higher foreign growth rate to the simple fact that it is measured from a lower base. Approximately 20 percent of all U.S. manufactured goods are leased and the major U.S. products leased internationally include aircraft, ships, and computers. 2/

The U.S. Economic Recovery Tax Act of 1981 introduced the concept of "Safe Harbor" leasing. The act allows companies to freely transfer the benefits of investment tax credit and accelerated depreciation among themselves, with little or no interference from the Internal Revenue Service, thus the term "Safe Harbor." 3/ One company preparing to enter the equipment-leasing business hopes to shelter $5 to $9 of taxable income for each $1 invested in leasing. 4/ The new tax law was written mainly to bring relief to ailing U.S. industries, therefore very little, if any, safe harbor leasing takes place outside the United States.

Increasing inflation and high-interest rates have decreased the amount of working capital available to U.S. and foreign businesses, restricting their ability to purchase equipment or expand their facilities. Leasing provides these businesses with the means to acquire necessary equipment or plant facilities with minimal capital outlay. One executive stated that leasing can usually free 10 percent of the value of a transaction for investment in business, bolstering sales efforts, or productivity improvements. 5/

1/ Derived from official statistics of the U.S. Department of Commerce, the Economic Consulting Service, p. 199, and Business Week, Mar. 23, 1981, p. 96.

2/ Information obtained in conversation with industry representatives.

3/ "The Assault on 'Safe Harbor' Leasing", Industry Week, Jun. 14, 1982, pp. 84-88.

4/ Business Week, Mar. 23, 1981, p. 96.

5/ Industry Week, Dec. 8, 1980, pp. 39-42.

It has been increasingly recognized by financial institutions throughout the world that use rather than ownership of capital equipment generates profit. 1/ That concept and the complementary development of tax incentives have been the principal factors behind the rapid growth of the leasing industry.

Leasing has become more than just a method of obtaining needed equipment. Equipment lessors have become sources of needed capital to companies caught in a capital supply imbalance. The availability of capital equipment financing through leasing in less developed countries (LDC's) has provided a new source of capital for development. Investments in leased equipment promote the shift from taxable capital to a cost and contribute to a reduction in corporate income taxes. In addition, depreciation charges, interest payments, investment credits, and special energy credits provide extra deductions for the lessor. Lessees can enjoy the use of the most advanced machinery and equipment without paying the high costs of purchase or financing. Thus, lessees enjoy a credit facility which doesn't require large up-front capital outlays and doesn't infringe on cash flow.

The flexibility of lease contracts allows lessors and lessees to reach mutually satisfactory agreements. Both enjoy advantages not available in conventional purchase or loan financing of capital equipment. The lessee can usually obtain better terms on a lease contract than through outright purchase or loan financing and, in LDC's, domestic terms are rarely better than those obtained from foreign lessors. For U.S. manufacturers, leasing services provide a potential avenue by which they can increase exports of their products. By providing flexible contracts, with little or no up-front capital, lessors can help support the domestic capital markets of foreign countries, especially LDC's, and have stimulated economic development. The combination of all these factors has set a course of continued growth for the leasing industry. The U.S. industry expects to boost capital investment and stimulate economic development throughout the world, and to play an important role in merchandise trade growth.

U.S. Service Operations in Foreign Markets

Operating structure

Whether or not a U.S. leasing firm enters the international market depends on a number of factors, the most significant of which is the amount of expertise company personnel have in international leasing matters. Foreign tax laws, registration and licensing laws, and funding requirements are complex and generally serve to deter the inexperienced. However, industry officials agree that firms with personnel knowledgeable in those areas usually have little trouble in establishing themselves in foreign markets. 2/

1/ Lawrence M. Taylor, "International Leasing," a paper presented at the International Leasing Conference, Washington, D.C., Apr. 19-21, 1982.

2/ Information obtained in conversation with industry representatives.

U.S. leasing firms operating overseas include the major commercial banks, investment houses, financial subsidiaries of multinational business corporations, and leading independent leasing firms. There are approximately 60 U.S. firms providing leasing services overseas. 1/ Based on information supplied by the six questionnaire respondents, equipment leasing firms operate through affiliates (17 percent), wholly owned subsidaries or branches (50 percent), joint ventures (33 percent), and contractual arrangements (33 percent) (table 1). 2/ The joint ventures and contractual arrangements are often between manufacturing companies and financial or leasing firms, where the strengths of the individual companies complement one another. 3/

Most leasing companies are incorporated as limited liability corporations with specific powers to engage in the lease/hire of equipment and/or to provide various forms of asset financing. They are not self-sufficient in the capital market, but are generally dependent on funds obtained from the wholesale banking and securities markets if they are independent entities, or from parent or associated banks if they are subsidiaries or affiliates of commercial banks. 4/ In addition, leasing companies that are affiliates of bank-holding companies, subsidiaries of commercial banks, or those licensed as finance companies are subject to capital adequacy tests such as minimum paid-in capital, solvency, and liquidity ratios. Leasing companies are also indirectly subject to controls on credit expansion imposed on lending institutions through market creditworthiness criteria. In some instances, consortiums are formed to share the credit risks of leasing very expensive equipment. Generally, a U.S. leasing firm will seek to form a consortium with other U.S. or foreign companies when the risk exceeds $100 million. 5/

In Europe, loose associations of member leasing companies have formed what are known as leaseclubs. Leaseclubs are designed to reduce the difficulties associated with cross-border leasing and to improve their members' access to foreign markets. A leaseclub member from one country refers business to a member in another country on a reciprocal basis, usually charging a small fee when the referral is successful. There are currently five leaseclubs with approximately 130 members which have more than $2.8 billion of equipment on lease. 6/ This represents approximately 9 percent of the total value of equipment that European leasing firms currently have on

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1/ The International Operations of U.S. Service Industries: Current Data Collection and Analysis, and information obtained in conversations with industry personnel.

2/ Because firms may operate through more than 1 structure, percentages may not add to 100.

3/ World Leasing Yearbook, Hawkins Publishers, Ltd., London, England, 1981, p. 13.

4/ "Financing Capital Formation Through Leasing: The IFC Experience," a paper presented at the International Leasing Conference, Washington, D.C., Apr. 19-21, 1982.

5/ Information obtained in conversation with industry representatives.

6/ Lawrence M. Taylor, Jr., "International Leasing," a paper presented at the International Leasing Conference, Washington, D.C., Apr. 19-21, 1982.

lease. 1/ There are six U.S.-based leasing firms which are members of the five European leaseclubs.

U.S. companies engaged in leasing activities abroad are generally involved in secondary service activities such as financial services and computer and data processing services. These secondary activities are usually complementary to the leasing service activity, providing customers with a broader range of services to meet their specific needs.

Table 1.--Operating structures of principal service activity, and revenues associated with secondary service industry activities of equipment leasing and rental service firms in foreign markets, 1981 1/

Item	Revenues 2/	Number of responses	Percent of total respondents
	1,000 U.S. dollars		
Operating structure:			
Foreign affiliate	-	1	17
Joint venture	-	2	33
Subsidiary or branch	-	3	50
Contractual arrangements	-	2	33
Secondary service activity:			
Financial services	3/	3	50
Computer and data processing service	3/	1	17
Total	1,719,087	4	67

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 6 of 27 firms surveyed; respondents represent about 43 percent of the foreign revenue of the 60 major firms believed to be operating internationally in 1981.
2/ Calculated by the staff of the U.S. International Trade Commission from receivables, billings, or revenue data provided by respondents.
3/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Scope of operations

The services offered by U.S. leasing firms operating internationally include both cross-border and domestic leasing. A cross-border lease is an arrangement where the lessor is located outside the country where the lessee

1/ Derived from figures provided in a pamphlet, Leaseclubs Leads You Around the World, Leaseclub Coordination Office, Paris, France and World Leasing Yearbook, Hawkins Publishers, Ltd., London, England, 1982, p. 19.

is located. Due to the complexity of legal, tax, and accounting problems associated with cross-border leasing, it is generally restricted to the financing of "big ticket" items, such as major items of plant or equipment, aircraft, and ships. Nevertheless, cross-border leasing has grown rapidly into an attractive source of capital equipment financing throughout the world. 1/ It is an important form of international leasing for banks, finance houses, the subsidiaries of multinational firms, and even some independent leasing firms. U.S. leasing firms reportedly have 75 percent of the world cross-border leasing market. 2/

A more important development in leasing services for U.S. firms has been the establishment of subsidiaries or partnerships in leasing companies in foreign countries. The advantages of this form of leasing activity over cross-border leasing include local control of the firms' business, access to local financial markets, and knowledge of the local leasing market and its competition. There are also disadvantages, the most significant being the long leadtime and the cost of setting up a foreign company in compliance with foreign rules and regulations.

Growth trends and U.S. investment

The six respondents to the Commission's questionnaire show investment in the physical assets of foreign operations grew an estimated 12 percent from $6.8 billion in 1980 to $7.6 billion in 1981, and the number of foreign establishments increased 19 percent from 32 in 1980 to 38 in 1981 (table 2). 3/ This growth is not restricted to U.S. leasing firms, but affects foreign firms as well. It reflects growth in both established leasing markets, such as aircraft and ships, and in new markets, such as energy production equipment and industrial plants and machinery.

Leasing has already penetrated certain markets to a high degree. 4/ Those markets include materials handling systems, machine tools, computer and data processing markets, and energy-related industries where capital requirements are high, such as oil and gas exploration and drilling equipment. It is estimated that U.S. businesses acquired about 20 percent of their equipment by lease in 1980, compared with 13 percent in 1975 and 10 percent in 1970. 5/ Industry sources estimate that 20 percent of total U.S. leasing operations are

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1/ Lawrence M. Taylor, Jr., "International Leasing," A paper presented at the International Leasing Conference, Washington, D.C., Apr. 19-21, 1982.

2/ Information obtained in conversation with industry personnel, June 25, 1982.

3/ Although the numbers in table 2 represent only 6 firms' reponses to the Commission's questionnaire, this percentage growth in the number of foreign establishments of U.S. leasing firms is reported by industry representatives to be an indication of the trend throughout the industry.

4/ Industry Week, Dec. 8, 1980, p. 39.

5/ Ibid.

Table 2.--Indicators of activity in the foreign and domestic operations of equipment leasing and rental service firms, 1980-82

Item	Foreign	Domestic	Total
Estimated value of receivables, billings, or revenues: 1/ 2/			
1980------------------1,000 dollars--:	6,232,990	7,242,044	13,475,034
1981----------------------------do----:	5,761,758	8,974,430	14,736,188
1982----------------------------do----:	3/	3/	3/
Estimate of investment in physical assets 1/ 4/ in foreign operations:			
1980------------------1,000 dollars--:	6,825,220	-	-
1981----------------------------do----:	7,636,118	-	-
1982----------------------------do----:	3/	-	-
Number of establishments: 1/			
1980-----------------------------------:	32	50	82
1981-----------------------------------:	38	52	90
1982-----------------------------------:	46	56	102
Estimated 5/ value of total industry receivables, billings, or revenues:			
1980------------------1,000 dollars--:	10,500,000	37,200,000	47,700,000
1981----------------------------do----:	13,400,000	47,500,000	60,900,000
1982----------------------------do----:	17,100,000	60,700,000	77,800,000

1/ The data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 6 of 27 firms surveyed; respondents represent about 43 percent of the foreign revenue of the 60 major firms believed to be operating internationally in 1981.

2/ Excluding the value of any merchandise exports.

3/ Data submitted by respondents are not comparable and, therefore, have been deleted.

4/ Including the undepreciated book value of land, plant, and equipment.

5/ By the staff of the U.S. International Trade Commission based on discussions with industry and/or association representatives, and secondary sources.

Source: Compiled from data submitted in response to questionnaries of the U.S. International Trade Commission.

conducted overseas. 1/ The overall growth in foreign revenue generated by the equipment leasing and rental service industry is expected to be substantial. In 1981, foreign revenue for this sector is estimated to have increased about 28 percent from 1980, to $13.4 billion, accounting for about 12 percent of total service sector foreign revenue of $109.6 billion estimated for the 14 selected industries covered in the Commission's study (table 3).

Table 3.--Estimated total foreign revenue generated by the equipment leasing and rental service industry and estimated total foreign revenue for selected service industries, 1980-82

Year	Total foreign revenue for service industry 1/ (1)	Total foreign revenue for selected service industries 2/ (2)	Ratio of (1) to (2)
	1,000 U.S. dollars		Percent
1980	10,500,000	89,298,000	12
1981	13,400,000	109,611,000	12
1982	17,100,000	135,744,000	13

1/ Estimated based on discussion with industry and/or association representatives and secondary sources.
2/ Based on totaling Commission-estimated foreign revenue for each of the 14 selected industries covered in the study.

Source: Estimated by the staff of the U.S. International Trade Commission.

Because of favorable tax laws in many countries, including the United States, the lack of hard currency and ready capital in most less developed countries, and a general acceptance of leasing as a more financially advantageous business practice, the upward trend in international leasing is likely to continue. As the lesser developed countries establish their primary and secondary industries, the industry expects a great demand for new and used equipment. In addition, because the rate of equipment obsolescence is increasing, especially for high-technology products, more businesses, U.S. and foreign, will lease rather than buy equipment. U.S. leasing firms are active in many of these countries and are suitably positioned to take advantage of this increase in leasing activity.

The U.S. Economic Recovery Tax Act of 1981 has served as an impetus for companies which normally shunned leasing to embrace its use, and for companies which normally used leasing to increase their activity. The act made it possible for lessees to reduce their total payments by selling off unusable tax benefits, for lessors to reduce their tax bill by buying cutrate tax

1/ Information obtained in conversation with industry representatives.

benefits, and for the company that puts up the cash to get a higher rate of interest. Approximately 85 percent of the $18.2 billion of equipment acquired in 1981 under this new rule involved straight tax benefit transfers. 1/

Regional and country activity

The majority of respondents to the Commission's questionnaire conduct their foreign leasing activities in Europe, Canada, Mexico, the Far East, and Latin America (table 4). The countries of highest activity among respondents were the United Kingdom, Italy, Mexico, Canada, Brazil, and the Republic of Korea. Although Europe appears to be the most active market for U.S. leasing firms, a high percentage of respondents who conducted activities in Brazil (50 percent), Canada (50 percent), and Mexico (67 percent) in 1981 indicates a strong U.S. presence in these countries as well.

Discussions with industry representatives indicate that U.S. firms dominate the Latin American leasing market. The major reason is there are very few national leasing companies in Latin America. Also, when the leasing industry began to grow in the United States in the 1950's and 1960's, U.S. leasing firms provided their services to U.S. exporters of merchandise to Latin America. These services were beneficial to Latin American countries, which did not have the necessary capital to buy U.S.-made equipment. Thus, U.S. leasing firms virtually established the leasing industry in Latin America. For these reasons, there is very little competition in Latin America from Europe and other countries.

In other less developed countries U.S. lessors are experiencing competition from European and Asian leasing firms. The Japanese leasing industry is the most successful in Asia due primarily to the low rates they use to finance leasing activities. According to industry sources, Japanese rates are too low for other countries' leasing firms to compete.

There are few foreign leasing firms that are competitive in the United States since U.S. firms, having established the industry early in the 1950's, have a firm hold on the U.S. market. In addition, there is very little funding available to foreign leasing firms in the United States.

Trade in Merchandise Generated by Trade in Services

Accurate forecasts concerning current and future trends regarding the use of merchandise associated with international leasing operations are not available because no agency, organization, or publication reports comprehensive data on leasing operations. Estimates have been made which show that the total worldwide value of leased equipment doubled during 1975-80, and will probably continue to increase during the next 5 years, although at a slower rate. In an effort to gain further insight into the direct or indirect nature of merchandise trade generated by the equipment leasing service sector, several questions were posed in the Commission's questionnaire.

1/ Industry Week, June 14, 1982, p. 84.

Table 4.--Regions and countries in which revenue is generated by equipment leasing and rental service firms, 1980-82 1/

Region and country 2/	Number of responses			Percent of total respondents			Estimated revenue		
	1980	1981	1982	1980	1981	1982	1980	1981	1982
							1,000 U.S. dollars		
Middle East	1	2	0	17	33	0	3/	3/	
Iran	-	1	-						
Israel	-	1	-						
Pakistan	-	2	-						
Far East	4	4	3	67	67	50	832,947	849,428	3/
Australia	-	1	-						
China	-	2	-						
India	-	1	-						
Indonesia	-	1	-						
Japan	-	2	-						
Republic of Korea	-	3	-						
Philippines	-	1	-						
Latin America	3	3	3	50	50	50	3/	3/	3/
Argentina	-	2	-						
Brazil	-	3	-						
Chile	-	2	-						
Venezuela	-	2	-						
Europe	6	6	5	100	100	83	3,863,869	3,258,651	4/
Belgium	-	1	-						
West Germany	-	2	-						
France	-	2	-						
Italy	-	3	-						
Netherlands	-	1	-						
Spain	-	1	-						
United Kingdom	-	4	-						
Africa	1	1	1	17	17	17	3/	3/	3/
South Africa	-	1	-						
Canada	4	3	3	67	50	50	376,314	3/	3/
Mexico	5	5	4	83	67	67	85,972	90,853	4/
Other	3	3	3	50	50	50	3/	3/	3/

1/ Country listing is for 1981 only.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 6 of 27 firms surveyed; respondents represent about 43 percent of the foreign revenue of the 60 major firms believed to be operating internationally in 1981.

3/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.

4/ Data submitted by respondents are not comparable and, therefore, have been deleted.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

The number of positive responses to a series of questions asked to determine whether or not U.S. merchandise exports are generated by U.S. equipment leasing and rental service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
Do you believe that foreign merchandise might be used as a result of the services your firm provides abroad?----------------------------	4	67
Is U.S. merchandise specified or recommended in the course of providing your service?-------------	2	33
Are U.S. merchandise exports believed to be directly generated?-----------	3	50

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 6 of 27 firms surveyed; respondents represent about 43 percent of the foreign revenue of the 60 major firms believed to be operating internationally in 1981.

The majority of respondents do not specify or recommend the manufacturer of the equipment that is leased; it is generally the lessee who makes the decision concerning the origin of the equipment he intends to use. However, half the respondents believe U.S. merchandise exports are directly generated by their international leasing activities.

Because of the low response rate to the merchandise trade section of the questionnaire, the Commission is unable to extrapolate with certainty the value of U.S. merchandise exports directly generated by U.S. equipment leasing and rental service activities abroad. However, these industry respondents estimated that their service activities overseas resulted in the total U.S. export of approximately $57 million in goods in 1980 (table 5). On the basis of this estimate, the number of respondents, and the number of known firms in the industry, it is estimated that $851 million in U.S. merchandise exports flowed as a result of U.S. international equipment leasing and rental activities in 1980. However, it should be noted that at a confidence level of 95 percent this figure could be as low as the actual respondent's estimate of $57 million or as high as $2.6 billion. Respondents did not provide estimates of U.S. merchandise exports for 1981 and 1982 (table 5).

Table 5.--U.S. merchandise exports generated by U.S. equipment leasing and rental services abroad, 1980-82 1/

Year	Number of responses	Exports of U.S. merchandise estimated by respondents	Projected 2/ total: U.S. merchandise for the service industry	± 95 percent confidence limit for projected industry exports
		1,000 U.S. dollars		
1980	1	56,732	851,000	2,617,000
1981	-	-	-	-
1982	-	-	-	-

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 6 of 27 firms surveyed; respondents represent about 43 percent of the foreign revenue of the 60 major firms believed to be operating internationally in 1981.
2/ By the U.S. International Trade Commission.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

The primary commodities exported by U.S. companies for international leasing operations are motor vehicles, trailers and containers used for the transport of cargo, machinery and industrial equipment, business machines, ocean-going vessels, aircraft, railway rolling stock and locomotives, and medical equipment. 1/ U.S.-produced equipment is normally leased because the terms of the lease are more beneficial to the lessee, or the equipment leased is not readily available from any other source. The following tabulation depicts the general types of U.S. equipment leased worldwide in 1978 and 1979 and the percentage distribution of each to the total: 2/

Product	1978 (percent)	1979 (percent)
Motor vehicles	33	35
Machinery and industrial equipment	35	33
Business machines	20	19
Ships, aircraft, railway equipment	6	6
All other	6	7
Total	100	100

Most leased motor vehicles involve trucks or truck tractors and semi-trailers. It is common practice that cargo containers be used as truck trailers; the container is loaded onto an oceangoing vessel, and unloaded at the port onto a frame with wheels which can be pulled by truck tractor.

1/ World Leasing Yearbook, Hawkins Publishers, Ltd., London, England, 1981.
2/ Ibid, p. 15.

Virtually all international automobile leasing is through franchising contracts, rather than leasing operations, and such contracts are covered under the franchising services sector of this study. Of the remaining types of transportation equipment leased by U.S. firms to foreign firms or countries, aircraft leasing, which began in the 1970's, 1/ accounts for approximately 75 percent of the international leasing revenues. The domestic industry has only recently begun the international leasing of railway rolling stock (mostly to Canada) and only a very few oceangoing vessels have been leased to non-U.S. firms. 2/

The total value of equipment on lease worldwide (excluding automobiles and real estate) was estimated to be between $200 and $250 billion in 1981, 3/ whereas the total value of equipment on lease by U.S. firms in 1981 was estimated to be about about $46 billion. 4/ The value of equipment leased internationally and in the United States has doubled since 1975 and will probably increase by about 33 percent by 1985. 5/

Host countries where U.S. equipment leasing services are active also stand to benefit from the presence of U.S. services firms. The number of positive responses to a series of questions asked to determine whether or not host-country or third-country merchandise shipments 6/ are generated by U.S. equipment leasing and rental service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
Do you believe that foreign merchandise might be used as a result of the services your firm provides abroad?----------------------------	4	67
Are foreign or host-country products specified or recommended in the course of providing your service?----------	2	33

1/ The total number of questionnaire respondents in this service industry was 6 of 27 firms surveyed; respondents represent about 43 percent of the foreign revenue of the 60 major firms believed to be operating internationally in 1981.

1/ World Leasing Yearbook, Hawkins Publishers, Ltd., London, England, 1981, p. 272.

2/ Ibid, p. 267.

3/ World Construction, January, 1982, p. 34.

4/ Estimated by the staff of the U.S. International Trade Commission, based on figures provided in World Construction, January 1982, p. 34, and conversations with industry representatives.

5/ Industry Week, Sept. 3, 1979, p. 95.

6/ "Host-country merchandise shipments" refers to the shipments (within the host country) of host-country-manufactured products which are generated by U.S. service operations in the host-country market. "Third-country merchandise shipments" refers to the shipments of other foreign-manufactured products to a foreign market as a result of U.S. service operations in that market.

Third-country and host-country merchandise shipments resulting from U.S. equipment leasing and rental services abroad in 1981 were estimated by one firm as follows:

Item	Value (1,000 U.S. dollars)
Third country shipments----------------	0
Host-country shipments----------------	120,000

Significant examples, cited by industry sources, where the entry of U.S. services into foreign markets has benefited the economy of the host country or a third country include $120 million in dry cargo containers provided by host countries for U.S. leasing operations.

U.S. leasing companies serve not only foreign companies seeking U.S.-made equipment or alternate forms of financing, but also serve large U.S. multinational firms abroad. As leasing grows, trade in U.S.-made products is likely to grow. For example, there is little doubt that more aircraft will be leased in the future because of the heavy demand to replace current fuel-inefficient aircraft with more modern, fuel-efficient models. 1/ It is estimated that 6,100 new passenger jets will be needed by 1994, since many foreign carriers will be expanding their fleets, and will probably lease the new generation aircraft. The U.S. portion of the total value of these aircraft is estimated at $68.3 billion. 2/ This growth also applies to other types of equipment requiring large capital outlays, such as computer systems, oceangoing vessels, and oil rigs. The leasing of less expensive equipment, such as trucks, containers, and small business machines, will also show an increase because of capital restrictions and lessors specializing in a specific area instead of broad areas of equipment leasing. 3/ Auto leasing and rental is expected to grow 16 to 17 percent annually, with an estimated 40 percent of U.S. annual passenger car output on lease or rent by 1990. 4/

International Service Trade Barriers

Responses to the trade barriers section of the equipment leasing services questionnaire provided very little information regarding the U.S. industry's perception of trade barriers that affect their foreign business. Indicative of the type of nontariff measures which most concern at least one industry respondent is the listing in table 6.

Similarily, discussion with industry personnel revealed no specific barriers to trade imposed by foreign governments, but indicated that U.S. personnel's lack of expertise in foreign leasing matters was the major factor

1/ World Leasing Yearbook, 1981, p. 272.
2/ Ibid, p. 22.
3/ Ibid, p. 276.
4/ Ibid, p. 70.

Table 6.--Trade barriers to international services in the equipment leasing and rental industry 1/

Category and barrier	Number of responses	Percent of total respondents
Right of establishment	1	17
Credit, investment, or financial activity restrictions	1	
Administrative/ownership restrictions	1	
Entry of service personnel and specialized tools	1	
Restrictive government/business regulations	1	
Special deposit requirement for foreign companies	1	
Trade in goods	1	17
Local purchase requirements	1	
Restricting entry of equipment or supply	1	
Trade in services	1	17
Other (withholding taxes)	1	
Technical issues	1	17
Governmental paper requirement for importing	1	
Foreign exchange controls	1	17
Restrictions on remittances	1	
Convertibility limitations	1	

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 6 of 27 firms surveyed; respondents represent about 43 percent of the foreign revenue of the 60 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

limiting U.S. leasing activity in foreign countries. Some impediments to trade in international leasing services that vary from country to country are: (1) whether or not a country has statutory provisions for leasing services (no such provisions exist in Denmark, Hong Kong, Ireland, Italy, the Netherlands, Switzerland, or Sweden 1/); (2) funding and currency exchange regulations; (3) whether or not there are licensing and registration requirements; (4) tax laws applicable to leasing transactions; (5) capital structure, ownership, and financial management requirements; (6) restrictions regarding access to imported equipment, foreign personnel, or to producer services sourced outside the importing country; and (7) restrictions on marketing techniques. U.S. industry representatives who have been successful in conducting leasing transactions abroad indicated a need for U.S. lessors to conduct more market research to better acquaint themselves with foreign markets and operating practices.

1/ "Financing Capital Formation Through Leasing: The IFC Experience," and "Legal Aspects of International Leasing," presented at the International Leasing Conference, Washington, D. C., Apr. 19-21, 1982.

Other factors addressed by industry representatives that hinder U.S. leasing activity abroad are the need for the U.S. Export-Import Bank to develop a program specifically dealing with lease financing and for the Overseas Private Investment Corporation (OPIC) to develop a better understanding of the problems encountered by U.S. leasing firms in foreign markets.

Specifically, Eximbank needs to provide export financing to small- and medium-sized businesses as an incentive to stimulate exports of merchandise that can be leased. Also, there is currently no effective domestic insurance program to cover export credit risk. U.S. banks currently have credit risk allocations on a country-by-country basis. If the cost of a lease contract exceeds the risk allocation, the bank cannot finance the deal. OPIC is currently in the process of developing a lease insurance program, which is expected to be operative by the beginning of the next fiscal year.

Although the United States has tax treaties with some countries (Belgium, France, Germany, Canada, the Netherlands, Switzerland, and the United Kingdom, to name a few), each country's treaty is different. Some treaties are based on the Organization for Economic Cooperation and Development (OECD) model and treat lease payments as royalties subject to withholding taxes; other treaties provide for zero withholding on lease payments. Industry representatives have stated that there is a need for a model tax treaty provision applicable to all international leasing activity. Similarly, the 10-percent investment tax credit (ITC) is limited to domestic assets. Industry personnel would like to see the ITC expanded to include equipment and other assets in foreign countries. Tax incentives generally do not exist in most foreign markets, the exception being LDC's where up to 100 percent of the tax liability can be written off when a wholly or partially owned subsidiary is setup by a U.S. firm. LDC's use this incentive as a means to attract foreign firms which, in turn, provide the LDC with an inflow of capital equipment.

Conditions of Competition in Current and Potential Service Markets

U.S. leasing firms are competitive in all aspects of both domestic and foreign operations. Because of high-interest rates and a general lack of funding, there are very few foreign leasing firms operating in the United States. 1/ However, the United Kingdom, France, and Japan all have leasing firms which effectively compete with U.S. leasing firms in the international markets. 1/ The primary foreign markets for U.S. leasing firms are the United Kingdom, Germany, and France. Other areas of rapid growth are Central and South America and the Far East. 1/

Industry spokesman have indicated that in certain product areas, such as computers, aircraft, and energy-related products, the United States enjoys a technological advantage that ensures its competitiveness in international markets. Energy-related products include those for drilling, completion, and

1/ Information obtained in conversation with industry representatives.

production of oil and gas wells, both onshore and offshore. Leasing services include rental of equipment for well cementing, production simulation, well testing, and well perforating. Other equipment includes gas compression equipment, barges, offshore mobile-drilling rigs for exploratory drilling, and platform rigs for development drilling. Competition for international contracts is generally based upon personnel competence, equipment suitability, availability, and comparative day rates and mobilization fees for the equipment. Most contracts are won or lost on the basis of technical capability and availability, two aspects in which U.S.-based firms are competitive.

According to industry sources, the competitive disadvantages of U.S. firms relate to host-nations' requirements for varying degrees of domestic participation in leasing projects. Specific regulations include personnel requirements regarding mandatory hiring of domestic professionals and the licensing of foreign professionals. Other competitive disadvantages cited include discriminatory taxation, foreign exchange restrictions, capital requirements, and foreign government procedures which favor domestic firms. The specific nature of these barriers and their effect on the equipment leasing industry are discussed in a later segment of this report.

Because of the rapid growth in leasing services, the field remains open to new investors. In times of high inflation and economic uncertainty, leasing remains an attractive alternative to outright purchase or a direct loan to finance the purchase of equipment. Gas and oil companies, transport companies, industrial corporations, and other service industries are constantly demanding equipment to meet their needs. 1/

Respondents to the leasing services questionnaire indicated that Mexico was the major source of revenue in 1981. The amount of revenue generated by U.S. firms in the Mexican market and the number of competing firms indicate that Mexico is a large market for leasing activity. Most of the competing firms are national; compared with the United Kingdom where most competition comes from worldwide firms, and Japan where all competition comes from worldwide firms (table 7). The table also shows that, among questionnaire respondents, U.S. firms compete actively with each other in the United Kingdom, Canada, and West Germany. U.S. leasing firms attributed their success in the Mexican market to financial strength (table 8). In fact, respondents indicated financial strength to be an ingredient of success in every market except Argentina, where market experience and superior quality associated with U.S. products were the chief reasons for the U.S. leasing firms' success. Likewise, financial strength, market experience, and superior quality were named as competitive strengths of U.S. leasing firms in potential foreign markets (table 9). Although technology and price were not mentioned by questionnaire respondents as playing a role in the success of U.S. leasing firms in existing or potential foreign markets, it is known from industry discussions that the United States must maintain a technological lead in certain equipment areas in order to compete in international leasing markets.

1/ Industry Week, "Equipment Leasing: A Recession Option," Sept. 3, 1979, pp. 94-95.

Table 7.— Number of firms competing 1/ with U.S. equipment leasing and rental service firms abroad, by principal service markets 2/ in order of revenue generated, 1981 3/

Service market	Number of competing firms				
	Total	National	Regional	World-wide	Other U.S. firms
Mexico	25	15		10	
Spain					
Argentina	8			8	
United Kingdom	39	4	6	17	12
Japan	14			14	
Canada	20	4		4	12
West Germany	20	4		4	12

1/ Based on 3 responses by questionnaire respondents.

2/ Other principal service markets for the industry may not be listed here if respondents did not identify the number of competing firms.

3/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 6 of 27 firms surveyed; respondents represent about 43 percent of the foreign revenue of the 60 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 8.--Likely reasons 1/ for the competitive strength of U.S. equipment leasing and rental service firms in foreign service markets 2/

Service market	Lower price	Technology lead	Financial strength	Experience in the market or service	Superior quality association
Far East:					
Japan		1	1		
Europe:					
West Germany			1		
United Kingdom			1		1
North America and Mexico:					
Mexico			1		1
Latin America:					
Argentina				1	
Total		1	4	1	2

1/ The importance of each reason is indicated by the number of times each was designed, based on 3 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 6 of 27 firms surveyed; respondents represent about 43 percent of the foreign revenue of the 60 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 9.--U.S. equipment leasing and rental service firms' competitive strengths 1/ in potential foreign markets 2/

Potential service market	Lower price	Technology lead	Financial strength	Greater experience	Superior quality
Far East:					
Australia			1		
Peoples' Republic of China			1	1	1
Japan			1		
Europe:					
Greece			1	1	1
France			1		
Africa:					
Nigeria			1	1	1
Total			6	3	3

1/ The importance of each reason is indicated by the number of times each was designated, based on 1 response.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service was 6 of 27 firms surveyed; respondents represent about 43 percent of the foreign revenue of the 60 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

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Financial Services

Executive Summary

1. International revenues for U.S. commercial bank operations were approximately $56.4 billion in 1981; international revenues generated by investment firms cannot be broken out of domestic revenue estimates.

2. Exports are both indirectly and directly associated with U.S. financial activities abroad. By far the largest portion of trade in goods is generated indirectly by international banking activities such as trade financing. Trade in goods directly related to international financial activities is primarily limited to telecommunication, computer, and data processing equipment. Industry respondents to the Commission's questionnaire estimated that their service activities overseas resulted in the total U.S. export of approximately $564 million in goods in 1981.

3. Approximately half of the questionnaire respondents indicated that host- or third-country merchandise shipments might be generated as a result of U.S. financial service activities abroad; however, the estimated value of such shipments was negligible.

4. Trade barriers, such as foreign-exchange controls and limitations on the establishment of foreign-based banks in certain countries, were most frequently indicated by questionnaire respondents. Governments regulate banks in order to control the financial flows of local and foreign currency for monetary policy reasons, therefore these barriers are not expected to be altered except when economic situations demand a change.

5. Approximately 60 percent of the respondents indicated that their service activities would increase abroad as a result of eliminating existing international barriers. Most firms indicated a reduction in barriers would result in increased revenues from the Far East and Latin America. Twenty percent was the mode for these two regions. As for merchandise exports, respondents were equally divided between those indicating an increase and those indicating no effect on U.S. merchandise exports related to an elimination of barriers to services trade.

6. U.S. financial service firms operating abroad are experiencing competition with the greatest number of competing firms in the United Kingdom, Japan, and Brazil.

7. Generally, questionnaire respondents cited experience in the market or service area as the primary reason for the success of foreign firms competing in the international financial services market. This was followed by lower prices, political or regional bias, and government support.

8. Experience in the market or service area was cited most often by respondents as a likely reason for the success of U.S. financial service firms in foreign service markets.

Industry Profile

Definition and coverage

Those financial services provided by the banking industry include many forms relating to money, its use and distribution, as well as other fiduciary activities. The banking industry is composed of commercial banks (Standard Industrial Classification (SIC) 60), investment banks (SIC 62), and official banks or facilities (e.g., central banks, development banks, and organizations such as the Agency for International Development and the Export/Import Bank). The official banks (e.g., central banks) are political in nature, and this study will exclude them except to mention their role and effect on the international financial market.

Commercial banks, whether nationally or State chartered, are establishments which perform intermediation, i.e., the bringing together of borrowers and lenders for a fee. Such banks accept deposits and make loans. Investment bankers, on the other hand, deal in the issuance of securities (stocks and bonds) and act as underwriters (buyers of issues for distribution in primary or secondary markets).

The 17 financial service industry respondents to the Commission's questionnaire (out of the 42 surveyed) represent about 19 percent of the foreign revenues of the 205 financial service firms believed to be operating internationally in 1981. Most of the 17 respondents belong to the commercial banking sector.

Highlights in 1981

- DOMESTIC REVENUE generated by the U.S. commercial banking industry was estimated to be $192.4 billion. Investment firms revenue for the same year was approximately $19.8 billion.
- U.S. ESTABLISHMENTS of federally insured banks numbered 14,416, and investment firms numbered 390 (New York Stock Exchange operations) with 4,170 sales offices operating domestically.
- U.S. EMPLOYMENT averaged over 1.5 million persons in U.S.-based commercial banks and 51,603 representatives in investment firms.
- INTERNATIONAL REVENUE for U.S. commercial bank operations was approximately $56.4 billion, and the international revenue generated by investment firms is included in the $19.8 billion domestic revenue figure which cannot be broken out.
- FOREIGN ESTABLISHMENTS of U.S. commercial banks numbered 1,127, and U.S. investment firm dealers located overseas were estimated to be 247.
- FOREIGN EMPLOYMENT figures for U.S. commercial banks are included in the domestic employment figure and cannot be broken out. U.S. investment firms' representatives overseas numbered 1,996.

- o U.S. TRADE BALANCE for U.S. commercial banks located in the United States was $3.9 billion in surplus; composed of claims on foreign parties (such as loans and bankers acceptances) by U.S. banks (excluding their foreign branches and subsidiaries) of $250.1 billion and foreign liabilities (such as U.S. deposits by foreigners and interbank loans to U.S. banks), of U.S.-based banks which were $246.2 billion.

Industry structure

U.S. institutional structure.--Within the United States, four types of depositing institutions exist--commercial banks, savings and loans associations, mutual savings banks, and credit unions. The relative importance of each is indicated as follows: 1/

Type of institution 1/	Percent of total assets	
	1969	1977
Commercial banks:		
Domestic offices	65.6	57.4
Overseas offices	3.3	10.1
Savings and loans associations	20.0	22.6
Mutual savings banks	9.1	7.3
Federal credit unions	1.9	2.7
Total	100	100
Total assets----(billion dollars)	810.8	2,031.7

1/ Only federally insured institutions are included; however, they accounted for over 90 percent of total assets.

Two points are worth noting. First, total assets have grown since 1969, and second, overseas operations have become more important in commercial banking activities.

Beside the fact that commercial banks, savings and loans associations, mutual savings banks (as of 1978), and credit unions are federally or State chartered, their deposits are subject to regulation and examination by various Federal agencies--the Federal Deposit Insurance Corporation (FDIC), the Federal Savings and Loan Insurance Corporation, and the National Credit Union Administration--as well as State authorities. Regulation of these institutions are carried out through instruments of monetary policy such as

1/ Costs and Margins in Banking: an international survey, Organization for Economic Co-operation and Development, Paris, France, 1980, p. 295.

reserve requirements, discount window 1/ availability and rates, and restrictions on open market activities. 2/

Because savings and loans associations, mutual savings banks, and credit unions basically operate within the United States, discussion of depository institutions will be limited to commercial banks throughout the remainder of this study.

International institutional structure.--Because of the number of services offered, geographical location, and regulations, international banks vary in organizational structure and physical presence (i.e., buildings, employees). The structure of the banks may be based on product line (such as, consumer loans, credit card operations, and leasing), geographical activity or a combination of the two. Physical presence ranges from representative offices, which act as analysts and coordinators of deals, to subsidiaries or branches performing full-service banking activities. The major types of operating structure identified in the Commission's questionnaire are discussed in the section on "U.S. Service Operations in Foreign Markets."

The services offered by international banks are diverse. Typical services include issuing letters of credit and accepting medium- to long-term loans, interbanks loans, finance leasing, financial analysis, and issuance of securities.

Domestic and international revenue for the financial service industry ($269 billion) accounted for 32 percent of total service trade, valued at $837 billion in 1981 for the 14 service sectors covered in this study.

U.S. banking operations abroad.--The number of federally insured U.S. commercial banks was 14,435 in 1980 (14,416 in 1981). About 180 of these U.S. commercial banks were operating overseas with at least one branch or subsidiary; foreign branches totaled 800. Total assets of U.S. overseas branches and subsidiaries were approximately $366.4 billion in 1980; branches accounted for about 85 percent of this total, according to the Federal Reserve Board. 3/ The number of U.S. commercial bank foreign subsidiaries in 1980 totaled 943; however, more than 80 percent of the value of total foreign assets, $55.9 billion, was accounted for by the top 100 subsidiaries located abroad. In fact, the majority of U.S. international activity can be attributed to a relatively small number of banks.

1/ The discount window is a means by which the Federal bank can control the flow of money into the economy. The various member banks of the Federal Reserve System can go to the "Fed Window" and borrow at a given rate of interest. Limitations on the amount available to each bank and the cost of borrowing, i.e., the interest rate charged, can be adjusted in order to stimulate or subdue borrowing.

2/ Costs and Margins in Banking: an international survey, Organization for Economic Co-operation and Development, Paris, France, 1980, p. 298.

3/ Includes only branches of banks which are members of the Federal Reserve System with assets of more than $1 million (estimated to represent around 95 percent of all foreign branches of U.S. commerical banks).

Foreign banking operations in the U.S. market.--The U.S. Department of Commerce placed the number of offices--branches, subsidiaries, representative offices and agencies--of foreign banks operating in the United States at about 350 in 1980. Concentration was in the traditional money centers--New York (around 200 establishments were located here), Chicago, and San Francisco, though some expansion into other cities has occurred. Assets of all foreign banks in the United States totaled more than $140 billion in 1980.

Aquisition has been the major convenient and inexpensive entrance method into the U.S. market. In fact, interstate aquisition and branching capabilities, as well as aggressive pricing in loan bids were cited by the U.S. Department of Commerce as the principal reasons for foreign banks' successful operations in the United States.

Recent trends and outlook

The year 1980 was a year of strong growth in the international financial markets. Even in an environment of high and volatile interest rates on U.S. dollar transactions, unsettled exchange rates, and pronounced economic and political uncertainties, the international banking sector continued to be a major source of credit and principal outlet for the oil-producing-exporting countries (OPEC) surplus to be recycled. Conditions for lending were said to have remained very easy; there was no shortage of funds nor general slowdown in international market growth in 1980. 1/

Clients in the international finance market have become extremely sensitive to liquidity and interest rate variations. As a result of market fluctuations, customers are requiring faster means of communication and data processing, coupled with a demand for their banks to offer an ever-increasing number of services.

International banks, confronted with the recycling of OPEC oil money to governments to fund balance-of-payments problems and large development loans, have increased consortium and syndicated loan participation. Such arrangements enable the banks to enter or remain in markets that would otherwise be closed by reducing costs to customers, diversifying risk and allowing participation in loans that any one bank would be unable to make.

Inflation has increased the need for banking services, as businesses require more working capital and become less able to finance equipment replacement and/or plant expansion. Industry sources indicate that, because of their experience and established connections in the various markets, U.S. banks should be able to continue to compete effectively for a share in such increases in lending.

According to World Bank and International Monetary Fund sources, reduced ability of official facilities to recycle "oil money" and/or to finance medium- to long-term needs may force commercial and investment banks to increase their international activities. Official banks or agencies will

1/ Bank for International Settlements' 1981 annual report.

probably perform the analytical analysis for development and project loans, as private syndicates pool funds for the loans. Thus, an increase in forms of cobanking (such as commercial and development banks or commercial banks and the World Bank) is likely to take place in the near future.

Communication and data processing speed are likely to be the determining factors in a bank's position in the future international market. With video machine attachments to home telephone systems or computers, banks could gain market share without actual physical presence, which would help reduce the cost of funds. "Self-service" may be the key word in banking of the eighties. Today, U.S. banks are perhaps the most innovative banks in the world using the latest technology and willing, in many cases, to change the traditional role of banks 1/. Industry spokesmen believe that the combination of the availability of the most current technology and the disposition of U.S. bankers to accept and implement change should enable the U.S. banks to play an even greater part in the international financial markets in the years to come.

U.S. Service Operations in Foreign Markets

Operating structure

The international financial market is divided into three categories based primarily on maturity. The shortest time-frame market (6 months to 1 year) is known as the Eurocurrency market, followed by a medium-term market (2 to 8 years) called the Eurocredit market, and lastly the long-term Eurobond market (8 to 50 years). Commercial banks tend to operate in the Eurocurrency and Eurocredit markets, while investment banks are generally more active in the Eurobond and foreign bond markets.

There are five distinct forms of international lending: "1) import/export financing, 2) loans to corporations and/or their foreign branches, subsidiaries, or affiliates with parent guarantee or other form of support, 3) loans to foreign local companies, partnerships and individuals including, for example, foreign entities of U.S. corporations that borrow on their own without any form of support from the parent, 4) loans or placements to foreign banks or to overseas branches of U.S. banks, and 5) loans to governments or to governmental entities." 2/

Net profit of foreign branches of U.S. banks was estimated at $2.4 billion in 1981, up from $2.0 billion in 1980. 3/ There have been constant increases in income generated from operations of noninterest fiduciary activities such as management fees, participant fees, and fees associated with the issuance of traveler's or cashier's checks. This increase in fiduciary activity income illustrates the growing importance of fiduciary activities to

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1/ "Hammers of change: Banking's Response to the New Environment," Economic Review, September 1981, pp. 34-36.

2/ John F. Mathis, Offshore Lending by U.S. Commerical Banks, Banker's Association for Foreign Trade and Robert Morris Associates, November 1978, p. 10.

3/ Comptroller of the Currency.

the international banking community. U.S. banks probably lead activities in this area due to their lead positions in syndicated loans and creative management style.

In international operations, the U.S. banking industry has traditionally operated in five distinct forms: correspondent, representative, agency, branch, and subsidiary. In addition to these traditional forms of international banking, consortiums and syndicates have developed out of the need to create sources of funds for medium- to long-term lending.

The first form, correspondent banking, is used primarily for trade financing by banks with limited market activity. No physical presence is required, since banking activities are carried out through a foreign bank in a particular foreign market, in return for the U.S. bank's performance of foreign banking needs in the United States or in another country where that bank is not active.

The second, the representative office, requires limited physical presence in the market. Representative offices are small, operate with few people and have low overhead operating costs. Basically, the representative office acts as a liaison between U.S. firms wanting to enter the foreign market and the foreign private or public sectors interested in obtaining the U.S. product or service. No deposits are accepted nor loans made by representative offices; their main function is to develop loans in which their parent bank could participate.

The third, an agency, is closely related to a representative office, performing virtually the same function. However, an agency may or may not be considered part of the bank which it represents. The primary difference between a representative office and an agency is that the agency is allowed to accept deposits for the bank.

The fourth, a branch, requires physical presence in the market; therefore, much greater costs are associated with it than with the previous forms. A foreign branch is an office located in the market and considered to be part of the parent bank. Branches provide all banking services allowed by the host country, and a branch can accept deposits and make loans.

Lastly, the subsidiary, a separate entity from the parent bank, is set up as an Edge Act or Agreement corporation under the U.S. International Banking Act of 1978. This form of foreign banking allows for the issuance of securities (which is forbidden under the other forms), and prescribes separate deposit requirements and tax provisions.

Two forms of international banking that have emerged recently are consortium and syndication. Consortium banking is a result of market demand for diverse skills and multicountry coverage. In a consortium, commercial banks from various countries group together under a cooperative shield to provide comprehensive financial service for corporate and governmental clients on an ongoing basis. Functions of a consortium include "arranging and managing large financing, syndication and underwriting the handling of private placements, mergers and acquisitions, and financial counseling." 1/

Syndication is also a form which pools various banks' resources, in order to satisfy medium-term financial needs. However, syndication resembles more a brokered loan offering than a consortium, because of the inclusion of the "best effort" clause (the lead bank will make its "best effort" to solicit the neccessary participants with available funds and desire to make the loan at the agreed upon interest rate for the one-time loan request). Syndication is a result of external and/or internal constraints on the banks, and does not take place due to the lack of knowledge of, or presence in, the international market.

Responses to the Commission's questionnaire indicate that subsidiaries and branches are the most common operating forms internationally (see table 1), followed by an "other" category which includes correspondent banking, agencies, and representative offices. Out of this grouping, correspondent banking was mentioned most often. It appears that the more traditional banking forms are still the major methods of doing business abroad.

1/ John Mathis, ed., Offshore Lending by U.S. Commercial Banks, Banker's Association for Foreign Trade and Robert Morris Associates, November 1978, p. 12.

Table 1.--Operating structures of principal service industry, and revenues associated with secondary service industry activities of financial service firms in foreign markets, 1981 1/

Item	Revenues 2/	Number of responses	Percent of total respondents
	1,000 U.S. dollars		
Operating structure:			
Foreign affiliate	-	5	29
Joint venture	-	3	18
Licensing	-	1	6
Subsidiary or branch	-	15	88
Franchising	-	1	6
Other	-	9	53
Secondary service activity:			
Consulting and management services	3/	1	6
Equipment leasing and rental services	3/	1	6
Insurance services	3/	1	6
Financial advisory services	3/	1	6
Total	7,934	4	23

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 17 of 42 firms surveyed; respondents represented about 19 percent of the foreign revenue of the 205 major firms believed to be operating internationally in 1981.
2/ Calculated by the staff of the U.S. International Trade Commission from receivables, billings, or revenue data provided by respondents.
3/ Withheld to avoid disclosing figures for individual companies.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Scope of operations

As a group, U.S. international banks offer a total service package worldwide and are major participants in the world financial markets. In general, the scope of activities include: 1) receipt of deposits and making short-term loans (the Eurocurreny market described in the industry profile), 2) tapping savings and mobilizing them in the form of medium-term loans (the Eurocredit market), and 3) issuing bonds (the Eurobond market). As indicated earlier, commercial banks tend to operate in the first and second markets; investment banks in the latter. 1/

1/ Carlos Pagano, Evolucion y perspectivas del financiamento externo de la banca de formento latinoamericana, Asociacion Latinoamericana de Instituciones Financieras de Desarrollo (ALIDE), 1979, p. 30.

In the case of commercial banks, a further distinction can be made between those banks that primarily operate in the "wholesale" banking category (e.g., bank to bank, bank to corporation, or bank to central bank) and those that also engage in various "retail" forms (consumer banking). Approximately 75 percent of international financial market transactions take place through the interbank system, typically a wholesale form of banking, which consists primarily of short-term deposits and transfers, most ranging in duration from 3 to 6 months. 1/

The medium-term market has emerged as an extension of the short-term market. Demand (principally from governments) for medium-term loans has risen, especially since 1973. Governments need more funds in order to correct balance-of-payment problems and for various development projects which, it is hoped, will create exports, and thus generate the needed international exchange to repay loans and lower their trade deficits. Funds for such loans come primarily from short-term deposits, which the U.S. banks transform into medium-term loans via "the renewable feature"--the medium-term loans are renewed at the prevailing interest rate during the loan period, with renewal corresponding to the deposit duration (refered to as matching maturities).

The international bond market has experienced slower development than the other two markets, since fluctuating rates have made depositors less willing to place long-term funds, and information about the issuers (the borrowers) is difficult, if not impossible, to obtain. The placement of bonds internationally can be in a single country (known as a foreign bond in the domestic market), or in more than one market, via a syndicate of financial institutions (investment banks, brokers, and so forth). The investment banks act as directors, selecting a group of underwriters with international contacts and brokers who are dispersed geographically.

Growth trends and U.S. investment

Overview of the international financial markets.--New international bank lending, after accounting for double counting due to redepositing and exchange rate effects, was estimated to be around $165 billion in 1980 compared with $125 billion in 1979, reflecting a 32-percent increase in lending.

"The volume of new issues in the international bond market increased by $4.7 billion to 22.5 billion. Foreign issues in national markets, on the other hand, seem to have been adversely affected by inverted yield curves, interest rate volatility, and exchange rate uncertainties, so that their volume declined by $4.2 billion to 15.8 billion. As a result, the total volume of international issues was more or less unchanged. Excluding redemptions of earlier issues, as well as double-counting resulting from bond issues or bond holdings by the banks themselves, the international bond markets may be estimated to have added $21 billion to the amount of finance obtained in the form of bank credit last year (1980), bringing the total growth of international credit . . . to about $186 billion." 2/

1/ Ibid.

2/ Bank for International Settlements, Fifty-First Annual Report, Basle, Switzerland, June 1981, p. 99.

Factors which influenced international market activities were--

(1) the large OPEC surplus of funds,
(2) high Euro-deposit rates and uncertainties in bond and stock markets,
(3) weak borrowing demand from prime domestic customers (in developing countries), and
(4) governmental and supranational organizations soliciting participation of commercial banks in project and trade financing in developing countries.

U.S. international activity.--The number of international branches and subsidiaries has continued to grow over the past two decades due primarily to the expansion of international trade. According to sources at the Federal Reserve Board, in 1980 there were 787 U.S. branch banks overseas and 943 subsidiaries with U.S. majority interest located abroad. The top 100 subsidiaries represented an estimated 80 percent of total assets of subsidiaries in 1980 ($55.9 billion in all).

Though growth still is occurring in U.S. bank expansion into international markets, it had slowed from the expansionary sixties and early seventies. The U.S. banks operating internationally became less aggressive in their lending activities during the late 1970's. The International Monetary Fund suggests that demand for funds domestically--coupled with higher interest rates, reflecting capital shortage in the United States, high debt ratios in certain countries (some countries were paying interest amounting to 50 percent of the debt), and bank failures due to too much risk in too few countries--provoked U.S. banks to reconsider their international loan positions. However, the U.S. banks still competed effectively in the international market.

Three indicators of activity were used in the Commission's survey to determine the relative importance of foreign and domestic activity and trends--revenue, investment in physical assets abroad, and the number of establishments. Foreign operations of U.S. banks are estimated to have accounted for approximately 41 percent of total revenue generated by the respondents' financial activities during 1980 and 1981 (see table 2). Table 3 shows the increased importance of financial service foreign revenue in the service sector. In 1981, the industry's foreign revenue accounted for 51 percent of the total foreign revenue generated by the 14 selected service industries. Revenue generated abroad by our survey's respondents increased 28 percent from $8.3 billion in 1980 to around $11 billion in 1981, and revenue generated by domestic operations of the same group of banks rose 30 percent from $12 billion to approximately $15.7 billion. Of those firms which were able to estimate both 1981 and 1982 revenue, total response indicated that foreign revenue should increase slightly, about 4 percent; domestic revenue generation should rise about 8 percent in 1982.

Investments in physical assets abroad by responding banks showed an estimated 271-percent jump from 1980 to 1981, rising from $187 million to $693 million. The year 1982 should show almost no increase in this category

Table 2.--Indicators of activity in the foreign and domestic operations of financial service firms, 1980-82 1/

Item	Foreign	Domestic	Total
Estimated value of receivables, billings, or revenues: 1/ 2/			
1980--------------1,000 dollars--:	8,335,753	12,068,157	20,403,910
1981----------------------do----:	10,695,151	15,659,059	26,354,210
1982----------------------do----:	3/	3/	3/
Estimate of investment in physical assets 1/ 4/ in foreign operations:			
1980--------------1,000 dollars--:	186,669	-	-
1981----------------------do----:	693,376	-	-
1982----------------------do----:	3/	3/	3/
Number of establishments: 1/			
1980-------------------------------:	231	1,221	1,452
1981-------------------------------:	645	2,389	3,034
1982-------------------------------:	3/	3/	3/
Estimated 5/ value of total industry receivables, billings, or revenues: 6/			
1980--------------1,000 dollars--:	41,500,000	149,300,000	190,800,000
1981----------------------do----:	56,400,000	192,400,000	248,800,000
1982----------------------do----:	75,000,000	240,500,000	315,500,000

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 17 of 42 firms surveyed; respondents represented about 19 percent of the foreign revenue of the 205 major firms believed to be operating internationally in 1981.

2/ Excluding the value of any merchandise exports.

3/ Data submitted by respondents are not comparable and, therefore, have been deleted.

4/ Including the undepreciated book value of land, plant, and equipment.

5/ By the staff of the U.S. International Trade Commission based on discussions with industry and/or association representatives, and secondary sources.

6/ Foreign and domestic revenues are not reported separately and cannot be estimated separately for investment banks and, therefore, are not included in these figures. However, total consolidated revenues for investment firms for 1980, 1981, and 1982 were estimated at $16.0 billion, $19.8 billion, and $18.1 billion, respectively.

Source: Compiled from data submitted in response to questionnaries of the U.S. International Trade Commission.

Table 3.--Estimated total foreign revenue generated by the financial service industry and estimated total foreign revenue for selected service industries, 1980-82

Year	Total foreign revenue for service industry 1/ (1)	Total foreign revenue for selected service industries 2/ (2)	Ratio of (1) to (2)
	1,000 U.S. dollars		Percent
1980	3/ 41,500,000	89,398,000	46
1981	3/ 56,400,000	109,611,000	51
1982	3/ 75,000,000	135,744,000	55

1/ Estimated based on discussion with industry and/or association representatives, and secondary sources.

2/ Based on totaling Commission estimated foreign revenue for each of the 14 selected industries covered in the study.

3/ Foreign and domestic revenues are not reported separately and can not be estimated separately for investment banks and, therefore, are not included in these figures.

Source: Estimated by the staff of the U.S. International Trade Commission.

for the respondents. Of those banks providing data for 1981 and 1982, all indication is that increased investment in physical assets will be limited to around 8 percent in 1982.

The number of foreign establishments of responding banks nearly tripled from 1980 to 1981, and the number of domestic establishments doubled. The number of foreign and domestic U.S. banking establishments are expected to grow in 1982 but at a much slower pace (the respondents indicated that they expected a 15-percent growth in the number of their foreign branches and only a 2-percent growth in the number of their domestic establishments in 1982).

Industry spokesmen believe that the 1980's may, in the long run, revive a new expansionary period as U.S. regulations are removed, which will allow a more competitive position to be taken by the U.S. banks according to industry sources. For example, certain States (notably New York) now provide a free-trade-zone atmosphere (International Banking Facilities (IBFs)), allowing offshore banking facilities to move back into the United States. This reduces overhead costs and allows the State to develop into an international banking center. No reserve requirements, no capital to asset ratios, no FDIC insurance requirement nor regulation Q restrictions (which sets a maximum permissible rate payable on time and savings deposits) are imposed in these areas. 1/ Also, interstate banking by U.S. banks may soon be allowed. (Presently, only foreign banks can provide interstate banking services.)

1/ Federal Reserve Bulletin, January 1982, pp. 35-36.

Foreign assets of U.S.-based banks expanded by $41 billion in 1980, more than twice as much as assets in 1979, whereas liabilities increased only modestly. The principle geographical distribution of new foreign loans was directed toward nonoil developing countries; at the same time, the flow of funds from the developing countries nearly came to a standstill. OPEC countries drew down their U.S. deposits by $0.7 billion, whereas in 1979 they had made new deposits of $5 billion. 1/ Figures for January-June 1981 indicate increased lending activity by internationally active U.S. banks. Total international loans by U.S. banks (with at least one branch having made at least $20 million in loans) was $398.1 billion as of June 31, 1981, compared with $361.4 billion at yearend 1980. Interbank loans have accounted for the bulk of lending--$175.9 billion during January-June 1981 compared with $158.5 billion at yearend 1980. Corporate and private nonbank loans have represented the second largest lending type--$85.9 billion, as of June 31, 1981, compared with $80.5 billion at yearend 1980. Public borrowing was $49.8 billion during January-June 1981; $47.5 billion at yearend 1980. 2/

Latin America remained (and is likely to remain) the region in which most of the banks responding to the questionnaire were active, followed by Europe and the Far East (see table 4).

The region with the highest dollar revenue generated by the responding banks to the survey was Europe, followed by Latin America in both 1980 and 1981. However, there seems to be a shift to the Far East and from the Middle East and Africa in 1982.

1/ Bank for International Settlements, Fifty-First Annual Report, Basle, Switzerland, June 1981, pp. 118-19.

2/ Comptroller of the Currency.

Table 4.--Regions and countries in which revenue is generated by financial service firms, 1980-82 1/

Region and country 2/	Number of responses			Percent of total respondents			Estimated revenue		
	1980	1981	1982	1980	1981	1982	1980	1981	1982
							1,000 U.S. dollars		
Middle East	7	12	6	41	71	35	37,800	48,864	17,852
Bahrain	-	3	-						
Iran	-	1	-						
Israel	-	5	-						
Kuwait	-	3	-						
Pakistan	-	3	-						
Saudi Arabia	-	9	-						
Turkey	-	3	-						
United Arab Emirates	-	2	-						
Far East	11	15	11	65	88	65	248,278	431,391	220,516
Australia	-	6	-						
Taiwan	-	6	-						
India	-	1	-						
Indonesia	-	1	-						
Japan	-	13	-						
Republic of Korea	-	6	-						
New Zealand	-	2	-						
Philippines	-	3	-						
Latin America	12	16	12	71	94	71	270,713	501,790	216,421
Argentina	-	10	-						
Brazil	-	14	-						
Chile	-	4	-						
Colombia	-	2	-						
Panama	-	1	-						
Peru	-	1	-						
Uruguay	-	1	-						
Venezuela	-	10	-						
Europe	10	14	11	59	82	65	501,645	773,658	384,105
Belgium	-	2	-						
West Germany	-	9	-						
Greece	-	1	-						
France	-	7	-						
Italy	-	5	-						
Portugal	-	1	-						
Spain	-	2	-						
United Kingdom	-	11	-						
Africa	2	9	2	12	53	12	3/	24,283	3/
Algeria	-	5	-						
Cameroon	-	1	-						
Egypt	-	5	-						
Guinea	-	1	-						
Ivory Coast	-	3	-						

See footnotes at end of table.

Table 4.--Regions and countries in which revenue is generated by financial service firms, 1980-82 1/--Continued

Region and country 2/	Number of responses			Percent of total respondents			Estimated revenue		
	1980	1981	1982	1980	1981	1982	1980	1981	1982
							1,000 U.S. dollars		
Liberia	-	1	-						
Nigeria	-	5	-						
South Africa	-	3	-						
Zaire	-	1	-						
Canada	5	12	8	29	71	47	19,289	79,518	96,296
Mexico	9	15	11	53	88	65	119,464	214,016	74,658
Other	4	6	4	24	35	24	339,620	652,588	342,722

1/ Country listing is for 1981 only.
2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 17 of 42 firms surveyed; respondents represent about 19 percent of the foreign revenue of the 205 major firms to be operating internationally in 1981.
3/ Withheld to avoid disclosing figures for individual companies.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Trade in Merchandise Generated by Trade in Services

One question that has been neglected in previous publications related to the financial services industry is whether or not physical goods exports are in any way generated by service activities abroad. In many books there are statements made and examples given showing the interdependence of U.S. banks upon the activity of their clients. The most common theory is that U.S. banks established operations overseas as more and more of their domestic customers required banking services for their foreign operations. Thus, one could say that the financial service has followed merchandise trade. But what is the linkage of merchandise exports to financial service operations abroad? What does it take to operate branches and/or subsidiaries? From where are the products which are needed to establish a bank sourced? These are some of the questions asked by the Commission's questionnaire in order to better understand the product/service relationship.

This relationship can be characterized based on a number of insights provided by questionnaire respondents. The number of positive responses to a series of questions asked to determine whether or not U.S. merchandise exports are generated by U.S. financial service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
Do your believe that U.S. merchandise might be used as a result of the services your firm provides abroad?----------------------------	11	65
Is U.S. merchandise specified or recommended in the course of providing your service?------------	5	29
Are U.S. merchandise exports believed to be directly generated?-----------	6	35

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 17 of 42 firms surveyed; respondents represent about 19 percent of the foreign revenue of the 205 major firms believed to be operating internationally in 1981.

The number of positive responses to a series of questions asked to determine whether or not host-country or third-country merchandise shipments 1/ are generated by U.S. financial service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
Do your believe that foreign merchandise might be used as a result of the services your firm provides abroad?------	8	47
Are foreign or host-country products specified or recommended?-------------	0	0

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 17 of 42 firms surveyed; respondents represent about 19 percent of the foreign revenue of the 205 major firms believed to be operating internationally in 1981.

Estimated third-country and host-country merchandise shipments resulting from U.S. financial services abroad in 1981 were as shown in the following tabulation:

Item	Value (1,000 U.S. dollars)
Third-country shipments----------------	0
Host-country shipments-----------------	27

Commercial banking industry respondents in the questionnaire indicated that trade in goods are both indirectly and directly related to the bank's ability to offer financial services abroad. The largest portion of trade in goods indirectly generated by international banking activities takes place because of the establishment of credit lines and introductions of U.S. sellers to foreign buyers. The types of goods covered in this "trade finance" activity are virtually all U.S. manufactured products. The point is made by some industry sources, however, that if U.S. banks were not performing the services mentioned above, other foreign based banks would; therefore, the trade level would quite likely remain approximately the same, i.e., U.S. manufacturers would obtain financing elsewhere. One industry source estimated that about 5 percent of indirect trade in exports is attributable solely to U.S. commercial banks being able to operate in the international market. Though this percentage is small, the dollar amount for trade financing is large. Another point about this indirect service/trade relationship which should be

1/ "Host-country merchandise shipments" refers to the shipments (within the host country) of host-country-manufactured products which are generated by U.S. service operations in the host-country market. "Third-country merchandise shipments" refers to the shipments of other foreign-manufactured products to a foreign market as a result of U.S. service operations in that market.

recognized is that very little overseas presence (if any) is required, since the service for the most part is provided via correspondent banking networks. Thus, most service barriers probably do not have significant impact upon the indirectly related exports.

A much smaller amount of export trade is directly linked to international banking operations. Because of the relatively low response rate to the merchandise trade section of the questionnaire, the Commission is unable to extrapolate with certainty the value of U.S. merchandise exports directly generated by U.S. financial service activities abroad. However, industry respondents estimated that their service activities overseas resulted in the total U.S. export of approximately $564 million in goods in 1981 (table 5). On the basis of this estimate, the number of respondents, and the number of known firms in the industry, it is estimated that nearly $8.3 billion in U.S. merchandise exports flowed as a result of U.S. international banking activities in 1981. However, it should be noted that at a confidence level of 95 percent this figure could be as low as the actual respondent's estimate of $564 million or as high as $25 billion. For estimates of U.S. merchandise exports for 1980 and 1982, refer to table 5.

Commerical banks surveyed cited office equipment, paper products, and data processing equipment as examples of exports which are generated to support banking facilities abroad (see table 6). These products would most likely be affected by the amount of international banking operations. There was also an indication that a significant portion of these service-related exports are considered to be high-technology products. Several countries have attempted to get international banks to use public telecommunications services or downgrade the equipment presently used by the banks. The U.S. banks have resisted since timing is one of the most important selling features to clients depositing large sums, and will become an increasingly significant competitive factor in providing international services. Potential losses could amount to thousands of dollars per day for a single large-depositing client if competitors were able to process information faster.

Table 5.--U.S. merchandise exports generated by U.S. financial services abroad, 1980-82 1/

Year	Number of responses	Exports of U.S. merchandise estimated by respondents	Projected 2/ total: U.S. merchandise for the service industry	± 95-percent confidence limit projected industry exports
		1,000 U.S. dollars		
1980	3	512,000	7,497,000	15,243,000
1981	3	564,000	8,259,000	16,766,000
1982	3	617,000	9,035,000	18,287,000

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 17 of 42 firms surveyed; respondents represent about 19 percent of the foreign revenue of the 205 major firms believed to be operating internationally in 1981.
2/ By the U.S. International Trade Commission.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 6.--Estimated U.S. merchandise exports resulting from financial services abroad, by types and by principal markets, 1981 1/

Type	U.S. exports used in providing services 2/	Number of firms indicating U.S. merchandise exports to--							
		Middle East	Far East	Central and South America (excluding Mexico)	Europe	Africa	Canada	Mexico	All other
	1,000 U.S. dollars								
Total	56,000								
Machinery and equipment	2,000								
Telecommunications equipment	400								
Data processing (computing) equipment	1,600								

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 17 of 42 firms surveyed; respondents represent about 19 percent of the foreign revenue of the 205 major firms believed to be operating internationally in 1981.
2/ U.S. exports were estimated but respondents could not identify the specific type in all cases; thus, the subcategories do not add to the total shown.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

International Service Trade Barriers

Industry leaders indicated that all foreign-based banks entering, or attempting to enter, a market are confronted with a broad range of barriers. In many cases, the host government restricts activities in either a conspicuous or inconspicuous manner. For instance, certain countries do not allow the establishment of foreign-bank branches and/or subsidiaries. Examples of less restrictive barriers include the requirement of governmental approval to transfer capital, various service and operation restrictions, biased debt to capital ratio's favoring indigenous banks, restrictions on remittances of currencies abroad (exchange control), and barriers affecting all industries, such as discriminatory taxation, and employment and ownership restrictions.

As an example, the approval requirement by a host government to transfer capital in or out of its borders permits that government to favor its domestic-based banks. Foreign banks in a host country usually have foreign currency (their home currency) deposits from which they lend. If a government limits the amount of the foreign-based bank's deposit currency that can be brought into the country, it can seriously restrain the bank's activity in the market. Limitation on the amount of currency a bank can transfer out of a country also reduces the bank's ability to use that capital in the most profitable way. The transfer of capital restrictions produces higher interest charges to foreign bank borrowers in a host country, which tend to force these borrowers to the indigenous banks for loans.

In general, restrictions on U.S. banks (other than employment or taxation-type restrictions) tend either to limit, or reduce, the size of lendable funds or directly restrict the amount and/or type of activity. However, governments realize that too much regulation depletes their market of much needed capital.

In the Commission survey, the major barrier heading most frequently responded to was "foreign exchange controls"; barriers commonly cited under this heading were "restrictions on remittances" and "convertibility limitations on various currencies" (see table 7). Ranked second, and of equal importance, were "right of establishment" and "trade in service." Under the right of establishment heading credit, investment, and financial activity restrictions were often indicated as barriers to international financial service activities. "Restrictive government/business regulations and administrative procedures" was mentioned more frequently than any other barrier listed under "trade in service." 1/

After having chosen barriers which the company had experienced in international markets, the various firms surveyed were requested to indicate the direction and extent of change a reduction or elimination of these barriers would have on their international service activities and on the flow of export merchandise related to their service activities abroad.

1/ Note the preceding discussion of barriers to financial service operations.

Table 7.--Trade barriers to international services in the financial services industry 1/

Category and barrier	Number of responses	Percent of total respondents
Right of establishment	10	59
Restrictive employment regulations (e.g., local labor requirement)	3	
Credit, investment, or financial activity restrictions	7	
Administrative/ownership restrictions	5	
Citizenship/residency requirements	2	
Restrictive government/business regulations	7	
Limiting number of establishments	2	
Grandfather clause requiring practice before specified date	2	
Special deposit requirement for foreign companies	3	
Commission terms less favorable than national companies	1	
Trade in goods	1	6
Local purchase requirements	1	
Trade in services	10	59
Restrictive government/business regulations and administrative procedures	7	
Restriction related to resident firm preference (fixed percentage of service must be provided by domestic resident companies)	2	
Employment related restrictions on nonnationals	6	
Operating/ownership restrictions	4	
Discriminatory taxation	2	
Prohibition on services offered by nonresident companies	3	
Other (withholding tax on interest/dividends)	4	
Other (prohibition of foreign capital)	1	
Technical issues	3	18
Privacy restrictions	1	
Governmental paper requirement for importing	2	
Government procurement	2	12
Preference given to national firms	1	
Shipment restricted to National flag carriers partially or completely	2	
Subsidies/countervailing duties	3	18
Tax benefits (e.g., rebate or tax breaks)	2	
Direct financial aid to local firm by government	1	
Preferential financing arrangements	3	
Standards/certification	1	6
Health and safety requirements	1	

See footnote at end of table.

Table 7.--Trade barriers to international services in the financial services industry 1/--Continued

Category and barrier	Number of responses	Percent of total respondents
Foreign exchange controls	11	65
Restrictions on remittances	10	
Convertibility limitations	9	
Delays in obtaining foreign exchange permit	7	

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 17 of 42 firms surveyed; respondents represent about 19 percent of the foreign revenue of the 205 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

The number of responses to a question to determine the economic effects of international barriers to U.S. services trade and associated product exports in financial service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
What effect, if any, would reduction or removal of service trade barriers have upon your receivables, billings, or revenues in current or potential country markets?:		
Increase	10	59
Decrease	0	0
No effect	6	35
What effect, if any, would reduction or removal of service trade barriers have upon potential U.S. products exports in current or potential country markets?:		
Increase	7	41
Decrease	0	0
No effect	7	41

1/ The total number of questionnaire respondents in this service inaustry was 17 of 42 firms surveyed; respondents represented about 19 percent of the foreign revenue of the 205 major firms believed to be operating internationally in 1981.

The majority of financial service industry firms responding to the questionnaire indicated that their service activities overseas would increase as a result of reducing or eliminating the existing international barriers. Respondents to the second question were divided equally between those companies which indicated an increase and those which indicated no effect on export merchandise trade related to their international service activities.

Most firms indicated that a reduction in barriers would result in increased service revenues from the Far East and Latin America (table 8). Twenty percent was the mode for these two regions. As for merchandise exports directly and indirectly generated by banking services, respondents cited all types of manufactured goods; "machinery and equipment" was cited most often (table 9).

Table 8.--Estimated changes in revenues absent trade barriers to international business of financial service firms, by areas 1/

Area and direction of change	Number of responses	Percentage change						
		10	20	30	40	50	60	80
Middle East:								
Increase	3		3					
Decrease								
Far East:								
Increase	8	2	3	1		1		1
Decrease								
Latin America:								
Increase	6	1	3			2		
Decrease								
Europe:								
Increase	4	2	1			1		
Decrease								
Africa:								
Increase	2	2						
Decrease								
Canada:								
Increase	4	3	1					
Decrease								
Mexico:								
Increase	4	2				1	1	
Decrease								
Other:								
Increase	-							
Decrease								

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 17 of 42 firms surveyed; respondents represent about 19 percent of the foreign revenue of the 205 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 9.--Estimated changes in U.S. merchandise exports absent trade barriers to international business at financial service firms, by types 1/

Type and direction of change	Number of responses	Percentage change						
		10	20	30	40	50	60	80
Machinery and equipment:								
Increase	3			2			1	
Decrease								
Agricultural, animal and vegetable products:								
Increase	2				1			1
Decrease								
Forest products:								
Increase	1		1					
Decrease								
Textiles, apparel, and footwear:								
Increase	2	1				1		
Decrease								
Chemicals and related products:								
Increase	1		1					
Decrease								
Minerals and metal products:								
Increase	1		1					
Decrease								
Miscellaneous manufactures:								
Increase	2		1			1		
Decrease								

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 17 of 42 firms surveyed; respondents represent about 19 percent of the foreign revenue of the 205 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Conditions of Competition in Current and Potential Service Markets

Foreign clients in the international financial market use certain criteria to determine with which banks they will deal. Status and size, nationality, experience in the market (i.e., prior ties), and local presence are all important factors which foreign lenders and borrowers consider.

The stature and size of the bank is important to the client's overall plan to use the international capital market and the cost of borrowing. As a general rule of thumb, large loans require a major bank as a leader in a syndicate, since smaller banks do not have the stature to gather enough participants. Also, large-deposit banks are able to quote lower interest rate costs.

Nationality is of concern to international clients because the bank's deposit base may have special appeal, if the international finance market should falter. In the case of U.S. banks, bankers could rely on domestic dollar resources in troubled times, thus giving U.S. banks a competitive edge, since the U.S. dollar is still and remains today the most demanded international currency (even if "currency baskets" are becoming more frequent, no one currency is more important internationally than the U.S. dollar). 1/

Experience in a market or the local presence of a bank often leads to repetitive use. Local branches make banks accessible to borrowers, help the bank to develop an understanding of local service needs, and can give intangible political influence such as gaining local support to influence governmental decisions and making political contacts within the country.

Though U.S. commercial and investment banks are considered to have a competitive advantage partially due to status, size, and experience in the market, they are restricted to some degree in all markets. Regulations by host countries and by the United States range from restrictions on banking activities to indirect restrictions such as reserve requirements. Thus governments (foreign and the U.S.), and their need to regulate banks, are perhaps the major barrier to U.S. expansion overseas, though no direct regulation of the overall international market exists. The nature of international service trade barriers and their effect on the financial services sector are discussed in the section on "International Service Trade Barriers."

U.S. international banks enjoy a competitive edge in the world market. Industry sources claim that U.S. banks have an edge due to (1) market presence, (2) experience, (3) their deposit-base currency being "the" international currency, and (4) lending analysis based on the borrowers ability to generate funds, rather than the traditional asset lending technique.

It was around the time of the Second World War that U.S. banks began to play such an important role in the international market. After the end of World War II, the United States owned most of the world's gold supply; its

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1/ P.A. Wellons, Borrowing by Developing Countries on the Euro-Currency Market, Development Centre of the Organization for Economic Co-operation and Development, Paris, France, 1977, pp. 60-65.

factories were not damaged by the war and were actually geared up for overproduction. Many U.S. banks followed their corporate clients as they moved into international markets to sell their products. The U.S. banks have remained major participants in the international finance market ever since. However, the dollar having lost some of its international stature and two large international bank failures in the 1970's have led to more prudent styles in lending by U.S. banks. This has occurred at a time when U.S. banks are facing aggresive competition from English, French, German, and Japanese banks.

The Commission survey attempted to obtain up-to-date information on the competitive stance of U.S. financial service firms versus their international counterparts in the world market, as well as competitive strengths U.S. firms might have in potential markets where they do not yet operate.

The United Kingdom and Japan were the markets in which the largest amount of foreign revenue was generated by the responding firms (see table 10). The number of competing firms in these markets also was significant. The United Kingdom was cited as having mostly regional banks operating within its borders. In fact, it would seem that London remains the international center for financial service operations. Japan, on the other hand, was cited by respondents as having more national firms than any other type.

Table 11 shows a listing of base countries of banks which compete in the international financial services market and likely reasons for the success of the banks of these countries in the internatonal market. Generally, "experience in the market or service area" was cited most often, followed by "lower prices," "political or regional bias," and "government support."

Table 12 shows the competitive strengths of U.S. financial service firms in foreign service markets. In general, "experience in the market or service area" was cited most often as a likely reason for success. It appears that experience in a market is extremely important for any bank in the international market. U.S. banks have played a major role in international finance for approximately 40 years operating in most world regions, and thus are major competitors due in part to their wide network in and knowledge of the world market. "Risk philosophy" was cited by respondents under the "other" category.

The final table (table 13) shows the same information as table 12 except that the markets listed are potential markets for the respondents. "Greater experience" once again was cited more often than any other reason for success; however, "financial strength" and "technology lead" were also frequently indicated by our respondents as likely reasons for success in potential markets. This is interesting because these two reasons--financial strength and technology--are often cited today by bankers as the most likely reasons for future growth and/or survival in international markets. Under the "other" category, respondents listed service specialization, membership in a worldwide financial network, and a broad range of services offered as other strengths.

Table 10.--Number of firms competing 1/ with U.S. financial service firms abroad, by principal service markets 2/ in order of revenue generated, 1981 3/

Service market	Number of competing firms				
	Total	National	Regional	World-wide	Other U.S. firms
United Kingdom	490	50	310	90	40
Japan	280	125	55	60	40
Canada	80	10	50		20
Mexico	100	-	-	-	-
Brazil	400	-	-	-	-
Venezuela	60	-	-	-	-
Costa Rica	100	-	-	60	40
Other	100	-	-	60	40
Taiwan	28	8	6	7	7
France	40	10	5	15	10

1/ Based on 4 responses by questionnaire respondents.
2/ Other principal service markets for the industry may not be listed here if respondents did not identify the number of competing firms.
3/ Data are for questionnaire respondents only. Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 17 of 42 firms surveyed; respondents represent about 19 percent of the foreign revenue of the 205 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 11.--Likely reasons 1/ for competing firms' success in world financial service markets, by base countries of firms 2/

Base country	Lower price	Technology expertise	Preferential financing	Experience in the market or service	Superior quality association	Political or regional bias	Government support	U.S. restrictions
Taiwan	1		1	1		1	1	
Japan	1	1	1	2		1	3	
Republic of Korea				1		1		
Philippines						1		
West Germany			1			1		
France	1	1	1	1		1	2	
United Kingdom	2	1	1	3		1	1	
Other	3	2		1	1			
Total	8	5	5	9	1	7	7	

1/ The importance of each reason is indicated by the number of times each was designated, based on 5 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 17 of 42 firms surveyed; respondents represent about 19 percent of the foreign revenue of the 205 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 12.--Likely reasons 1/ for the competitive strength of U.S. financial service firms in foreign service markets 2/

Service market	Lower price	Technology lead	Financial strength	Experience in the market or service	Superior quality association	Other
Far East:						
Japan	1		1	2	1	1
Central and South America (excluding Mexico):						
Brazil	1		1			
Costa Rica				1	1	
Venezuela	1			1		
Europe:						
United Kingdom			1			1
North America and Mexico:						
Canada						1
Mexico				1		
Other				1	1	
Total	3		3	6	3	3

1/ Data are for questionnaire respondents only. The importance of each reason is indicated by the number of times each was designed, based on 5 responses; respondents represent about 19 percent of the foreign revenue of the 205 major firms believed to be operating internationally in 1981.

2/ The total number of questionnaire respondents in this service industry was 17 of 42 firms.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 13.--U.S. financial service firms' competitive strengths 1/ in potential foreign markets 2/

Potential service market	Lower price	Technology lead	Financial strength	Greater experience	Superior quality	Other
Far East:						
China			1			
Taiwan		2	1	3	1	
Japan	1					
Republic of Korea		1	1	2	1	2
Philippines			1			2
Central and South America (excluding Mexico):						
Brazil	1	1	1			1
Venezuela	1					
Europe:						
Italy			1	1		
Spain		1	1	2	1	
North America and Mexico:						
Canada			1	2		3
Mexico		1	1		1	1
Total	3	6	9	10	4	9

1/ The importance of each reason is indicated by the number of times each was designated, based on 6 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service was 17 of 42 firms surveyed; respondents represent about 19 percent of the foreign revenue of the 205 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

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Franchising Services

Executive Summary

1. International revenues in foreign establishments of U.S. franchisors are estimated at $2.7 billion in 1981.

2. Although the total dollar amount of U.S. merchandise exports related to franchising is unknown, such exports are directly generated. Respondents to the Commission's questionnaire estimated that exports of U.S. merchandise generated by their foreign franchise activities totaled more than $14 million in 1981. The principal areas of merchandise exports were data processing equipment, motor vehicles, automotive products, food service and related equipment, and various chemical products.

3. Two-thirds of questionnaire respondents indicated that host- or third- country merchandise shipments might be generated as a result of U.S. franchising service activities abroad. Respondents estimated the value of such shipments generated by their foreign franchise activities to be over $11 million in 1981.

4. Questionnaire respondents reported a wide range of barriers to services trade. Most respondents indicated there were restrictive actions related to the right of establishment with problem areas in (1) restrictive employment regulations, (2) credit, investment, or financial activity restrictions, (3) administrative/ownership restrictions, and (4) restrictive government/business regulations. Also significant were restrictions related to trade in services, customs valuation, and foreign exchange controls.

5. The dollar impact of international trade barriers to the U.S. franchising industry is not known, but questionnaire respondents and other industry sources indicate that numerous barriers are limiting both their foreign revenues and U.S. merchandise exports. According to industry sources, U.S. franchising operations in less developed countries, particularly in Central and South America, have been minimal due in large part to various trade barriers. Further, Canada and the Far East were both cited by most respondents as areas where service activities would increase if barriers were removed--Canada by 10 to 50 percent and the Far East by 10 to 40 percent.

6. Respondents indicated that foreign competition outside the United States was, by far, greatest in Canada. Respondents provided no indication of the reasons for the success of foreign firms in international markets. Industry sources stated that U.S. franchising firms are generally competitively strong in most foreign markets.

7. Most respondents felt that superior quality associated with their firm or the United States was a definite competitive strength for U.S. franchising firms. Market and service experience followed closely as a factor in the strength of U.S. firms.

Industry Profile

Definition and coverage

Franchising is a form of distribution that involves a licensing agreement between the franchisor, or owner of a product, service, or tradename, and the franchisee, or affiliated dealer, to market the franchisor's goods or services. There are two basic types of franchising--product and tradename franchising, and business format franchising. 1/ Product and tradename franchising generally involves identification of the franchisee with the franchisor's product; the franchisee may be relatively independent in marketing the product. Business format franchising is a more integrated distribution system of the two types where the agreement between the franchisor and franchisee generally includes a marketing strategy, uniform products, standardized operating procedures, quality control measures, and managerial and technical assistance from the franchisor.

Franchises are based on an agreement which may contain provisions for financial terms, use of trademarks, renewal, contract duration, product and process requirements, management and operational aid, territoriality, and other business considerations. Financial terms generally involve an initial franchise or license fee (which may be substantial), royalty payments (usually based on sales), training, advertising, and other fees. Since trademarks are usually a franchisor's most valuable asset, usage by the franchisee is generally tightly controlled and ownership of the trademark is maintained by the franchisor. Franchise agreements may last anywhere from a year to perpetuity; most are long term, with more than 80 percent of those in effect in 1980 lasting for more than 10 years. Virtually all franchise agreements provide an opportunity for renewal; almost 90 percent of expired agreements in 1980 were renewed. Many franchise agreements require strict adherence to usage of ingredients and production processes by the franchisee in order to maintain product uniformity and integrity in each establishment. Franchise agreements may also require the franchisor to provide training and education for managerial and operational requirements of the franchisee or to actually provide management services.

Franchising is included in the Standard Industrial Classification (SIC) 6794. The individual services that franchising comprises are classified under various other SIC groups.

The 15 franchising service industry respondents to the Commission's questionnaire (out of 71 surveyed) are estimated to represent less than 1 percent of the foreign revenues of the 280 franchising service firms believed to be operating internationally in 1981. The respondents represent a wide range of types of franchised businesses and are both relatively large and small within their respective businesses.

1/ Most of the basic industry data used in this report was obtained from Franchising in the Economy, 1980-1982, U.S. Department of Commerce, Washington, D.C., January 1982.

Highlights in 1981

- o DOMESTIC SALES in U.S. establishments of the franchising service sector are estimated to have totaled $380 billion.

- o U.S. ESTABLISHMENTS of nearly 1,600 franchisors numbered 447,000, of which 361,000 were franchised.

- o U.S. EMPLOYMENT in these establishments is estimated at nearly 5 million, including part-time workers and proprietors.

- o INTERNATIONAL REVENUES in foreign establishments of U.S. franchisors are estimated at $2.7 billion.

- o FOREIGN ESTABLISHMENTS of 280 U.S. franchisors operating internationally totaled more than 20,000.

- o U.S. TRADE BALANCE data for the U.S. franchising sector are not available, but the balance is believed to be positive and substantial.

Industry structure

Franchisors may directly franchise an individual establishment, grant multiunit franchises, or grant an area or master franchise agreement covering a large area such as a state or region. Most franchisors permit multiunit ownership. In 1977, the latest available data of this type, of 1116 franchising firms surveyed by the U.S. Department of Commerce, 304 granted regional franchises, 42 granted state franchises, and 543 granted other territorial franchises. 1/

Franchisors may operate their establishments as company-owned or as franchisee-owned units; most franchisors are involved in dual distribution, with both company- and franchisee-owned units in their chains. Most franchise establishments in the United States are owned by the franchisee. Of the 447,000 domestic franchise establishments operating in 1981, 361,000, or 81 percent, were franchisee owned and 86,000, or 19 percent, were owned by the franchisor. Business format franchising accounted for 265,000 establishments, or 59 percent of the total, in 1981; there were about 182,000 product and tradename franchising establishments, or 41 percent of the total, that year.

Franchising comprises a large variety of products and services. Product and tradename franchising, which is the more traditional form, consists primarily of automobile and truck dealers, gasoline service stations, and soft drink bottlers. Sales by these establishments account for about three-fourths of total U.S. franchise sales. Business format franchising, which is a relatively new form, accounts for the remainder of total franchise sales and includes restaurants, retailing, automotive products and services, hotels and motels, convenience stores, grocery stores, auto and truck rental services, and many others.

1/ U.S. Department of Commerce, Franchising in the Economy, 1976-1978, Washington, D.C., January 1978.

Gasoline service stations are by far the most numerous kind of franchising establishment, with 151,000 establishments, or 34 percent of the total, operating domestically in 1981, followed by restaurants (64,000, 14 percent), business aids and services (44,000, 10 percent), and automotive products and services (41,000, 9 percent).

Automobile and truck dealers lead all types of franchising in terms of sales, with total revenues in 1981 of $164.8 billion, or 43 percent of the total. The next most important are gasoline service stations ($105.1 billion, 28 percent), and restaurants ($31.6 billion, 8 percent).

Services provided through franchising encompass the types of business conducted by other service industries included in this report since it is a method of distribution of goods and services. Among these are educational services, hotels and motels, equipment leasing, and certain management and consulting services; however, coverage of these specific services in the separate industry reports exclude the franchising method of operation and concentrate on the institutional or corporate service operation.

Recent trends and outlook

Franchising has grown significantly in the United States in the past decade. In 1970, there were 396,000 establishments with sales of $117 billion. By 1981, the number of establishments reached 447,000 and sales totaled $380 billion; this was a 13-percent increase in the number of establishments and more than three times the sales recorded in 1970.

Although the scope of total operations of U.S. franchisors in foreign markets is relatively small compared with domestic franchise operations, this area has been growing in recent years. From 1975 to 1980, the number of U.S. firms involved in international franchising increased by about one-fourth from 222 to 279. The total number of establishments associated with these firms increased by more than 85 percent during the same period from about 11,000 to about 20,500. 1/

Several factors have contributed to the growth in franchising, especially in the business format type. The growth of the suburbs and suburban-type shopping centers, the increasing mobility of housewives, the increase in the number of working women, rising intercity travel, the decline of independent business establishments serving small rural communities, and the expansion of mass merchandising are among many reasons for the recent growth in franchising as a business system. 2/

The growth in franchising in recent years also reflects, in part, certain advantages resulting from franchising. For an entrepreneur starting a new business establishment, franchising offers immediate recognition and identification with a known product or service, thus facilitating market entry. For a company developing new markets, franchising offers cost

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1/ The U.S. Department of Commerce data do not include product and tradename franchising in international markets.

2/ Charles L. Vaughn, Franchising, Lexington, Mass., 1979, pp. 23-29.

advantages, as capital is raised from the franchisee and overhead and risks are reduced. Franchising may also enable a firm to more closely monitor and control product uniformity and quality. This aids in developing consumer acceptance of the goods and services that are provided. Another advantage of franchising is the flexibility to change products or services due to shifts in consumer preferences or market locations. Since a distribution chain has been established in a franchise system, product or service inputs may be substituted or introduced in order to meet changing demand. If markets change, a firm may shift resources to new locations with a minimum of cost and disruption to current operations.

The demand for franchising as a business method has been increasing as evidenced by the sector growth. Within the franchise system, demand has been increasing for new types of products and services. For example, as new car prices have been rapidly rising, there has been a concomitant increase in the demand for used cars, and a new franchise for exclusively used car dealerships is now being offered. 1/ First Interstate Bank Corp. of California is offering franchises to banks in order to offset competition from nonbank institutions and to expand in compliance with interstate banking regulations. 2/ There has also been an increase in franchise activities in such sectors as business aids and services, legal services, real estate, high-technology goods and services, personal care services, and most recently, franchised remodeling contractors.

The domestic business environment for franchising has been changing in recent years. Perhaps the major considerations of the franchising business environment are legal. First, there are recent State and Federal laws regarding disclosure of a franchisor's operations to prospective franchisees. In 1970, the California Franchise Investment Law was enacted; it was the first franchise disclosure law in the United States. By 1980, there were 16 States with disclosure laws. 3/ In 1979, the Federal Trade Commission effected the "Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures" (16 CFR 436), which made disclosure a Federal requirement.

In addition to disclosure requirements, antitrust legislation must also be considered. The application of such legislation to franchising has been increasing recently, as certain provisions of a franchise agreement may be interpreted as constituting restrictive trade practices. Such provisions include termination and renewal, tied buying, and exclusive territorial arrangements. Many State laws as well as Federal antitrust legislation address these issues. In addition, several States require that a franchisor register before offering any franchises within a particular State.

On the business side, franchising is experiencing several structural trends. There is a trend toward mergers and acquisitions. Large corporations have been acquiring existing franchise operations as an expeditious and less

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1/ "New Used-Car Franchise Begun," The Washington Post, June 18, 1982, p. D-8.

2/ Business Week, Apr. 5, 1982, pp. 29-30.

3/ U.S. Department of Commerce, Franchising in the Economy, 1978-1980, Washington, D.C., January 1980.

costly manner of market entry and diversification. Many of the largest franchising chains are owned by large corporations. Some examples are Kentucky Fried Chicken (Heublin), Pizza Hut (Pepsico), Dunhill Personnel System (Canteen Corp. of America, a TWA subsidiary), Midas International (IC Industries), Manpower (Parker Pen Co.), among others. Rising construction and operating costs, difficulty in recruiting and training personnel, and increased Government regulations regarding franchising are factors in this trend. For the same reasons, there has also been a trend toward multiunit franchisee ownership and toward franchisors granting large regional licenses. For example, in the fast-food sector, in 1981 Chart House, Inc. was a franchisee of 365 Burger King units, Collins Food International of 232 Kentucky Fried Chicken units, and Spartan Food Systems of 231 Hardee's units. 1/

Recent economic conditions have depressed most business activities. Persistent inflation and record-high interest rates have caused failures and dampened business expansion in many business sectors. Within the franchising sector, declines were experienced by certain domestic industries in recent years. Automobile and truck dealers, gasoline service stations, and automotive products and services franchises in particular have been affected by poor economic conditions, especially in 1980.

The franchising method offers some insulation from adverse economic conditions. The effects of scarcity of capital, rising costs, and declining profit margins are lessened by franchising due to the advantages discussed earlier. According to the latest Department of Commerce survey of franchisors, 125 franchisors failed in 1981. This represented about 8 percent of all franchisors surveyed that year, a rate which is low compared with that of general business failures, particularly of small businesses. In addition, 250 new franchisors entered in 1981.

Franchising is expected to grow steadily in the United States during the next decade. As population and lifestyles change, there will be increasing demand for consumer goods and services that are offered conveniently through the franchise system.

International franchising is also expected to continue expanding. Government and industry sources indicate that several U.S. franchising firms intend to enter foreign markets or expand existing foreign operations during the next several years.

U.S. Service Operations in Foreign Markets

Operating structure

Business format franchising is the principal type of operation in foreign markets. Most U.S. franchisors operate in foreign markets through foreign franchisee-owned establishments. The general business and legal environment in the particular market will determine the operational structure. Generally,

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1/ Restaurants and Institutions, Cahners Publishing Co., Chicago, Ill., July 15, 1981, pp. 125-130.

the tax system, antitrust regulations, foreign investment controls, disclosure requirements, and foreign exchange restrictions are among the principal factors involved in developing the organizational structure of U.S. franchisors' overseas operations.

Most firms sell their outlets to a franchisee, but some may also operate company-owned units or enter joint-venture arrangements depending on the business environment. According to the U.S. Department of Commerce, about 265 of the total of U.S. franchising firms operating in foreign markets in 1980 sold outlets to franchisees or licensees, about 30 operated their own establishments, and about 20 were involved in joint ventures. Most U.S. franchises in foreign markets are master or area franchises covering a large area, sometimes an entire country.

Table 1 shows results concerning respondents' operating structure in foreign markets. Of 15 firms responding, 93 percent used franchising. The other operating structures given were licensing (27 percent), subsidiary or branch (20 percent), and foreign affiliate and joint venture (13 percent each). Of the firms responding, 60 percent used only franchising, 38 percent used more than one operating structure, and only one firm did not use franchising at all.

Table 1.--Operating structures, and revenues associated with secondary service industry activities of franchising service firms in foreign markets, 1981 1/

Item	Revenues	Number of responses	Percent of total respondents
	1,000 U.S. dollars		
Operating structure:			
Foreign affiliate	-	2	13
Joint venture	-	2	13
Licensing	-	4	27
Subsidiary or branch	-	3	20
Franchising	-	14	93
Secondary service activity	2/	-	-

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 71 firms surveyed; respondents are estimated to represent less than 1 percent of the foreign revenue of the 280 major firms believed to be operating internationally in 1981.

2/ No secondary activities were indicated by the service industry respondents.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Scope of operations

Various industry sources indicate that franchising offers many advantages to U.S. firms entering foreign markets. As in the domestic market, the advantages of immediate identification and recognition apply to international franchising. Franchising may offer some protection against tradename infringement by registration and use in a foreign market. The risk of expropriation is diminished by franchising, since foreign outlets are generally owned and staffed by foreign nationals. And, when the domestic market becomes saturated and growth declines, foreign markets offer opportunities for expansion.

Government statistics indicate that foreign operations generally provide a relatively small share (usually less than 4 percent) of total income for U.S. franchising firms, especially since most foreign outlets are owned by franchisees that pay a fee and/or royalty on their sales. However, expansion into international markets is outpacing domestic growth. During 1976-80, the total number of foreign establishments associated with U.S. franchising firms increased at an average annual rate of about 13 percent compared with a rate of less than 1 percent for domestic establishments.

U.S. franchising operations in foreign markets offer a wide variety of products and services as in the domestic market. Automobile and truck rental services are the leading type of franchise in terms of number of foreign establishments with about 4,800 such outlets in 1980. Most of these are located in continental Europe, where there were about 1,300 outlets, or 27 percent of the total in 1980. Other major areas with such establishments in 1980 were Mexico, Canada, Australia, the United Kingdom, and Japan. Restaurants are the second most numerous type of franchise with nearly 4,000 such establishments outside the United States in 1980. The major markets were Canada (where about a third are located), Japan, the United Kingdom, and Australia. Other leading types of franchises are nonfood retailing (about 2,600 establishments in 1980) and automotive products and services (about 1,800 establishments in 1980) with more than half of these located in Canada.

Growth trends and U.S. investment

International franchising by U.S. firms has been growing steadily in recent years. Nonfood retailing had the highest growth rate of all the types of franchised businesses operating overseas, with the number of foreign establishments increasing nearly twofold during 1976-80. Also showing strong international growth was the broad category including educational products and services, equipment rental services, convenience stores, and miscellaneous services. This category, mainly consisting of convenience stores, also increased nearly twofold in the number of foreign establishments during 1976-80. The percentage growth rates of foreign establishments for other types of franchised businesses during this period include automobile and truck rental services (105 percent), food retailing (83 percent), business aids and services (61 percent), and restaurants (50 percent).

Of the 15 total respondents to the questionnaire, 9 reported estimated foreign and domestic revenues for 1980-82. Revenues from the respondents' foreign franchise operations is estimated to increase 27 percent from $9.7 million in 1980 to $12.3 million in 1982 compared with revenues from their domestic operations of $123.6 million in 1980 to $178.9 million in 1982, or an increase of 45 percent during this period. The number of foreign establishments reported by the respondents was estimated to increase 5 percent from 743 in 1980 to 781 in 1982, and the number of their domestic establishments was estimated to increase 2 percent from 6,145 in 1980 to 6,230 in 1982 (table 2).

Table 2.--Indicators of activity in the foreign and domestic operations of franchising service firms, 1980-82

Item	Foreign	Domestic	Total
Estimated value of receivables, billings, or revenues: 1/ 2/			
1980------------------1,000 dollars--:	9,715	123,607	133,322
1981----------------------------do----:	12,584	150,603	163,187
1982----------------------------do----:	12,309	178,926	191,235
Estimate of investment in physical assets 1/ 3/ in foreign operations:			
1980------------------1,000 dollars--:	4/	-	-
1981----------------------------do----:	4/	-	-
1982----------------------------do----:	4/	-	-
Number of establishments: 1/			
1980----------------------------------:	743	6,145	6,888
1981----------------------------------:	741	6,175	6,916
1982----------------------------------:	781	6,230	7,011
Estimated 5/ value of total industry receivables, billings, or revenues:			
1980------------------1,000 dollars--:	2,500,000	-	-
1981----------------------------do----:	2,700,000	40,622,000	43,322,000
1982----------------------------do----:	2,700,000	-	-

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 71 firms surveyed; respondents are estimated to represent less than 1 percent of the foreign revenue of the 280 major firms believed to be operating internationally in 1981.

2/ Excluding the value of any merchandise exports.

3/ Including the undepreciated book value of land, plant, and equipment.

4/ Data submitted by respondents are not comparable and, therefore, have been omitted.

5/ By the staff of the U.S. International Trade Commission, based on discussions with industry and/or association representatives, and secondary sources.

Source: Compiled from data submitted in response to questionnaries of the U.S. International Trade Commission.

Total foreign revenues generated by the entire franchising sector are estimated to increase from $2.5 billion in 1980 to $2.7 billion in 1982, or by 8 percent. In 1982, total foreign revenues generated by the franchising industry will account for about 2 percent of total service sector foreign revenue of $135.7 billion estimated for the 14 selected industries included in the study (table 3).

Table 3.--Estimated total foreign revenue generated by the franchising service industry and estimated total foreign revenue for selected service industries, 1980-82

Year	Total foreign revenue for service industry 1/ (1)	Total foreign revenue for selected service industries 2/ (2)	Ratio of (1) to (2)
	1,000 U.S. dollars		Percent
1980	2,500,000	89,398,000	3
1981	2,700,000	109,611,000	2
1982	2,700,000	135,744,000	2

1/ Estimated based on discussion with industry and/or association representatives, and secondary sources.
2/ Based on totaling Commission-estimated foreign revenue for each of the 14 selected industries covered in the study.

Source: Estimated by the staff of the U.S. International Trade Commission.

Regional and country activity

Canada is the predominant market for U.S. franchising firms with international operations. In 1980, nearly 210 U.S. franchising firms (about three-fourths of the total operating in foreign markets) and about 7,200 associated outlets (about a third of all foreign establishments related to U.S. franchising firms) were located in Canada. Nonfood retailing, with more than 1,500 outlets, was the prevalent type of U.S. franchise in Canada, followed by restaurants (1,200) and automotive products and services (1,000). Japan is the second major foreign market for U.S. franchisors. In 1980, about 55 U.S. firms with about 3,400 foreign establishments, or 20 percent of total U.S. firms involved in international franchising and 16 percent of total establishments associated with these firms, operated franchises in Japan. Restaurants predominated in this market with substantial U.S. franchising operations also in food retailing and automobile and truck rental services. Other major foreign markets for U.S. franchisors in 1980 were the United Kingdom (55 franchisors, 2,000 establishments) and Australia (50 franchisors, 1,500 establishments).

The respondents to the questionnaire indicated that most of their activities were in Canada and the Far East. In 1981, of 15 respondents, 11 operated in Canada and 8 operated in the Far East (with 5 each in Australia and Japan) (table 4). Six respondents reported operations only in Canada in 1981.

Trade in Merchandise Generated by Trade in Services

Franchising by U.S. firms in foreign markets generates merchandise trade exports both from the United States and elsewhere. Also, the growth of foreign franchisors imitating the U.S. operations may generate U.S. merchandise exports. U.S. products may be used if possible, but in many cases, foreign-sourced merchandise are used due to the business climate in a particular market. The number of positive responses to a series of questions asked to determine whether or not U.S. merchandise exports are generated by U.S. franchising activities abroad was as shown in the following tabulation:

Question	Number of respondents 1/	Percent of total respondents
Do you believe that U.S. merchandise might be used as a result of the services your firm provides abroad?-----	11	73
Is U.S. merchandise specified or recommended in the course of providing your service?--------------------------	11	73
Are U.S. merchandise exports believed to be directly generated?---------------	8	53

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 71 firms surveyed; respondents represent less than 1 percent of the foreign revenue of the 280 major firms believed to be operating internationally in 1981.

Because of the relatively low response rate to the merchandise trade section of the questionnaire, the Commission is unable to extrapolate with certainty the value of U.S. merchandise exports directly generated by U.S. franchising service activities abroad. However, these industry respondents estimated that their service activities overseas resulted in the total U.S. export of approximately $14 million in goods in 1981 (table 5). On the basis of this estimate, the number of respondents, and the number of known firms in the industry, it is estimated that about $288 million in U.S. merchandise exports flowed as a result of foreign activities of U.S. franchising firms in 1981. However, it should be noted that at a confidence level of 95 percent their figure could be as low as the actual respondents' estimate of $14 million or as high as $742 million. For estimates of U.S. merchandise exports for 1980 and 1982, refer to table 5.

Machinery and equipment was the principal category of U.S. merchandise exported as a result of respondents' foreign franchising activities. Nearly $12 million, or 82 percent of the total 1981 value reported, was in this

Table 4.--Regions and countries in which revenue is generated by franchising service firms, 1980-82 1/

Region and country 2/	Number of responses			Percent of total respondents			Estimated revenue		
	1980	1981	1982	1980	1981	1982	1980	1981	1982
							1,000 U.S. dollars		
Middle East	1	3	1	7	20	7	3/	3/	3/
Bahrain	-	1	-						
Kuwait	-	1	-						
Saudi Arabia	-	2	-						
United Arab Emirates	-	1	-						
Far East	7	8	7	47	53	47	563	594	674
Australia	-	5	-						
Taiwan	-	1	-						
Indonesia	-	1	-						
Japan	-	5	-						
Malaysia	-	1	-						
Philippines	-	2	-						
Thailand	-	1	-						
Latin America	1	3	1	7	20	7	3/	3/	3/
Chile	-	1	-						
Panama	-	2	-						
Europe	2	3	2	13	20	13	3/	3/	3/
Belgium	-	1	-						
West Germany	-	1	-						
France	-	1	-						
Netherlands	-	1	-						
United Kingdom	-	1	-						
Canada	11	11	9	73	73	60	8,747	11,503	11,070
Mexico	2	2	2	13	13	13	3/	3/	3/

1/ Country listing is for 1981 only.
2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 71 firms surveyed; respondents are estimated to represent less than 1 percent of the foreign revenue of the 280 major firms believed to be operating internationally in 1981.
3/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 5.—U.S. merchandise exports generated by U.S. franchising services abroad, 1980-82 1/

Year	Number of responses	Exports of U.S. merchandise estimated by respondents	Projected 2/ total: U.S. merchandise for the service industry	+ 95 percent confidence limit for projected industry exports
		1,000 U.S. dollars		
1980	7	7,501	161,000	226,000
1981	8	14,428	288,000	454,000
1982	7	24,100	517,000	920,000

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 71 firms surveyed; respondents are estimated to represent less than 1 percent of the foreign revenue of the 280 major firms believed to be operating internationally in 1981.
2/ By the U.S. International Trade Commission.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

category; the bulk of exports were data processing equipment. Other machinery and equipment cited was motor vehicles, automotive products, and food service and related equipment (table 6). Chemical and related products (petroleum products, waxes, plastic products) made up most of the remainder of U.S. merchandise exports reported by respondents. Also specified, although very small in value, were processed food, paper products and printed matter, fabric and carpet, and employee uniforms and apparel, and souvenirs.

Foreign establishments of U.S. franchising firms purchase U.S. merchandise for a variety of reasons. First, many formulations and processes of the U.S. franchisor are proprietary in nature and may be required to maintain product integrity. The contract between the U.S. franchisor and the foreign franchisee may specify that U.S. ingredients or equipment must be utilized. This is particularly true in the restaurant and fast-food industry. Technological advantages of certain U.S. equipment may stimulate exports to foreign franchising operations. Also, a general demand for particular U.S. goods in foreign markets may cause such goods to be exported and distributed in the U.S.-affiliated foreign franchise establishments.

Table 6.--Estimated U.S. merchandise exports resulting from franchising services abroad, by types and by principal markets, 1981 1/

Type	U.S. exports used in providing services 2/	Number of firms indicating U.S. merchandise exports to--							
		Middle East	Far East	Central and South America (excluding Mexico)	Europe	Africa	Canada	Mexico	All other
	1,000 U.S. dollars								
Total	14,428	2	3	3	1		6	1	
Machinery and equipment	11,880	1	1	1	1			1	
Food service & related equipment	140		1	1			1		
Motor vehicles	328						1		
Automotive products	200	1	1	1			1		
Data processing (computing) equipment	10,870		1	1	1		1	1	
Agricultural, animal and vegetable products	470	1	1	1					
Processed food	470	1	2	1					
Forest products	26								
Paper products	-								
Printed matter	-								
Textiles, apparel, and footwear	21	1	1	1			1		
Fabric and carpet	21	1	1	1			1		
Chemicals and related products	2,027						1		
Plastic products (serving and storage)	41								
Petroleum products blends	1,816	1	1	1			1		
Waxes and paints	80	1	1	1			1		
Miscellaneous manufactures	4						1		
Souvenirs	4						1		

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 71 firms surveyed; respondents are estimated to represent less than 1 percent of the foreign revenue of the 280 major firms believed to be operating internationally in 1981.

2/ U.S. exports were estimated but respondents could not identify the specific type in all cases; thus, the subcategories do not add to the totals shown.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Foreign merchandise shipments also supply U.S. franchise operations in foreign markets. The number of positive responses to a series of questions asked to determine whether or not host-country or third-country merchandise shipments 1/ are generated by U.S. franchising activities abroad was as shown in the following tabulation:

Question	Number of respondents 1/	Percent of total respondents
Do you believe that foreign merchandise might be used as a result of the services your firm provides abroad?-----	10	67
Are foreign or host-country products specified or recommended in the course of providing your service?--------------	5	33

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 71 firms surveyed; respondents represent less than 1 percent of the foreign revenue of the 280 major firms believed to be operating internationally in 1981.

Estimated third-country and host-country merchandise shipments identified by five questionnaire respondents as resulting from U.S. franchising activities abroad were as shown in the following tabulation:

Item	Value (1,000 U.S. dollars)
Third-country shipments--------------	5,550
Host-country shipments---------------	5,610

Proximity to markets, cost factors, government requirements, demand for foreign merchandise, the nature of the franchise agreement, and the type of franchise operation all determine the scope and magnitude of these foreign-sourced shipments. Significant examples, cited by industry sources, where the entry of U.S. franchising into foreign markets has benefited the economies of the host country or a third country include the creation of employment and new construction in addition to the use of host- or third-country merchandise.

1/"Host-country merchandise shipments" refers to the shipments (within the host country) of host-country-manufactured products which are generated by U.S. service operations in the host-country market. "Third-country merchandise shipments" refers to the shipments of other foreign-manufactured products to a foreign market as a result of U.S. service operations in that market.

International Service Trade Barriers

U.S. franchising firms operate in numerous foreign markets that present a diverse range of conditions and requirements. Impediments do exist that affect all types of U.S. business operations abroad and these may adversely affect the entry or expansion of U.S. franchising firms into certain foreign markets. The industry believes that the effect of impediments has been minimal thus far. The U.S. franchisors' continued expansion of operations into foreign markets suggests that foreign laws and regulations have not severely restricted international business. Specific trade barriers cited by respondents are shown in table 7 and are discussed below.

The full scope of the impediments to international franchising is not known, but selected problem areas have been identified in the United States Trade Representative inventory of service trade barriers. Also, the American Bar Association has published an extensive survey of foreign laws and regulations affecting international franchising. These impediments affect the operational aspects of foreign-located U.S. franchising establishments as well as the ability of U.S. firms to gain access to foreign markets. In many foreign markets, the government limits the payment of licensing fees, royalties, or profits. There may be specific limitations based on percentages, or foreign exchange restrictions may affect the repatriation of fees, royalties, or profits to U.S. franchising firms. Also, administrative procedures may cause delays in the remittance of franchise royalties or fees. Many governments restrict foreign investment and ownership, thus requiring U.S. franchising firms to delegate ownership of their foreign establishments to foreign interests. There are foreign governmental requirements to utilize local resources such as labor, raw materials, and capital goods, which may affect the quality and uniformity of U.S. franchisors' products. In some markets, problems exist concerning copyright and trademark protection, due either to the absence of laws or to ineffective enforcement. A related problem is one of governmental limitations on franchise agreements. If a short-term contract between a U.S. franchisor and a foreign franchisee is mandated and there is inadequate trademark protection, competition may increase due to imitation or counterfeiting. Foreign government-imposed consumer price ceilings or controls may pose difficulties to foreign-located U.S. franchising operations when they require rate increases. And, import controls, health and safety requirements, and industry standards in foreign markets may restrict the use of certain U.S. merchandise that is needed in foreign establishments of U.S. franchising firms to maintain product integrity.

Some laws and requirements affecting U.S. franchisors in certain markets follow: 1/

Canada.--The Foreign Investment Review Act provides for the review of foreign acquisitions and business commencements within Canada in order to determine if any significant benefits will be created. U.S. franchisors may be subject to review under a variety of circumstances. For example, a review may be required if a U.S. franchisor intends to operate company-owned units,

1/ Most of this information was derived from various issues of Current Legal Notes published by the International Franchise Association, and from conversations with industry sources.

Table 7.--Trade barriers to international services in the franchising industry 1/

Category and barrier	Number of responses	Percent of total respondents
Right of establishment	10	67
Restrictive employment regulations (e.g., local labor requirement)	4	
Credit, investment, or financial activity restrictions	4	
Administrative/ownership restrictions	3	
Citizenship/residency requirements	1	
Restrictive government/business regulations	3	
Grandfather clause requiring practice before specified date	1	
Special deposit requirement for foreign companies	1	
Commission terms less favorable than national companies	1	
Trade in goods	5	33
Restrictive regulations or administrative procedure	2	
Local purchase requirements	5	
Restricting entry of equipment or supply	1	
Trade in services	7	47
Restrictive government/business regulations and administrative procedures	3	
Restriction related to resident firm preference (fixed percentage of service must be provided by domestic resident companies)	1	
Employment related restrictions on nonnationals	2	
Operating/ownership restrictions	3	
Discriminatory taxation	3	
Technical issues	6	40
Contract enforcement problems	1	
Time limitations on franchise agreements	4	
Governmental paper requirement	2	
Discriminatory standards requirements	1	
Licensing	3	20
Licensing procedures	2	
Licensing restrictions (e.g., quotas)	2	
Refusal to license or renew	1	
Commercial counterfeiting	6	40
Inadequate patent or trademark enforcement	5	
Unclear definitions of trademark, patent, imported goods, or counterfeit goods	4	

See footnote at end of table.

Table 7.--Trade barriers to international services in the franchising industry 1/--Continued

Category and barrier	Number of responses	Percent of total respondents
Government procurement	3	20
Preference given to national firms	2	
Prohibition of foreign services contracts (bilateral or multilateral)	1	
Other (Blacklisting of certain U.S. firms)	1	
Customs valuation	7	47
Discrimination in customs valuation between computer and data processing services transmitted through a tele-communications system of transferred through physical software products	1	
Discriminatory tariffs and customs procedures	6	
Subsidies/countervailing duties	3	20
Tax benefits (e.g., rebate or tax breaks)	3	
Direct financial aid to local firm by government	1	
Standards/certification	3	20
Health and safety requirements	1	
Origin declaration	1	
Local labor or material requirements	1	
Other (Labeling requirements)	1	
Foreign exchange controls	7	47
Restrictions on remittances	6	
Convertibility limitations	4	
Delays in obtaining foreign exchange permit	4	

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 71 firms surveyed; respondents are estimated to represent less than 1 percent of the foreign revenue of the 280 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

if administrative offices are to be present, or if the U.S. franchisor retains the option to acquire a franchisee-owned establishment upon termination of the franchise agreement. The Foreign Investment Review Agency may require a copy of the franchise agreement, an application, and further business information during its review. Generally, a review is made if a franchisor is to own an establishment, but in some cases even the proposal of a franchisee-owned establishment may attract review.

Antitrust issues in Canada are addressed by the Combines Investigation Act. Most provisions are general, but some are directed at franchising. Certain practices may be interpreted as reviewable offenses subject to review by the Restrictive Trade Practices Commission. The most prominent of these practices are exclusive dealing (when a franchisee is required to deal specific products), tied selling, and market restriction (concerning territoriality). Such activities are usually reviewed after a complaint has been filed. If a review finds the activity lessens competition, the activity must stop. A U.S. franchisor must be careful in constructing a franchise agreement with these factors in mind.

Disclosure is required in the province of Alberta. The Alberta Franchises' Act is generally patterned after U.S. franchise disclosure laws. In addition, a national franchise law is currently under consideration by the Canadian Uniform Law Commission concerning registration, disclosure, termination, and other provisions.

In the province of Quebec, the Charter of the French Language, in effect since 1977, requires that the French language generally be used when conducting business. Therefore, the franchise agreement, trademarks, and other written material may be required to be in French.

Japan.--In Japan, the Foreign Investment Law affects franchise agreements. Any agreement which lasts more than a year must be validated. This applies to each individual agreement and may discourage direct franchising. Most U.S. franchisors in Japan grant master franchises, but the validation of a master franchise agreement may depend on that of any subfranchise agreements.

Operational restrictions also apply to franchising in Japan. Governmental approval is necessary to transfer funds to and from branch offices. Approval would also be necessary for a U.S. franchisor to transfer trademarks, franchise rights, and know-how. Such approval may be contingent on the validation of any franchise agreements involved.

Disclosure is required in Japan under the Retailers Laws; however, the disclosure requirements are less extensive in Japan than in the United States. Another important aspect of any franchise agreement is termination. In Japan, franchise agreements are regarded as continuous contracts. Such contracts are more difficult to terminate than others, and U.S. franchisors must consider this when entering into a franchise agreement in Japan.

In addition to Japanese requirements affecting franchising in general, there are requirements and considerations pertaining to particular sectors. For example, fast-food franchises must be approved by the Ministry of Agriculture, Forestry, and Fisheries. Local approval must also be obtained under the Food Sanitation Act.

United Kingdom.--Registration of franchise agreements may be required by the Office of Fair Trading. There are certain restrictions regarding prices, supply, manufacturing agreements, and other practices. Registration is not necessarily required of a U.S.-based franchisor and exemptions may be available.

The Competition Act of 1980 is concerned with antitrust activities. This act has not generally affected franchising as of yet, but decisions regarding such practices as discriminatory pricing, tied buying, third-line forcing, and others may set precedents that could be applied to franchising in the future.

In addition to United Kingdom antitrust regulations, U.S. franchisors operating in the United Kingdom must comply with those of the European Community (EC), specifically articles 85 and 86 of the Treaty of Rome. However, the EC antitrust laws are intended to supplement member countries' national laws and may not necessarily affect U.S. franchisors.

Australia.--U.S. franchisors operating in Australia must comply with the Trade Practices Act of 1974. This act contains provisions concerning false and misleading advertising, warranties, exclusive dealing, restraint of trade, third-line forcing, and others. For example, third-line forcing is illegal per se, but tied-buying arrangements are not necessarily illegal. Also, a franchisors' limiting a franchisee's suppliers is illegal except in certain cases where quality standards are involved.

Certain local and regional regulations also may affect a U.S. franchisor operating in Australia. Local authorities may be strict on site development. One industry source indicated that in order to build a new establishment in a particular location, a use permit must be obtained to operate the business. Many local governments have been restricting such permits, according to the source, because of an unfavorable perception of the franchise system and of U.S. business interests in Australia. The incidence of this problem varies by location.

Another problem involves attracting prospective franchisees. In the Australian State of New South Wales, any offer of a franchise opportunity constitutes a public offering, and the offering company must be publically owned. There is a possibility that this type of legislation may be introduced at the Federal level.

The remittance of royalties from Australia must be approved by the Australian Reserve Bank, but approval is readily given in most cases.

Mexico.--Market entry into Mexico is difficult for U.S. franchisors. There are numerous laws and regulations regarding foreign business operations in Mexico. These are not targeted at but may affect franchising. The Foreign Investment Law of 1973 prohibits foreign ownership in excess of 49 percent of a new firm's total equity. Also, the majority of management must be national.

Franchising agreements must be registered due to the Transfer of Technology Statute of 1973. Approval by the National Registry of Technology Transfer may be denied under a variety of criteria. These concern royalty payments (rates), contract duration, supply restrictions, whether the technology offered by the U.S. franchisor is available in Mexico, and other criteria.

Also, the Trademark Law of 1976 requires that foreign and Mexican trademarks be linked. U.S. franchisors must register and display or advertise their trademarks along with the Spanish-language equivalents.

Brazil.--Market entry is also difficult in Brazil for U.S. franchisors. All contracts involving transfer of technology, including franchise agreements, must be registered with the National Institute of Industrial Property. There is a limitation on trademark royalties of 1 percent and on knowledge and technique royalties of 1 to 5 percent. There is a time limitation of 10 years on receiving trademark royalties and of 5 years on knowledge and technique royalties. Also, the timelag for trademark registration may take several years, during which time royalties are not payable. A U.S. franchisor may not be allowed to limit a franchisee from using his system after the expiration of the agreement. Other restrictions concern tied buying, designation of certain suppliers, and limiting the franchisee to solely operating the franchise establishment.

Table 7 shows specific trade barriers encountered by respondents to the questionnaire. Barriers were cited in every category except professional qualification restrictions. Most respondents (10) indicated that there were restrictive actions related to the right of establishment, with problem areas in (1) restrictive employment regulations, (2) credit, investment, or financial activity restrictions, (3) administrative/ownership restrictions, and (4) restrictive government/business regulations. Restrictions related to trade in services, customs valuation, and foreign exchange controls were each cited by seven respondents.

The number of responses to a question to determine the economic effects of international barriers to U.S. services trade and associated product exports in franchising activities abroad, was as shown in the following tabulation:

Question	Number of respondents 1/	Percent of total respondents
What effect, if any, would reduction or removal of service trade barriers have upon your receivables, billings, or revenues in current or potential country markets?:		
Increase	9	60
Decrease	0	0
No effect	6	40
What effect, if any, would reduction or removal of service trade barriers have upon potential U.S. products exports in current or potential country markets?:		
Increase	8	53
Decrease	0	0
No effect	7	47

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 71 firms surveyed; respondents represent less than 1 percent of the foreign revenue of the 280 major firms believed to be operating internationally in 1981.

Canada and the Far East, where most U.S. foreign franchising operations are located, were both cited by most respondents as areas where activities would increase. According to the respondents, revenues in Canada would increase by 10 to 50 percent; revenues in the Far East would increase by 10 to 40 percent if current trade barriers were eliminated (table 8).

Respondents indicating that reduction or removal of trade barriers would have a positive effect on U.S. merchandise exports estimated that such exports would increase by 10 to 80 percent for machinery and equipment and by 10 to 50 percent for agricultural, animal, and vegetable products and for textiles, apparel, and footwear (table 9).

Table 8.--Estimated changes in revenues absent trade barriers to international business of franchising service firms, by areas 1/

Area and direction of change	Number of responses	Percentage change						
		10	20	30	40	50	60	80
Middle East:								
Increase	-							
Decrease								
Far East:								
Increase	4	1	2		1			
Decrease								
Latin America:								
Increase	2			1		1		
Decrease								
Europe:								
Increase	-							
Decrease								
Africa:								
Increase	-							
Decrease								
Canada:								
Increase	4	1		2		1		
Decrease								
Mexico:								
Increase	2					1		1
Decrease								
Other:								
Increase	-							
Decrease								

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 71 firms surveyed; respondents are estimated to represent less than 1 percent of the foreign revenue of the 280 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 9.--Estimated changes in U.S. merchandise exports absent trade barriers to international services in the franchising service firms, by types

Type and direction of change	Number of responses	Percentage change						
		10	20	30	40	50	60	80
Machinery and equipment:	3	1		1				1
Increase								
Decrease								
Agricultural, animal, and vegetable Products:								
Increase	3	1			1	1		
Decrease								
Forest products:								
Increase	1					1		
Decrease								
Textiles, apparel, and footwear:								
Increase	3	2				1		
Decrease								
Chemicals and related products:								
Increase	2	1	1					
Decrease								
Minerals and metals:								
Increase	-							
Decrease								
Miscellaneous manufactures:								
Increase	1			1				
Decrease								

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 71 firms surveyed; respondents are estimated to represent less than 1 percent of the foreign revenue of the 280 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

One industry source said that he encountered a barrier in the United States to his foreign franchising operations. A major problem was in training foreigners in the United States. To obtain visas for the trainees, a waiting period of up to 6 months was encountered. This forced the company to consider moving its international operations office overseas, thus adding extra expense to the business and resulting in a loss of foreign exchange to the United States.

Foreign franchising operations in the United States are relatively small in scope, but competition is increasing. Most foreign franchisors in the United States are from Canada, but franchisors from the United Kingdom, Western Europe, and Japan are also entering the U.S. market. Concentration is in the food, retailing, and automotive products franchises. Foreign firms operating in the United States must comply with the same Federal and State regulations and requirements as do U.S. franchisors. For many foreign firms, U.S. disclosure requirements are either new or more comprehensive than in their domestic markets or in other markets. This may also be the case with U.S. antitrust legislation and its application to franchising, and registration requirements, all of which may vary by State. Specific regulations may pose barriers to foreign franchisors in the United States. For instance, the Imperial Group, Ltd., a distiller based in the United Kingdom, encountered difficulties in purchasing Howard Johnson Co. because of certain State laws prohibiting distillers from distributing liquor.

Conditions of Competition in Current and Potential Service Markets

U.S. franchising operations in foreign markets are generally patterned after those in the United States since most are located in countries with similar business environments. U.S. franchising in foreign markets is concentrated in Canada, Japan, and Western Europe--areas that generally possess stable economies with high standards of living that support a strong demand for consumer and business goods and services that are generally offered through the franchise system.

U.S. firms operating franchises in foreign markets generally hold a competitive advantage in that U.S. firms are more experienced in operating under this system and in many cases were first to market their products and services in foreign markets by franchising. Also, consumers in the foreign markets generally have reacted positively to the U.S. franchise concept owing to the previously mentioned factors of product identification, uniformity, and quality control.

There are certain negative aspects of foreign franchising that confront U.S. firms. Cultural resistance to certain products or even to the franchise method may be encountered in certain areas. Operating franchises in distant markets may cause difficulties in controlling trade secrets and maintaining product integrity and effective management control. There is also the possibility of competition arising through imitation.

Management techniques and systems applications have been tailored to the franchise method of operation in the United States and are being used internationally. For example, computerized systems for reservations in the automobile rental and hotel-motel franchising sectors developed by U.S. franchisors gave them a competitive edge in foreign markets by providing an additional service in the form of convenience to their customers. Also, many U.S. franchising firms first developed foreign markets for their products and services and were able to capture the market before foreign competition started. For example, U.S. firms first developed the market in Japan for Western-style fast food franchises. Now, U.S. fast-food franchisors command most of that market.

The major U.S. firms operating franchises in foreign markets tend to be leading firms in the U.S. market, although smaller U.S. franchising firms are also entering the international arena. The latest U.S. Department of Commerce survey indicates that about 150 U.S. franchisors, mostly small- and medium-sized firms, are considering entering foreign markets before 1984. Also, conversations with industry members not yet operating internationally indicated that many of these firms are examining international operations to increase their growth. Most of these firms are involved in business aids and services, restaurant and fast foods, and nonfood retailing.

Foreign franchising operations in the United States are limited relative to the total industry markets, but activity has been increasing. The major foreign firms with franchises in the United States are from Canada and the United Kingdom and mainly operate restaurants and fast-food establishments, clothing and furniture retail establishments, and automotive products and services establishments. According to the U.S. Department of Commerce, 44 foreign firms operated fast food franchises in the United States in 1980, with revenues highest in establishments owned by citizens of the United Kingdom, West Germany, Switzerland, Canada, Japan, and France. Major foreign firms franchising in the United States have often acquired existing U.S. franchises. Imasco, Ltd., a Canadian firm involved with tobacco, drug retailing, and packaged foods (and 49 percent owned by the British American Tobacco Co. of the United Kingdom), recently fully acquired Hardee's Food Systems. 1/ Imasco then acquired (through Hardee's) Burger Chef from General Foods. 2/

J. Lyon and Co., Ltd., of the United Kingdom, owns Baskin-Robbins and Tastee-Freeze. Also, as mentioned earlier, Howard Johnson Co. was recently acquired by Imperial Group, Ltd., a large United Kingdom distiller. Travelodge International, a hotel/motel chain, is owned by Trusthouse Forte, a United Kingdom lodging and foodservice conglomerate.

There is potential for U.S. franchising firms to expand into undeveloped foreign markets. In many developing areas, such as South America, the Middle East, and Asia, incomes are rising as is the demand for goods and services which may be marketed through the U.S. franchise method. U.S. firms may have an advantage for certain goods and services in certain markets due to reputation and demand for particular U.S. brands or trademarks. One industry source said that his company has received requests from several Asian countries to operate in their markets. However, in order to successfully expand their foreign business opportunities, U.S. franchising firms must develop market information in potential markets and work with foreign governments to reduce any barriers to their operations.

The competitive environment of U.S. franchising companies in foreign markets can be characterized based on a number of insights provided by questionnaire respondents. Respondents to the Commission's questionnaire indicated that foreign competition outside of the United States was, by far,

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1/ "Imasco: Canadian policy sparks a sally into U.S. drugs and fast food," Business Week, Apr. 20, 1981, pp. 64-69.

2/ Feedstuffs, Mar. 15, 1982, p. 53.

greatest in Canada, with Canadian regional firms most prevalent (table 10). Table 11 gives the perceptions of the respondents to the questionnaire of their competitive strengths in foreign markets. Most of the respondents felt that superior quality associated with their firm or base country (i.e., the United States) was a definite competitive strength. Greater experience in the market or in the service area, and a lead in technology were the other major competitive advantages. Table 12 shows anticipated competitive strengths in the respondents' potential foreign markets. Again, superior quality was the most cited advantage, followed by greater experience and advanced technology.

Table 10.--Number of firms competing 1/ with U.S. franchising firms abroad, by principal service markets 2/ in order of revenue generated, 1981 3/

Service market	Number of competing firms				
	Total	National	Regional	World-wide	Other U.S. firms
Japan	17	5	1	10	1
Canada	454	43	400	5	6
Panama	6	2		4	
Australia					
United Arab Emirates	4	1		3	

1/ Based on 7 responses by questionnaire respondents.

2/ Other principal service markets for the industry may not be listed here if rerespondents did not identify the number of competing firms.

3/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 71 firms surveyed; respondents are estimated to represent less than 1 percent of the foreign revenue of the 280 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 11.--Likely reasons 1/ for the competitive strength of U.S. franchising firms in foreign service markets 2/

Service market	Lower price	Technology lead	Financial strength	Experience in the market or service	Superior quality association	Other
Middle East:						
United Arab Emirates				1	1	
Far East:						
Australia		1		1	2	1
Japan		1		2	2	
Central and South America (excluding Mexico):						
Panama		1		1	2	
Europe:						
France	1			1	1	1
North America and Mexico:						
Canada	1	3	1	5	6	1
Total	2	6	1	11	14	3

1/ The importance of each reason is indicated by the number of times each was designated, based on 7 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 71 firms; respondents are estimated to represent less than 0.5 percent of the foreign revenue of the 280 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 12.--U.S. franchising service firms' competitive strengths 1/ in potential foreign markets 2/

Potential service market	Lower price	Technology lead	Financial strength	Greater experience	Superior quality	Other
Middle East:						
Bahrian				1	1	1
Saudi Arabia		1		1	1	1
Far East:						
Australia		1			1	1
New Zealand		2		1	2	
Thailand				1	1	1
Central and S. America (excluding Mexico):						
Brazil						1
Peru				1	1	1
Europe:						
United Kingdom					1	
Africa:						
South Africa		1		1	1	
N. America and Mexico:						
Mexico		1			1	
Total		6		6	10	6

1/ The importance of each reason is indicated by the number of times each was designated, based on 5 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service was 15 of 71 firms surveyed; respondents are estimated to represent less than 1 percent of the foreign revenue of the 280 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

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Health Services

Executive Summary

1. International revenues for U.S. investor-owned or investor-managed hospitals are estimated to have been $600 million in 1981.

2. Industry respondents to the Commission's questionnaire estimated that their health services activities overseas resulted in merchandise exports of approximately $56 million. The origin of the hospital project architect will largely determine the source of manufactured goods. It is typical for new hospital construction in foreign countries to lead to considerable U.S. exports of construction materials, supply inventories, appliances for the hospital and associated housing, and ancillary items including food and luxury items for use of the U.S. workers. In addition, foreign hospitals run by U.S. hospital management companies (HMCs) generally purchase U.S.-made equipment and systems for the initial supply of these hospitals.

3. Eighty percent of the questionnaire respondents indicated that host- or third-country merchandise shipments might be generated as a result of U.S. health service activities abroad. Industry respondents to the questionnaire estimated that over $19 million of such shipments were generated in 1981, believed to consist principally of pharmaceuticals, medical supplies, and equipment. Contracts with foreign construction firms to build hospitals, and employment of foreign nationals to staff hospital facilities were cited as benefits to the economies of these countries resulting from the entry of U.S. health services into foreign markets.

4. Trade barriers most frequently cited by questionnaire respondents were in the areas of right of establishment, trade in services, and standards/certification. More specifically, ownership restrictions, restrictions on repatriation of profit, import restrictions, delays in government approval for projects, and labor restrictions on U.S. personnel were cited.

5. Despite the number of foreign trade restrictions identified by industry sources as affecting the sector, their overall impact on the total volume of foreign trade appears to be minimal. Only one-fifth of all respondents felt service revenues or U.S. merchandise exports would increase if all barriers were removed.

6. Until recently, U.S. HMC's have encountered virtually no foreign competition outside of the Middle East. In the Middle East, competition has become intense because of the availability of petrodollars, and most of the competition has been from the British. U.S. HMC's are beginning to face increased competition in the Third World from companies organized within the host countries and from other developed countries.

7. U.S. health service firms point out that competing foreign firms often obtain a competitive advantage in international activity as a result of the significant support by their respective embassy or consular personnel in identifying commercial opportunities, facilitating procedural requirements, and providing leads on potential international projects.

8. One respondent indicated that the likely reasons for the success of foreign competing firms in world health services markets are government support and preferential financing.

9. Questionnaire respondents indicate the success of U.S. firms in foreign markets stems primarily from greater experience in providing health services and from their reputation for quality service.

Industry Profile

Definition and coverage

Health services as defined for purposes of this profile are limited to hospitals (Standard Industrial Classification (SIC) 806), because it is within this segment of the overall health care industry (SIC 80) that the most significant opportunities lie for U.S. firms to provide health services in foreign countries. In general, hospitals are establishments primarily engaged in providing diagnostic services, extensive medical treatment including surgical services, and other services. These establishments have an organized medical staff, inpatient beds, and equipment and facilities to provide complete health care. General medical and surgical hospitals are engaged primarily in providing general medical and surgical services and other hospital services. Psychiatric hospitals are engaged primarily in providing diagnostic medical services and inpatient treatment for the mentally ill. Specialty hospitals are engaged primarily in providing diagnostic services, treatment, and other hospital services for patients with specified types of illnesses, except mental. 1/

The firms covered in the Commission's survey are investor-owned firms that offer health care services in foreign markets and are believed to account for almost all the companies offering health care services outside the United States. The five health services industry respondents to the Commission's questionnaire represent about 75 percent of the foreign revenues of the seven health services firms surveyed and believed to be operating internationally in 1981.

1/ Office of Management and Budget, Standard Industrial Classification Manual 1972, p. 332.

Highlights in 1981

- o DOMESTIC EXPENDITURES for hospital care amounted to $112 billion.
- o U.S. ESTABLISHMENTS included 7,000 hospitals of which about 1,300 were investor-owned and investor-managed hospitals. The other 5,700 hospitals were owned and operated either by government entities or nonprofit organizations.
- o U.S. EMPLOYMENT by the hospital industry is estimated to have been about 4 million.
- o INTERNATIONAL REVENUE for U.S. investor-owned or investor-managed hospitals is estimated to have been $600 million.
- o FOREIGN ESTABLISHMENTS of U.S. investor-owned or investor-managed hospitals totaled 43 with 8 additional hospitals under construction.
- o FOREIGN EMPLOYMENT by U.S. investor-owned or investor-managed hospitals is estimated to have been 20,000.
- o U.S. TRADE BALANCE is believed to be positive based upon the limited operations of foreign health services firms in the United States.

Industry structure

U.S. hospital structure.--Within the United States basically four types of hospitals exist--Federal hospitals operated by the Federal Government, non-Federal Government hospitals operated by State or local governments, voluntary nonprofit hospitals operated by churches or other nonprofit organizations, and proprietary hospitals operated by individuals, partnerships, or corporations for profit.

Comparative data on hospital statistics illustrate some important trends. 1/ For example, the total number of hospitals declined 4 percent during 1974-79, from 7,370 in 1974 to 7,085 in 1979, whereas the total number of hospital beds declined 6 percent. That is, a substantial (34 percent) reduction in long-term hospital beds offset an increase in the number of short-term hospital beds. The large decrease in long-term hospital beds was, for the most part, the result of the use of more effective drugs in the treatment of mental illnesses and of tuberculosis. Growth in the number of proprietary hospital beds was greater than the increases in other types of short-term hospital bed ownerships. This indicates that the investor-owned hospitals are offering hospital care at competitive or lower cost than other types of ownership.

1/ U.S. Department of Health and Human Services, Health United States-1981, December 1981, pp. 183, 192.

Domestic hospital care expenditures increased from $34 billion in 1972 to $76 billion in 1978 and soared to an estimated $112 billion in 1981. 1/ This enormous and rapid increase in hospital care expenditures was, and is, straining individual, private, and government reimbursement programs and has led to various cost containment initiatives. Within this environment, hospital-management companies (HMCs) have flourished. The structure of these firms is discussed in the following sections.

Hospital-management company structure.--Organizationally, most HMCs are structured like other investor-owned corporations. It is, however, through their operational structure that HMCs have had the greatest impact on the hospital industry. The advent of the provision of management services as well as the consolidation of proprietary hospitals marked the beginning of hospital-management companies. Simply stated, HMCs apply mass-merchandising principles typical of retail chains or franchised business to hospital operations. These techniques include large-volume purchasing of hospital supplies, and centralized, computerized, and standardized procedures for billing, purchasing, and operations. HMCs also manage numerous hospitals in many locations and thereby obtain economies of scale not available to most single-unit hospitals. 2/

The HMCs offer their services in several ways. The larger HMCs have purchased or built proprietary hospitals. In many instances old hospitals were refurbished and reequipped with modern medical equipment and facilities. In addition to managing and operating hospitals owned by them, most HMCs operate hospitals on a contract basis for other owners, such as State and local governments. 3/ The remainder of the discussion will concentrate on the operations of profit-oriented HMCs. The domestic operations of the HMCs provide them with the revenue, financial resources, and basic organizational infrastructure necessary for international operations.

International hospital structure.--In general, all hospitals provide both diagnostic and treatment services for patients with a variety of medical conditions, both surgical and nonsurgical. On a world basis, hospital structure is much like that in the United States in terms of hospital ownership or administration, except in those countries under central government control such as the People's Republic of China and the U.S.S.R. Excluding U.S. hospitals, there were approximately 200,000 hospitals listed by the United Nations World Health Organization in 1980, of which about 64,000 were located in the People's Republic of China and about 24,000 were located in the U.S.S.R. 4/

Of the approximately 112,000 world hospitals (other than U.S. hospitals and those located in the People's Republic of China and the U.S.S.R.), 46,000 (41 percent) were designated as being under government administration, and

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1/ U.S. Department of Commerce, 1982 Industrial Outlook, January 1982, p. 406.

2/ William Harris, "Running a Hospital is No Different from Running a Store," Forbes, Sept. 29, 1980, pp. 105-109.

3/ "The Money in Curing Hospitals," Business Week, June 25, 1979, pp. 56, 62.

4/ World Health Organization, World Health Statistics 1980, 1980, pp. 18-119.

11,000 (10 percent) were designated as proprietary hospitals. The remaining 55,000 hospitals (49 percent) were either nonprofit hospitals or were undesignated as to type of administration.

According to industry sources, the world hospital care system is structured around two basic models. The British model is physician oriented in that most management decisions are made by physicians, and all financial needs are met by a national health service funded by the government. This system has been said to require no accountability as to delivery cost and there is no knowledge of what the health care dollar is paying for and no systematic way of evaluating the quality of the service provided. The American model is one in which professional managers are responsible for overall hospital operations, and this type of management is said to require individual accountability and a cost-conscious approach reflected in the operation of hospitals, which would include accounting and personnel departments. A comparative measure of success was cited by the 300 to 400 hospitals developed from scratch by U.S. health services firms, whereas the British national services haven't built more than five new facilities in the past 10 years.

U.S. hospital operations abroad.--There are currently about seven domestic HMCs that account for most U.S. health services activities in foreign countries. These firms own or manage 43 hospitals with approximately 6,200 beds in countries other than the United States. Three or four of them account for over 90 percent of the foreign health services business done by U.S. firms. Domestic and international revenue ($22.6 billion) for the investor-owned health services industry accounted for about 3 percent of total U.S. service sector trade valued at $837 billion in 1981 for the 14 service industries covered in this study.

Recent trends and outlook

Cost-containment considerations and new treatments have slowed the growth in numbers of domestic hospitals and hospital beds, whereas domestic growth of HMCs has been increasing because of their basic operating premise of providing excellent hospital facilities and care, often at a reduced cost. The number of U.S. hospitals owned or operated by all investors increased from about 1,300 in 1980 to about 1,325 in 1981, and the number of U.S. hospitals owned or operated by HMCs increased from about 800 in 1980 to about 900 in 1981. 1/ The number of all U.S. hospitals has declined from 7,340 in 1974 to an estimated 7,000 in 1981. Domestic hospital care expenditures in investor-owned or investor-operated hospitals are estimated to have been $18.8 billion in 1980, $22.0 billion in 1982, and are projected to be $25.6 billion in 1982.

Movement of domestic HMCs into international operations and expansion of foreign operations of the HMCs have been increasing rapidly. The concensus among several company representatives in the international field is that U.S. health care expertise, both technical and managerial, is the best in the world

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1/ Federation of American Hospitals, 1982 Director Investor-Owned and Hospital Management Companies, 1982, pp. 6-32.

and as a result is highly sought after. As an example, one industry source noted that Australia has asked the firm to assist in determining how much it costs to deliver health care in certain areas of the country. The U.S. expertise and service capability did not exist 10 to 15 years ago and, according to industry sources, cannot be duplicated outside the United States. Foreign competition consists mainly of government-supported consortiums put together for a specific purpose. An example cited by the industry is a big push by foreign competition to provide computerized hardware, but not the systems infrastructure and health management technology which provides the competitive edge for the U.S. firms.

Growth rates of 20 to 50 percent per year have been suggested by firms in the health services industry. The growing demand overseas for health care services is also reflected in the worldwide health care budget which, according to discussions with industry representatives, in real terms is one of the three or four largest industries as measured by share of gross national product, or its equivalent, for each country. In 1981, foreign revenue for the health services industry is estimated to have increased about 50 percent, from $400 million in 1980 to $600 million in 1981. This accounted for less than 1 percent of total service sector foreign revenue of $109.6 billion estimated for the 14 selected service industries covered in the Commission's study.

According to discussions with industry representatives, a significant development, which will affect business in the health care sector over the next 10 years, is recognition of the need for efficiency in health care delivery. Because every country faces the problem of limited resources and higher costs, this will require management technology which exists now in the United States, but which can be relatively quickly transferred to foreign countries. The significant advantage that the United States now holds will gradually disappear, industry sources believe.

Another development is that disease patterns throughout the world are changing. As rudimentary health care is provided through immunizations, improvements in sanitation, and the development of new drugs, there is a corresponding increase in need for care of advanced diseases that need high-technology health care which is found only in hospitals or similar health care facilities.

Domestically, the birth rate decreased 39 percent during 1955-78 and, during the same period, life expectancy increased to a record 73 years. 1/ Therefore, since the demand for health care services is a function of age, there is a trend of increasing demand on the U.S. health care system. 2/

1/ U.S. Department of Health and Human Services, Health United States - 1980, December 1980, pp. 17, 23.

2/ U.S. Department of Health and Human Services, Health United States - 1981, December 1981, p. 15.

U.S. Service Operations in Foreign Markets

Operating structure

Three major aspects of international health care services are service contracts to manage hospitals for foreign governments, development projects to construct and manage foreign hospital facilities, and ancillary services ("unbundled services") which includes bits and pieces of technology required to operate and to train personnel. The HMCs use traditional methods to operate in foreign markets which include foreign affiliates, joint ventures, or the establishment of a subsidiary or branch.

Industry sources indicate that a typical organization structure in international operations is a joint venture (U.S./foreign) to build a local business with U.S. management and systems technology; many foreign countries require this joint venture arrangement when a non-national firm is involved. This is advantageous to the U.S. firms which are capital intensive and need the financing, and want the local physicians as part of the service package; however, U.S. antitrust laws are a matter of concern, as pointed out under the section on international barriers.

Firms submitting information for this study, as shown in table 1, characterized their operating structures in foreign health services as subsidiaries or branches, joint ventures, or foreign affiliates. Operating structure is perhaps best illustrated by examples of the foreign operations of some of the larger domestic HMCs. Of the five U.S. HMCs responding to the Commission's questionnaire, four firms primarily characterize their foreign operations as subsidiaries or branches, one as a foreign affiliate, and one as a joint venture. The following information was obtained, for the most part, from the annual reports of the various firms and discussions with industry representatives.

One of the largest of the U.S. HMCs made its entry into the foreign health services market with the signing of an agreement to manage a 250-bed hospital in Saudi Arabia. Since then, the firm has signed a managment contract to operate an additional 100-bed hospital in that country. In addition, the firm has acquired 10 hospitals in Australia which it operates, and it operates two hospitals and related health care facilities in Brazil. This firm also has a managment contract for a 150-bed hospital in Panama.

Another domestic HMC entered the foreign market through the purchase of a hospital in the United Kingdom. Subsequently the firm purchased another hospital in the United Kingdom and has acquired hospitals in Switzerland and Mexico. According to company representatives, this firm is cautious with regard to international operations. Equity investments are sought only in those locations where the firm feels the climate for free enterprise is favorable, and where the firm can make a reasonable return on its investment.

Table 1.--Operating structures of principal service activity and revenues associated with secondary service industry activities of health service firms in foreign markets, 1981 1/

Item	Revenues	Number of responses	Percent of total respondents
	1,000 U.S. dollars		
Operating structure:			
Foreign affiliate	-	1	20
Joint venture	-	1	20
Subsidiary or branch	-	4	80
Secondary service activity:			
Consulting and management services	2/	1	20

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 5 of 7 firms surveyed; respondents represent about 75 percent of the foreign revenue of the 7 major firms believed to be operating internationally in 1981.

2/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

The first U.S. HMC to enter the international market has now established a branch office in the United Kingdom. By 1981, this firm had opened six hospitals in the United Kingdom and had three more under construction. The firm also owns a 100-bed hospital in Switzerland, and manages 1 hospital in France and 1 in Spain. Outside of Europe, the firm owns and operates 2 hospitals in Australia and is constructing a 146-bed hospital in Singapore. In Egypt, the firm is managing a 300-bed hospital and, in Latin America, it is managing construction of a 120-bed hospital in Brazil and a 150-bed hospital in Ecuador. The firm has a contract to open and manage a 355-bed hospital in Saudi Arabia.

One of the four largest domestic HMCs just entered the foreign health care market in 1980 but, nevertheless, has developed a substantial amount of contract health care business in Saudi Arabia. The firm also acquired the foreign operations of another HMC which included five hospitals in Australia and several management contracts in Europe and the Middle East.

As shown in table 2, foreign operations account for a small fraction of the revenue of investor-owned or investor-operated health services firms. Of total estimated industry revenue of $22.6 billion in 1981, foreign operations accounted for an estimated $600 million. The respondents to the Commission's questionnaire represent firms that account for about 20 percent of the total industry revenue and for about 75 percent of the foreign revenue in 1981. The data show a 32-percent increase in foreign revenues from 1980 to 1981. Reporting firms projected a foreign revenue increase of 18 percent for 1982.

Table 2.--Indicators of activity in the foreign and domestic operations of health service firms, 1980-82

Item	Foreign	Domestic	Total
Estimated value of receivables, billings, or revenues: 1/ 2/			
1980------------------1,000 dollars--	336,141	3/	3/
1981----------------------------do----	444,384	3/	3/
1982----------------------------do----	525,800	3/	3/
Estimate of investment in physical assets 1/ 4/ in foreign operations:			
1980------------------1,000 dollars--	3/	-	-
1981----------------------------do----	3/	-	-
1982----------------------------do----	3/	-	-
Number of establishments: 1/			
1980-----------------------------------	25	3/	3/
1981-----------------------------------	30	3/	3/
1982-----------------------------------	32	3/	3/
Estimated 5/ value of total industry receivables, billings, or revenues:			
1980------------------1,000 dollars--	400,000	18,800,000	19,200,000
1981----------------------------do----	600,000	22,000,000	22,600,000
1982----------------------------do----	700,000	25,600,000	26,300,000

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 5 of 7 firms surveyed; respondents represent about 75 percent of foreign revenue of the health services firms believed to be operating internationally in 1981.
2/ Excluding the value of any merchandise exports.
3/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.
4/ Including the undepreciated book value of land, plant, and equipment.
5/ By the staff of the U.S. International Trade Commission based on discussions with industry and/or association representatives, and secondary sources.

Source: Compiled from data submitted in response to questionnaries of the U.S. International Trade Commission.

Scope of operations

As shown in table 3, the health services foreign revenue is a small part (less than 1 percent) of total foreign revenues from services activities. Domestic HMCs are in a position to offer an extremely broad scope of health services. These services can range from a simple management contract for a single hospital to the management of all aspects of the construction and operation of major hospital complexes. Such services can include assistance in site selection, design of hospitals, construction management, equipment procurement and installation, staffing, training, and day-to-day operations of hospitals and related facilities.

Table 3.--Estimated total foreign revenue generated by the health services industry and estimated total foreign revenue for selected service industries, 1980-82

Year	Total foreign revenue for service industry 1/ (1)	Total foreign revenue for selected service industries 2/ (2)	Ratio of (1) to (2)
	1,000 U.S. dollars		Percent
1980	400,000	89,398,000	3/
1981	600,000	109,611,000	3/
1982	700,000	135,744,000	3/

1/ Estimated based on discussion with industry and/or association representatives, and secondary sources.
2/ Based on totaling Commission-estimated foreign revenue for each of the 14 selected industries covered in the study.
3/ Less than 1 percent.

Source: Estimated by the staff of the U.S. International Trade Commission.

A major portion of U.S. health services activities is bringing foreign facilities up to U.S. technology levels. Once an HMC has been granted a contract, it is difficult and expensive to switch to a company from a different country after major capital investment has been made to purchase U.S. medical equipment and knowhow. Therefore, the initial contract is very critical to perpetuation of the service. The selection of either the U.S. or British model has a major impact on scope of operations.

Regional and country activity

As discussed in the section on operating structure, most of the foreign activity of U.S. HMCs is concentrated in Europe (mostly the United Kingdom), the Middle East (mostly Saudi Arabia), Australia, and Central and South America. These activities are summarized in table 4.

Table 4.--Regions and countries in which revenue is generated by health service firms, 1980-82 1/

Region and country 2/	Number of responses			Percent of total respondents			Estimated revenue		
	1980	1981	1982	1980	1981	1982	1980	1981	1982
							------1,000 U.S. dollars------		
Middle East	2	3	2	40	60	40	3/	3/	3/
Saudi Arabia	-	2	-						
Far East	1	1	1	20	20	20	3/	3/	3/
Australia	-	1	-						
Latin America	2	2	2	40	40	40	3/	3/	3/
Brazil	-	1	-						
Colombia	-	1	-						
Europe	3	3	3	60	60	60	3/	3/	3/
United Kingdom	-	3	-						

1/ Country listing is for 1981 only.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 5 of 7 firms surveyed; respondents represent about 75 percent of the foreign revenue of the 7 health services firms believed to be operating internationally in 1981.

3/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Most of the growth in revenues received by the U.S. HMCs has resulted from the increased value of service management contracts awarded to the U.S. HMCs in the Persian Gulf countries, particularly from Saudi Arabia. In contrast, foreign capital investments by the U.S. HMCs have been concentrated outside of the Persian Gulf in countries where the U.S. HMCs have been permitted to own hospitals in part or totally. The U.S. HMCs have recently committed major amounts for capital investment in England, Switzerland, Brazil, Venezuela, and Singapore.

Trade in Merchandise Generated by Trade in Services

The relationship of health service activity in foreign markets and U.S. merchandise exports can be characterized based on a number of insights provided by questionnaire respondents. The number of positive responses to a series of questions asked to determine whether or not U.S. merchandise exports are generated by U.S. health service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
Do you believe that U.S. merchandise might be used as a result of the services your firm provides abroad?-----	3	60
Is U.S. merchandise specified or recommended in the course of providing your service?---------------------------	3	60
Are U.S. merchandise exports believed to be directly generated?--------------	3	60

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 5 of 7 firms surveyed; respondents represent about 75 percent of the foreign revenue of the 7 major firms believed to be operating internationally in 1981.

Because of the relatively low response rate to the merchandise trade section of the questionnaire, the Commission is unable to extrapolate with certainty the value of U.S. merchandise exports directly generated by U.S. health services activities abroad. However, these industry respondents estimated that their service activities overseas resulted in the total export of approximately $56 million in goods in 1981 (table 5). On basis of this estimate, the number of respondents, and the number of known firms in the industry, it is estimated that about $77 million in U.S. merchandise exports flowed as a result of U.S. international health services activities in 1981. However, it should be noted that at a confidence level of 95 percent this figure could be as low as the respondents' estimate of $56 million or as high as $128 million. For estimates of U.S. merchandise exports for 1980 and 1982, refer to table 5.

Table 5.—U.S. merchandise exports generated by U.S. health services abroad, 1980-82 1/

Year	Number of responses	Exports of U.S. merchandise estimated by respondents	Projected 2/ total: U.S. merchandise for the service industry	+ 95% percent confidence limit for projected industry exports
		1,000 U.S. dollars		
1980	4	42,200	59,080	53,370
1981	4	56,241	77,168	72,338
1982	3	53,350	74,830	77,068

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 5 of 7 firms surveyed; respondents represent about 75 percent of the foreign revenue of the 7 major firms believed to be operating internationally in 1981.

2/ By the U.S. International Trade Commission.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

The greatest value of merchandise exports is generated when domestic HMCs are building and equipping new foreign hospitals, or refurbishing old ones. Such exports can occur when the HMCs are building hospitals owned by them, or when they have management contracts to equip or reequip hospitals. Most of the exports are related to medical instruments and equipment such as X-ray machines, surgical equipment, and other medical appliances. There was also an indication by respondents that a significant portion of equipment exports, principally X-ray and electromedical equipment, are considered to be high-technology products; 1/ respondents reported that 50 to 100 percent of services-related-product exports in 1981 consisted of high-technology items. There are, and this varies from firm to firm, also exports of consumables such as drugs, routine hospital supplies, and even food and luxury items for the use of foreign-based U.S. workers. Specific types of U.S. merchandise exports resulting from health service activities abroad are shown in table 6.

1/ High technology encompasses items of a high unit value, relative to the product field, and representing the leading edge of new technology with clear and superior performance characteristics.

Table 6.--Estimated U.S. merchandise exports resulting from health services abroad, by types and by principal markets, 1981 1/

Type	U.S. exports used in providing services	Number of firms indicating U.S. merchandise exports to-- Middle East	Far East	Central and South America (excluding Mexico)	Europe	Africa	Canada	Mexico	All other
	1,000 U.S. dollars								
Total	56,241	2			2				
Machinery and equipment	16,811	2			1				
X-ray and electromedical equipment and supplies	2,581	2			1				
Data processing (computing) equipment	9,130	2							
Office machines and equipment	100	1							
Vehicles	5,000	1							
Agricultural, animal and vegetable products	5,000	1							
Food beverages	5,000	1							
Forest products	600	1							
Paper products	500	1							
Printed matter	100	1							
Textiles, apparel, and footwear	700	2			2				
Fabric and carpet	150				2				
Woven (disposable) products	200	1							
Nonwoven (disposable) products	200	1							
Institutional linens	150	2							
Chemicals and related products	7,950	2			1				
Drugs and related products	5,500	2							
Medical specialities (plastic sutures, etc.)	2,180	2			1				
Cleaning compounds	120	2							
Soaps and detergents	100	1							
Sponge, rubber and plastics products	50	1							
Minerals and metals	100	1							
Scientific and laboratory glassware	100	1							
Miscellaneous manufactures	25,080	2			2				
X-ray and electromedical equipment	2,350	1							
Surgical appliances and supplies	7,000	2							
Dental equipment and optical instruments	1,000	2							
Ophthalmic goods and optical instruments	1,000	2							
Furniture and fixtures	2,730	2			2				
Medical supplies, etc	8,000	1							
Surgical and medical instruments and apparatus	3,000	1							

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 5 of 7 firms surveyed, based on 4 responses. Respondent represents about 75 percent of the foreign revenue of the 7 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

The number of positive responses to a series of questions asked to determine whether or not host-country or third-country merchandise shipments 1/ are generated by U.S. health service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
Do you believe that foreign merchandise might be used as a result of the services your firm provides abroad?----	4	80
Are foreign or host-country products specified or recommended in the course of providing your service?-------------	3	60

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 5 of 7 firms surveyed; respondents represent about 75 percent of the foreign revenue of the 7 major firms believed to be operating internationally in 1981.

Estimated third-country (2 responses) and host-country (3 responses) merchandise shipments resulting from U.S. health services abroad in 1981 were as shown in the following tabulation:

Item	Value (1,000 U.S. dollars)
Third-country shipments--------------------	13,000
Host-country shipments---------------------	6,353

Specific examples, cited by industry sources, where the entry of U.S. services into foreign markets has benefited the economies of the host country or a third country include the purchase of pharmaceuticals, medical supplies, and equipment primarily from European countries; employment of foreign nationals required to staff and operate hospital and psychiatric facilities; and a multimillion dollar contract with a European firm to construct a building for a new hospital in Europe.

1/ "Host-country merchandise shipments" refers to the shipments (within the host country) of host-country-manufactured products which are generated by U.S. service operations in the host-country market. "Third-country merchandise shipments" refers to the shipments of other foreign-manufactured products to a foreign market as a result of U.S. service operations in that market.

International Service Trade Barriers

Trade barriers resulting from U.S. imposed restrictions

Certain U.S. laws have been cited by HMC representatives as constituting a barrier to foreign trade expansion as well as a competitive handicap, since foreign competitors are not subject to equivalent restrictive legislation.

The Foreign Corrupt Practices Act (FCPA), in particular, was cited by HMC representatives as constituting a severe barrier to foreign trade expansion. Allegedly, in many Third-World countries, money commonly passes to government officials or other influential people to receive government favors including contracts. Because of the law's ambiguity in distinguishing between commissions, minor gifts, and bribes, the FCPA has been blamed for the failure of U.S. HMCs to gain entry in a number of less developed countries (LDC's), including Indonesia, Nigeria, and various Latin-American countries. Even in countries where U.S. HMCs are currently very active, such as in Saudi Arabia, the FCPA was cited by one HMC representative as being the major reason why the company failed to obtain more contracts. Moreover, the FCPA, by requiring investigations of local agents (required in many countries including Saudi Arabia) caused considerable strain between the U.S. HMC and the local agent.

U.S. antiboycott laws, primarily aimed at preventing U.S. companies from complying with the Arab boycott of Israel, were also cited by several HMC representatives as constituting a barrier to foreign trade expansion. Some Arab countries have been inflexible in their demand that U.S. companies must not comply with U.S. antiboycott laws. The result has been that no U.S. HMC can expect to gain entry in those countries. One industry representative estimated that the loss of only one of these countries as a market could eventually cost U.S. HMC's up to a billion dollars in lost revenue. Other Arab States have been more tolerant in their handling of U.S. antiboycott laws. However, these laws can create problems for HMCs in their dealing with even these more moderate Arab countries. An HMC, for example, that has inadvertently put language in a contract that does not meet the fine legal distinctions required by even moderate Arab States may find itself losing a contract.

U.S. antitrust laws have been cited by some industry representatives as inhibiting foreign expansion because joint ventures, required to be competitive in certain foreign markets, could be challenged in court as violating the antitrust acts. The dubious legality of such joint ventures inhibits foreign expansion because it prevents HMCs from sharing financing costs and other risks.

Problems stemming from the uncertainty of the U.S. laws are often worse than the laws themselves in preventing U.S. companies from expanding overseas business. U.S. HMCs, at a considerable cost, must abandon some potential enterprises and monitor their business practices to assure that they are not violating U.S. laws. The cost of complying with U.S. laws in Saudi Arabia alone has been estimated to be about a half-million dollars a year for one HMC.

Another problem that was cited by many HMC representatives as having significantly inhibited U.S. expansion possibilities was U.S. tax laws. The

United States is the only country, outside of the Philippines and North Korea, that taxes its citizens on income earned while working abroad. In order not to price themselves out of the market, U.S. HMCs have been, in many cases, forced to preferentially hire non-Americans for many positions overseas. The recently revised tax laws which exempt U.S. citizens from paying income taxes on money earned abroad, if they earn $75,000 or less, are expected to lead to a marked increase in the employment of U.S. personnel overseas by U.S. HMCs. This should help the growth of U.S. HMCs which is largely dependent on their ability to provide trained American personnel. In spite of the changes in U.S. personal income tax laws, HMC representatives still believe that U.S. tax laws handicap U.S. HMCs competitively since U.S. taxes on U.S. corporations operating overseas are said to be higher than that for any other country.

Trade barriers resulting from restrictions imposed by the host country

Restrictions imposed by the host country were cited by HMC representatives as constituting a barrier to foreign trade expansion. Specific barriers identified by companies responding to the questionnaire are shown in table 7 and discussed below.

Ownership restrictions were viewed to be a problem for HMCs operating in Latin America, Australia, and Canada. However, ownership restrictions have not caused serious problems for U.S. HMCs operating in Europe. In the Persian Gulf, although ownership by foreigners is prohibited, U.S. HMCs have not encountered serious problems because their operations have been profitable as a result of management contracts. Although many HMCs would be willing to accept foreign commitments involving either ownership or management contracts, there was a general reluctance for certain U.S. HMCs to become involved in a situation where they would have to make major investments without having majority ownership. In the case of Mexico, minority ownership was viewed as being more acceptable than in other countries since the Government of Mexico permits the U.S. HMC to retain full operational control.

Another concern frequently cited by HMC representatives involved restrictions on repatriation of profits. These restrictions were viewed as causing serious problems for the HMCs in Latin America and parts of Asia. Repatriation of profits restrictions were not viewed as a problem in the Persian Gulf, Southeast Asia, or Europe. Several U.S. HMC representatives indicated that they had considered setting up hospitals in Brazil and India but were dissuaded because of restrictions on repatriation of profits. These restrictions often do not represent a problem in the initial period of setting up a health facility in a foreign country since initial profits are often either small or absent and the U.S. HMC usually is intent on investing more funds in the host country anyway. However, repatriation of profit restrictions often become a problem for the HMC when profits have increased and further major investments in the host country are not contemplated.

Table 7.--Trade barriers to international services in the health industry 1/

Category and barrier	Number of responses	Percent of total respondents
Right of establishment	5	100
Restrictive employment regulations (e.g., local labor requirement)	4	
Credit, investment or financial activity restrictions	1	
Administrative/ownership restrictions	4	
Entry of service personnel and specialized tools	2	
Citizenship/residency requirements	4	
Restrictive government/business regulations	3	
Trade in goods	2	40
Restrictive regulations or administrative procedure	1	
Restricting entry of equipment or supply	3	
Trade in services	3	60
Restrictive government/business regulations and administrative procedures	3	
Restriction related to resident firm preference (fixed percentage of service must be provided by domestic resident companies)	1	
Employment related restrictions on nonnationals	3	
Operating/ownership restrictions	3	
Discriminatory taxation	1	
Prohibition on services offered by nonresident companies	1	
Government procurement	1	20
Preference given to national firms	1	
Shipment restricted to National flag carriers partially or completely	1	
Customs valuation	1	20
Discriminatory tariffs and customs procedures	1	
Subsidies/countervailing duties	2	40
Direct financial aid to local firm by government	2	
Preferential financing arrangements	1	
Standards/certification	3	60
Health and safety requirements	1	
Origin declaration	1	
Local labor or material requirements	2	

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 5 of 7 firms surveyed; respondents represent about 75 percent of the foreign revenue of the 7 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Import restrictions were also cited by several HMC representatives as representing a barrier to foreign trade expansion in circumstances where a similar product was produced in the host country or sold by local representatives. Problems have arisen when the item produced in the host country (which was often an item representing a low or an intermediate level of technology such as an operating table) was of inferior quality or sold by an importer who was unreliable in getting shipments delivered on time. In Australia, the import fee for a U.S. item that was also manufactured in the host country has been about 30 percent of assessed value, whereas in Mexico the import fee has reportedly been much higher. In Saudi Arabia, where there is no significant home industry manufacturing medical supplies, problems arose in importing computers used for medical purposes because of the presence of a local, and reportedly unreliable, importer of computers.

Ameliorating the effects of these restrictions, to some extent, has been a willingness by the host country to modify or even rescind restrictions when requested by the U.S. HMC. An Australian Government order requiring a U.S. HMC operating in Australia to divest itself of 35 percent of equity within 3 years was postponed when the U.S. HMC persuaded the Australian Government that their business would suffer. A high import fee imposed by the Mexican Government on electrical hospital beds was rescinded when the U.S. HMC persuaded the Mexican Government that the imported electric hospital beds were required if the high quality of medical service being provided was to be maintained.

Other trade barriers that have been encountered by U.S. HMCs, especially in developed foreign countries, include difficulty and delay in getting government approval for health-care-related projects and labor restrictions imposed on U.S. personnel. In Australia, for example, a U.S. HMC could employ only four U.S. employees. In certain countries, these restrictions were made more severe as a result of governmental policies that sought to discourage growth of private health care facilities.

A barrier that was ubiquitously cited by HMC representatives involved the difficulty they faced in getting through red tape, particularly in Saudi Arabia. One HMC representative stated that his company's greatest problem is a requirement by certain host countries that the HMC must operate as a local rather than as a U.S. company. This represented a problem because losses suffered during the entry period could not be declared as tax losses by the parent company. Some countries have explicitly imposed restrictions on investor-owned hospitals. In Japan, investor-owned hospitals are banned outright, making it virtually impossible for an HMC to enter that market. In West Germany, legislation severely restricts the ability of investor-owned hospitals to expand operations. Although there may be ways to get around that law, the restrictive legislation has made it very difficult for investor-owned hospitals in the recent past to enter the West German market.

Political barriers can be one of the most important obstacles to foreign trade expansion. HMCs had to abandon operations in Lebanon and Iran because of internal political upheavals. Tensions between the U.S. Government and Libya caused the HMC operating there to decide to withdraw from that country although relations between the HMC and the host government were good. Discord between the Government of Egypt and patrons from the Persian Gulf countries as a result of Egypt's signing of the Camp David Agreement reportedly forced a U.S. HMC to postpone plans for a major hospital project in Egypt. 1/ 2/

One of the most subtle types of barrier encountered has been caused by cultural differences between U.S. citizens and those of other countries. Hospital management techniques must often be modified before they can be applied to a hospital located outside of the United States. In Europe, for example, HMCs may find it virtually impossible to fire employees or to hire part-time help. In the Middle East, HMCs must instruct their staff on the special requirements for working in Moslem countries, especially on the tradition requiring strict separation of the sexes. In Japan, the idea of operating hospitals for profit is so alien that a U.S. HMC representative believes that it would be virtually impossible for an HMC to attract either physicians or patients.

Despite the number of foreign trade restrictions identified by industry sources as affecting the health services sector, their overall impact on the total volume of foreign trade appears to have been rather minimal. The number of responses to a question to determine the economic effects of international barriers to U.S. services trade and associated product exports in health service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
What effect, if any, would reduction or removal of service trade barriers have upon your receivables, billings, or revenues in current or potential country markets?:		
Increase	1	20
Decrease	0	0
No effect	4	80
What effect, if any, would reduction or removal of service trade barriers have upon potential U.S. products exports in current or potential country markets?:		
Increase	1	20
Decrease	0	0
No effect	3	60

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 5 of 7 firms surveyed; respondents represent about 75 percent of the foreign revenue of the 7 major firms believed to be operating internationally in 1981.

1/ "Royce Diener: Crusader for Profitable Private Hospital," World Business Weekly, May 4, 1981, p. 21.
2/ According to conversations with industry representatives.

Overall there appears to be very little effect of reducing existing barriers; however, one firm reported information which indicates that the reduction or removal of barriers could increase revenues by 20 percent in the Far East and 10 percent in the Middle East and Latin America, and increase U.S. exports of medical-related equipment 10 percent or more in various manufacturing sectors (tables 8 and 9).

Table 8.--Estimated changes in revenues absent trade barriers to international business of health service firms, by areas 1/

Area and direction of change	Number of responses	Percentage change						
		10	20	30	40	50	60	80
Middle East:								
Increase	1	1						
Decrease								
Far East:								
Increase	1		1					
Decrease								
Latin America:								
Increase	1	1						
Decrease								
Europe:								
Increase	-							
Decrease								
Africa:								
Increase	-							
Decrease								
Canada:								
Increase	-							
Decrease								
Mexico:								
Increase	-							
Decrease								
Other:								
Increase	-							
Decrease								

1/ Data for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 5 of 7 firms surveyed, based on 1 response; respondents represent about 75 percent of the foreign revenue of the 7 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 9.--Estimated changes in U.S. merchandise exports absent trade barriers to international business of health service firms, by types 1/

Type and direction of change	Number of responses	Percentage change						
		10	20	30	40	50	60	80
Machinery and equipment:								
Increase	1			1				
Decrease								
Agricultural, animal and vegetable products:								
Increase	1	1						
Decrease								
Forest products:								
Increase	1	1						
Decrease								
Textiles, apparel, and footwear:								
Increase	1	1						
Decrease								
Chemicals and related products:								
Increase	1	1						
Decrease								
Minerals and metal products:								
Increase	1	1						
Decrease								
Miscellaneous manufactures:								
Increase	1	1						
Decrease								

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 5 of 7 firms surveyed, based on 1 response; respondents represent about 75 percent of the foreign revenue of the 7 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Conditions of Competition in Current and Potential Service Markets

During the course of this study only one foreign-owned HMC was identified as operating in the United States. The firm is a closed corporation under U.S. law and, therefore, no financial data are available from public sources. Industry sources, however, indicated that the firm's U.S. operations are quite small in comparison with the foreign operations of U.S. HMCs.

U.S. health services industry has been well suited to meet foreign competition for a number of reasons. The U.S. hospital management company as it developed in the United States was designed to provide an extremely wide range of health-care-related services, from overall hospital management to specific medical services (unbundled services), and has also proven an ideal vehicle to meet the needs of the foreign health care market as well. No foreign country has developed the infrastructure that could compete with the U.S. HMCs outside of the home country. In addition, the U.S. HMCs' expertise has been based largely on the professionalism of the hospital manager, a profession that is relatively unknown outside the United States. In Europe, members of the medical profession manage hospitals and other health services facilities. These physician managers are reportedly not as skilled as the U.S. hospital managers in dealing with management problems that arise in health facilities. As an example, U.S. HMC representatives report that no foreign consortium could match the U.S. HMC in turnaround time required to make a hospital operational in Saudi Arabia.

Foremost among the management resources developed by U.S. HMCs is a worldwide network of recruiting facilities. Making extensive use of the computer, a U.S. HMC is able to recruit health personnel at all levels of responsibility from North America, Europe, the Middle East, and Southeast Asia.

U.S. HMCs also have a competitive edge in those countries in which the U.S. Government has a special relationship, especially those involving extensive commercial or military relations between the United States and the host country. These commercial or military relations have naturally lead to numerous contacts between American businessmen and foreign government officials and businessmen. Reportedly, these personal contacts have proven essential in a number of cases for laying the groundwork for a health care contract. 1/

Perhaps the greatest competitive advantage enjoyed by U.S. HMCs operating overseas, according to industry representatives, is derived from the outstanding reputation that American medical techniques have acquired throughout the world. Particularly significant are the quality and sophistication of U.S. medical instrumentation and the rigorous quality control that U.S. medical techniques are subject to, especially for acute care.

The expansion of U.S. HMCs into the foreign market has not been without problems. U.S. HMCs are facing increasingly stiff competition from foreign governments or foreign consortia that are government sponsored and financed. Foreign markets that initially appeared to offer security and high profits at times offered neither. Governments that had initially welcomed the U.S. HMCs have on occasion become indifferent or even hostile. U.S. regulations adopted to ensure fair trade often exacerbated the problems facing the U.S. HMCs in the foreign market, with benefit to the foreign competition.

According to industry representatives, probably the most formidable competitive disadvantage faced by U.S. HMCs in the foreign market has been their inability to match the financing terms offered by the foreign competitors. The French have reportedly taken away contracts from U.S. HMCs in Latin America because they have been willing to finance at rates as low as 3 percent. Several HMC representatives expressed the view that some nations including Korea, Japan, and Bangladesh will be undercutting the U.S. technology advantage with government financing and advantageous labor costs.

1/ Thomas W. Lippman, "Firm's Success Linked to Prominent Saudis," The Washington Post, Apr. 7, 1982, pp. D7-D8.

In the Persian Gulf and Southeast Asia, financing disadvantages have not yet become a serious problem for the HMCs because those countries that are negotiating health service contracts have the ability to do their own financing. Some industry representatives have expressed concern, however, that as many of these countries take on increased budgeting commitments, they will also be apt to award health care contracts to those companies or consortia that offer advantageous financial terms.

Allegedly, foreign consortia involved in health care services exports have many other advantages over the U.S. HMCs in the foreign markets because they are government financed and sponsored. For example, during contract negotiations a foreign consortium is often represented by a prestigious government official, who may be far more influential than the representative of the U.S. HMC competing for the same contract. The British, for example, have sent the Prime Minister on a mission to Saudi Arabia to help secure health services contracts. 1/ Foreign consortia do not have to be concerned about requirements mandated by most countries requiring guarantees of performance or utilization of advanced payments since the home government offers insurance at reduced rates to meet those contingencies.

Industry sources point out that they cannot leverage the seed money for the up front project development fund hurdle (generally about $250,000) financed by competing governments. This preliminary financing is a critical competitive factor in gaining contracts. U.S. firms absorb this to the extent feasible to remain competitive, but availability of up front money could increase international business substantially (tenfold by one estimate).

The United States has recently attempted to alleviate some of these competitive disadvantages that U.S. companies operating overseas have faced. Industry sources point out that the U.S. Department of Commerce and the United States Trade Respresentative have been responsive in trying to ensure that during contract negotiations in the international market, the U.S. company is represented by a U.S. Government official who is on the same level as the government official representing the foreign competitor. The U.S. Overseas Private Investment Corp. insures letters of credit required by LDC's at a reasonable rate. 2/ Some HMC representatives believe, however, that certain U.S. Government agencies have shown relatively little interest in helping the U.S. HMCs expand international operations, reportedly because these agencies have not been sufficiently aware of the important role that U.S. HMCs can play not only in promoting U.S. business abroad but also in promoting international goodwill toward the United States. The Agency for International Development (AID), for example, was viewed by HMC representa- tives as structured to favor low-overhead firms which allegedly do not have the experience to implement successful health care systems. If the difficulties with AID could be overcome, HMC representatives believe it could assist in preliminary funding to open up other foreign market opportunities.

1/ Paul Chesseright, "UK Win 150 Million Pound Hospitals Package from Saudi Arabia," Financial Times, May 26, 1981, p. 4.

2/ "Third World Giving U.S. Business a Better Break Abroad," Business Week, Aug. 3, 1981, p. 39.

U.S. HMC representatives further point out that even when the U.S. Government has been solicited by various Third-World countries to help contract out health care services, that U.S. Government commercial personnel have often shown relatively little concern or attention in facilitating procedural requirements, and in providing the necessary assistance to assure that U.S. firms are afforded an equal opportunity to foreign competitors in securing the health services contracts offered. Frequently, industry representatives claim that when a foreign country wants health services from a U.S. firm, it takes a major effort to process a request for bid through the U.S. Government. After U.S. firms expend time and money to bid on contracts, then the U.S. Government opens the bidding worldwide. As a result, industry members assert that the existence of preferential financing places the U.S. firms at a clear competitive disadvantage.

In addition to direct competitive pressures, U.S. HMCs face other problems in attempting to expand or even maintain foreign operations. Many of the contracts negotiated with Third World governments have fixed terms. Extension or renewal of these contracts requires renegotiations in which the host government rigorously attempts to receive better terms. A contract can be lost if the U.S. HMC refuses to accept the new terms offered by the host government. Another problem cited by industry sources in providing international health services is the great sensitivity in the Third World to royalty agreements and licensing procedures. There is a significant reluctance to utilize management services and often a bias against technology transfer. For example, industry points out that a substantial competitive problem exists in Mexico to acquiring the necessary technology to develop hospital facilities as well as some other segments of the economy. Representatives indicated the solution requires government-to-government arrangements to assure needed understanding.

Competitive posture of U.S. HMCs operating in the foreign market

In spite of the advantages enjoyed by the foreign consortia, U.S. HMCs have made remarkable progress in expanding foreign operations since entering the foreign health care market in 1970. Although competition from foreign governments or foreign consortia has become increasingly intense, the U.S. HMCs continue to hold a predominant share of the health care market.

Until recently, U.S. HMCs have encountered virtually no foreign competition outside of the Middle East. In the Middle East, competition (as shown in table 10) has become intense because of the great availability of petrodollars. Reportedly, a hospital management contract in Saudi Arabia could easily pay up to 10 times as much as an equivalent contract outside of the Persian Gulf area. It is to be expected that this much money could lure numerous suppliers of health care hoping for a contract. Likely reasons for competing firms' success in world health services markets cited by one respondent to the Commission's questionnaire are government support and preferential financing (table 11).

Most of the competition encountered in the Middle East by U.S. HMCs has come from the British. In Saudi Arabia, probably the largest importer of health services, the British hold about 25 percent (in terms of dollar value) of the health services contracts awarded to foreign governments or companies

Table 10.--Number of firms competing 1/ with U.S. health services firms abroad, by principal service markets 2/ in order of revenue generated, 1981 3/

Service market	Number of competing firms				
	Total	National	Regional	World-wide	Other U.S. firms
Brazil	5	5	-	-	-
Australia	5	3	-	-	2
North Yemen	10	-		2	8
Saudi Arabia	25	5	-	10	10
United Arab Emirates	2	-	-	-	2

1/ Based on 2 responses by questionnaire respondents.

2/ Other principal service markets for the industry may not be listed here if respondents did not identify the number of competing firms.

3/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 5 of 7 firms surveyed; respondents represent about 75 percent of the foreign revenues of the 7 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 11.--Likely reasons 1/ for competing firms' success in world health service markets, by base countries of firms 2/

Base country	Lower price	Technology expertise	Preferential financing	Experience in the market or service
France				
Jordan			1	
United Kingdom			1	
United States	1			
Total	1		2	

Base country	Superior quality association	Political or regional bias	Government support	U.S. restrictions
France		1	1	1
Jordan			1	1
United Kingdom		1	2	2
United States				
Total		2	4	4

1/ The importance of each reason is indicated by the number of times each was designated, based on one response.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 7 firms surveyed; respondents represent almost 60 percent of the foreign revenue of the 10 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

in 1981, valued at about $200 million. In contrast, U.S. HMCs hold about 70 percent of the contracts awarded, worth more than $500 million. A predominantly goverment-owned British company provides about half of the hospital management services provided by the British in the Middle East. In spite of the fact that this firm is predominantly government owned, it is unique among European providers of health care in the Middle East in that it often acts independently of the British Government. The firm has even competed with the British Government for health care contracts. The British HMC is similar to U.S. HMCs in that it is a relatively unified and stable organization that offers a wide range of medical services.

The remainder of the health care contracts serviced by the British in the Middle East are obtained through direct government-to-government negotiations. These health care services are provided by a consortium of British companies that are organized on an ad hoc project-to-project basis that is typical of European health care services provided in the Middle East. According to HMC representatives, these consortia are handicapped because they lack a sense of organization and stability.

In addition to the U.S. and foreign HMCs, such as the British Government, other governments including those of France, Denmark, Sweden, Spain, and the government on Taiwan have been seeking health care contracts in the Middle East, with the Danes, the Swedes, and the people of Taiwan, having achieved some degree of success. The people of Taiwan, for example, staff a 500-bed hospital in Saudi Arabia and reportedly charge only about 20 percent of the rate that a U.S. HMC would charge. Prospects for expansion of operations by Taiwan in the foreign health care market appear limited according to industry sources, however, because most countries in the Middle East prefer Western medical know-how. Industry analysts also believe that the expansion projects for other European countries in the health care market in the Middle East are limited because those countries have not demonstrated sufficient sensitivity in reacting to different cultures. Outside of the Middle East, U.S. HMCs have encountered virtually no competition from foreign companies or governments seeking to export health services until very recently. The French Government, perhaps in response to the fact that there is a surplus of physicians in France, has long been active in the field of hospital construction and has recently begun to seek health services contracts in Panama, Trinidad, and Malaysia.

In addition to competition from foreign governments exporting health care services, U.S. HMCs are beginning to face increased competition in the Third World from companies organized within the host countries. In Saudi Arabia, for example, in response to the success of foreign companies, a 100-percent Saudi company has been formed which hires Westerners to staff and manage hospitals. In the case of Saudi Arabia, the need for more and improved health care services is so great that U.S. HMCs will also probably expand operations and receive increased revenues despite increased local and foreign competition. Industry sources estimate that U.S. HMCs could receive several billion dollars a year in revenues from Saudi Arabia within less than 10 years. One HMC representative believes however, that as local participation increases, HMC revenues from Saudi Arabia will begin to taper off in about 5 years. Likely reasons for the competitive strength of U.S. health service firms in foreign service markets will continue to be their extensive experience and superior quality association, as noted by respondents to the Commission's questionnaire (tables 12 and 13).

Industry spokesmen believe that in the long run, U.S. HMCs operating in the Third World must prepare for the inevitable increased involvement of local enterprises in health care services by organizing joint ventures. U.S. HMCs will be less conspicuous but will be playing a key role in providing backup support for the local enterprises. The skill with which the U.S. HMCs can satisfy the growing demand within the Third World for medical services and also provide for increased local participation will determine, to a large extent, the future of U.S. health service exports.

Table 12.--Likely reasons 1/ for the competitive strength of U.S. health service firms in foreign service markets 2/

Service market	Lower price	Technology lead	Financial strength	Experience in the market or service	Superior quality association
Middle East:					
North Yemen--------				1	1
Saudi Arabia-------		1	1	2	2
United Arab Emirates---------					
Europe:					
Australia----------		1	1	1	1
Central and South America (exclud- ing Mexico):					
Brazil-------------		1	1	1	1
Colombia-----------				1	
Europe:					
United Kingdom-----		1	1	2	1
Other--------------		1	1	1	1
Total------------		5	5	10	8

1/ The importance of each reason is indicated by the number of times each was designated, based on 4 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 5 of 7 firms; respondents represent about 75 percent of the foreign revenues of the 7 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 13.--U.S. health service firms' competitive strengths 1/ in potential foreign markets 2/

Potential service market	Lower price	Technology lead	Financial strength	Greater experience	Superior quality
Africa:					
Egypt				1	1
Morocco				1	1
Middle East:					
Saudi Arabia		1	1	1	1
Far East:					
Malaysia		1	1	2	2
Europe:					
Spain		1	1	1	1
United Kingdom		1	1	1	1
N. America and Mexico:					
Mexico		2	2	2	2
Total		6	6	10	10

1/ The importance of each reason is indicated by the number of times each was designated, based on 3 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service was 5 of 7 firms surveyed; respondents represent about 75 percent of the foreign revenue of the 7 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

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Hotel and Motel Services

Executive Summary

1. International revenue for U.S. hotel/motel operations is estimated at $2.3 billion for 1981.

2. Respondents to the Commission's questionnaire indicated that their U.S. merchandise exports generated from their hotel/motel operations overseas were approximately $18 million in 1981. The bulk of these exports were for items such as (1) machinery and equipment; (2) furniture and fixtures; and (3) agricultural products.

3. All questionnaire respondents indicated that host- or third-country merchandise shipments might be generated as a result of U.S. hotel and motel service activities abroad. Such shipments were estimated by one respondent firm to be $120 million in 1981.

4. Among the nontariff measures cited as hampering operations of U.S.-based firms, the most frequently enforced restrictions pertain to employment regulations. Other barriers are delays in obtaining foreign exchange permits, restrictions on payments, extensive paperwork required by the government to import merchandise, and credit and investment restrictions.

5. In response to Commission questions, all respondents indicted that the removal of barriers to trade in services would result in increased U.S. exports of related products. Three out of four respondents also indicated that foreign revenue would increase by a range of 40 to 80 percent in Latin America, Canada, and Mexico if the service trade barriers were reduced or removed.

6. U.S. firms experience wide-ranging competition from foreign firms; however, the success of U.S. firms is borne out of the fact that 7 out of 10 major hotel/motel chains operating worldwide are U.S. based. As a result, a considerable amount of the competition that U.S. firms face in foreign countries is from other U.S. firms.

7. Questionnaire respondents indicate that foreign firms' success in foreign markets, such as West Germany, the United Kingdom, and Canada, is attributed to lower prices, preferential financing, political and regional bias, and to a lesser extent, experience in the market.

8. According to questionnaire respondents, the competitive success of U.S.-based hotel/motels in both domestic and foreign markets is due primarily to its financial strength, reputation for quality, and superior marketing abilities.

Industry Profile

Definition and coverage

The hotel/motel service industry, a vital part of the tourism industry, is listed under Standard Industrial Classification (SIC) 7011. This SIC group covers all commercial establishments known as hotels, motels, motor hotels, and tourist courts which are open to the general public on a seasonal or year-round basis. These establishments provide lodging and may provide meals, entertainment, and other services. SIC 7011 does not include rooming and boarding houses (SIC 7021), trailor space and camping facilities (SIC 7032 and 7033), hotels and lodging houses that are used on a membership basis (SIC 7041), and residential facilities such as children's homes and rest homes (SIC 8361). 1/

The U.S. hotel/motel industry generates revenue primarily by its operations under management contracts and franchise agreements. The firms surveyed in the hotel/motel service industry for the Commission's study consist largely of those firms which generate foreign revenues through management contract operations; those hotel/motel firms which primarily employ franchising in foreign operations were surveyed as part of the franchising service industry. Information describing the general nature of franchise agreements (SIC 6794) is covered in the franchising industry report of this Commission study. Specific aspects of hotel/motel franchising are discussed here because of the importance of the franchise method of operation to this service industry and the lack of response to the Commission questionnaires by hotel/motel franchise companies.

The four hotel/motel service firm respondents (of the 7 surveyed) to the Commission's questionnaire represent almost 60 percent of the foreign revenues of the 10 hotel/motel corporate service firms believed to be operating internationally in 1981.

Highlights in 1981

- DOMESTIC SALES were estimated at $26.4 billion.
- U.S. ESTABLISHMENTS with payroll are estimated to be 55,000.
- U.S. EMPLOYMENT is estimated at 1.1 million.
- INTERNATIONAL REVENUES for U.S. hotel/motel operations are estimated at $2.3 billion.
- FOREIGN ESTABLISHMENTS for approximately 40 U.S. hotel/motel chains have been constructed.
- U.S. TRADE BALANCE for the hotel/motel industry is positive given the relatively few foreign hotel/motel operations in the United States.

1/ U.S. Department of Commerce, Monthly Selected Services Receipts, January 1981, p. 1.

Industry structure

Most U.S. hotel/motel firms are privately owned and operated; however, those that generate the bulk of revenue are generally publicly held companies that operate through management contracts and franchise agreements. Currently, management contracts and franchise agreements are preferred by the hotel/motel industry as opposed to total ownership/joint ventures because each method of operation provides company identification and provision of specialized services, but requires no major capital investment in the facility.

Management contracts are agreements made by hotel management companies or hotel chains with hotel owners/investors to manage their hotel for certain financial considerations. Industry sources have indicated that the standard management contract is usually 5 percent of gross sales plus 10 percent of operating profit and generally runs 20 to 25 years, with options to extend for a longer term.

A hotel/motel franchise is a contractual agreement made between the hotel/motel chain or parent company (franchisor) and the hotel/motel owners/investors or franchise holders (franchisee). The franchisor receives an initial fee and a percent of gross room sales from the franchisee for the right to use the franchisor's services. It is the responsibility of the franchisee to provide the physical facility and to maintain satisfactory operating standards and quality control as required by the franchisor. The services provided by the franchisor to the franchisee generally includes trade name, collective purchasing (i.e., for furniture, fixtures, towels, stationary), national advertising support, reservation services, and other related considerations. Most hotel/motels, both domestic and international, that use the company name are franchised units. 1/ On the other hand, some facilities operated through management contracts do not bear the U.S. corporate name.

The major factors determining whether a management contract or franchise agreement is to be used by a hotel/motel firm are the location and size of the facility, the management capabilities of the investor, and the need of the owner/investor. Industry sources have indicated that generally the larger facilities (400 rooms or more) located in heavily traveled tourist and commercial areas, and which require more sophisticated management, are operated under management contracts.

Services typically offered by hotels and motels include sleeping accommodations; food and beverage facilities; telephone, laundry, and postal services; and in some instances conference rooms, recreational facilities, entertainment, and specialized food operations. However, the larger metropolitan areas that generally receive a large number of foreign travelers may also offer additional services such as currency exchange, travel agent facilities, and language assistance.

1/ Standard & Poors, "Continued Profit Growth Anticipated;" Industrial Survey, Sept. 10, 1981, p. 19.

From 1980 to 1981, the U.S. hotel/motel industry increased its total revenue by an estimated 10 percent, from $24 billion to $26.4 billion. 1/ Total sales for this industry were distributed among three areas: (1) lodging sales represented 60 percent, (2) food and beverage sales were 35 percent, and (3) other sales, which include telephone and laundry, were 5 percent. 2/ Domestic and international revenue ($28.7 billion) for the hotel/motel service industry accounted for about 3.4 percent of total U.S. service trade, valued at $837 billion in 1981 for the 14 service industries covered in this study.

Recent trends and outlook

A most significant recent trend affecting the domestic and international operations of the U.S. hotel/motel industry is the increasing emphasis on catering to foreign travelers. Until recently, foreign travelers in the United States have experienced difficulties in exchanging foreign currencies and obtaining language assistance. In order to overcome these problems many domestic hotel/motels in the larger metropolitan areas are providing currency exchange services and are hiring public relations specialists with foreign language abilities. These international services have been provided by some foreign hotel/motel firms for many years. By adding these services, U.S. hotel/motels can better serve the foreign travelers.

Industry growth is largely characterized by many of the larger hotel/motel chains expanding in both economy lodging and the luxurious, full service facilities. Several hotel/motel chains now offer three levels of accommodations: (1) luxury, which caters to the more affluent traveler; (2) deluxe, which generally caters to the business traveler and offers limited amenities; and (3) economy, which caters to travelers that simply want a place to sleep for the night. Many hoteliers have found that the traveler seeking luxury accommodation are increasing in number, despite the current recession. Most new construction is taking place in higher traffic downtown and airport locations. Industry sources have reported that the airport hotel division is now the fastest growing sector and that occupancy rates are 15 percent higher than for those in other locations. 3/

An economic factor that has been having an adverse impact upon this industry is inflation, which has resulted in rapid increases in costs for transportation, restaurant meals, and lodging. 4/ In addition, business travelers (traditionally accounting for 60 percent of room occupancy in hotel/motels) have become extremely conscious of controlling costs and have scaled back travel expenditures. Further, to better utilize their time many of these businesses are increasingly relying on communication devices, such as conference calling programs, high-speed telex, and teleconferencing, in lieu of travel.

1/ John M. Keeling, "The Lodging Industry and the Economy: A Status Report," May 14, 1982, pp. 1 and 16.

2/ Laventhol and Horwath, U.S. Lodging Industry, 1981, p. 29.

3/ Silvia Porter, "Airport Hotels Growing Into Major Industry," Washington Post, Sec. D., Feb. 9, 1982, p. 13.

4/ "U.S. Lodging Industry: Today and Tomorrow," Lodging Hospitality, December 1981, p. 40.

Additional developments expected to affect competitiveness within the U.S. hotel and motel industry in the next few years include expansion of telecommunication systems for referrals and reservations, a shift from total ownership to franchise agreements and management contracts, increases in the prestige and amenities available in hotel/ motels (e.g., the all-suite concept), extension of the total service concept (e.g., 24-hour valet and room service), and creation of different levels of price and service within a hotel/motel chain. By adding these services, the competitive posture of the U.S. industry will be improved, both domestically and internationally, by allowing them to effectively compete against foreign hotel/motel chains that already employ many of these new developments.

U.S. Service Operations in Foreign Markets

The operating structure for U.S. hotel/motels in foreign markets is similar to that in the United States. The foreign operations follow four distinct patterns: (1) direct ownership; (2) leasing of foreign-owned property; (3) franchise agreements; and (4) management contracts. According to industry spokesmen, the latter two account for the majority of operations. U.S.-based firms are shifting away from total ownership because of (1) political uncertainty, which could result in hotel/motel facilities being expropriated; (2) unpredictable exchange rates; and (3) the nontariff barriers placed on U.S.-owned operations abroad, particularly employment practices and currency restrictions. There are advantages for both the foreign investor and the U.S. hotel/motel operation when engaging in franchise agreements and management contracts. The advantage to foreign owners is that their facility remains under local capital control while gaining U.S. prestige and management skills. The benefits gained by the U.S. hotel/motel operation include no capital outlay and no risk of ownership in politically unstable areas.

U.S. management contract operations are in strong demand internationally because travelers recognize U.S. hotel/motel names and associate these names with high-quality, reliable services and facilities. In 1980, of 10 major hotel chains that operated worldwide, 7 were U.S.-based. 1/ Industry sources have reported that U.S.-operated hotel/motels are leaders in this industry and have a competitive advantage internationally because of more advanced marketing and service techniques which enable them to attract wealthy clientele that they intend to serve.

During 1981, international revenues from U.S.-based firms totaled $2.3 billion, or about 9 percent of total U.S. revenue from the hotel/motel industry. 2/ The first international market venture taken by a U.S. chain was to Puerto Rico in 1949. Industry sources have reported that since that time approximately 40 U.S. hotel/motel chains have moved overseas. Industry sources have also indicated that by 1990, international revenues may increase to as much as 20 percent of total U.S. revenue because of the long-range trend toward increased travel to Europe where most U.S.-based foreign establishments are located. The increased travel to Europe is a result of increased foreign vacation travel and increased worldwide business operations there.

1/ "Joining the Big League," The Economist, Dec. 27, 1980, p. 53.
2/ Estimated by the U.S. International Trade Commission staff.

As set forth in table 1, questionnaire respondents indicated that the operating structures of hotel/motel firms in foreign markets were primarily subsidiaries or branches (including management contracts) and joint ventures, and to a lesser extent they were operated under franchising and licensing arrangements. According to questionnaire respondent's data in table 2, the estimated value of foreign revenue will increase by 10 percent, from $1.29 billion in 1980 to $1.41 billion in 1982. The number of foreign

Table 1.--Operating structures of principal service activity, and revenues associated with secondary service industry activities of hotel and motel service firms in foreign markets, 1981 1/

Item	Revenues	Number of responses	Percent of total respondents
	1,000 U.S. dollars		
Operating structure:			
Foreign affiliate	-	1	25
Joint venture	-	2	50
Licensing	-	1	25
Subsidiary or branch	-	4	100
Franchising	-	1	25
Other	-	1	25
Secondary service activity:			
Franchising	2/	1	25

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 7 firms surveyed; respondents represent almost 60 percent of the foreign revenue of the 10 major firms believed to be operating internationally in 1981.

2/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 2.--Indicators of activity in the foreign and domestic operations of hotel and motel service firms, 1980-82

Item	Foreign	Domestic	Total
Estimated value of receivables, billings, or revenues: 1/ 2/			
1980------------------1,000 dollars--:	1,285,860	3,011,654	4,297,514
1981----------------------------do----:	1,339,384	3,594,629	4,934,013
1982----------------------------do----:	1,412,807	4,127,404	5,540,311
Estimate of investment in physical assets 1/ 3/ in foreign operations:			
1980------------------1,000 dollars--:	521,015	-	-
1981----------------------------do----:	651,120	-	-
1982----------------------------do----:	700,177	-	-
Number of establishments: 1/			
1980-----------------------------------:	361	1,898	2,259
1981-----------------------------------:	374	1,901	2,275
1982-----------------------------------:	428	1,899	2,327
Estimated 4/ value of total industry receivables, billings, or revenues:			
1980------------------1,000 dollars--:	2,100,000	24,000,000	26,100,000
1981----------------------------do----:	2,300,000	26,400,000	28,700,000
1982----------------------------do----:	2,530,000	29,000,000	31,530,000

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 7 firms surveyed; respondents represent almost 60 percent of the foreign revenue of the 10 major firms believed to be operating internationally in 1981.

2/ Excluding the value of any merchandise exports.

3/ Including the undepreciated book value of land, plant, and equipment.

4/ By the staff of the U.S. International Trade Commission based on discussions with industry and/or association representatives, and secondary sources.

Source: Compiled from data submitted in response to questionnaries of the U.S. International Trade Commission.

establishments will increase by almost 20 percent, from 361 in 1980 to 428 in 1982. Throughout the 1980-82 period foreign revenue from the hotel/motel industry will account for about 2 percent of foreign revenue of the total service sector under study (table 3).

Another important aspect of the U.S. hotel/motel industry overseas is the corporate link between this industry and the air transportation industry. The agreements made between these industries are aimed at providing reciprocol business for each sector. Illustrative of such a merger is Hilton International which is a subsidiary of Trans-World Airlines. Advantages of such a merger include using the same accounting systems and provisions for overseas offices. Industry sources have indicated that acquisitions of hotel/motels by the airline industry of foreign competitors occur occasionally.

Table 3.--Estimated total foreign revenue generated by the hotel and motel service industry and estimated total foreign revenue for selected service industries, 1980-82

Year	Total foreign revenue for service industry 1/ (1)	Total foreign revenue for selected service industries 2/ (2)	Ratio of (1) to (2)
	1,000 U.S. dollars		Percent
1980	2,100,000	89,398,000	2
1981	2,300,000	109,611,000	2
1982	2,530,000	135,744,000	2

1/ Estimated based on discussion with industry and/or association representatives, and secondary sources.
2/ Based on totaling Commission-estimated foreign revenue for each of the 14 selected industries covered in the study.

Source: Estimated by the staff of the U.S. International Trade Commission.

During the 1970's, U.S. hoteliers were establishing units primarily in Western Europe, the Caribbean, and to a lesser extent the oil-rich, developing countries of the Middle East. Unlike the Western European and Caribbean markets which largely require promotion directed to a constant influx of tourists, the Mideast marketing effort is primarily geared at providing lodging to businessmen that would later establish industries and bring technological advancements to their countries. This market also encouraged competitors to develop a travel industry because it would bring in additional revenue. Industry sources have indicated that 75 percent of the world's tourists will choose Europe as their principle destination by 1990. 1/ As a result, U.S. hotel/motel operations are establishing more facilities in

1/ "Europe Moving Up Out of Latest Slump," Service World International, June 1981, p. 45.

Europe. Meanwhile the relative stability in hotel costs and warm climate continues to contribute to the success of the hotel/motel industry in the Caribbean. As shown in table 4, respondents to the Commission's questionnaire indicate that the regions generating most revenue in 1981 were Europe, the Far East, the Middle East, and Latin America.

Trade in Merchandise Generated by Trade in Services

The number of positive responses to a series of questions asked to determine whether or not U.S. merchandise exports are generated by U.S. hotel motel service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
Do you believe that U.S. merchandise might be used as a result of the services your firm provides abroad?-------------------------------	4	100
Is U.S. merchandise specified or recommended in the course of providing your service?----------------	3	75
Are U.S. merchandise exports believed to be directly generated?-----------	4	100

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 7 firms surveyed; respondents represent almost 60 percent of the foreign revenue of the 10 major firms believed to be operating internationally in 1981.

Because of the relatively low response rate to the merchandise trade section of the questionnaire, the Commission is unable to extrapolate with certainty the value of U.S. merchandise exports directly generated by U.S. hotel/motel activities abroad. However, these industry respondents estimated that their service activities overseas resulted in the total U.S. export of approximately $18 million in goods in 1981 (table 5). On the basis of this estimate, the number of respondents, and the number of known firms in the industry, it is estimated that $45 million in U.S. merchandise exports flowed as a result of U.S. international hotel and motel activities in 1981. However, it should be noted that at a confidence level of 95 percent this figure could be as low as the actual respondent's estimate of $18 million or

Table 4.--Regions and countries in which revenue is generated by hotel and motel service firms, 1980-82 1/

Region and country 2/	Number of responses			Percent of total respondents			Estimated revenue		
	1980	1981	1982	1980	1981	1982	1980	1981	1982
							------1,000 U.S. dollars------		
Middle East	3	4	3	75	100	75	3/	197,864	3/
Bahrain	-	1	-						
Israel	-	1	-						
Jordan	-	2	-						
Kuwait	-	2	-						
Saudi Arabia	-	2	-						
Turkey	-	1	-						
United Arab Emirates	-	3	-						
Far East	3	3	3	75	75	75	3/	3/	3/
Australia	-	2	-						
India	-	1	-						
Indonesia	-	1	-						
Japan	-	2	-						
Malaysia	-	1	-						
Papria-New Guinea	-	1	-						
Philippines	-	1	-						
Latin America	2	4	3	50	100	75	3/	178,227	3/
Argentina	-	1	-						
Brazil	-	2	-						
Chile	-	2	-						
Columbia	-	1	-						
Panama	-	1	-						
Venezuela	-	3	-						
Europe	3	4	3	75	100	75	3/	262,149	3/
Belgium	-	2	-						
West Germany	-	3	-						
France	-	2	-						
Netherlands	-	1	-						
United Kingdom	-	2	-						
Africa	3	3	3	75	75	75	3/	3/	3/
Egypt	-	3	-						
Kenya	-	1	-						
Nigeria	-	1	-						
South Africa	-	1	-						
Sudan	-	1	-						
Tunisa	-	1	-						
Canada	3	3	3	75	75	75	3/	3/	3/
Mexico	2	3	2	50	75	50	3/	3/	3/
Other	2	2	2	50	50	50	3/	3/	3/

1/ Country listing is for 1981 only.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 7 firms surveyed; respondents represent almost 60 percent of the foreign revenue of the 10 major firms believed to be operating internationally in 1981.

3/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

as high as $51 million. For estimates of U.S. merchandise exports for 1980 and 1982, refer to table 5.

Table 5.--U.S. merchandise exports generated by U.S. hotel and motel services abroad, 1980-82 1/

Year	Number of responses	Exports of U.S. merchandise estimated by respondents	Projected 2/ total: U.S. merchandise for the service industry	+ 95 percent confidence limit for projected industry exports
		1,000 U.S. dollars		
1980	4	14,613	37,000	5,000
1981	4	18,134	45,000	6,000
1982	4	19,433	49,000	17,000

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 7 firms surveyed; respondents represent almost 60 percent of the foreign revenue of the 10 major firms believed to be operating internationally in 1981.

2/ By the U.S. International Trade Commission.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Throughout the 1980-82 period, the four respondents to the Commission's questionnaire will account for about 40 percent of the total projected exports of U.S. merchandise for this service sector. Most of the export items reported by three respondents in table 6 were (1) machinery and equipment, particularly food service, laundry, air-conditioning/refrigeration and telecommunication hardware as well as office equipment and motor vehicles; (2) agricultural products, which included processed foods and meats; (3) miscellaneous goods, such as furniture and fixtures; and (4) textile and apparel items, namely institutional linens, employee uniforms, and carpeting. The destination for the majority of these exports was the Middle East followed by Central and South America, and Mexico.

In some instances, it was reported that when a U.S.-based firm is engaging in negotiations to establish a hotel/motel in a foreign market it will specify that the machinery and equipment needed to operate the facility be purchased from the United States. This is because the local economy may not produce these items. On the other hand, items which are frequently replaced and which are produced by the more labor intensive industries (e.g., textiles, agriculture, etc.) are usually procured locally by the U.S. hotel/motel operation in foreign markets.

All of the questionnaire respondents indicated that host-country products and/or imports from third countries are used in their foreign hotel/motel operations abroad. The number of positive responses to a series of questions asked to determine whether or not host-country or third-country merchandise

Table 6.--Estimated U.S. merchandise exports resulting from hotel and motel services abroad, by types and by principal markets, 1981 1/

Type	U.S. exports used in providing services 2/	Number of firms indicating U.S. merchandise exports to-- Middle East	Far East	Central and South America (excluding Mexico)	Europe	Africa	Canada	Mexico	All other
	1,000 U.S. dollars								
Total	18,134	3	1	1	2	1	1	1	1
Machinery and equipment	3,862	2	1	1	1	1	1		
Food service equipment	1,803	3	1	1	2	1	1	1	1
Food processing machinery	250	1			1			1	1
Commercial laundry equipment	529	2		1	1	1	1	1	1
Air-conditioning & refrigeration equipment	680	2					1	1	1
Telecommunication equipment	350	1					1	1	1
Office machines and equipment	200	1						1	1
Motor vehicles and accessories	50	1							1
Agricultural, animal, and vegetable products	3,850	1	1						
Processed food	2,850	2	1		1			1	1
Meat products (animal)	1,000	1							1
Forest products	490	2	1	1	2		1	2	
Paper products	260	1	1	1	1			1	1
Industrial paperboard and packaging	130	1			1			1	1
Printed matter	100	2	1	1	2		1	2	1
Textile, apparel, and footwear	1,002	3	2	2	3	1	1	2	
Institutional linens	406	3	2	1	2		2	1	1
Employee uniforms and apparel	260	1	1	1	1	1			
Fabric and carpet	336	1	1	1		1	1		
Chemicals and related products	330	3	2	2	3	1	1	2	1
Cleaning compounds	21	1	1	1					
Soaps and detergents	29	1		1				1	
Cosmetics and toilet preparations	100	1			1			1	1
Guestroom supplies	180	1	1	1	1	1	1	1	
Minerals and metals	309	3	1	1	2		1	1	1
Flatware (utensils)	216	1			2			1	
Glass and ceramic tableware	87	1	1	1	1		1		
Steel mill products	6								
Miscellaneous manufactures	3,291	2	1	2	3	1	1	1	1
Furniture and fixtures	3,041	1		1	1	1	1		1
Sportring goods and leisure-time equipment	225	1			1			1	1
Audiovisual equipment	25	1			1			1	1

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 7 firms surveyed; respondents represent almost 60 percent of the foreign revenue of the 10 major firms believed to be operating internationally in 1981.
2/ Based on 3 responses. U.S. exports were estimated but respondents could not identify the specific type in all cases; thus, the subcategories do not add to the total shown.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

shipments 1/ are generated by U.S. hotel/motel service activities abroad, were as shown in the following tabulation.

Question	Number of responses 1/	Percent of total respondents
Do you believe that foreign merchandise might be used as a result of the services your firm provides abroad?------------------------------	4	100
Are foreign or host-country products specified or recommended in the course of providing your service?------------------------------	2	50

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 7 firms surveyed; respondents represent almost 60 percent of the foreign revenue of the 10 major firms believed to be operating internationally in 1981.

Third-country and host-country merchandise shipments estimated by one firm as a result of its U.S. hotel/motel services abroad in 1981 were as shown in the following tabulation:

Item	Value (1,000 U.S. dollars)
Third-country shipments----------------	60,000
Host-country shipments-----------------	60,000

Significant examples, cited by industry sources, where the entry of U.S. hotel/motel services into foreign markets has benefited the economies of the host country or a third country include (1) increasing employment opportunities; (2) promoting host cities and countries as business centers; and (3) stimulating local economies by adding tourism and travel trade.

International Service Trade Barriers

According to U.S. industry officials, before and after a hotel or motel becomes operational in a foreign country, trade barriers often emerge. The barriers most often cited by the U.S. hotel/motel industry as impeding foreign operations and international expansion include (1) discriminatory foreign

1/ "Host-country merchandise shipments" refers to the shipments (within the host country) of host-country-manufactured products which are generated by U.S. service operations in the host-country market. "Third-country merchandise shipments" refers to the shipments of other foreign-manufactured products to a foreign market as a result of U.S. service operations in that market.

exchange controls; (2) discriminatory taxation; (3) restrictions regarding domestic personnel; (4) discriminatory tariffs and customs procedures; (5) quantitative and qualitative restrictions on service companies; and (6) restrictions regarding foreign personnel.

Discriminatory foreign exchange restrictions are controls used by a foreign government and its central bank to block the transfer of funds out of their country. For example, the franchise fee charged by a hotel/motel chain is usually a sizable amount and at times cannot be transferred to the franchisor in the United States when the foreign bank determines that its currency reserve is falling below minimum requirements. Other situations where this measure may have an adverse effect include payments for goods imported from abroad, interest on loans from parent companies, technical services and fees, and taxes on dividends. Because of delays in foreign government authorization, it has been reported that currency transfers (remittances) have sometimes been wholly or partially blocked for periods as long as several years.

In the area of taxation, the host government may employ tax practices which contribute to unfair business standards. The discriminatory taxation problem most often faced by U.S. hoteliers include nondeductible office overhead expenses and nondefinitive tax laws which discourage tax planning. Industry sources have indicated that in some instances, discriminatory taxes have actually discouraged firms from establishing operations in a country where discriminatory taxes are used.

The restrictions placed upon U.S. hotel/motels by host governments when employing domestic personnel (particularly in South America), are oftentimes costly and cumbersome. These restrictions come in the form of preventing a hotel/motel operation from terminating surplus or nonproductive employees, and unreasonable severance and termination benefits which in many instances cannot be accrued or deducted.

Discriminatory tariffs and customs procedures used against U.S. hotel/motels by host governments include restrictions on the importation of equipment needed in the operation of this service industry. These restrictions are designed to discourage equipment imports in favor of equipment produced locally, which may not meet specifications required to maintain quality standards of U.S.-operated facilities.

The U.S. hotel/motel industry, to a more limited degree, is also subject to quantitative and qualitative laws imposed by foreign governments. These restrictions are primarily geared toward foreign investment controls which limit the percentage share that a U.S. firm can own in a company. In addition, there are restrictive controls for granting trademark licenses on hotel/motel names and logos, as well as requirements for approval by local economic planning boards for technical assistance activities associated with hotel/motel expansion or remodeling projects. These measures can significantly hamper traditional competitive advantages available to U.S.-based firms.

Another type of employee restriction cited by industry sources as used by the host government is that concerned with foreign personnel. In many instances work permits for foreign employees are difficult to obtain, extend, or renew. Because of immigration restrictions, which sometimes prevent bringing in trained people from other parts of the world, it is difficult to find employees within the host country with the expertise and management skills needed to efficiently operate a hotel/motel.

Of the six previously mentioned trade barriers, respondents to the Commission's questionnaire have alleged that restrictive employment regulations on both nonnationals and local nationals and local purchase requirements were the barriers most frequently enforced, as shown in table 7. Other trade barriers mentioned included those involving credit and investment restrictions, citizenship and residency requirements for personnel, paperwork required to import merchandise, restrictions on remittances, and delays in obtaining foreign exchange permits.

All questionnaire respondents reported that their service activities overseas would increase, as a result of reducing or eliminating existing barriers. The number of responses to a question to determine the economic effects of international barriers to U.S. services trade and associated product exports in hotel and motel service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
What effect, if any, would reduction or removal of service trade barriers have upon your receivables, billings, or revenues in current or potential country markets?:		
Increase	3	75
Decrease	0	0
No effect	1	25
What effect, if, any would reduction or removal of service trade barriers have upon potential U.S. product export in current or potential country markets?:		
Increase	4	100
Decrease	0	0
No effect	0	0

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 7 firms surveyed; respondents represent almost 60 percent of the foreign revenue of the 10 major firms believed to be operating internationally in 1981.

Table 7.--Trade barriers to international services in the hotel and motel industry 1/

Category and barrier	Number of responses	Percent of total respondents
Right of establishment	4	100
Restrictive employment regulations (e.g., local labor requirement)	4	
Credit, investment or financial activity restrictions	3	
Administrative/ownership restrictions	1	
Entry of service personnel and specialized tools	3	
Citizenship/residency requirements	3	
Restrictive government/business regulations	2	
Special deposit requirement for foreign companies	1	
Trade in goods	4	100
Restrictive regulations or administrative procedure	2	
Local purchase requirements	4	
Restricting entry of equipment or supply	2	
Trade in services	4	100
Restrictive government/business regulations and administrative procedures	2	
Restriction related to resident firm preference (fixed percentage of service must be provided by domestic resident companies)	1	
Employment related restrictions on nonnationals	4	
Operating/ownership restrictions	2	
Discriminatory taxation	1	
Prohibition on services offered by nonresident companies	1	
Other (government price restrictions or controls)	1	
Technical issues	4	100
Contract enforcement problems	2	
Time limitations on franchise agreements	1	
Governmental paper requirement	3	
Discriminatory standards requirements	1	
Licensing	2	50
Licensing procedures	2	
Licensing restrictions (e.g., quotas)	1	
Refusal to license or renew	1	
Commercial counterfeiting	2	50
Inadequate patent or trademark enforcement	2	
Unclear definitions of trademark, patent, imported goods, or counterfeit goods	1	

See footnote at end of table.

Table 7.--Trade barriers to international services in the hotel and motel industry 1/--Continued

Category and barrier	Number of responses	Percent of total respondents
Government procurement	2	50
Preference given to national firms	1	
Governmental import or distribution monopoly	1	
Prohibition of foreign services contracts (bilateral or multilateral)	1	
Shipment restricted to National flag carriers partially or completely	1	
Customs valuation	1	25
Discriminatory tariffs and customs procedures	1	
Standards/certification	2	50
Health and safety requirements	1	
Local labor or material requirements	2	
Professional qualification restrictions:	1	25
Professional license required to practice	1	
Foreign exchange controls	4	100
Restrictions on remittances	3	
Convertibility limitations	2	
Delays in obtaining foreign exchange permit	3	

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 7 firms surveyed; respondents represent almost 60 percent of the foreign revenue of the 10 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Respondents indicating that reduction or removal of trade barriers would have a positive effect on foreign revenues, indicated that revenue would increase from 40 to 80 percent in Latin America, Canada, and Mexico (table 8). Respondents also indicated that the reduction or removal of trade barriers would result in a 40 to 80 percent increase in product trade for machinery and equipment, agricultural, forest, and textile products, as well as miscellaneous manufactures such as furniture and fixtures (table 9).

Table 8.--Estimated changes in revenues absent trade barriers to international business of hotel and motel service firms, by areas 1/

Area and direction of change	Number of responses	Percentage change						
		10	20	30	40	50	60	80
Middle East:								
Increase	3	1	1	1				
Decrease								
Far East:								
Increase	2	1	1					
Decrease								
Latin America:								
Increase	2				1	1		
Decrease								
Europe:								
Increase	3	1		2				
Decrease								
Africa:								
Increase	2		1	1				
Decrease								
Canada:								
Increase	2		1					1
Decrease								
Mexico:								
Increase	3	1					1	1
Decrease								
Other:								
Increase	1	1						
Decrease								

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 7 firms surveyed; respondents represent almost 60 percent of the foreign revenue of the 10 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 9.--Estimated changes in U.S. merchandise exports absent trade barriers to international business of hotel and motel service firms, by types 1/

Type and direction of change	Number of responses	Percentage change						
		10	20	30	40	50	60	80
Machinery and equipment:								
Increase	3		2		1			
Decrease								
Agricultural, animal and vegetable products:								
Increase	3		1	1		1		
Decrease								
Forest products:								
Increase	2	1				1		
Decrease								
Textiles, apparel, and footwear:								
Increase	4		2	1		1		
Decrease								
Chemicals and related products:								
Increase	3		2	1				
Decrease								
Minerals and metal products:								
Increase	1		1					
Decrease								
Miscellaneous manufactures:								
Increase	4		2			1		1
Decrease								

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 7 firms surveyed; respondents represent almost 60 percent of the foreign revenue of the 10 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Conditions of Competition in Current and Potential Service Markets

The competitive posture and strengths of U.S.-based hotel/motels in domestic and foreign markets have been reported by an industry source as excellent. This is due primarily to the outstanding reputation held by U.S. hotel/motel chains as well as their innovative management and marketing abilities.

The U.S.-based hotel/motel industry is almost entirely composed of deluxe- and economical-type operations with a comparatively small amount of luxury hotel/motels. The deluxe and economical hotel/motels are characterized as being location and price competitive, whereas the luxury hotel/motels compete most effectively through offering unique services, amenities, and facilities. In some instances a hotel or motel has no direct competitors; this usually occurs when there is a lack of nearby competition or when it is the only facility in the area that caters to a specific type of clientele. By contrast, U.S.-based hotel/motels that expand internationally are most often the luxury type and they compete on a similar basis to those which are located in the United States.

Another competitive factor, particularly for the large hotel/motel chains, is the widespread use of referral services. The referral system is used both domestically and internationally and is based upon a communication system which links hotel units. The advantages of such a system are that it reduces the worry of a traveler finding a room upon reaching a destination and it assists other units in the chain to reduce vacancies.

In less developed countries, U.S.-based firms face competition from hotel/motel operations that are owned and in some instances managed by their governments. 1/ In general, governments involved in the hotel/motel industry attempt to discourage the establishment of foreign-based operations. They also attempt to keep track of that country's tourism trade so that its economic and social impact can be measured.

Overall there is little competition from foreign-owned hotel/motels in the United States. However, foreign-owned chains have been established in several U.S. cities, such as New York and San Francisco, where they effectively compete for the sophisticated hotel guest, who is not concerned about cost, by providing a European atmosphere through a luxury-type facility.

Most U.S. hotel/motels that expand internationally are luxury hotels which compete effectively against foreign-owned and foreign-operated hotel/motels that offer similar services, such as currency exchange, travel assistance, and business or recreational facilities. The success of the U.S. firm is borne out of the fact that 7 out of 10 major hotel/motel chains operating worldwide were U.S.-based. As a result, a considerable amount of the competition that U.S. firms face in foreign countries is from other U.S. firms.

The competitive environment of U.S. hotel and motel companies in foreign markets can be characterized based on insights provided by a limited number of questionnaire respondents. Questionnaire responses indicate that over one-third of the competing hotel/motels are U.S.-based, as shown in table 10. The competing firms' success in foreign markets, such as West Germany, the United Kingdom, and Canada, has been attributed to lower prices, preferential financing, political and regional bias, and to a lesser extent experience in the market (table 11). On the other hand, U.S. hotel and motel service firms have indicated in table 12 and 13 that their competitive advantages in established and potential service markets are in financial strength, outstanding service, expertise in the market, and technological superiority. This confirms the contention made earlier that U.S.-based firms are competitive not only because of their reputation but also because they are leaders in the management and marketing field.

1/ "LDC's Depend on State and Private Chains," Service World International, June 1981, p. 77.

Table 10.--Number of firms competing 1/ with U.S. hotel/motel service firms abroad, by principal service markets 2/ in order of revenue generated, 1981 3/

Service market	Number of competing firms				
	Total	National	Regional	World-wide	Other U.S. firms
United Kingdom	8	4	2	2	
Mexico	15	4	2		9
Bahamas	15		5	8	2
West Germany	8	1	3	4	
Saudi Arabia	19	5	1	4	9
Netherlands	10	3			7

1/ Based on 2 responses by questionnaire respondents.

2/ Other principal service markets for the industry may not be listed here if respondents did not identify the number of competing firms.

3/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 7 firms surveyed; respondents represent almost 60 percent of the foreign revenue of the 10 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 11.--Likely reasons 1/ for competing firms' success in world hotel and motel service markets, by base countries of firms 2/

Base country	Lower price	Technology expertise	Preferential financing	Experience in the market or service
West Germany	1		1	
United Kingdom	1		1	
Canada				1
Total	2		2	1

Base country	Superior quality association	Political or regional bias	Government support	U.S. restrictions
West Germany		1		
United Kingdom		1		
Canada				
Total		2		

1/ The importance of each reason is indicated by the number of times each was designated, based on one response.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 7 firms surveyed; respondents represent almost 60 percent of the foreign revenue of the 10 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 12.--Likely reasons 1/ for the competitive strength of U.S. hotel and motel service firms in foreign service markets 2/

Service market	Lower price	Technology lead	Financial strength	Experience in the market or service	Superior quality association
Europe:					
West Germany			1		1
United Kingdom			1		1
Africa:					
Egypt		1	1	1	1
N. America and Mexico:					
Canada		1	2	2	1
Mexico		1	1	1	1
Other	1	1	1	1	1
Total	1	4	7	5	6

1/ The importance of each reason is indicated by the number of times each was designed, based on 2 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 7 firms; respondents represent almost 60 percent of the foreign revenue of the 10 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 13.--U.S. hotel and motel service firms' competitive strengths 1/ in potential foreign markets 2/

Potential service market	Lower price	Technology lead	Financial strength	Greater experience	Superior quality
Middle East:					
Iraq		1	1	1	1
Far East:					
New Zealand		1	1	2	2
Thailand				1	1
Central and S. America (excluding Mexico):					
Panama		1	1		1
Europe:					
Greece		1		1	1
Italy		1	1	1	1
Africa:					
Egypt		1		1	1
Nigeria				1	1
Total		6	4	8	9

1/ The importance of each reason is indicated by the number of times each was designated, based on 3 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service was 4 of 7 firms surveyed; respondents represent almost 60 percent of the foreign revenue of the 10 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

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Insurance Services

Executive Summary

1. International revenues for U.S. insurance operations totaled approximately $6.5 billion in 1981.

2. Most companies and industry sources as well do not believe that direct merchandise exports are generated for use by the insurance services sector, but they indicate there may be an indirect relationship through certain product standard specifications stemming from insurance financing for worldwide construction projects.

3. Forty percent of questionnaire respondents indicated that host- or third-country merchandise shipments might be generated as a result of U.S. insurance service activities abroad. Industry sources indicate that computers, word processors, and other office equipment may be purchased as U.S. international carriers open branches or subsidiaries overseas.

4. The trade barriers to insurance services cited most frequently by respondents were in areas of (1) right of establishment, (2) trade in services, (3) foreign exchange controls, and (4) licensing.

5. The exact dollar impact of international barriers to the U.S. insurance industry is difficult to determine, however most questionnaire respondents and industry sources agree that there are an abundance of trade barriers to doing business on an international scale. Most would like to see some U.S. Government intervention on their behalf. About 60 percent of respondents reported that their service revenues abroad would increase in the range of 10 to 50 percent in most regions of the world as a result of reduction or removal of existing barriers. Generally, respondents did not believe U.S. merchandise exports would increase if service barriers were eliminated.

6. Competition in the insurance industry, both in the domestic and international markets, is extremely intense. There are several hundred firms competing for business in world markets, with the most intense competition for U.S. firms found in Canada and the EC.

7. There are a variety of reasons why U.S. firms felt they lost business to foreign competitors in world markets. The overwhelming reason cited by questionnaire respondents was lower prices offered by competitors, particularly in the United Kingdom. Political or regional bias was the next most frequently cited reason.

8. U.S. firms believe that financial strength is the most likely reason for their competitive strength in existing foreign markets. Other principal reasons include experience in the market or service, and superior quality association.

Industry Profile

Definition and coverage

The basic function of insurance is to provide the insured with a secure means of protection against financial losses arising from unexpected events. The industry also offers a wide range of additional services including risk analysis, loss prevention advice and savings and investment programs. The insurance industry transfers risks--among individuals and companies and also between national, regional, and international markets. Certain aspects of the insurance industry are considered to be inherently "international," i.e. (1) transport insurance, including marine and aviation; (2) political risk insurance; (3) insurance of very large risks; and (4) reinsurance. 1/

This study focuses on insurance firms that have known operations in foreign markets. These companies offer a variety of insurance plans including life, accident and health insurance, fire, marine, and casualty insurance; hospital and medical insurance; and reinsurance. Insurance brokers were not included.

The 15 insurance service industry respondents to the Commission's questionnaire (of 28 firms surveyed) represent an estimated 66 percent of foreign revenues of the estimated 60 insurance service firms believed to be operating internationally in 1981.

Highlights in 1981

- o DOMESTIC REVENUES were estimated at approximately $65 billion.
- o U.S. ESTABLISHMENTS numbered more than 5,000 companies which operated a variety of regional, branch, and subsidiary offices.
- o U.S. EMPLOYMENT averaged approximately 1.8 million persons.
- o INTERNATIONAL REVENUE for U.S. insurance operations totaled approximately $6.5 billion.
- o FOREIGN ESTABLISHMENTS are operational for an estimated 60 U.S. insurance companies with operations in over 130 countries.
- o FOREIGN EMPLOYMENT figures are believed to represent only a small percentage of total employment in the insurance industry but exact figures are not available.
- o U.S. TRADE BALANCE in insurance premiums is believed to be positive since there are only a small number of known foreign firms operating in the U.S. market.

1/ Reinsurance is insurance which one firm buys from another in order to write an amount of insurance on a single risk greater than its capital assets would permit. "International Trade Issues in Insurance", International Trade Administration, U.S. Department of Commerce, "International Trade Issues in Insurance," Oct. 5, 1981, p. 1.

Industry structure

There are over 5,000 insurance companies in the United States, ranging in size from small, independent agencies to multibillion dollar conglomerates that operate hundreds of local offices. Many of these larger companies have foreign operations in one or more countries, with the home office located in the United States. While the international operations are of increasing importance to many domestic insurers, and may generate large amounts of revenue, the international operations of the total insurance industry account for a relatively small percentage of total domestic revenues. Domestic and international revenues ($71.5 billion) for the insurance service industry account for nearly 9 percent of total U.S. service trade of $837 billion in 1981 for the 14 service industries covered in this study.

The insurance industry in the United States is regulated by the 50 individual States with each State having its own insurance Commission or Commissioner, which determines the specific regulations, including the rate structures, for operating in that State. This complex array of State regulations has affected the international operations of some insurance companies by placing restrictions on the flow of currency or other types of capital requirements.

Basically, the U.S. industry, as well as the international insurance industry, can be divided into two segments: life insurance and general insurance. The life insurance industry, which accounts for premium receipts of approximately $102 billion, consists of approximately 2,000 underwriting companies and 1/2 million employees. These companies posted a record in 1981 for new life insurance purchases of nearly $604 billion, representing a rise of 11 percent from what it was in 1980. Life insurance in force in the United States reached a new high of nearly $3.9 trillion in 1981, rising more than 9 percent above 1980. Over 145 million policyholders were covered by some type of life insurance policy, including ordinary (or whole life) insurance and term life insurance. Life insurance companies also underwrite a substantial amount of health and accident insurance. A chief source of income for many U.S. life insurance companies are various types of pension plans covering an estimated 26.1 million persons, according to the American Council of Life Insurance. 1/

The general insurance industry includes all other types of insurance, particularly property and casualty insurance. It also encompasses fire, marine, surety, title, product liability, and automobile insurance. Several thousand firms sell some form of general insurance, with the bulk of the business written by about 1,000 companies that operate in nearly all States. Automobile insurance accounts for about 40 percent of total premium volume of the general insurance industry. Many general insurance carriers are also involved in selling reinsurance either on a domestic or international basis.

1/ U.S. Department of Commerce,"Life Insurance," The U.S. Industrial Outlook 1982, Ch. 46, pp. 400-404.

Recent trends and outlook

Despite high rates of inflation and volatile interest rates, the insurance sector has achieved a continued small growth in recent years in both the domestic and international markets. According to industry sources, certain types of insurance, such as reinsurance and political risk insurance, offer more potential for growth and profit than others such as life insurance. These types of insurance are necessary on practically every major international project and are not affected as directly as consumer related insurance such as life insurance by the combined effects of inflation and higher interest rates.

The rise in interest rates in recent years has adversely affected many insurance companies by imposing a severe liquidity drain. Many companies lent large sums to borrowers on a long-term basis expecting interest rates to decline. When interest rates remained high, many firms were left holding long-term below market-rate commitments. Additionally, policyholders borrowed billions against the cash value of their whole-life insurance policies at rates of 5 to 8 percent so they could place their funds in higher yielding money market funds. This drained off funds that insurers could have used for more attractive investments. The life insurance industry has also been threatened by two other trends: (1) the decline in sales of whole-life policies and (2) the defection of many young adults from the entire life insurance market as they turn to other investments they believe to be more profitable. As the life insurance market becomes less profitable, many companies have moved into the property/casualty business. Premiums in this type of insurance rise as the value of the insured object inflates, making the policies more profitable. 1/

Another competitive development, affecting insurance industry growth propects, is the establishment of subsidiaries or "captives," by many domestic noninsurance companies, which are generally based beyond the scope of U.S. tax laws and State regulators in locations such as Bermuda and the Cayman Islands. These captives write insurance or reinsurance for their parent companies, though some of them take on outside customers as well. Offshore captives have advantages for multinational companies as standards for capitalization, investments and financial reporting are generally looser than standards in the United States. 2/

A significant development in recent years regarding the insurance sector has been the enormous growth in the size of financial risks, especially with regard to product liability. As the size of insurance settlements continues to grow, insured companies are forced to pay higher premiums and insurance companies are being forced to accept larger and larger risks. Another development of special concern to international insurers is the increase of restrictions on foreign insurers, particularly in Third World or developing countries. These restrictions are frequently the result of the rising

1/ Ibid., Ch. 46, p. 400.

2/ Daniel Hertzberg, "Some States Trying to Lure New Insurers," Wall Street Journal, Feb. 26, 1982, p. 29.

feelings of nationalism in many of these areas and a desire to prevent valuable capital assets from leaving the country. U.S. companies also face the threat of nationalization or expropriation.

The insurance industry is facing many changes in the coming years and hopes to respond by acknowledging the realities of the marketplace, including continued high-interest rates and the possibilities of rapid inflation. Competition within the industry is likely to intensify, with many companies striving to improve their line of products, offering premium discounting and liberalized policy provisions. In an effort to improve their competitive position in the investment area, many companies are beginning to index the interest rate on many of their loans to ensure that the companies will no longer be saddled with low-interest-rate loans in times of high inflation. The industry is also expecting increased opportunity for its pension-related business, resulting from the recently enacted Federal tax act. 1/

Since the United States is regarded as the primary insurance market in the world, foreign insurance companies increasingly have opened branch offices and subsidiaries in the United States. Many foreign investors find smaller U.S. companies particularly attractive as investments. Although the total business conducted by foreign-owned firms in the United States is believed to be relatively small, these developments have created some concern in the domestic industry, because they anticipate further penetration by the foreign insurers.

U.S. Service Operations in Foreign Markets

Scope of operations

As in the United States, insurance is a carefully regulated industry in most countries and every international company must operate within the framework of foreign insurance laws. Basically, insurance companies sell insurance in a foreign market either as an admitted or nonadmitted insurer. Admitted insurance is sold by a company licensed or registered to do business in the country where the property or risk is located; nonadmitted is not licensed or registered, although in some countries it is legal to sell insurance in this manner. 2/

For most major international insurers, the method of operation in foreign markets is moving more towards joint venture or affiliated companies, especially in most Third World markets. This type of operation can take two forms: 1) Minority or majority shareholding participation in a national insurance company, for which the company becomes a vehicle for insuring risks in the host country, and 2) appointment of a national insurance company to serve as the local insuring vehicle, but without equity shareholding participation by the U.S. company.

1/ U.S. Department of Commerce, op. cit., Ch. 46, pp. 403-404.

2/ Sherman J. Olson, "Foreign Laws and Markets-A World Tour of Insurance," Risk Management, November 1980, p. 37.

Most countries have detailed regulations as to the total percentage of any local company that can be owned by a foreign or multinational company, however, in both cases, the U.S. company is normally the major reinsurer of the portfolio of the national insurance company. 1/ In affiliate operations, U.S. companies are allowed to own a limited share of a foreign company, which varies from country to country. Most companies would prefer no limits on their ownership of foreign operations but have accepted this as a precondition for doing business in certain foreign markets. In addition, this procedure allows some flexibility from U.S. regulations and also reduces the risks of nationalization. Experiments with joint ventures and with direct mail operations are receiving greater attention within the insurance industry with varying degrees of success. Table 1 indicates that the majority of the companies who responded to the questionnaire operate subsidiaries, branches or foreign affiliates. A much smaller percentage of respondents operated joint ventures.

Occasionally, a U.S. company writing an overseas insurance portfolio may write a policy on a "Home-Foreign" basis. This method entails writing a standard U.S. policy for the home office of a U.S.-insured company, collecting the premium in dollars and paying any losses in dollars, but the policy insures the overseas interests of the U.S. company. 2/ Industry sources indicate that this method of operation is illegal in a number of foreign countries since the host country, in effect, has no control over insurance transactions covering risks located in their jurisdiction.

The more traditional operating method used by the insurance business is the appointment of general agents in the countries in which they desire to do business. Many of these agents are trained by experienced U.S. personnel. Through a series of legal transactions, varying from country to country, the agent is empowered by the host country to transact insurance business. This method of doing business is more common for life insurance companies and is being phased out by many of the international companies in favor of the joint-ownership or affiliated company, which helps companies avoid the risks for potential expropriation or nationalization.

1/ International Insurance Advisory Council, Chamber of Commerce of the United States, "Position Paper on International Insurance and Reinsurance," July 12, 1972.

2/ Ibid.

Table 1.--Operating structures of principal service activity, and revenues associated with secondary service industry activities of insurance service firms in foreign markets, 1981 1/

Item	Revenues	Number of responses	Percent of total respondents
	1,000 U.S. dollars		
Operating structure:			
Foreign affiliate	-	12	80
Joint venture	-	7	47
Licensing	-	1	7
Subsidiary or branch	-	13	87
Other	-	5	33
Secondary service activity:	2/		

1/ The data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 28 firms surveyed; respondents represent an estimated 66 percent of the foreign revenue of the estimated 60 major firms believed to be operating internationally in 1981.

2/ No secondary activities were indicated by the service industry respondents.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

The majority of U.S. insurers maintain direct branch operations in at least one or more of the markets in which they do business. Branches are usually established in countries where companies are already doing a significant amount of business. Generally, branches are set up along the same lines as the home office with underwriting, claims, and other specialized departments. Most companies employ a significant number of "locals" in their branch operations, which provides valuable management training for the nationals of developing countries. 1/

Reinsurance and political risk insurance are transacted by large, multinational corporations or frequently between companies and national governments in cases where insurance is a state owned monopoly. Insurance or reinsurance on very large projects or for castastrophic-type disasters is dispersed among a number of companies or brokers since the financial risks are too great for a single company to assume.

The U.S. Government has become involved in the international insurance arena by organizing and supporting two semi-autonomous organizations. The Federal Credit Insurance Association (FCIA) represents approximately 50 private insurance companies and underwrites U.S. exporters against commercial

1/ International Insurance Advisory Council, op. cit., p. 10.

credit risks. The Overseas Private Investment Corporation (OPIC) formed in 1969, brought together several federal foreign insurance programs that encourage U.S. corporations to invest in countries in which they would otherwise not be interested because of political risks.

Growth trends and U.S. investment

Table 2 indicates, that for questionnaire respondents, foreign revenues accounted for approximately 8 percent of total revenues in 1981. On the basis of estimated data for the entire industry, the ratio was 9 percent in 1981, and was unchanged from the previous year. Foreign revenues of questionnaire respondents increased 10 percent from 1980 to 1981. The table shows limited growth in both foreign and total revenues. Table 2 also shows a 13-percent growth rate for investment in physical assets in foreign operations between 1980 an 1981. The number of establishments remained essentially unchanged for the period 1980-81.

Table 2.--Indicators of activity in the foreign and domestic operations of insurance service firms, 1980-82

Item	Foreign	Domestic	Total
Estimated value of receivables, billings, or revenues: 1/ 2/			
1980------------------1,000 dollars--:	3,797,552	44,165,225	47,919,777
1981---------------------------do----:	4,178,515	47,011,238	51,189,754
1982---------------------------do----:	4,672,974	53,483,177	58,200,153
Estimate of investment in physical assets 1/ 3/ in foreign operations:			
1980------------------1,000 dollars--:	4/	-	-
1981---------------------------do----:	4/	-	-
1982---------------------------do----:	4/	-	-
Number of establishments: 1/			
1980----------------------------------:	851	1,335	2,186
1981----------------------------------:	856	1,353	2,209
1982----------------------------------:	862	1,350	2,212
Estimated 5/ value of total industry receivables, billings, or revenues:			
1980------------------1,000 dollars--:	6,000,000	63,000,000	69,000,000
1981---------------------------do----:	6,500,000	65,000,000	71,500,000
1982---------------------------do----:	7,000,000	68,000,000	75,000,000

1/ The data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 28 firms surveyed; respondents represent an estimated 66 percent of the foreign revenue of the estimated 60 major firms believed to be operating internationally in 1981.

2/ Excluding the value of any merchandise exports.

3/ Including the undepreciated book value of land, plant, and equipment.

4/ Data submitted by respondents are not comparable and, therefore, have been deleted.

5/ By the staff of the U.S. International Trade Commission based on discussions with industry and/or association representatives, and secondary sources.

Source: Compiled from data submitted in response to questionnaries of the U.S. International Trade Commission.

U.S. insurance companies with foreign operations remitted an estimated $6.5 billion or more in dividends, royalties, fees, and income from their overseas policies and investments in 1981; this represents about 6 percent of total revenue of $109.6 billion for the 14 selected service industries covered in this study (table 3). Although international business generally represents a small portion of total firm revenues (this percentage varies greatly from firm to firm), industry sources indicate that a great deal of emphasis will be placed on expanding foreign operations as competition continues to intensify in the domestic market.

Table 3.--Estimated total foreign revenue generated by the insurance service industry and estimated total foreign revenue for selected service industries, 1980-82

Year	Total foreign revenue for service industry 1/ (1)	Total foreign revenue for selected service industries 2/ (2)	Ratio of (1) to (2)
	1,000 U.S. dollars		Percent
1980	6,000,000	89,398,000	7
1981	6,500,000	109,611,000	6
1982	7,000,000	135,744,000	5

1/ Estimated based on discussion with industry and/or association representatives, and secondary sources.
2/ Based on totaling Commission estimated foreign revenue for each of the 14 selected industries covered in the study.

Source: Estimated by the staff of the U.S. International Trade Commission.

Regional and country activity

In 1981, the United Kingdom, Australia and Canada were the most active country markets for insurance firms responding to the questionnaire (table 4). Most insurance companies directed their international operations to Europe and Latin America in 1981. In terms of revenues, Europe and the North American markets (Canada and Mexico) were the largest markets, followed by the Far East and Latin America.

Table 4.--Regions and countries in which revenue is generated by insurance service firms, 1980-82 1/

Region and country 2/	Number of responses			Percent of total respondents			Estimated revenue		
	1980	1981	1982	1980	1981	1982	1980	1981	1982
							------1,000 U.S. dollars------		
Middle East	5	6	5	33	40	33	17,784	23,330	20,468
Iraq	-	1	-						
Israel	-	5	-						
Kuwait	-	3	-						
Lebanon	-	3	-						
Saudi Arabia	-	5	-						
United Arab Emirates	-	1	-						
Far East	8	10	7	53	67	47	299,019	395,318	369,636
Australia	-	10	-						
Taiwan	-	5	-						
Japan	-	8	-						
Malaysia	-	1	-						
New Zealand	-	4	-						
Philippines	-	1	-						
Latin America	10	11	9	67	73	60	87,749	227,148	363,639
Brazil	-	6	-						
Chile	-	4	-						
Colombia	-	4	-						
Ecuador	-	1	-						
El Salvador	-	1	-						
Guatemala	-	2	-						
Panama	-	4	-						
Peru	-	1	-						
Venezuela	-	7	-						
Europe	10	12	9	67	80	60	1,238,613	1,714,578	417,980
Belgium	-	2	-						
West Germany	-	4	-						
France	-	9	-						
Italy	-	2	-						
Netherlands	-	5	-						
United Kingdom	-	12	-						
Africa	6	8	5	40	53	33	75,904	39,124	38,041
Algeria	-	1	-						
Ivory Coast	-	2	-						
Kenya	-	2	-						
Liberia	-	1	-						
Morocco	-	1	-						
Nigeria	-	3	-						
South Africa	-	8	-						
Zambia	-	1	-						
Zimbabwe	-	2	-						

See footnotes at end of table.

Table 4.--Regions and countries in which revenue is generated by insurance service firms, 1980-82 1/--Continued

Region and country 2/	Number of responses			Percent of total respondents			Estimated revenue		
	1980	1981	1982	1980	1981	1982	1980	1981	1982
							1,000 U.S. dollars		
Canada	9	10	8	60	67	53	895,758	1,098,689	1,111,527
Mexico	4	7	4	27	47	27	5,752	8,479	175,331
Other	9	9	8	60	60	53	294,051	342,079	173,627

1/ Country listing is for 1981 only.

2/ The data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 28 firms surveyed; respondents represent an estimated 66 percent of the foreign revenue of the estimated 60 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Trade in Merchandise Generated by Trade in Services

Based on information provided by questionnaire respondents, international trade in merchandise directly generated by the insurance service industry is negligible. There are small amounts of indirect product trade believed to be generated in the United States and by host and third countries as a result of insurance service activities abroad.

The number of positive responses to a series of questions asked to determine whether or not U.S. merchandise exports are generated by U.S. insurance service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
Do you believe that U.S. merchandise might be used as a result of the services your firm provides abroad?--	4	27
Is U.S. merchandise specified or recommended in the course of providing you service?------------------	1	7
Are U.S. merchandise exports believed to be directly generated?------------	0	0

1/ The data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 28 firms surveyed; respondents represent an estimated 66 percent of the foreign revenue of the estimated 60 major firms believed to be operating internationally in 1981.

1/ "Host-country merchandise shipments" refers to the shipments (within the host country) of host-country-manufactured products which are generated by U.S. service operations in the host-country market. "Third-country merchandise shipments" refers to the shipments of other foreign-manufactured products to a foreign market as a result of U.S. service operations in that market.

The number of positive responses to a series of questions asked to determine whether or not host-country or third-country merchandise shipments 1/ are generated by U.S. insurance service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
Do you believe that foreign merchandise might be used as a result of the services your firm provides abroad?------------------	6	40
Are foreign or host-country products specified or recommended in the course of providing your service?--	0	0

1/ The data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 28 firms surveyed; respondents represent an estimated 66 percent of the foreign revenue of the estimated 60 major firms believed to be operating internationally in 1981.

Industry sources indicate that computers, word processors, and other office equipment may be purchased as U.S. international carriers open branches or subsidiaries overseas. However, purchases of U.S. manufactured goods are often restricted because many foreign countries, including Canada, have laws that require companies to purchase locally produced goods. Another example of the indirect effects of insurance service activity on merchandise trade relates to product liability insurance. For example, before Polish hams could be shipped to the United States, foreign packing facilities had to be restructured in order to meet U.S. health requirements. Certain processing machinery was purchased, some from the United States, that would satisfy these requirements and meet U.S. insurance standards, thus minimizing product liability losses.

International insurance companies frequently are a major source of construction funds for many worldwide projects. U.S. insurers, providing financing for a particular construction site, usually require the construction company to meet U.S. safety and building standards, which are among the highest in the world. Risk managers from the United States, inspect these sites and often require that certain improvements be added to the site, such as sprinkler or fire alarm systems. Specifications for these products frequently require their purchase from the United States, but are subject to local purchase regulations. Thus, insurance financing may indirectly affect the purchase of U.S.- and foreign-produced goods.

1/ "Host-country merchandise shipments" refers to the shipments (within the host country) of host-country-manufactured products which are generated by U.S. service operations in the host-country market. "Third-country merchandise shipments" refers to the shipments of other foreign-manufactured products to a foreign market as a result of U.S. service operations in that market.

International Service Trade Barriers

Discussion with industry sources indicate that insurance operations in international markets can be affected by a number of restrictions tailored to the insurance industry specifically or by those that apply to investment generally. In many countries, regulations pertaining to foreign insurers are vague and can result in arbitrary or discriminatory decisions against foreign companies wishing to enter a market. Occasionally, problems develop when government regulatory bodies are allowed to exercise considerable discretion in interpreting regulatory procedures.

Sources point out that a particular problem for companies wishing to invest in a Third World country is the rising tide of nationalism within many of those countries. The need for strengthening national identity has led many countries to nationalize all financial-related operations or to assume majority control of the local operations. Most developing countries desire to be economically self-sufficient and although they need insurance services, they do not wish to see valuable capital assets leave the country. Other countries may take less drastic steps to protect their insurance industry, such as discriminatory tax laws favoring local over foreign operations, exclusion of foreign branch operations, requirements for local incorporation and local majority control of businesses, or compulsory investment in pet government funds held in public trust by financial institutions.

In a recent study published by the U.S. Department of Commerce entitled "International Trade Issues in Insurance," Commerce groups barriers to trade in insurance into three general categories: (1) access to market and establishment; (2) transaction and financial operations; and (3) equivalent competitive position. 1/ A detailed listing of trade barriers compiled from responses to the questionnaire, which largely confirm the trade problems cited in the Commerce study are provided in table 5; the citations provide specific examples of alleged measures employed to restrict international insurance trade, and are discussed below in the context of the three major categories. Several respondents mentioned barriers not specifically mentioned in table 5, these include administrative delays in acting on license applications, the cost of equipment and the fact that only local citizens were permitted to obtain a broker's license.

Restrictions on access to market and establishment may take several forms. These restrictions have the effect of either denying U.S. firms entry to a specific market or severely limiting their activities if they are allowed entry. Frequently, locals may be required to purchase insurance only from a State-owned insurance agency which creates a monopoly for the government. Some governments may pursue policies which discourage nationals from buying insurance from foreign companies, specifically by refusing to allow residents to charge premiums paid to foreign insurers as tax deductible business expenses. Another common restriction is to tax insurance placed with outside insurers. Arbitrary or discriminatory licensing procedures have been applied by some governments as a means of denying or limiting foreign participation in the market. Some foreign governments, especially in less developed countries

1/ International Trade Administration, U.S. Department of Commerce, "International Trade Issues in Insurance," Oct. 5, 1981.

Table 5.--Trade barriers to international services in the insurance services industry 1/

Category and barrier	Number of responses	Percent of total respondents
Right of establishment	13	87
Restrictive employment regulations (e.g. local labor requirement)	8	
Credit, investment or financial activity restrictions	7	
Administrative/ownership restrictions	8	
Entry of service personnel and specialized tools	4	
Citizenship/residency requirements	4	
Restrictive government/business regulations	7	
Limiting number of establishments	3	
Grandfather clauses requiring practice before specified date	3	
Reinsurance based on local assets	6	
Special deposit requirement for foreign companies	9	
Commission terms less favorable than national companies	3	
Other (delays in approving license applications)	1	
Trade in goods	3	20
Restrictive regulations or administrative procedure	1	
Local purchase requirements	1	
Restricting entry of equipment or supply	1	
Trade in services	13	87
Restrictive government/business regulations and administrative procedures	10	
Restriction related to resident firm preference (fixed percentage of service must be provided by domestic resident companies)	8	
Employment related restrictions on non-nationals	8	
Operating/ownership restrictions	10	
Discriminatory taxation	6	
Prohibition on services offered by non-resident companies	9	
Other (Investment problems with joint real estate ventures)	1	
Technical issues	4	27
Lack of security control	1	
Privacy restrictions	2	
Contract enforcement problems	2	
Strict responsibility requirements for handling consumer complaints	1	
Discriminatory bilateral agreements	1	
Governmental paper requirement for importing	1	
Discriminatory standards requirements	1	

See footnote at end of table.

Table 5.--Trade barriers to international services in the insurance services industry 1/--Continued

Category and barrier	Number of responses	Percent of total respondents
Licensing	8	53
Licensing procedures	5	
Licensing restrictions (e.g., quotas)	5	
Refusal to license or renew	6	
Government procurement	4	27
Preference given to national firms	4	
Prohibition of foreign services contracts (bilateral or multilateral	1	
Customs valuation	3	20
Discrimination in customs vaulation between computer and data processing services transmitted through a tele-communications system or trans-ferred through physical software products	2	
Discriminatory tariffs and customs procedures	1	
Subsidies/countervailing duties	2	13
Tax benefits (e.g., rebate or tax breaks)	2	
Insurance paid by government for local firm (e.g., inflation insurance)	1	
Direct financial aid to local firm by government	1	
Preferential financing arrangements	1	
Standard/certification	1	7
Health and safety requirements	1	
Professional qualification restrictions	2	13
Professional license required ro practice	1	
Other (broker license restricted to locals)	1	
Foreign exchange controls	11	73
Restrictions on remittances	11	
Convertibility limitations	9	
Delays in obtaining foreign exchange permit	6	

1/ The data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 28 firms surveyed; respondents represent an estimated 66 percent of the foreign revenue of the estimated 60 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

(LDC's), have recently prohibited any further establishment of branch operations or have required local companies to incorporate with existing branch offices. Finally, local governments can impose national majority ownership requirements.

Insurance executives have stated that restrictions on transactions and financial operations frequently impede the remittance of funds by insurers to their home office. Also, foreign admitted insurers may be required to meet and maintain more stringent minimum deposit requirements than those for the domestic companies. In a number of countries, various taxes, including income and premium taxes, fall more heavily on foreign-admitted insurers than on local insurance companies.

Industry sources also indicate that restrictions on competitive equality are becoming more prevalent as foreign governments attempt to develop their domestic insurance industries. Certain governments require that all insurance procured by government departments be placed with local insurance companies owned by local citizens. Foreign companies may be excluded from industry trade associations which provide a critical link to foreign regulators and market information. There are a wide variety of restrictions relating to employment (table 5) which may also be applied. Restrictions ranging from requirements that a certain number of local nationals be employed to delays in obtaining work permits can affect a foreign company's operations. Competitive equality restrictions also include regional agreements in the developing nations such as the Andean Pact which was created in 1968 with the signing of the Agreement of Cartagena by Chile, Colombia, Peru, Ecuador, and Bolivia. Chile has since resigned from the pact and Venezuela has joined. The concern of the pact has been primarily with creating a common market for trade in goods. Unlike the European Community (EC), it has not focused on the movement of capital, labor and services. The pact required multinational firms such as insurance companies to divest themselves of affiliates over a period of time and it has also imposed severe restrictions that determine who may invest within selected economic sectors. 1/ Industry sources believe that this agreement is also intended to reduce foreign participation in the insurance industries of signatory countries. Venezuela, in particular, has excluded foreign companies from conducting business. 2/

Industry sources have identified other barriers to doing business in Latin America including the fact that local authorities want all accounting information written according to their specifications. Although the companies generally keep computer records based on home-office standards, they must maintain a separate set of handwritten books. Additionally, many countries, including Mexico, decree the salary increase and the level of social benefits that the foreign company may offer to its employees.

A variety of channels are currently utilized by the insurance industry to address international issues and to deal with specific problems in international insurance operations. The Insurance Committee of the Organization for Economic Cooperation and Development meets twice a year, and

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1/ Ronald Kent Shelp, Beyond Industrialization: Ascendancy of the Global Service Economy, New York, NY., 1981, p. 113-114.

2/ Sherman J. Olson, "Foreign Laws and Markets-A World Tour of Insurance," Risk Management, November 1980, p. 38.

the Committee on Invisibles and Financing relating to Trade of the United Nations Conference on Trade and Development convenes meetings on insurance matters approximately every 2 years.

The insurance industry has attempted to adapt to the myriad of restrictions which limit its foreign trade and in certain cases has come to terms with the respective governments involved to become successful in many countries. However, all insurance companies responding to the questionnaire reported that their service activities overseas would increase, absent existing barriers. Discussion with industry sources suggests that the industry would like to see some U.S. Government intervention on its behalf to deal with continuing trade problems.

The number of responses to a question to determine the economic effects of international barriers to U.S. service trade and associated product exports in insurance service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
What effect, if any, would reduction or removal of service trade barriers have upon your receivable, billings, or revenues in current or potential country markets?:		
Increase	9	60
Decrease	0	0
No effect	3	20
What effect, if any, would reduction or removal of service trade barriers have upon potential U.S. products exports in current or potential country markets?:		
Increase	2	13
Decrease	0	0
No effect	7	50

1/ The data are for questionnaire respondents only. The total number of respondents in this service industry was 15 of 28 firms surveyed; respondents represent an estimated 66 percent of the foreign revenue of the estimated 60 major firms believed to be operating internationally in 1981.

Respondents indicating that reduction or removal of trade barriers would have a positive effect on foreign revenues, indicated that trade would increase in a range of 10 to 30 percent in Europe, 20 to 200 percent in Latin America, 30 to 80 percent in Canada and 50 to 100 percent in the Middle East (table 6).

Table 6.--Estimated changes in revenues absent trade barriers to international business of insurance service firms, by areas 1/

Area and direction of change	Number of responses	Percentage change							
		10	20	30	40	50	60	80	Other
Middle East:									
Increase	2					1			1(100)
Decrease									
Far East:									
Increase	4	1	1	1		1			
Decrease									
Latin America:									
Increase	5		1	1		1			2(100)
Decrease									(200)
Europe:									
Increase	4	3		1					
Decrease									
Africa:									
Increase	3	1				1			1(100)
Decrease									
Canada:									
Increase	6			1		4		1	
Decrease									
Mexico:									
Increase	2					2			
Decrease									
Other:									
Increase	-								
Decrease									

1/ The data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 28 firms surveyed; respondents represent an estimated 66 percent of the foreign revenue of the estimated 60 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Conditions of Competition in Current and Potential Service Markets

Competition in the insurance industry, both in the domestic and international markets, is extremely intense. There are several hundred firms competing for business in world markets. As the current recession in the U.S. continues, many companies have begun to tailor their policies to attract more customers in a stagnant domestic market. The growth of U.S. multinational corporations in general has generated increased opportunities for the U.S. insurance industry in world markets. U.S. corporations prefer to insure their international operations through a U.S. carrier unless they are prohibited from doing so by local regulations.

There are numerous competitive impediments which restrict international commerce in insurance. Many U.S. companies allege that they have found it increasingly difficult to gain access to foreign markets and to enjoy competitive opportunity equivalent to that of local insurers once inside the market. Additionally, there are special problems that must be considered in underwriting all insurance in a foreign country, such as the political climate, potential for terrorism or violence, and restrictions on the repatriation of currency to the home office. Many industry spokesmen point out that these currency restrictions, in general, have more negative impact than virtually any other competitive problems.

Industry sources indicate that U.S. companies enjoy virtually no specific technical or administrative advantage over other foreign-based large multinational insurance companies. However, U.S. companies may possess some competitive advantage in the fact that some of them are very large and have available more capital and cash reserves, which provide a greater opportunity to offer primary insurance or reinsurance on large international projects. This potential advantage is offset by the number of restrictions that nations impose on foreign insurers and on the freedom of residents to purchase insurance from international companies.

Due to proximity, Canada is probably the largest market for major U.S. insurers and many companies have operations there that they do not consider "foreign." The European market is particularly attractive to many U.S. insurers because of the opportunities for investment as well as potential insurance customers. However, U.S. companies face aggressive competition from English, French, and German companies. London is still one of the predominate insurance markets in the world, as well as being the home of the largest and most famous conglomerate, Lloyds.

According to industry sources, the EC presents several unique problems for companies wishing to do business in Europe. Since the establishment of the EC, in 1956, there has been a long liberalization process aimed at providing freedom of insurance trade in the EC. If a company is incorporated and headquartered in the EC, even if that company's capital is wholly or partially owned by interests outside the EC, it is nevertheless an EC company with the same rights and privileges as a company owned by the nationals of EC member-countries. However, companies not headquarted in the EC are subject to different treatment. The principal difference is that the treatment of agencies and branches from third countries is left to the discretion of local supervisory authorities. Thus, authorities are not prevented from applying more stringent financial requirements to non-EC companies, nor do they automatically have to issue licenses to applicants headquartered outside the EC, as they are obliged to do for qualified companies from EC countries. 1/ These regulations frequently make it more difficult for American companies to enter or expand in a market many industry sources believe is one of the most lucrative in the world.

1/ Ronald Shelp, Beyond Industrialization, p. 138.

The insurance market in Asia is centered around Japan which is probably the third or fourth largest market in the world. It is dominated by insurance companies associated with Japanese conglomerates and, although foreign insurance companies have been in the Japanese market for many years, they have an extremely small share of the market, not more than 2 to 3 percent. 1/ U.S. companies have operations in most other Asians countries and have been greatly interested in the People's Republic of China since the opening of diplomatic and economic relations.

Basically, most Third World and developing nations are viewed by the U.S. industry as potential markets for either entrance or expansion by most U.S. companies operating in world markets. The LDC's generally need expertise and capital, especially in areas relating to financial affairs and insurance. American companies are willing to provide these and additional services but must comply with a complex array of restrictions and the feelings of nationalism present in most of these countries. In many of these countries around the world, even where private insurance companies are allowed to operate, local government institutions are very prominent in providing workers compensation, group life and other types of insurance. 2/ U.S. companies are experienced in providing reinsurance or types of insurance the national companies are not prepared or willing to offer.

U.S. insurance companies operate principally in the industrialized nations of the world as evidenced by questionnaire respones in table 7. Canada, the United Kingdom and West Germany are shown to be principal markets. Third World countries appear to be important areas for potential development, although respondents were unable to identify the number of competing firms in all cases. Europe in general appears to be the geographical area with the largest number of competing firms.

There are a variety of reasons why U.S. firms felt they lost business in world markets. The overwhelming reason cited by questionnaire respondents was lower price, particularly in the United Kingdom. Political or regional bias was the next most frequently cited reason (table 8). The trade barriers were mentioned principally for Europe or other industrialized countries.

Table 9 shows that U.S. firms believe that financial strength is the most likely reason for their competitive strength in existing foreign markets. Other frequently mentioned reasons include experience in the market or service and superior quality association. Table 10 also shows that financial strength of U.S. firms is their greatest asset in potential foreign markets, along with superior quality and advanced technology. No U.S. firm that responded to this questionnaire felt that lower price was a competitive advantage.

1/ Sherman J. Olson, "Foreign Laws and Markets," Risk Management, November 1980, p. 43.
2/ Ibid, p. 50.

Table 7.--Number of firms competing 1/ with U.S. insurance service firms abroad, by principal service markets 2/ in order of revenue generated, 1981 3/

Service market	Number of competing firms				
	Total	National	Regional	World-wide	Other U.S. firms
Canada	11,988	182	11,618	41	147
United Kingdom	5,465	3,780	200	1,385	100
West Germany	405		43	347	15
Japan	68	22	7	31	8
France	375	229	50	90	6
Belgium	354	184	162		8
Netherlands	2,985	65	1,820	1,088	12
Australia	100	45	5	25	25
Brazil	95	80		10	5

1/ Based on 8 responses by questionnaire respondents.

2/ Other principal service markets for the industry may not be listed here if respondents did not identify the number of competing firms.

3/ The data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 28 firms surveyed; respondents represent an estimated 66 percent of the foreign revenue of the estimated 60 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 8.--Likely reasons 1/ for competing firms' success in world insurance service markets, by base countries of firms 2/

Base country	Lower price	Technology expertise	Preferential financing	Experience in the market or service	Superior quality association	Political or regional bias	Government support	U.S. restrictions
Australia	1			1		1		
Brazil			1	1		1		
West Germany	2			1		1		
France	3		1	2		3	1	
Italy	1							
Netherlands	2					1		
United Kingdom	6			2		3		
Canada	1				1			
Other	1			1		1		
Total	17		2	8	1	11	1	

1/ The importance of each reason is indicated by the number of times each was designated, based on 8 responses.
2/ The data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 28 firms surveyed; respondents represent an estimated 66 percent of the foreign revenue of the estimated 60 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 9.--Likely reasons 1/ for the competitive strength of U.S. insurance service firms in foreign service markets 2/

Service market	Lower price	Technology lead	Financial strength	Experience in the market or service	Superior quality association	Other
Far East:						
Japan		1	1	1	1	
New Zealand			1	1		
Central and South America (excluding Mexico):						
Panama			1			
Venezuela			1		1	1
Europe:						
Australia			1	1	1	
West Germany		1		1	1	
France	1	1	2	2	2	
Netherlands			1		1	2
United Kingdom		2	5	3	5	1
North America and Mexico:						
Canada		2	3	3	1	
Total	1	7	16	12	13	4

1/ The importance of each reason is indicated by the number of times each was designated, based on 8 responses.

2/ The data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 15 of 28 firms; respondents represent an estimated 66 percent of the foreign revenue of the estimated 60 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 10.--U.S. insurance service firms' competitive strengths 1/ in potential foreign markets 2/

Potential service market	Lower price	Technology lead	Financial strength	Greater experience	Superior quality	Other
Far East:						
China			1		1	1
Japan		1	1	1		
South Korea			1		1	1
India		1	1		1	
Indonesia		1	1		1	
Central and South America (excluding Mexico):						
Brazil		1	1	1	1	
Peru			1		1	1
Colombia		1	1		1	
Europe:						
Austria			1		1	
Belgium		1	1			
West Germany		3	1	1	2	
France		1	1	1	1	
Spain		1			1	
United Kingdom		2	2	1	1	
Africa:						
South Africa		1	1	1	1	
Other		1	1	1	1	
Total		15	16	7	15	3

1/ The importance of each reason is indicated by the number of times each was designated, based on 9 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service was 15 of 28 firms surveyed; respondents represent an estimated 66 percent of the foreign revenue of the estimated 60 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

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Motion Picture Services

Executive Summary

1. International billings for motion picture and television tape and film amounted to approximately $1.37 billion in 1981.

2. U.S. merchandise trade flows resulting from this industry's overseas activities are largely indirect. Motion picture and television films and tapes serve as advertisers, creating a demand among viewers for what they have seen.

3. Half of the questionnaire respondents indicated that host- or third-country merchandise shipments might be generated as a result of U.S. motion picture services abroad. Such shipments are generally considered to be indirect; for example, many foreign manufacturers are involved in making film-related products.

4. Despite many years of involvement and success in overseas markets, the motion picture services industry has encountered numerous trade barriers abroad. These barriers limit revenue and profit potential and may also inhibit expansion into new markets. Of particular concern to the industry is the effect trade barriers may have on industry efforts to capitalize on the new electronic technologies. Types of barriers cited most frequently were (1) right of establishment, (2) commercial counterfeiting, and (3) foreign exchange controls.

5. All questionnaire respondents indicated an increase in revenues, ranging from 10 to 30 percent, would occur if some or all trade barriers were removed. Three-quarters of all respondents indicated U.S. merchandise exports would increase if service barriers were removed.

6. For the most part, competition with U.S. films in any given country comes from that country's local industry. The success of U.S. films against local ones depends on the openness of a particular market as well as public tastes and preferences.

7. Questionnaire respondents indicated that market experience and the superior quality associated with U.S. films were the two principal reasons for the U.S. industry's competitive strength abroad.

Industry Profile

Definition and coverage

The motion picture industry consists of all establishments which produce and distribute motion pictures, exhibit motion pictures in commercially operated theaters, and furnish services directly to the motion picture industry. The industry also includes film and tape production and distribution for television. This study will focus on motion picture and television production, distribution, and allied services listed under Standard Industrial Classification categories 781 and 782.

Out of 10 firms surveyed, the 4 motion picture service industry respondents to the Commission's questionnaire represent about 30 percent of the foreign revenues generated by motion picture service firms operating internationally in 1981.

Highlights in 1981

- o DOMESTIC RECEIPTS for motion picture production, distribution, and services reached an estimated $7.12 billion. 1/
- o U.S. ESTABLISHMENTS involved in motion picture production, distribution, and services is believed to have declined from a total of 10,724 (1977), but the extent of the decrease is unknown.
- o U.S. EMPLOYMENT for motion picture production, distribution, and services was approximately 82,000. 2/
- o INTERNATIONAL BILLINGS for motion picture and television tape and film amounted to approximately $1.37 billion. 3/
- o FOREIGN ESTABLISHMENTS consisted primarily of film exchanges located in some 47 countries. 4/
- o FOREIGN EMPLOYMENT in film exchange offices numbered about 6,000. 4/
- o U.S. TRADE BALANCE data are unavailable, although revenues generated by U.S. firms operating overseas are estimated to be greater than revenues generated by foreign motion picture firms operating in the U.S. market.

Industry structure

Seven companies 5/ dominate domestic film production and distribution. These companies operate both domestically and internationally. There are numerous independent film production companies as well; about six or seven of these independents are considered "submajors." Some of the submajors have their own domestic distribution systems, but they and the other independent

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1/ Estimated, based on data from the U.S. Department of Commerce.
2/ Estimated, based on data from the Bureau of Labor Statistics, U.S. Department of Labor.
3/ Estimated, based on data from industry sources.
4/ Data supplied by the Motion Picture Export Association of America (MPEAA). This figure reflects member companies only; however, MPEAA members account for the bulk of foreign establishments and employment.
5/ Since MGM purchased United Artists (UA) in 1981, they are considered one company for purposes of this report.

production companies often rely on the major U.S. studios for foreign distribution. The major studios also help with financing and domestic distribution for some of the independents.

Historically, the motion picture industry has produced films for the theater market. However, the unpredictable nature of the theatrical film business, as well as the expanded earnings potential offered by new electronic technologies, has led many of the major film producers to diversify their operations. Areas of operations besides theatrical film production include television, radio, records, video games, and amusement parks. Television programing permits an easy transition from theatrical film production, allowing fuller use of equipment and personnel.

Domestic receipts for motion picture production, distribution, and services were estimated at $7.12 billion in 1981. International billings for motion picture and television tape and film amounted to approximately $1.37 billion. 1/ The industry's domestic and foreign revenues ($8.5 billion) are small compared with total service sector revenues, estimated at $837.0 billion in 1981 for the 14 service industries covered in this study. However, the motion picture industry's long involvement and success in overseas marketing make it important to U.S. services trade.

Recent trends and outlook

Acquisitions, joint ventures, and closures are changing the structure of the motion picture industry, both domestically and internationally. The roots of these changes lie in the decade of the 1970's, when real growth occurred in movie attendance and industry profits. Near the end of the 1970's, film production increased as new film companies formed and studios stepped up production. 2/ By 1979, U.S. film production reached 248 films, its highest level since 1972. 3/

The primary reason behind the new entrants and higher production levels was the large profit potential offered by post-theater film release. Video discs, video cassettes, and cable and pay television presented the opportunity for much greater earning potential than the usual sales to network television and television syndication. However, the motion picture industry anticipated prematurely the growth in these technologies; in 1980 and 1981, industry profits fell. 4/ Although U.S theater ticket sales in 1981 hit a new record at nearly $300 billion, the number of tickets sold (1.027 billion) declined from the number sold in 1979 (1.033 billion). Increased ticket prices accounted for the record sales figure. 5/ Overseas, theater attendance was up somewhat, and sales figures were down due to exchange rate disadvantages caused by the strength of the U.S. dollar.

1/ This figure may be understated, as it does not include nontheatrical motion pictures (other than those for television).

2/ Warner Communications Annual Report, 1980-81 p. 24.

3/ Todd McCarty, "U.S. Productions in '81 off by only 2%," Variety, Jan. 13, 1982, p. 52.

4/ Warner Communications, ibid., p. 24.

5/ "Inflation Cues '81 Film B.O. Record," Variety, Jan. 6, 1982, p. 1.

Also affecting film studios' profits is the rapid climb in production, advertising, and wage costs. The average U.S. film production cost in 1981 was $9.8 million, 75 percent higher than the average cost in 1978 of $5.6 million. 1/ Marketing costs increased as producers turned to more market research and advertising in an effort to reduce the number of unsuccessful releases. As a result, consolidation has occurred in overseas distribution. Domestically, several film companies have folded or been absorbed by other companies. Some companies have cut back on production. In 1981, U.S. film producers made only 205 films. 2/ Through April of 1982, U.S. producers started only 59 pictures, down from 92 during the corresponding period of 1981. 3/

Nevertheless, analysts still foresee high profit levels resulting from the new electronic technologies, 4/ and the U.S. motion picture industry has begun to prepare for the boom. Many of the major studios and various electronics and communications companies have formed joint ventures for video distribution in the United States and abroad. In overseas markets, where television programing is limited and cable television is largely unavailable, home video equipment is quite popular. Sales and rentals of prerecorded video cassettes have already begun to produce significant revenues for the industry, reaching over $300 million in the domestic market in 1981, according to one industry source. 5/ A similar trend is likely to occur abroad, although data are not available for foreign video cassette revenues.

The expected domestic and international expansion of cable and pay television (pay-TV) and home video will create more demand for the motion picture service industry's products. Some forecasters believe that by the mid-1980's, revenues from pay television will exceed domestic theatrical billings. 6/ In 1981 alone the number of subscriptions to pay networks rose 61 percent. Even a movie that is moderately successful in the theater today can generate $5 million from the pay cable market, compared with a few hundred thousand dollars a few years ago. 7/ Home video offers the possibility of substantial profits as well, especially in overseas markets with limited television programing. Already, 15 percent of homes with television in Scandinavia have video cassette recorders (VCR's), 8 to 10 percent of those in Great Britain and Germany, 7 percent in France, and 4 percent in the United States. 8/

The future impact of cable and pay-TV and home video on theatrical film revenues is widely debated. Some in the industry think the theatrical market will feel little, if any, effect. They argue that the new technologies will

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1/ "Majors' Average Production Costs," Variety, Dec. 30, 1981, p. 1.
2/ McCarthy, op. cit., p. 52.
3/ "Hollywood's Rivals Share Its Doldrums as Production Slows," The Wall Street Journal, May 13, 1982, p. 1.
4/ Warner Communications, ibid., p. 24.
5/ Warner Communications, ibid., p. 28.
6/ Warner Communications, ibid., p. 24.
7/ Warner Communications, ibid., p. 25.
8/ Laura Landro, "RCA, Coke Unit Form Venture on Home Video," The Wall Street Journal, June 29, 1982, p. 10.

appeal to a new market that seldom attends movie theaters. 1/ Other analysts foresee reduced theatrical attendance as theater ticket prices rise in response to efforts by theaters to compete for film rentals with cable and pay-TV and homevideo. 2/ Movie studios would prefer a healthy theater industry, for a film that does well at the boxoffice commands a higher price on both network and cable television and generates more home video interest than a film made just for television. 3/

More legal action may result as the expansion of the electronic technologies increases the number of disputes over copyright and royalty payments. Efforts of investigators with the Motion Picture Association of America (MPAA) have already resulted in civil suits against alleged videotape piracy by retailers in Chicago and San Diego; more suits are expected across the United States. 4/ The U.S. Congress is currently considering legislation to establish royalties on purchases of VCR's and blank video cassettes. Some European governments are also considering a tax on blank cassettes as well as tighter copyright laws. 5/ In what some industry analysts believe will be a landmark decision, the U.S. Supreme Court has agreed to decide if the use of VCR's to tape television shows violates Federal copyright law (A U.S. appeals court ruled in the fall of 1981 that such use was in violation of copyright law). 6/

U.S. Service Operations in Foreign Markets

The U.S. motion picture industry has a long history of involvement in foreign markets. Early in this century, U.S. filmmakers realized that once a film was produced, duplicate copies were inexpensive to make; these duplicates could be rented cheaply abroad and still be a profitable venture. By 1925, U.S. filmmakers had developed strong markets in Europe, the Far East, Latin America, and parts of Africa. U.S. distribution chains were set up worldwide and have remained ever since. 7/

While some domestic film production is done overseas (126 films were made abroad in 1979; 79 in 1981 8/), 9/ the U.S. motion picture industry's foreign operations consist mainly of marketing and distribution. Films are usually

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1/ Warner Communications, p. 25.

2/ Theodore A. Nelson, "Motion pictures," U.S. Industrial Outlook 1982. p. 421.

3/ Nelson, op. cit., p. 421.

4/ Landro, "Movie Firms Sue....." op. cit. p. 12.

5/ Syd Silverman, "Show Biz: Never the Same," Variety, Jan. 13, 1982, p. 72.

6/ Stephen Wermiel, "Supreme Court to decide if Copyright Law is violated in home use of video recorders, The Wall Street Journal, June 15, 1982, p. 4.

7/ Tino Balio, ed., The American Film Industry, Madison, Wis., 1976, pp. 387-409.

8/ Will Tusher, "Majors' O'Seas Gross 30-35% of Total?" Variety, Mar. 3, 1982, p. 5.

9/ The amount of filming done overseas depends on a variety of factors. Sometimes producers can take advantage of incentives such as low-interest loans, tax breaks, and cash subsidies. In other instances, a foreign locale may be more suitable to a film's theme.

rented, rather than sold. The industry relies heavily on its export markets to recover the high costs of film production. During the past several years, the foreign market has accounted for between 40 and 50 percent of total theatrical billings. 1/

Close to 90 percent of U.S. film exports originate from the seven major studios. 2/ All of the majors belong to the Motion Picture Export Association of America (MPEAA). 3/ Association members have offices in approximately 47 countries and employ some 6,000 people to assist in film negotiations and distribution. 4/

Licensing, subsidiaries, foreign affiliates and joint ventures are the primary arrangements made by the responding film companies for overseas distribution (table 1). Each major studio has an international division which handles foreign distribution. Although most major studios in the past had their own foreign distribution channels, costs in recent years have led some studios to consolidate their systems. The largest releasing organization overseas is United International Pictures (UIP), the result of a recent consolidation of two distribution systems. Three major studios 5/ participate in this system, which is trying to cover as many world markets as possible. The submajors and independent film companies often arrange film distribution overseas through the major studios' distribution channels.

When possible, a major studio will open its own subsidiary in a foreign country. This is the primary method of operation in major markets overseas. If the market does not justify that type of expense or if a country's laws do not permit such organizations, an agent may be licensed to arrange distribution in a given territory or territories, or other distribution arrangements are made, depending on what local laws allow. A substantial number of submajors and independents negotiate film distribution abroad through agents that deal with local representatives. In this arrangement, both the studio and the agent or subdistributor agree on a percentage of the gross and share the expenses involved.

Distribution of television film and tape is handled somewhat differently from that of theatrical distribution. According to industry sources, about 65 percent of foreign television revenues are generated by the major studios. As in theatrical distribution, the studios have sales organizations abroad. However, since television is not as prevalent as movie theaters, and since television sales are primarily to monopoly buyers, television sales organizations are neither as widespread nor as large as those for theatrical sales. 6/

1/ Tusher, op cit., p. 52.

2/ "Motion Pictures," International Operations of U.S. Service Industries: Current Data Collection and Analysis, Economic Consulting Services, 1981, p. 224.

3/ The MPEAA is a Webb-Pomerene association organized in 1946.

4/ Data provided by MPEAA.

5/ MGM-UA is counted as one although it may be distinguished as two major studios in some articles on the industry.

6/ Based on discussions with industry.

Table 1.--Operating structures of principal service activity, and revenues associated with secondary service industry activities of motion picture service firms in foreign markets, 1981 1/

Item	Revenues	Number of responses	Percent of total respondents
	1,000 U.S. dollars		
Operating structure:			
Foreign affiliate	-	2	50
Joint venture	-	2	50
Licensing	-	4	100
Subsidiary or branch	-	2	50
Franchising	-	1	25
Secondary service activity:	2/		

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 10 firms surveyed; respondents represent about 30 percent of the foreign revenues generated by motion picture service firms operating internationally in 1981.

2/ No secondary activities were indicated by the service industry respondents.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Questionnaire data on foreign operations were incomplete with regard to billings, operations, and number of establishments. The four respondents showed a slight increase in 1981 billings over what they were in 1980, in contrast to estimates for the entire sector which showed 1981 billings ($1.37 billion) slightly less than 1980 billings of $1.40 billion (table 2). Table 3 shows that foreign revenues for the motion picture service industry were approximately 1 percent of total foreign revenues for selected service industries.

U.S. film producers export to about 75 countries, but the major industrialized nations comprise the primary markets for both theatrical and television film sales. Europe is the primary market, followed by the Far East. Questionnaire data (table 4) appear to support this. Japan, Canada, France, West Germany, and the United Kingdom accounted for close to one-half of U.S. remittances in 1980. 1/ European countries and Japan are favored markets; they offer much potential for cable and satellite television, video cassettes and video discs due to their higher per capita spending for entertainment. 2/

1/ Nelson, op. cit., p. 421.

2/ Economic Consulting Services, "Motion Pictures,"op. cit., p. 230.

Table 2.--Indicators of activity in the foreign and domestic operations of motion picture service firms, 1980-82

Item	Foreign	Domestic	Total
Estimated value of receivables, billings, or revenues: 1/ 2/			
1980------------------1,000 dollars--:	433,800	3/	3/
1981-----------------------------do----:	436,300	3/	3/
1982-----------------------------do----:	3/	3/	3/
Estimate of investment in physical assets 1/ 4/ in foreign operations:			
1980------------------1,000 dollars--:	3/	-	-
1981-----------------------------do----:	3/	-	-
1982-----------------------------do----:	3/	-	-
Number of establishments: 1/			
1980-----------------------------------:	299	3/	3/
1981-----------------------------------:	298	3/	3/
1982-----------------------------------:	298	3/	3/
Estimated 5/ value of total industry receivables, billings, or revenues:			
1980------------------1,000 dollars--:	1,400,000	-	-
1981-----------------------------do----:	1,370,000	7,120,000	8,490,000
1982-----------------------------do----:	1,600,000	-	-

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 10 firms surveyed; respondents represent about 30 percent of the foreign revenues generated by motion picture service firms operating internationally in 1981.

2/ Excluding the value of any merchandise exports.

3/ Data submitted by respondents are not comparable and, therefore, have been deleted.

4/ Including the undepreciated book value of land, plant, and equipment.

5/ By the staff of the U.S. International Trade Commission based on discussions with industry and/or association representatives, and secondary sources.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 3.--Estimated total foreign revenue generated by the motion picture service industry and estimated total foreign revenue for selected service industries, 1980-82

Year	Total foreign revenue for service industry 1/ (1)	Total foreign revenue for selected service industries 2/ (2)	Ratio of (1) to (2)
	1,000 U.S. dollars		Percent
1980	1,400,000	89,398,000	2
1981	1,370,000	109,611,000	1
1982	1,600,000	135,744,000	1

1/ Estimated based on discussion with industry and/or association representatives, and secondary sources.

2/ Based on totaling Commission-estimated foreign revenue for each of the 14 selected industries covered in the study.

Source: Estimated by the staff of the U.S. International Trade Commission.

Trade in Merchandise Generated by Trade in Services

Merchandise trade generated by the motion picture industry is small in terms of products the industry uses to perform its services abroad. Some film prints, negatives and movie video cassettes are exported for distribution. The most sizable trade flows, however, are indirect: products viewed in movies and spin-off novelty items, for example. Although most of the merchandise trade generated by the motion picture services industry is of an indirect nature, there are indications of some use of U.S. and host-country merchandise in the service export efforts of the motion picture industry. The number of positive responses to a series of questions asked to determine whether or not U.S. merchandise exports are generated by U.S. motion picture service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
Do you believe that U.S. merchandise might be used as a result of the services your firm provides abroad?	2	50
Is U.S. merchandise specified or recommended in the course of providing your service?	0	0
Are U.S. merchandise exports believed to be directly generated?	1	25

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 10 firms surveyed; respondents represent about 30 percent of the foreign revenues generated by motion picture service firms operating internationally in 1981.

Table 4.--Regions and countries in which revenue is generated by motion picture service firms, 1980-82 1/

Region and country 2/	Number of responses			Percent of total respondents			Estimated revenue		
	1980	1981	1982	1980	1981	1982	1980	1981	1982 4/
							------1,000 U.S. dollars------		
Middle East	4	4	3	100	100	75	4,390	4,330	3/
Israel	-	3	-						
Lebanon	-	1	-						
Far East	4	4	4	100	100	100	70,050	76,250	3/
Australia	-	3	-						
Taiwan	-	1	-						
India	-	1	-						
Japan	-	3	-						
Philippines	-	1	-						
Latin America	4	4	4	100	100	100	48,550	47,600	3/
Argentina	-	3	-						
Brazil	-	3	-						
Panama	-	1	-						
Venezuela	-	2	-						
Europe	4	4	4	100	100	100	240,850	227,400	3/
West Germany	-	2	-						
France	-	3	-						
Italy	-	2	-						
United Kingdom	-	2	-						
Africa	4	4	4	100	100	100	10,280	10,330	3/
Egypt	-	2	-						
South Africa	-	2	-						
Kenya	-	1	-						
Morocco	-	1	-						
Canada	3	3	3	75	75	75	4/	4/	4/
Mexico	4	4	4	100	100	100	20,280	22,900	3/
Other	2	2	1	50	50	25	4/	4/	4/

1/ Country listing is for 1981 only.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 10 firms surveyed; respondents represent about 30 percent of the foreign revenues generated by motion picture service firms operating internationally in 1981.

3/ Data submitted by respondents are not comparable and, therefore, have been deleted.

4/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

The number of positive responses to a series of questions asked to determine whether or not host-country or third-country merchandise shipments 1/ are generated by U.S. motion-picture service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
Do you believe that foreign merchandise might be used as a result of the services your firm provides abroad?-------	2	50
Are foreign or host-country products specified or recommended in the course of providing your service?-------------	0	0

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 10 firms surveyed; respondents represent about 30 percent of the foreign revenues generated by motion picture service firms operating internationally in 1981.

Half of those responding to this part of the questionnaire felt that the export of motion pictures might encourage use of both U.S. and host-country merchandise abroad; the other half felt no such trade flows are generated. None of the respondents specifically recommended the use of either U.S. or host-country merchandise. Questionnaire data, as well as information from industry sources, do indicate direct trade in film prints and negatives and motion picture video cassettes. However, the value of exported prints and negatives lies in the rentals they generate, not in their face value, so it is difficult to put a dollar value on this type of trade.

Despite the lack of a significant direct link with merchandise trade, there is an indirect connection between the export of goods and the export of motion pictures. Film provides a medium for any country to exhibit its way of life, its values, and its products. The extensive distribution worldwide of U.S. films has facilitated this process. People throughout the world have attempted to copy the American lifestyle as perceived in motion picture films and television programs. In the 1920's films were credited with expediting the export of American automobiles. 2/ In the post-war years, Coca-Cola benefited from movies shown abroad. Adolphe Viezzi of Unifrance, the government agency representing French film producers, noted that "If it hadn't been for American movies, it would have taken Coca-Cola 20 years longer to penetrate the French market." 3/

1/ "Host-country merchandise shipments" refers to the shipments (within the host country) of host-country-manufactured products which are generated by U.S. service operations in the host-country market. "Third-country merchandise shipments" refers to the shipments of other foreign-manufactured products to a foreign market as a result of U.S. service operations in that market.

2/ Balio, op. cit., p. 390.

3/ *Variety*, Oct. 28, 1981, p. 29.

More recently the host of science fiction and adventure features such as "Star Wars," "Superman," and "The Dukes of Hazard" has generated numerous novelty items: toys and games, clothing, lunch boxes, sheets, and books, to name a few. Records from musicals such as "Saturday Night Fever," "Grease," and "Annie" are another byproduct of films. Indeed, since film production and distribution have become more costly, studios are relying more heavily on merchandising film-related products to spread their risk. Licensing of film characters can be quite lucrative; the producer of "Annie" will receive 6 to 10 percent of the wholesale price of licensed Annie products. 1/

Although U.S. film studios can benefit from trade in licensed products, it is difficult to determine the benefit to U.S. manufacturers due to the lack of data. Some U.S. toy manufacturers hold licenses to film and television characters, but many foreign manufacturers are involved as well in making film-related products.

International Service Trade Barriers

U.S. film exporters have been quite sucessful in overseas markets. U.S. motion picture films occupy approximately 40 percent of free world screen-time. 2/ However, trade restrictions in some areas of the world have hampered service trade expansion. Although not directed exclusively against U.S. companies, the economic effects of these restrictions have had an impact on the U.S. industry due to its strong presence in, and its reliance on, foreign markets. 3/ The frequency of certain trade barriers experienced by firms responding to the Commission's questionnaire is shown in table 5; the effects of these and other barriers to the motion picture sector are discussed as follows.

Quotas form one of the major barriers to U.S. film exports. A quota may restrict either the level of film imports, as in Brazil and India, or it may allocate screen-time among domestic and foreign film products, as in the United Kingdom, Canada, and France. 4/ Much uncertainty can be caused by these quotas, for they can be set or changed arbitrarily. Awarding of an import license may depend upon agreement to aid the local film industry (through buying or distributing a local film) or upon whether a distributor has a local office (often not the case for submajor and independent producers). 5/

1/ Stephen J. Sansweet, "Columbia Hoping Big "Annie" Promotion Will Turn Costly Film Into a Phenomenon," The Wall Street Journal, May 12, 1982, p. 29.

2/ U.S. Department of Commerce, "Motion Pictures," Recent Developments in U.S. International Service Industries, 1980 op. cit., p. 93.

3/ Ibid, p. 96.

4/ For cultural reasons, subparagraph (a) of art. IV of the GATT allows screen-time quotas for cinematograph films (excluding those shown on television). Subparagraph (d) states that these quotas shall be subject to negotiation for their limitation, liberalization, or elimination.

5/ Carol Balassa, "Trade Issues in the Motion Picture Industry," Office of the U.S. Trade Representatives, Dec. 4, 1981, pp. 3-4. This report was the source of much of the background material used in this section of the report.

Table 5.--Trade barriers to international services in the motion picture industry 1/

Category and barrier	Number of responses	Percent of total respondents
Right of establishment	3	75
Restrictive employment regulations (e.g. local labor requirement)	3	
Credit, investment or financial activity restrictions	2	
Administrative/ownership restrictions	1	
Restrictive government/business regulations	1	
Special deposit requirement for foreign companies	1	
Citizenship/residency requirements	1	
Trade in goods	1	25
Local purchase requirements	1	
Trade in services	2	50
Restrictive government/business regulations and administrative procedures	2	
Restriction related to resident firm preference (fixed percentage of service must be provided by domestic resident companies)	2	
Operating/ownership restrictions	1	
Technical issues	1	25
Time limitations on franchise agreements	1	
Lack of security control	1	
Contract enforcement problems	1	
Licensing	2	50
Licensing restrictions (quotas)	2	
Licensing procedures	1	
Commercial counterfeiting	3	75
Inadequate patent or trademark enforcement	3	
Unclear definitions of trademark, patent, imported goods, or counterfeit goods	3	
Other (piracy of films)	1	
Government procurement	1	25
Preference given to national firms	1	
Customs valuation	2	25
Discriminatory tariffs and customs procedures	2	
Subsidies/countervailing duties	1	25
Tax benefits (e.g., rebate or tax breaks)	1	
Standards/certification	2	50
Origin declaration	1	
Local labor or material requirements	2	

See footnote at end of table.

Table 5.--Trade barriers to international services in the motion picture industry 1/--Continued

Category and barrier	Number of responses	Percent of total respondents
Foreign exchange controls	3	75
Restrictions on remittances	3	
Convertibility limitations	2	
Delays in obtaining foreign exchange permit	3	

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 10 firms surveyed; respondents represent about 30 percent of the foreign revenues generated by motion picture service firms operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Local work requirements, used particularly in many Latin American countries, are another restrictive device. In film production, local actors or technicians may be required to make up a certain percentage of the work force. In film distribution, film companies may have to use local laboratories for dubbing or printmaking, or use local distributors for marketing films. These requirements limit a film company's control over the production and promotion of its products.

Restrictions on remittances limit repatriation of earnings by foreign film companies. In table 5, respondents indicated that their companies have experienced convertibility limitations and delays in obtaining foreign exchange permits in addition to restrictions on remittances. Brazil, Morocco, and the Philippines are among the countries employing these types of restraints. There is some concern within the industry that more countries will move to enact such barriers.

Many foreign governments allegedly subsidize local film companies, with the justification that the domestic market alone cannot sustain a domestic film industry. Subsidies are alleged to benefit film producers in Australia, Argentina, Belgium, and Canada, and other countries through reduced financial risk and creditor requirements. Subsidy funds may come from box office taxes on films; in effect, the taxes which U.S. filmmakers pay assist their competition. Certain forms of subsidies may also encourage film production within a foreign country, with mixed benefits for local as well as foreign film companies. Canada, for example, in recent years promoted movie production within the country by altering its tax structure to allow all expenses of movie investment to be written off in the first year (this has just been changed to limit first-year write-offs beginning in 1983). 1/ The Australian Government also provides tax incentives that benefit U.S. films

1/ Jon Schriber, "Sunset Boulevard North," Forbes, Sept. 28, 1981, pp. 60-61.

and tapes. 1/ However, while U.S. producers may gain in such situations, U.S. workers suffer since these incentives are frequently tied to the use of the local work force.

Monopoly controls, reported in use largely in Communist and developing countries, result when governments prohibit foreign distributorships; this is frequently achieved through creation of local film importing agencies which can lower rental prices and selectively admit films. Television programing is especially troubled by monopoly controls because in many countries television is either partly or wholly government-owned and/or government-operated. Sellers of television programing deal with one or two buyers whose selections of programs are based on various political, economic, and social reasons. For example, one of West Germany's two television stations has a TV Council composed of 66 people from political, religious, educational, labor, and industrial backgrounds. This Council determines what will be shown and then monitors programs. 2/

Piracy is another difficult problem for the U.S. motion picture industry. Although not a new problem, piracy has increased at home and abroad due to the growth of video cassettes. In Central and South America, the Middle East, and the United Kingdom, pirated video cassettes are widespread. Inadequate patent and trademark definitions and enforcement abroad are contributing to the piracy problem, as cited by questionnaire respondents (table 5). Satellite television transmissions may create additional piracy problems until agreements on copyright and royalty payments are made.

These and other barriers restrict U.S. motion picture trade in various ways. Trade barriers in some instances prevent films from realizing their full revenue and profit potential, thereby limiting reinvestment in the industry and aggravating financing problems. Restrictions in industrialized nations may impede expansion into television and home video, the industry's most promising sources of future revenues in those countries because of sluggish theatrical markets. And in countries such as China where expansion potential for the theatrical market is greatest, trade barriers to market entry are the most restrictive. All questionnaire respondents reported that their service activities overseas would increase with reduction or removal of existing barriers. The number of responses to a question to determine the economic effects of international barriers to U.S. services trade and associated product exports in motion picture service activities abroad was as shown in the following tabulation:

1/ Don Graves, "Australians Back U.S. Screen Tube Fare," Variety, Mar. 17, 1982, p. 3.

2/ "German TV: How It Works," Variety, Feb. 10, 1982, p. 74.

Question	Number of responses 1/	Percent of total respondents
What effect, if any, would reduction or removal of service trade barriers have upon your receivables, billings, or revenues in current or potential country markets:		
Increase----------------------------------	4	100
Decrease----------------------------------	0	0
No effect---------------------------------	0	0
What effect, if any, would reduction or removal of service trade barriers have upon potential U.S. products exports in current or potential country markets:		
Increase----------------------------------	3	75
Decrease----------------------------------	0	0
No effect---------------------------------	0	0

1/ The total number of respondents in this service industry was 4 of 10 firms surveyed; respondents represent about 30 percent of the foreign revenues generated by motion picture service firms operating internationally in 1981.

Respondents indicating that reduction or removal of trade barriers would have a positive effect on foreign revenues reported that trade would increase 10 to 30 percent in the Middle East, and from 10 to 20 percent in Latin America and the Far East (table 6).

Table 6.--Estimated changes in revenues absent trade barriers to international business of motion picture service firms, by areas 1/

Area and direction of change	Number of responses	Percentage change						
		10	20	30	40	50	60	80
Middle East:								
Increase	2	1		1				
Decrease								
Far East:								
Increase	2	1	1					
Decrease								
Latin America:								
Increase	2	1	1					
Decrease								
Europe:								
Increase	2	2						
Decrease								
Africa:								
Increase	2		2					
Decrease								
Canada:								
Increase	--							
Decrease								
Mexico:								
Increase	1		1					
Decrease								
Other:								
Increase	1		1					
Decrease								

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 10 firms surveyed; respondents represent about 30 percent of the foreign revenues generated by motion picture service firms operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Conditions of Competition in Current and Potential Service Markets

Its distribution system and the appeal of its films form the basis of the U.S. film industry's strength in world markets. Most countries make films for their own market, and perhaps for a few neighboring countries, but U.S. films and tapes have a more transnational character. Added to this is an extensive marketing system to distribute these films and tapes all over the world. Although questionnaire response was limited, the responses indicated that market experience and superior quality association were two reasons for this industry's competitive strength overseas (tables 7 and 8).

For the most part, competition with U.S. film in any given country comes from that country's local industry. The success of U.S. films against local ones depends on the openness of a particular market as well as the public demand. For example, in India, the world's largest movie producer, an average of 700 films are made each year. Government censorship combined with an audience of widely varied social, educational, and political backgrounds have created a difficult market for any foreign films to enter. Even locally produced films have only a 20-percent success rate. 1/ In Europe, where Italy and France are major filmmakers, U.S. films have been more successful because of fewer trade restrictions compared with other U.S. markets and wider acceptance of the subject matter. U.S. film companies in 1981 were estimated to have a 35-percent share of the French film market. 2/

In many instances, the U.S. film industry actually fosters the existence of local film industries. This occurs when U.S. film producers hire local workers, use local film laboratories, or keep theaters and television stations open by paying taxes and by creating an interest in motion pictures. Some countries probably could not maintain a domestic film industry without U.S. films and film producers.

There is resistance to U.S. film exports abroad, stemming in part from many countries' efforts to establish a natural cultural identity through film and other art forms. 3/ The strong presence of U.S. films sometimes seems to inhibit these aims, as Rene Thevenet, president of France's independent film producers' association noted:

> . . . competition in France from American pictures has become too difficult to put up with. They are too powerful. They have behind them an enormous English-language market, and they are making features of dimensions that we cannot match. 4/

1/ Charles Michener, "India's Frantic Film Industry," Newsweek, July 20, 1981, p. 70.

2/ Variety, Oct. 28, 1981.

3/ Balio, op. cit., pp. 387-409.

4/ "Though For Open Market, French Indies Seek 50% of U.S. Profits," Variety, Feb. 3, 1982, p. 42.

Table 7.--Likely reasons 1/ for the competitive strength of U.S. motion picture service firms in foreign service markets 2/

Service market	Lower price	Technology lead	Financial strength	Experience in the market or service	Superior quality association
Far East:					
Japan				1	
Europe:					
West Germany				1	2
France					1
United Kingdom				1	2
Total				3	5

1/ The importance of each reason is indicated by the number of times each was designated, based on 2 responses.

2/ The total number of questionnaire respondents in this service industry was 4 of 10 firms surveyed; respondents represent about 30 percent of the foreign revenues generated by motion picture service firms operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 8.--U.S. motion picture service firms' competitive strengths 1/ in potential foreign markets 2/

Potential service market	Lower price	Technology lead	Financial strength	Greater experience	Superior quality
Europe:					
France				1	1
United Kingdom				1	1
West Germany				1	1
Total				3	3

1/ The importance of each reason is indicated by the number of times each was designated, based on 1 response.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 4 of 10 firms surveyed; respondents represent about 30 percent of the foreign revenues generated by motion picture service firms operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

The relatively limited degree of success experienced by foreign films in the United States adds to the resentment felt abroad toward U.S. films. Although the U.S. market is open in terms of quotas and tariffs, foreign films and programs have had difficulty entering the U.S. market. Until the 1950's and 1960's, few foreign films were shown in the United States due to the major studios' control over exhibition facilities. 1/ Although U.S. imports of foreign films have increased and fared better in recent years, they have been unable to equal the influence of U.S. films in their own countries. Distribution entry costs are high, and it is doubtful any other country will find it worthwhile to construct a film distribution network comparable to that of the U.S. industry. 2/

1/ Balio, op. cit.
2/ Ibid.

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Transportation Services, Air

Executive Summary

1. International revenues of U.S. scheduled airlines amounted to $6.4 billion of which an estimated $2.7 billion was received from non-U.S. nationals, traveling on U.S. flag carriers in 1981.

2. An estimated $57 million in U.S. merchandise exports are generated as a result of the services provided by U.S. airlines abroad. Airlines confirmed that U.S. merchandise is specified and exports are directly generated as a result of their services. Major merchandise exports included engines and parts and data processing, food preparation, and material handling equipment.

3. No data were received from questionnaire respondents which indicated that host- or third-country merchandise shipments might be generated as a result of U.S. air transportation service activities abroad.

4. Industry sources believe the most economically significant trade barriers faced by U.S. carriers are (a) the discriminatory access to and use of computer reservation systems when in competition with national carriers, (b) unreasonable charges for use of airports and en-route navigation systems, and (c) restrictions on operations.

5. The elimination of these practices and charges against U.S. carriers is estimated to have the potential to add $100 million to net earnings of the industry.

6. U.S. airlines compete in a group of the strongest airlines in the world, both in terms of operating revenues and revenue passenger miles. The top 15 world airlines account for 48 percent of the world's total scheduled traffic (passenger miles). U.S. airlines account for about 50 percent of the operating revenues of the top 15 world airlines.

7. The major competitive advantage of U.S. airlines operating internationally is their size, leadership in offering worldwide services, broad application of state-of-the-art technology, a large domestic market available for international business, and marketing/management organization.

Industry Profile

Definition and coverage

The air transportation industry consists principally of U.S. certificated scheduled airlines carrying passengers and freight. This service industry also includes certificated supplemental air carriers and noncertificated airlines, air taxis, and general aviation. The industry provides domestic and foreign air transportation of freight and passengers, operates and maintains terminal facilities, and coordinates handling services for freight and passengers at airports.

The corresponding Standard Industrial Classification (SIC) category is 45--Transportation by Air which includes, SIC 4511 (Air Transportation-Certificated Carriers), SIC 4521 (Air Transportation-Noncertificated Carriers), SIC 4582 (Airports and Flying Fields), and SIC 4583 (Airport Terminal Services).

Three airline companies responded to the Commission's questionnaire of the 23 air transportation service firms surveyed and believed to be operating internationally in 1981. Insufficient data (without disclosing the confidential operations of individual companies) were provided in the questionnaire to allow preparation of trade tables consistent with other service industry segments of this study. This report is largely based on discussions with industry and/or association representatives, and secondary sources.

Highlights in 1981

- DOMESTIC REVENUE generated by the air transportation service industry was estimated at $30.4 billion, consisting of U.S. scheduled airlines, supplemental air carriers, general aviation, air taxis, and other service functions to the airlines.

- U.S. ESTABLISHMENTS numbered 86 U.S. scheduled airlines and several hundred air taxi, general aviation, and charter operators.

- U.S. EMPLOYMENT was 462,000 persons, of which 349,864 were employed by the U.S. scheduled airlines, including international trunks.

- INTERNATIONAL REVENUE of U.S. scheduled airlines was $6.4 billion, of which an estimated $2.7 billion was received from non-U.S. nationals, traveling on U.S. flag carriers.

- FOREIGN ESTABLISHMENTS of U.S. scheduled airlines are estimated to be 980 U.S.-airline-owned ticket offices, cargo and maintenance facilities, and other support facilities.

- FOREIGN EMPLOYMENT is estimated at 12,000 non-U.S. nationals (excluding foreign-owned travel agency personnel) by U.S. airlines in their overseas establishments. This figure includes personnel at airport and off-airport locations such as ticket offices, sales, maintenance, cargo, and service facilities.

- U.S. TRADE BALANCE for international air transportation is a negative $1.1 billion. This trade balance represents the difference between receipts (exports) and payments (imports) for freight, passenger fares, and port expenditures. 1/

1/ U.S. Department of Commerce, Bureau of Economic Analysis, International Transportation Transactions of the United States, By Type (197601981 preliminary), June 1982.

Industry structure

Historically, up to January 1981, the organizational structure of the U.S. scheduled airline services were differentiated among seven types of operating authority granted by the Civil Aeronautics Board (CAB). However, as a result of simplifying CAB procedures, the classification of carriers has been reduced to four major carrier groups: (1) Majors (domestic and international) with annual operating revenues of $1 billion and over; (2) Nationals (domestic and international), $75 million to $1 billion; (3) Large Regionals, $10 million to $74.9 million; and (4) Medium Regionals, up to $9.9 million. There are also a large number of small charter airlines; however, their significance has decreased greatly since the scheduled airlines began to provide chartering service with deregulation of the industry.

Domestic and international revenue of $36.8 billion for the airline industry was generated by passengers, freight, U.S. mail, express, charter, public service, and such other revenues as excess baggage, foreign mail, miscellaneous operating revenues and revenues of supplemental and noncertificated airlines, and other transportation services. Domestic revenue generally accounts for about 80 percent of total operating revenues.

By far, the largest carrier group is the Majors (12), which accounted for nearly $30.5 billion of the airline industry's total operating revenues in 1981. This carrier group principally provides service between major cities within the United States and in intercontinental traffic. The National carriers (17), including all-cargo carriers, serve principal regional markets of the United States, connecting smaller traffic centers with larger metropolitan areas. These airlines traditionally served short-haul (average 420 miles) traffic routes, but since deregulation in 1978, they have dropped less profitable routes, consolidated their services, and rapidly expanded into national and international markets. In 1981, these carriers generated total operating revenues of $5.2 billion. The Large and Medium Regionals (57), including "commuters" and 18 new airlines, largely provide localized service and serve small regional centers. These carriers accounted for $0.8 billion of total operating revenues.

Domestic and international revenue ($36.8 billion) for the entire air transportation service industry accounted for 4.4 percent of total U.S. service trade, valued at $837 billion, in 1981 for the 14 service sectors covered in this study.

Recent trends and outlook

The current economic recession in the United States and world wide markets has caused all airline traffic to decline. Total U.S. scheduled domestic and international traffic measured in revenue passenger-miles (RPM's) declined about 3 percent in 1980 and again in 1981 by about 2.5 percent. 1/ International traffic (RPM) of U.S. carriers in 1981 declined about 8 percent from its 1980 level according to the CAB.

1/ Air Transport Association of America and CAB.

Fuel prices have significantly affected airline costs, rising from a cost 11 cents per gallon in 1970 to $1.07 cents in April 1981. Fuel price increases in 1981 alone added about $1.5 billion to airline operating costs which represented about 30.5 percent of operating expenses compared to 12.7 percent in 1970. In addition, total interest costs have tripled in the last 4 years, with each percentage increase in the prime interest rate adding $30 million to interest expense. The rise in prime rates in 1981 added $100 million of interest expense to the airlines cost structure. 1/

Strikes also have a major impact on airline costs. In 1980 and 1981, there were major strikes against airlines in the United Kingdom, Italy, Spain, Portugal, Denmark, Sweden, and France, which all affected the operations of U.S. international airlines. To illustrate the cost of strikes, the Professional Air Traffic Controllers Association (PATCO) strike in August 1981 is estimated to have caused a net loss of $150 million to U.S. carriers, not including revenue losses, which are estimated to be considerably larger. 2/ The International Air Transport Association (IATA) estimates the effect of the PATCO strike at $400 million to $500 million on non-U.S. airlines. 3/

Several structural changes in the airline industry have contributed to its unprofitable condition since deregulation. First, routes were restructured, i.e., the airlines were free to drop the unprofitable routes and compete on the more attractive, densely traveled routes. Thus, price cutting became the norm as revenues became less important to a larger number of airlines serving competitive and high-density routes with essentially the same number of passengers as before deregulation (or even fewer passengers due to the sluggish economy). Second, services and aircraft had to be more competitive and efficient, which meant additional capital outlays.

Major U.S. carriers with international operations carried 23.4 million passengers in 1980, representing an increase of 44 percent over the number in 1970 (16.2 million). Air cargo in 1980 compared with that in 1970 (5 billion ton-miles) was up 2 billion ton-miles, representing a growth of 40 percent. 4/

Between 1982 and 1990, the growth of the U.S. airlines will depend on a number of crucial factors, including the nature of recovery in the domestic and international economies, airline safety, fuel costs, the ability to generate capital, and an efficient air traffic control system. The industry expects it will need to meet substantial capital requirements in the years immediately ahead to remain competitive, by investing in fleet moderuization to increase aircraft efficiency and reduce energy consumption.

U.S. domestic traffic is expected to grow at an average rate of 4.7 percent per year between 1980 and 1990 compared with a forecast of 6.8 percent

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1/ Air Transport Association of America.

2/ Ibid.

3/ International Air Transport Association, The State of the Air Transport Industry, 1981, p. 41.

4/ Air Transport Association of America, Air Transport 1981.

for U.S. international traffic. 1/ Total world traffic is expected to grow 6.1 percent per year based on 1.0 trillion revenue passenger-kilometers (RPK's) in 1980 increasing to 2.0 trillion RPK by 1990. 2/

There will be great variations in traffic growth between the regions of the world. 3/ The large and mature regional markets (50 percent of world traffic) are forecast to experience growth that is lower than average. On the other hand, air traffic in the developing countries (25 percent of world traffic) has been increasing in relative importance and will continue to become an increasingly important market for U.S. international airlines. Forecasts to 1990 for these areas are as follows: Transpacific, 8.0-percent annual growth rate; Western Hemisphere, 7.9 percent; European intercontinental flows, 8.0 percent; and intra-Asia/Oceania, 9.5 percent.

U.S. Service Operations in Foreign Markets

Operating structure

U.S. carriers with international operations conduct business with approximately 85 foreign countries throughout the world. Bilateral agreements between governments largely control the international business operations of the air transportation industry. 4/

The Bermuda I type of bilateral agreement, conceived after World War II and periodically updated, is still in force (as of January 1982) with approximately 66 countries involved. Basically they regulate routes and pricing; the frequency and the level of service are left to the airlines. Routes are designated from and to a country, with intermediate points defined for scheduled as well as chartered service. Pricing is strictly regulated and sets forth the requirements for establishing prices to be charged by designated airlines for services over the agreed routes. Prices have to be approved by both governments before they become effective. These types of agreements are essentially restrictive and are a compromise between regulation and open competition, designed to create a balance of economic benefits for each country.

The Bermuda II bilateral agreement, negotiated during 1977 between the United States and the United Kingdom, provided more open access in routes between the countries and triggered a major turning point in U.S. international aviation policy toward a more liberalized series of "open sky" agreements, according to industry sources.

Parallel to these bilateral agreements, a system was developed by which international carriers, acting in concert through the IATA, worked out fares and rates for submission to governments for review and approval. The result

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1/ Lockheed-California Co., World Air Traffic Forecast 1970-1990, EATF/3274, September 1981.

2/ Ibid.

3/ Ibid.

4/ Air Transport Association of America, Air Service Rights in U.S. International Air Transport Agreements, a compilation of scheduled and charter Service Provisions contained in U.S. Bilateral Aviation Agreements, Feb. 16, 1981.

of this system was higher priced service channeled over a few major routes. To counteract certain restrictive competitive effects of this process and to work toward an "open sky" policy, the United States negotiated a more liberalized bilateral agreement with 15 countries. These agreements are generally characterized by increased operational flexibility for airlines and less government regulation of services.

International structure of U.S. airlines.--International air transportation is provided principally by nine major air lines. The international revenue of these nine airlines was $5.9 billion, as table 1 shows.

Table 1.--International and domestic revenues of U.S. airlines providing international air transportation, by principal airlines, 12 months ending June 30, 1981

(In millions of dollars)

Airline	Total	Total operating revenues	
		Domestic	International
American	3,854	3,498	356
Braniff 1/	1,339	950	389
Continental	983	875	108
Delta	3,555	3,411	144
Eastern	3,680	3,330	349
Northwest	1,770	1,158	611
Pan American	3,662	841	2,720
Trans World	3,386	2,272	1,113
United	4,532	4,532	-
Western	1,058	955	103
Subtotal	27,819	21,822	5,893
Other	7,809	6,369	628
Total, certificated	35,628	28,191	6,521

1/ Currently not operating.

Source: CAB, Air Carrier Financial Statistics, Twelve Months Ended June 30, 1981.

Major U.S. carriers with international service accounted for 17.9 percent of all airline revenues in 1980. They served points between the United States and foreign countries with an average length of haul of approximately 2,500 miles. As a result of deregulation, there are a growing number of other airlines in the National category, discussed in the report profile, that serve international markets. The total international revenue of these airlines was $628 million for the 12 months ended June 30, 1981 (or approximately equal to 10 percent of the revenues of all U.S. international carriers).

Some airlines tend to operate as a subsidiary of a holding or parent company in conjunction with other related services. For example, Trans World

Corp. wholly owns Trans World Airlines, Canteen Corp. Hilton International Co., and Century 21 Real Estate Corp. 1/ Pan American World Airways Inc. is the owner of Pan Am World Services Inc., providing a wide range of technical and management contract services in engineering and design, general aviation, aerospace and base support, and through a subsidiary, Airline Operations Training, Inc., provides training to domestic and foreign students in aviation related fields. 2/

The estimated international revenue generated by the air transportation service industry in 1981 was $6.4 billion, representing 6 percent of the estimated $109.6 billion in total service sector foreign revenues of the 14 service industries covered in the Commission study (table 2 and 3).

Scope of operations.--International air travel from and to the United States consisted of 39.5 million passengers 3/ (arrivals and departures) in 1980 (representing 34 percent of world international passengers). This represents a growth of 107 percent from 18.9 million passengers in 1970 (table 4) or more than 7 percent per year compounded annually. The U.S. flag share of the 39.5 million passengers was 49 percent in 1980 and has been steadily declining since 1970 when it was 55 percent.

Table 2.--Indicators of activity in the foreign and domestic operations of air transportation service firms, 1980-82

Item	Foreign	Domestic	Total
Estimated 1/ value of total industry receivables, billings, or revenues: 2/			
1980------------------1,000 dollars--:	6,543,000	27,442,000	33,985,000
1981----------------------------do----:	6,390,000	30,362,000	36,752,000
1982----------------------------do----:	6,760,000	32,932,000	39,692,000

1/ By the staff of the U.S. International Trade Commission based on discussions with industry and/or association representatives, and secondary sources.

2/ Excluding the value of any merchandise exports.

Source: Estimated by the staff of the U.S. International Trade Commission.

1/ Trans World Corp., Annual Report 1981.

2/ Pan American World Airways, Inc., 1981 Annual Report.

3/ Does not include an estimated 9.4 million persons traveling between Canada and the United States (arrivals and departures) by commercial aircraft.

Table 3.--Estimated total foreign revenue generated by the air transportation service industry and estimated total foreign revenue for selected service industries, 1980-82

Year	Total foreign revenue for service industry 1/ (1)	Total foreign revenue for selected service industries 2/ (2)	Ratio of (1) to (2)
	1,000 U.S. dollars		Percent
1980	6,543,000	89,298,000	7
1981	6,390,000	109,611,000	6
1982	6,760,000	135,744,000	5

1/ Estimated based on discussion with industry and/or association representatives, and secondary sources.
2/ Based on totaling Commission-estimated foreign revenue for each of the 14 selected industries covered in the study.

Source: Estimated by the staff of the U.S. International Trade Commission.

Table 4.--The international air passenger market from and to the United States, 1970, 1978, 1979, and 1980

Item	1970	1978	1979	1980
Persons traveling by air--------thousands--	18,960	32,750	37,296	39,519
Persons traveling by U.S.-flag carriers--------thousands--	10,470	16,381	18,945	19,397
U.S. share of international air transport market--------percent--	55	50	51	49
Persons traveling by foreign-flag carriers--------thousands--	8,490	16,369	18,350	20,115
Foreign flag share of international air transport market--------percent--	45	50	49	51

Source: U.S. Department of Transportation.

Historically, the United States has held a leadership position in international air transportation. The decline of the U.S. flag share of the market has several reasons. In the two decades following World War II, the European carriers captured a larger share of the market due to their post-World War II expansion. In the last decade, the newly industrialized and third-world nations required more air travel as a result of increased world tourism, and these national carriers have acquired an increasing share of international traffic, which is partially attributable to the more open competitive environment. Additionally, U.S. citizens constitute a declining share of all world travelers, which affects market share because a country's citizens are more likely to use its flag carriers than are foreign nationals.

Regional and country activity.--International air traffic flows between the United States and other countries in 1981 is shown in table 5. Traffic between the United States and Europe was the dominant volume, accounting for 38.2 percent of the total, followed by Central America and Mexico (18.2 percent) the Caribbean (16.9 percent), Japan and other Far East (12.9 percent), South America (8.4 percent), Oceania (3.1 percent), Middle East (1.5 percent), and Africa (0.7 percent).

The increase of traffic (arrivals and departures) to all regions was 2.9 percent for the 12 months ending October 31, 1981. Passenger volume increased to all regions except the Caribbean, where volume decreased 1.1 percent, and ranged from 1.5 percent in Europe to 9.7 percent in the Middle East. 1/

The U.S. flag carriers' share of the market was 49 percent to all regions; however, there were great differences between the regions. U.S. flag airlines carried 70 percent of the traffic to and from the Caribbean. In the most heavily traveled European market, U.S. flags carried 41 percent. In the newly emerging markets of Africa, the Middle East, and the Far East, the U.S. airlines' share was the smallest, between 35 and 39 percent. 2/

During the same period, 50 countries accounted for 96 percent of all U.S. international air passengers. However, the top 20 countries accounted for as much as 80 percent. Traffic on the average to and from the 50 countries increased 3 percent, whereas great differences existed in traffic increases between the individual countries. For example, in the over 30 percent increase were Finland, Singapore and the Mariana Islands; between 20 and 30 percent were the Philippines, Argentina, Taiwan, Guatemala, Saudi Arabia, and El Salvador and among the 10 largest traffic volume countries, traffic increased between 4.8 and 10.8 percent in the United Kingdom, Mexico, Japan, Venezuela, Dominican Republic, and the Netherlands; traffic volumes declined to and from West Germany, Bahamas, France, and Italy.

1/ Department of Transportation, Transportation System Center. Data does not include Canada.

2/ Ibid.

Table 5.—U.S. international air passengers' arrivals and departures, 1981 1/

Source/destination	Air passengers: Canada included	Air passengers: Canada excluded	Percent of total: Canada included	Percent of total: Canada excluded
	-----Millions-----			
Canada	9,664	-	19.3	-
Central America and Mexico	7,353	7,353	14.6	18.2
Caribbean	6,864	6,864	13.6	16.9
South America	3,444	3,444	6.8	8.4
Europe	15,510	15,510	30.8	38.2
Africa	307	307	.6	.7
Middle East	667	667	1.3	1.6
Japan and other Far East	5,272	5,272	10.5	12.9
Oceania	1,267	1,267	2.5	3.1
Total	50,348	40,684	100.0	100.0

1/ Includes scheduled and chartered services, U.S. and foreign flag carriers, and revenue- and nonrevenue-generating passengers.

Source: Prepared by the Commission staff based on data from the Department of Transportation, Transportation System Center, Passenger Travel Between U.S. and World Regions, Arrivals and Departures, News, Office of Public Affairs, 1982; and Statistics Canada, Travel Between Canada and Other countries, March 1982, catalog 66001.

Trade in Merchandise Generated by Trade in Services

The airlines occupy a unique position in U.S. foreign trade. They are the users, promoters, and marketeers of the world's most advanced aircraft/engine/aerospace technology. The airlines do not create this technology, but they facilitate exports by creating a need for support and complementary high-technology products throughout the world.

The international services of airlines directly generate exports for their own consumption. For example, engines, hydraulic oil, parts, and other expendible items, such as liquor kits, are brought into a country duty free. On the other hand, permanent pieces of equipment such as tractors, vehicles, jet ways and computers (reservation hardware) reportedly present a cost problem, since tariffs on certain items are often two to three times their value. Nearly all of the food and fuel is bought locally in the host country. U.S. carriers have superior reservations systems and ground handling equipment, and their competitive advantage in this area in foreign markets is largely dependent on obtaining the equipment from U.S. sources.

As a result of discussions with airlines and certain data submitted for the Commission study, it is estimated that the international service of U.S. carriers generates an annual volume of between $40 million to $70 million in exports, or 0.6 to 1.2 percent of their international revenues ($6.4 billion in 1981). While there is no direct relationship between revenues and exports, the association is suggested since the larger airlines need more equipment at foreign stations. On the other hand, the size of the exports depends on the kind of items the airline wishes to export to a certain country and the items that can be imported in the country duty free. An estimate of U.S. exports in 1980 by type, generated by foreign operations of all U.S. airlines is presented in the following tabulation:

Type	Value (million dollars)
Aircraft and parts	17
Ground and maintenance equipment	6
Food service equipment	8
Material-handling equipment	3
Printed matter	12
Uniforms	2
Plastic food and beverage containers	9
Total	57

The industry believes that international presence of U.S. airline operations generates greater exports on an indirect basis. Exports of civilian aircraft, engines, parts, and accessories from the United States approximated $14 billion in 1980. The purchase decisions of U.S. airlines encourages the sale of similar aircraft to foreign carriers and often influences production decisions of new aircraft. They point out further that the U.S. carriers' role in equipment exports cannot be determined precisely, but it is probably significant. For example, the pioneering role of the U.S. carriers in establishing international standards of passenger and cargo services, which still provides a U.S. competitive advantage in foreign markets, has a positive effect on associated product exports.

No data were received from questionnaire respondents which indicated that host- or third-country merchandise shipments 1/ might be generated as a result of U.S. air transportation service activities abroad.

U.S. international carriers have an interest in stimulating increased international trade and travel. Advertising promotions and presence around the world results in tourist flows to the United States. Foreigners traveling on U.S. airlines are estimated to have spent $12.7 billion in the United States 2/ during 1980, largely on U.S. carrier tickets, hotel, food, and ground transportation. Provision of international marketing and shipping information, and promotion of ancillary services to attract new exporters, supplements the Government's export promotion efforts.

1/ "Host-country merchandise shipments" refers to the shipments (within the host-country) of host-country-manufactured products which are generated by U.S. service operations in the host-country market. "Third-country merchandise shipments" refers to the shipments of other foreign-manufactured products to a foreign market as a result of U.S. service operations in that market.

2/ International Economic Policy Association, Aviation Services in America's International Trade: A Review Under Open Skies, 1981.

Technology used by the U.S. international air carriers also helps foreign nations to build their support and ancilliary industries, examples of which would be catering, computer services, telecommunication, tourist agencies, aerospace manufacturing, aircraft maintenance services, and cargo-handling facilities. Some U.S. airlines have been involved in operating, managing, and maintaining aircraft for another country. Others provide maintenance service and marketing on a contractual basis.

International Service Trade Barriers 1/

U.S. carriers allege that the following nontariff barriers exist in providing service to foreign routes:

1. Financial benefits are believed to be extended to most foreign national airlines by their Government, which the U.S. carriers are required to pay in order to operate in the country. One method that this can occur is in pension fund payments, which are not required by a foreign national carrier, such as one European airline which laid off all employees over the age of 55; a U.S. carrier could not afford the cost of such action and remain competitive.

2. Ground-handling labor rules imposed by foreign governments are widespread and prevent a U.S. carrier from differentiating its service when competing with a national carrier. Airlines point out they must accept the personnel which the airport provides, and in a joint service arrangement, the national carrier is served first. U.S. carriers pay a high price for lower quality service and personnel than it could provide with hiring rights.

3. Airlines are required to "hire-for-life" primarily in South American markets; however, they could hire their own people (the few allowed) if they could get work visas, which are virtually impossible to obtain; many locals are desired, but cannot be hired by a U.S. carrier. Airlines are generally only permitted to hire sales personnel and reservation (telephone) agents.

4. U.S. carriers face problems in marketing their services and utilizing their far superior reservations system; getting their computer-associated equipment through foreign customs is very expensive and often requires payments of 2 to 3 times the value of the product. An extensive example of the reservation problem that U.S. airlines face in Europe is well illustrated in a congressional statement. 2/

1/ Information in this section was largely obtained in interviews with airline representatives.

2/ Statement of C.E. Meyer, Jr., president and chief executive officer, Trans World Airlines, Inc., before the Subcommittee on Investigation and Oversight of the Committee of Public Works and Transportation, U.S. House of Representatives, July 20, 1981.

5. A U.S. carrier is very vulnerable if it can't get its hardware into the country, and often, all reservations must be made through a foreign national travel agency. In such cases, the U.S. carrier does not have equal access to the computer reservation system, and the foreign national carrier receives preferential treatment (i.e., a U.S. carrier ticket is handwritten, whereas foreign national carrier processing is virtually automatic). South America and the Caribbean also pose a major reservation problem. Mexico is a lesser problem, and equal access to data banks has been achieved.

6. Another area of major concern to U.S. airlines is the fact that they cannot advertise service (i.e., through-freight rates and intermediate stops) in Latin America, whereas the foreign national carriers can do so freely. For example, a direct flight schedule from Latin America via Atlanta to New York cannot advertise its New York destination. A national carrier flight can cite intermediate and end destinations, although it often requires a plane change. Although advertising rights are a part of the bilateral agreements, many points (such as the above) which ultimately cause problems are not initially addressed, because they are taken for granted as standard operating procedure in the United States.

7. Higher landing fees and user fees exist for U.S. carriers in Europe, compared with those of foreign national airlines. Existing bilateral agreements which limit access rights for U.S. carriers in Japan and England are viewed by industry sources as unreasonable.

8. U.S. carrier pricing and capacity have frequently been the target of restrictions, and foreign countries (i.e. Brazil) have demanded an agreement on operating procedures in cases where a U.S. carrier would not discuss pricing and capacity.

9. All-cargo carriers point out that the U.S. airlines face substantial competition in freight from JAL (Japan Airlines), Scandanavian Airlines System, Lufthansa, and generally from all established foreign carriers, which obtain significant assistance from their governments. For example, 43 percent of JAL is owned by the Government. Consequently, there is a constant interchange of personnel between JAL and the Government, and competitive decisions affecting JAL and a U.S. airline will naturally favor JAL. Also, industry representatives assert that foreign governments argue in negotiations for air freight rights on an equal basis with passenger rights, whereas U.S. air freight rights are frequently "traded-off" in favor of passenger carrier gains.

10. All-cargo carriers also cite restrictions (often monopolies by national personnel) on ground handling activity and facilities (including customs procedures, warehousing, and handling personnel) by foreign governments as a convenient way to create a market barrier. For example, while Korean Airlines built a warehouse and ground handling facility at the Los Angeles airport for $29 million, a U.S. company has been attempting for years to construct a warehouse to service its flights in Korea.

While airlines agree that most of the trade barriers listed in the Commission questionnaire are applicable to U.S. airlines, they consider the elimination of (1) discriminatory access to computer reservations, (2) restrictions on flight operations, and (3) discriminatory airport and on-route navigational charges as steps which would provide the greatest benefit to the industry. Based on discussions with industry sources and limited estimates available, 1/ these discriminatory practices and unreasonable charges which are quantifiable may amount at a minimum to $100 million annually for the U.S. international carriers.

Conditions of Competition in Current and Potential Service Markets

In 1980, U.S. international carriers offered service from approximately 70 cities of the United States. 2/ The U.S. carriers offering international service serve virtually every continent and island of the globe, connecting to over 125 countries, principalities, dependencies, and serving hundreds of cities of political, cultural, economic, tourist, and scenic importance. 3/

The major competitive advantages of U.S. airlines operating internationaly is their size, leadership in offering worldwide services, broad application of state-of-the-art technology, a large domestic market available for international business, and marketing/management organization. For example, U.S. carriers are generally recognized as having superior reservations systems and ground handling equipment, and their competitive advantage in this area is reflected by the reported difficulties encountered in obtaining the equipment and in utilizing their own personnel at many airports around the world. Ranking the world's approximately 206 scheduled airlines, five U.S. flag carriers are among the world's largest airlines (domestic and international services) along with representative carriers in France, United Kingdom, Japan, Canada, and West Germany.

1/ Ibid., p. 7.
2/ Civil Aeronautics Board.
3/ Ibid.

U.S. airlines compete among a group of the strongest airlines of the world in terms of operating revenue or revenue passenger-kilometers (RPK's) as shown for 1980 in table 6.

Table 6.--The largest airlines of the world based on revenue passenger-kilometers and total operating revenues, 1980

Airline	Revenue passenger-kilometers			Total operating revenues
	Domestic	International	Total	
	Billions			Billion dollars
United	61.4	.4	61.8	4.5
American	41.7	3.6	45.3	3.9
Braniff 1/	12.1	7.0	19.1	1.4
Eastern	42.7	2.3	45.0	3.5
Pan Am	14.0	34.3	48.3	3.6
British Airways	1.8	38.3	40.1	4.1
Japan Airlines	7.5	21.3	28.8	2.9
Air France	4.1	21.3	25.4	3.0
Lufthansa	2.1	18.9	21.0	3.0
TWA	29.8	15.9	45.7	3.4
Quantas	2/	15.7	15.7	1.0
KLM	2/	14.0	14.0	1.7
Alitalia	1.7	11.2	12.9	1.6
Air Canada	1.4	11.1	12.5	1.6
Swiss Air	.2	10.6	10.8	1.4
Subtotal	220.5	239.40	446.2	40.6
Total, world	478.0	466.2	944.2	87.5

1/ Currently not operating.
2/ Not available.

Source: IATA, World Air Transport Statistics, 1980 and International Civil Aviation Organization.

The international service of the above airlines together account for 51.3 percent of the world's total scheduled traffic (466.2 billion RPK's). The U.S. airlines are financially dominant as measured in operating revenues. Of the above-shown airlines, the U.S. carriers account for about 50 percent of the operating revenues of $40.6 billion.

In view of the significant access granted to foreign flag carriers in the U.S. market, industry representatives provided the following views on problems in gaining fair access to foreign markets and approaches taken to resolve certain concerns:

1. Foreign government ownership is an important factor to counter in order for U.S. airline companies to compete successfully. Industry points out that a U.S. carrier could be provided an offsetting advantage, such as controlled access of foreign carriers to the U.S. market to offset a government monopoly.

2. Certain industry representatives emphasize that an advantage to foreign air freight carriers in gaining U.S. market access is that the U.S. frequently obtains only "theoretical access or offsetting advantages" in foreign markets in negotiation of route agreements, where the U.S. firms have no viable market opportunity and obtain limited immediate benefit. As a result, U.S. air freight carriers' market shares have been shrinking. Industry cites as an example, granting Taiwan access to New York City (the most important access point in the U.S.), which opened major markets on the east and west coasts (also recently granted) for the first time. In return, the U.S. asked for free currency remittance, which represents a potential cost savings but doesn't generate revenues; however, Taiwan imposed controlled currency limits by regulation, and the 3-years required to complete the negotiations further diminished the value of the initial trade-off.

3. Generally, the size of the foreign market for which U.S. firms can compete is limited. One industry representative pointed out that national carriers have a lock on about 60 percent of the market, and therefore, U.S. carriers end up competing in a small segment. Industry representatives stressed that the U.S. Government cannot afford to limit its focus to improving competition among U.S. carriers, but rather must emphasize the need to address how the United States can effectively compete with the increasingly stronger foreign carriers.

4. Most U.S. airlines prefer to handle their own problems with a host country when they arise, since any U.S. Government action is likely to be viewed by the host country as harsh treatment of the problem and result in reciprocal action which may be harmful to the U.S. carriers' business and prestige.

5. While some carriers of the air passenger segment of the industry generally see no major competitive problem in the U.S. passenger market as a result of the access enjoyed by foreign carriers, the U.S. cargo carriers point to the lack of U.S. Government support for the cargo segment of the industry, which contends that air freight rights are "traded-off" to obtain air passenger gains.

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Transportation Services, Maritime

Executive Summary

1. International revenues generated by the maritime service industry are estimated to have been $5.8 billion in 1981.

2. Direct U.S. product exports generated by the industry for its own use in providing its service in foreign markets are minimal. Indirectly, U.S. maritime transportation services generate merchandise exports in that they facilitate the international transport of cargo.

3. Over sixty percent of questionnaire respondents indicated that host- or third-country merchandise shipments might be generated by U.S. maritime transportation services abroad. Two companies indicated a total of over $97 million of such shipments in 1981. These shipments are principally for support at foreign port facilities and for foreign bulk carriers acquired to support U.S. shipping operations abroad.

4. Nontariff measures hamper operations of U.S.-based maritime firms. Among these barriers, the most frequently enforced restrictions mentioned by industry sources were restrictive foreign government policies designed to nurture their own merchant marine, particularly cargo preference schemes.

5. Half of the questionnaire respondents reported that maritime service activities overseas would increase as a result of reducing or eliminating existing barriers, in the range of 10 to 30 percent in increased revenue principally in the Middle East, Far East, and Latin America. Generally, increases in U.S. merchandise trade were not expected.

6. The U.S. maritime transportation industry does not enjoy a competitive edge in the world market, as indicated by its progressively declining share of total trade carried by the world's ships. According to industry sources, the U.S. industry is vitally affected by closed market activity and intense rate competition in trade in northern Europe and the Far East.

7. The success of foreign firms in providing world maritime transportation service is generally attributed to the lower prices they are able to offer.

8. Questionnaire respondents identified superior quality service as the most important competitive strength of U.S. maritime transportation firms in world markets.

Industry Profile

Definition and coverage

The U.S. maritime transportation industry consists essentially of liner or scheduled service; nonliner or tramp service; and tanker service. This industry report is limited to those services providing freight and passenger transportation on ocean waterways. The corresponding Standard Industrial Classification category is 441 (Deep Sea Foreign Transportation). This study does not include detailed coverage of maritime services generated by "Flag of Convenience" vessels registered with such countries as Liberia and Panama or by "cross trading" (i.e., ocean transportation between two countries in a vessel registered to a third nation), because there is limited information openly available.

The 37 firms surveyed represent the 3 basic segments of the industry. The eight maritime service industry respondents to the Commission's questionnaire represent about 20 percent of the foreign revenues of the estimated 37 important maritime firms believed to be operating internationally in 1981.

Highlights in 1981

- DOMESTIC REVENUE generated by the U.S. maritime industry is estimated to have been $4.6 billion.
- U.S. MARITIME COMPANIES numbered an estimated 180, of which 9 were liner companies, which operated 581 vessels.
- U.S. EMPLOYMENT is estimated to have been 210,000 persons.
- INTERNATIONAL REVENUE generated by the maritime service industry is estimated to have been $5.8 billion.
- FOREIGN EMPLOYMENT for the maritime industry is believed to have been included in the domestic employment figure.
- U.S. TRADE BALANCE for the maritime industry is believed to have been in a deficit position given the more competitive posture of foreign shipping in the world market.

Industry structure

The maritime transportation industry is subject to a high level of government participation and regulation. The government provides subsidies, special tax and depreciation regulations, as well as preferential treatment (e.g., utilization of U.S. vessels in grain shipments) for shipbuilding and utilization of flag carriers. 1/ In fiscal year 1981, for example, 22 U.S.

1/ As of the publication of this report, the Congress and the Administration were evaluating the need for changes in the current antitrust and regulatory rules affecting the maritime industry, including considerations to allow expanded foreign construction and ownership of U.S. merchant vessels and creation of a new federally owned fleet for defense purposes.

shipping companies received government subsidies averaging $1.8 million for each of 165 ships. These subsidies, which have existed since 1936, are paid to eight companies that operate U.S. flag merchant ships on international routes. The purpose is to enable the U.S. operators to compete against foreign carriers that have low costs for labor, maintenance, and insurance, and to allow trade with foreign shippers on a more equal basis.

At yearend 1981, the privately owned U.S. flag, deep-draft oceangoing merchant fleet totaled 581 vessels (including 59 in inactive status) with a cargo-carrying capacity of 22 million deadweight tons. Compared with other merchant fleets of the world, the privately owned U.S. fleet was ranked 8th on a deadweight basis and 11th on the basis of number of ships. By way of contrast, Greece is now the world leader with 2,928 oceangoing ships, closely followed by the Soviet Union with 2,530 ships. The latest available data indicate that U.S. oceanborne foreign trade (cargo value) was about $294 billion and that of this cargo an estimated $42 billion was carried by the U.S. flag fleet.

The typical services offered by the estimated 180 U.S.-flag-shipping companies include transport of containerized cargoes, dry bulk freight (coal, grain, ores), tanker cargoes (petroleum and liquified natural gas (LNG)), and passengers. The active fleets represented by these companies in 1980 consisted of a 282 U.S. nonliner service and tanker service fleet (of freighters, tankers, bulk carriers, intermodal vessels, passenger/cargo ships, tug/barge vessels, and LNG tankers), and a U.S. liner service fleet of about 250 ships which primarily handle containerized cargo.

The U.S. liner fleet has traditionally occupied the principal position of importance in the U.S. maritime industry, due to its more than double cargo volume ($118 billion) compared with each of the other service fleets; however, it has experienced a steady decline 1/ since 1970 when there were 19 companies, and today there are 9 with a number of these reported to be in financial distress. On the other hand, certain U.S. dry bulk carriers and tankers have maintained a relatively stable competitive position although unable to add sufficient capacity to improve their potential in foreign cargo transport.

Estimated domestic and foreign revenue for the maritime transportation services industry ($10.4 billion) accounted for slightly more than 1 percent of total U.S. service trade estimated at $837 billion in 1981 for the 14 service industries covered in this study.

Recent trends and outlook

The capacity of the world's fleet has doubled to over 650 million deadweight tons since 1970, yet the volume of world seaborne trade has fallen in the past few years further intensifying the world competition. 2/ During this worldwide downturn, while the value of total U.S. foreign-trade cargo

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1/ As of January 1982, there were 241 vessels reported to be in the regularly scheduled U.S. liner fleet.

2/ "Shipwrecked by Recession," The Economist, Mar. 13, 1982, p. 74.

also has increased significantly--from $124.2 billion in 1974 to $294.3 billion in 1980 (137 percent)--the percentage of U.S. vessels used to transport this cargo has declined from 17.7 percent in 1974 to about 14 percent in 1980. In fact, industry points out, this is the core of the U.S. shipping and shipbuilding industries' problems. The United States is the world's largest trading nation, yet U.S.-flag ships have accounted for a progressively declining share of the total trade carried by the world's ships. Industry sources indicate that one important reason for this development is that U.S.-flag carriers have not invested sufficient amounts in new U.S.-built efficient dry bulk carriers and tankers to achieve full potential in foreign trade operations. Moreover, the U.S. ships that have been built, particularly prior to 1970, were of relatively small size requiring larger manning scales and overall higher operating costs. As a result, an increasing number of U.S. companies contracted to build ships in foreign shipyards and register them under so-called "flags of convenience registries" which further reduced dependence on U.S.-registered flag ships.

An industry source cited favorable loans (in some cases 80 percent financing with as low as 9-percent interest) for the purchase of cargo ships by the Korean Government as an example of the difficulty faced by the U.S. industry and the continued need for subsidies to compete on an equal footing. As another illustration, representatives cited the fact that Korea could produce a container ship equivalent in size to an aircraft carrier at a cost of $55 million, although a much smaller sized U.S. vessel would cost about $116 million, with an actual cost outlay of $58 million by the U.S. shipping company.

With U.S. world trade expanding, the present need and potential for the U.S. maritime industry, particularly for bulk carriers and tankers, seems apparent. A study by the U.S. Maritime Administration estimated that U.S. bulk trades could reach 550 million tons by the year 2000 from their present estimated 350 million tons. If this prediction is accurate, the U.S. flag share of bulk cargoes could rise to four percent in the 1980s from their present estimated 1 percent and possibly reach 10 percent by the year 2000. Such optimism must of course be tempered by the fact that the industry faces some major problems. Industry sources fear for example, that dry bulk carriers, the only bright spot on the shipping market during the past years, might be affected by the growing overexpansion of shipping capacity previously discussed. The scheduled liner trades also face major problems, particularly growing competition from nonconference outsiders. Such outsiders have been quite successful in undercutting the rate structures set by the conferences thus obtaining the conferences' high margin cargoes.

U.S. Service Operations in Foreign Markets

Operating structure

The three segments of the U.S. shipping industry--scheduled liner services, non-liner service, and tankers--operate in an intensely competitive world market which has been suffering from a worldwide economic downturn. This competitive environment is further complicated for certain segments which operate in a conference system. The bulk trades operate as a free market system, according to an industry source, whereas the liner trade operates through a conference system characterized as a legalized cartel wherein foreign carriers allegedly enjoy certain advantages, such as rebating and an ability to avoid filing tariffs, which place U.S. carriers at a competitive disadvantage.

Liner service.--Liner service is a scheduled operation by a common carrier whose ships operate on a predetermined and fixed itinerary over a given route, at relatively regular intervals. These operations are advertised considerably in advance of sailing in order to solicit cargo from the public.

Nonliner service.--Nonliner service is consists of tramp and other types of nonscheduled service which do not conform to the criteria for a common carrier in liner service. A tramp ship, in traditional terms, is one that operates on an irregular or nonscheduled basis from one port of lading to one port of discharge--carrying one dry cargo commodity, usually of low value--and from one shipper to one consignee. Some vessels in irregular service, however, may carry mixed cargoes of bulk and containerized goods. The tramp operator does not usually hold himself out as a common carrier and his ship is free to operate anywhere on any terms, not infrequently being chartered out on "time" terms. U.S.-flag tramp ships make up virtually the last remnants of the war-built merchant fleet. The 18 bulk carriers and combination carriers, totaling 548,000 deadweight tons, are considered from the standpoint of total overall fleet age and modernity to be the weakest link in the U.S. maritime industry. Of the 18 vessels believed to be operating, 11 were in foreign trade, 3 were in domestic trades; 2 were chartered to the Military Sealift Command (MSC), 1 was laid-up and 1 was undergoing conversion. When these ships, especially the nine that are 30 years or older, become inoperative from structual deficiencies or accident, they usually are not replaced by their owners.

Tanker service.--The U.S.-flag tanker fleet, until enactment of the Merchant Marine Act of 1970 which increased construction subsidies, lacked large productive tankers with which to compete effectively in the transporting of foreign trade. Notwithstanding the relatively recent increase in the construction of certain tankers between 1971 and 1979, such as Liquid Natural Gas (LNG) carriers, and tug-barge bulk liquid systems carriers, tanker cargoes carried by U.S.-flag ships in foreign trade have actually decreased, because many of the ships went into the intercoastal domestic trade. Moreover, industry points out, it is not that the new technologically advanced ships are inadequate in competing for greater cargo shares, but rather that there are not enough of these "labor savers" that have been placed in foreign trade by the U.S. industry. It should be noted, however, that although the U.S.-flag-tanker fleet constitutes less than 4 percent of the world tanker fleet, the percentage may be considerably higher since U.S. companies, primarily the U.S.-based multinational oil companies, have sizable fleets registered in other countries.

As set forth in table 1, questionnaire respondents indicated that the operating structures of maritime industry firms were primarily other than foreign affiliates and subsidiaries or branches (although these categories are far from insignificant). The "other" category reflects utilization of non-U.S.-registered flag ships by U.S. maritime companies. Two companies also pointed out that their international operations included consulting services and ancillary services related to oil exploration and refining.

Table 1.—Operating structures of principal service activity, and revenues associated with secondary service industry activities of maritime transportation service firms in foreign markets, 1981 1/

Item	Revenues	Number of responses	Percent of total respondents
	1,000 U.S. dollars		
Operating structure:			
Foreign affiliate	-	3	38
Subsidiary or branch	-	2	25
Other	-	5	63
Secondary service activity:			
Consulting and management services	2/	1	13
Other	2/	1	13
Total	2/	2	25

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 8 of 37 firms surveyed. Respondents represent about 20 percent of the foreign revenues of the estimated 37 major firms believed to be generating internationally in 1981.

2/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Scope of operations

The conference system, both the "closed" and "open" systems, is one of the oldest and most enduring institutions of the international shipping industry. 1/ The so called "closed" conferences were formed to bring an order to an industry whose savage price wars were threatening international trade; today there are nearly 400 of them. Conference members meet to discuss rates, coordinate sailing schedules, decide whose ships will serve which ports on what dates, and pool cargoes. Currently, many conferences in trades outside the United States are closed, with the result that the United States is denied membership and thus, is effectively denied access to the transporting of specific types of cargo.

U.S. scheduled liner trade, according to industry sources, is vitally affected by closed market activity and intense rate competition, particularly in trade in northern Europe and the Far East. This is illustrated, industry sources point out, by the inherent competitive disparity under which U.S. and foreign carriers operate. In the open conference system applicable to many U.S. carriers, independent (foreign) carriers can enter ships to compete for cargo originating from the United States, whereas in closed conferences the

1/ John G. Hubbell, "Save Our Merchant Marine," Resources Digest, March 1982, p. 124.

historical participants figure up anticipated tonnage and allocate among members, with stringent restrictions on expansion, and virtually no opportunity exists for entry of other carriers. This means that if an independent attempts to come into the market, the foreign governments would likely subsidize to drive them out (called "fighting ship"). In addition, although the U.S. carriers can only offer "dual rate" contracts, which allows a volume discount if shipment is made by carriers within a conference, foreign competitors (particularly in European countries) provide "deferred rebates" to assure service continuity, which returns 10 to 15 percent of the shipping cost after a certain period of time (usually 9 months). Often this problem is aggravated, industry sources note, since foreign carriers don't file their tariffs as required of U.S. carriers.

Still another facet peculiar to the maritime industry, briefly cited previously, is the phenomenon known as cross trading; that is, ocean transportation between two countries other than the vessel's nation of registry. Many of the carriers competing as cross traders in U.S. foreign commerce orginate from nations that restrict or exclude U.S. maritime cross traders. Bilateral agreements entered into by the United States with certain countries provide the foreign carriers with wide access to U.S. cross trades, but do not allow comparable access by U.S.-flag carriers.

Growth trends and U.S. investment

Certain trends occurring in international shipping trade are likely to have a dampening effect on total revenues generated by maritime transportation services. One development affecting liner trade, according to industry sources, is reduced participation of U.S. shipowners in major conference trade. Shipowners in the Far Eastern Freight Conference, industry representatives point out, have slipped from carrying almost 85 percent of trade between Northern Europe and the Far East in 1975 to less than 70 percent in 1980. During the same period, in the North Atlantic Conference, members' trade dropped from almost 60 percent to about 45 percent.

In another area, many world competitors have switched registry of their vessels to flags of convenience in order to cut costs, particularly labor costs. Between 1970 and 1981, for example, Liberia and Panama--the two most widely used flags--increased their share of the world fleet from 18 percent to 25 percent. U.S. companies, which are subject to strict regulation, cannot easily shift to such flags of convenience according to industry sources.

Currently the U.S. "flag of convenience" fleet consists of at least 639 ships--425 of them tankers (table 2). Such vessels are owned by U.S. corporations and thus, are effectively under U.S. control. Consequently, the U.S. merchant fleet is much larger than it would be were it measured only in terms of U.S.-flag ships. Conversely the shipping fleets of such countries such as Liberia and Panama may consist in the large part of U.S.-owned ships that are only registered in that country. The "flags of convenience" vessels are almost entirely tankers and dry bulk cargo vessels.

Considering these trends, overall growth in foreign revenue generated by the maritime transportation service industry is expected to be moderate. According to questionnaire respondents' data in table 3, the estimated value

Table 2.--Foreign flag ships owned by U.S. companies or foreign affiliates of U.S. companies incorporated under the laws of the United States, as of January 1, 1982

Country of Registry	Total			Tankers			Freighters*			Bulk & Ore Carriers		
	No.	Gross Tons	Dead-weight Tons	No.	Gross Tons	Dead-weight Tons	No.	Gross Tons	Dead-weight Tons	No.	Gross Tons	Dead-weight Tons
Total	639	30,239,486	60,892,022	425	26,275,734	53,472,233	99	508,522	625,975	115	3,455,230	6,793,814
Liberia	378	20,707,707	42,538,308	242	17,374,333	36,053,747	40	281,063	391,906	96	3,052,311	6,092,655
Panama	95	2,999,426	5,973,213	63	2,772,465	5,626,023	23	85,599	91,319	9	141,362	255,871
United Kingdom	69	2,951,496	5,527,037	50	2,738,292	5,215,223	12	62,960	60,073	7	150,244	251,741
France	11	1,279,754	2,540,084	11	1,279,754	2,540,084	-	-	-	-	-	-
Germany (West)	6	643,267	1,298,721	6	643,267	1,298,721	-	-	-	-	-	-
Netherlands	6	545,379	1,080,032	6	545,379	1,080,032	-	-	-	-	-	-
Saudi Arabia	2	250,824	514,756	2	250,824	514,756	-	-	-	-	-	-
Norway	10	248,517	448,848	10	248,517	448,848	-	-	-	-	-	-
Belgium	5	167,691	292,069	2	56,378	98,522	-	-	-	3	111,313	193,547
Argentina	7	127,306	213,682	7	127,306	213,682	-	-	-	-	-	-
Denmark	5	74,636	128,985	5	74,636	128,985	-	-	-	-	-	-
Canada	12	76,832	110,089	12	76,832	110,089	-	-	-	-	-	-
Australia	2	32,469	51,558	2	32,469	51,558	-	-	-	-	-	-
Honduras	7	47,301	48,472	-	-	-	7	47,301	48,472	-	-	-
Italy	2	25,960	44,159	2	25,960	44,159	-	-	-	-	-	-
South Africa	1	18,939	31,102	1	18,939	31,102	-	-	-	-	-	-
British Colonies	12	19,102	24,459	-	-	-	12	19,102	24,459	-	-	-
Finland	3	8,373	13,177	3	8,373	13,177	-	-	-	-	-	-
Costa Rica	3	5,852	8,384	-	-	-	3	5,852	8,384	-	-	-
Singapore	1	2,010	3,525	1	2,010	3,525	-	-	-	-	-	-
Greece	2	6,645	1,362	-	-	-	2	6,645	1,362	-	-	-

* - Includes three combination passenger and cargo ships.

Source: U.S. Department of Transportation, Foreign Flag Merchant Ships Owned by U.S. Parent Companies, January 1982, p. 2

Table 3.--Indicators of activity in the foreign and domestic operations of maritime transportation service firms, 1980-82

Item	Foreign	Domestic	Total
Estimated value of receivables, billings, or revenues: 1/ 2/			
1980------------------1,000 dollars--:	958,172	418,174	1,376,346
1981---------------------------do----:	1,040,074	543,686	1,583,760
1982---------------------------do----:	1,056,695	579,929	1,636,624
Estimate of investment in physical assets 1/ 3/ in foreign operations:			
1980------------------1,000 dollars--:	320,872	-	-
1981---------------------------do----:	382,441	-	-
1982---------------------------do----:	383,889	-	-
Number of establishments: 1/			
1980-----------------------------------:	158	81	239
1981-----------------------------------:	164	78	242
1982-----------------------------------:	153	79	232
Estimated 4/ value of total industry receivables, billings, or revenues:			
1980------------------1,000 dollars--:	5,855,000	4,345,000	10,200,000
1981---------------------------do----:	5,751,000	4,649,000	10,400,000
1982---------------------------do----:	5,954,000	4,546,000	10,500,000

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 8 of 37 firms surveyed; respondents represent about 20 percent of the foreign revenues of the estimated 37 major maritime firms believed to be operating internationally in 1981.

2/ Excluding the value of any merchandise exports.

3/ Including the undepreciated book value of land, plant, and equipment.

4/ By the staff of the U.S. International Trade Commission based on discussions with industry and/or association representatives, and secondary sources.

Source: Compiled from data submitted in response to questionnaries of the U.S. International Trade Commission.

of foreign revenues will increase slightly in 1982 from the $1.0 billion in 1981. In 1982, such foreign revenues are expected to remain about the same. Investment in foreign operations is reported by respondents to be about $380 million and the number of foreign establishments are thought to have increased in 1981, but with the worldwide slump the number is expected to decline in 1982 by about 3 percent. In 1982, foreign revenue for this sector is estimated to increase slightly to $5.9 billion, which accounts for about 4 percent of total service sector foreign revenue of $135.7 billion, estimated for the 14 selected industries covered in the Commission's study (table 4).

Liner service.--The most recent information available indicates that total tonnage of cargo carried in liner service during 1980 increased 4 percent over 1979 and reached 59.3 million long tons (table 5). However, the participation of U.S.-flag vessels experienced its fourth consecutive year of decline, falling to 27.3 percent. Total tonnage carried by U.S.-flag liners increased 2 percent and totaled 16.2 million long tons. The total dollar value of liner service cargoes increased 14.1 percent and totaled $136.9 billion. U.S.-flag vessels accounted for 29 percent of the total liner dollar value with $39.2 billion, representing an increase of 20.6 percent over that in 1978 (table 5).

Nonliner service.--U.S. oceanborne nonliner service foreign trade tonnage totaled a record 356 million long tons during 1980, the latest data available, which was an increase of 14 percent over that in 1979. Nonliner export tonnage totaled 229 million long tons, which was double the import tonnage of 114 million long tons. Nonliner export tonnage increased 20 percent, whereas import tonnage suffered a 4-percent decrease. The total dollar value of cargoes shipped in nonliner service increased 20 percent and reached $74.1 billion. Import nonliner cargoes were valued at $26.5 billion, whereas nonliner exports totaled $35.5 billion. However, U.S.-flag participation in nonliner service was at a low of 1.2 percent during 1980. The previous low was registered at 1.0 percent during 1979. U.S.-flag vessels carried a total of 4.1 million long tons, valued at $1.3 billion during 1980.

Tanker service.--During 1980, the latest year for which data are available, total tanker service tonnage showed a decrease of 16 percent from 1979, and totaled 356.3 million long tons. U.S.-flag vessels carried 2.2 percent of this total tonnage, reaching 7.9 million long tons, which represented a decrease of 50 percent. The total value of tanker cargoes amounted to $83.3 billion, for an increase of 33 percent, whereas the U.S.-flag cargoes totaled $1.8 billion, representing a decrease of 14 percent.

Regional and country activity

As shown in table 6, maritime industry respondents to the Commission's questionnaire indicated that U.S. oceanborne foreign trade garners revenue from virtually every region of the world. The regions generating the most revenue in 1981 were the Far East followed by Europe. The volume of Far Eastern trade in 1981-82 is expected to be running at much more than double the European trade, based on the limited responses by maritime companies; this apparent trend is supported by the recent decision of a major U.S. company to rejoin the Trans-Pacific Freight Conference of Japan and Korea effective September 1, 1982.

Table 4.--Estimated total foreign revenue generated by the maritime service industry and estimated total foreign revenue for selected service industries, 1980-82

Year	Total foreign revenue for service industry 1/ (1)	Total foreign revenue for selected service industries 2/ (2)	Ratio of (1) to (2)
	1,000 U.S. dollars		Percent
1980	5,855,000	89,398,000	7
1981	5,751,000	109,611,000	5
1982	5,954,000	135,744,000	4

1/ Estimated based on discussion with industry and/or association representatives, and secondary sources.
2/ Based on totaling Commission-estimated foreign revenue for each of the 14 selected industries covered in the study.

Source: Estimated by the staff of the U.S. International Trade Commission.

Table 5.--Total liner trade (imports and exports): 1977-1980

Year	Tons	Value
	Thousands of long tons	Millions of dollars
1980 total	59,300	136,900
Percent change from previous year	+4	+16.4
U.S. flag share	16,200	39,200
Percent change from previous year	+3.2	+20.7
U.S. percent of total	27.3	28.7
1979 total	57,029	117,614
Percent change from previous year	+1.0	+17.7
U.S. flag share	15,705	32,479
Percent change from previous year	-1.7	+13.7
U.S. percent of total	27.5	27.6
1978 total	56,491	99,912
Percent change from previous year	+18.3	+21.5
U.S. flag share	15,977	28,572
Percent change from previous year	+10.8	+13.2
U.S. percent of total	28.3	28.6
1977 total	47,754	82,261
Percent change from previous year	-4.0	-8.4
U.S. flag share	14,418	25,245
Percent change from previous year	-6.2	+5.6
U.S. percent of total	30.2	30.7

Source: U.S. Department of Commerce, United States Oceanborne Foreign Trade Routes, August 1981 and Department of Transportation, Marad' 81, (Preliminary Draft Report) July 15, 1982.

Table 6.--Regions and countries in which revenue is generated by maritime transportation service firms, 1980-82 1/

Region and country 2/	Number of responses			Percent of total respondents			Estimated revenue		
	1980	1981	1982	1980	1981	1982	1980	1981	1982
							------1,000 U.S. dollars------		
Middle East	1	1	1	13	13	13	3/	3/	3/
Far East	3	2	3	38	25	38	3/	3/	3/
Taiwan	-	2	-						
Japan	-	1	-						
South Korea	-	1	-						
Latin America	-	2	1	0	25	13	-	3/	3/
Panama	-	2	-						
Europe	3	2	2	38	25	25	3/	3/	3/
West Germany	-	1	-						
Ireland	-	1	-						
Netherlands	-	1	-						
United Kingdom	-	1	-						
Africa	2	2	-	25	25	0	3/	3/	-
Egypt	-	1	-						
Liberia	-	1	-						
Mexico	1	1	-	13	13	0	3/	3/	-
Other	1	-	-	13	0	0	3/	-	-

1/ Country listing is for 1981 only.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 8 of 37 firms surveyed; respondents represent about 20 percent of the foreign revenues of the estimated 37 major firms believed to be operating internationally in 1981.

3/ Data which would disclose confidential operations of individual concerns may not be published and, therefore, have been deleted from this report.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Trade in Merchandise Generated by Trade in Services

The nature of direct U.S. product exports generated by the U.S. maritime industry for its own use in providing service in foreign markets is minimal. The number of positive responses to a series of questions asked to determine whether or not U.S. merchandise exports are generated by U.S. maritime transportation service activities abroad was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
Do you believe that U.S. merchandise might be used as a result of the services your firm provides abroad?------------------------------	2	25
Is U.S. merchandise specified or recommended in the course of providing your service?----------------	1	13
Are U.S. merchandise exports believed to be directly generated?-----------	0	0

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 8 of 37 firms surveyed; respondents represent about 20 percent of the foreign revenue of the estimated 37 major firms believed to be operating internationally in 1981.

This low positive response supports general information obtained in industry discussions that the transport of cargo for its customers is the major U.S. merchandise trade activity associated with maritime activities abroad.

Ocean transportation is a vital part of the world's system of international trade. By far the largest part of U.S. export and import trade is handled by oceangoing vessels; by value, some two-thirds of U.S. international trade moved by sea in 1978, and by weight the percentage is higher. Table 7 depicts the magnitude of this merchandise trade, as well as that portion of it carried by U.S.-flag ships.

Table 7.—U.S. exports, 1/ imports, and apparent trade of merchandise, by method of transportation, 1978-80

Item	Waterborne trade	Other	Total	Ratio of waterborne trade to total
	Million dollars			Percent
Apparent trade:				
1978	192,748	122,808	315,556	61
1979	237,670	150,237	387,907	61
1980	283,759	177,624	461,383	62
Exports:				
1978	77,268	66,310	143,578	54
1979	97,579	84,072	181,651	54
1980	118,835	101,714	220,549	54
Imports:				
1978	115,480	56,498	171,978	67
1979	140,091	66,165	206,256	68
1980	164,924	77,910	242,834	68

1/ Export data includes foreign merchandise that has entered the United States as an import and is subsequently reexported; however, they exclude Department of Defense shipments.

Source: Compiled from official statistics of the U.S. Department of Commerce.

Host-country and third-country product shipments 1/ can also occur as a result of U.S. maritime services, especially for support at foreign port facilities, as indicated by some industry sources. The number of positive responses to a series of questions to determine whether or not host-country or third-country merchandise shipments are generated by U.S. maritime transportation service activities abroad was as shown in the following tabulation:

1/ "Host-country merchandise shipments" refers to the shipments (within the host country) of host-country-manufactured products which are generated by U.S. service operations in the host-country market. "Third-country merchandise shipments" refers to the shipments of other foreign-manufactured products to a foreign market as a result of U.S. service operations in that market.

Question	Number of responses 1/	Percent of total respondents
Do you believe that foreign merchandise might be used as a result of the services your firm provides abroad?----------------------------	5	63
Are foreign or host-country products specified or recommended in the course of providing your service?---	1	13

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 8 of 37 firms surveyed; respondents represent about 20 percent of the foreign revenue of the estimated 37 major firms believed to be operating internationally in 1981.

Two companies attributed the following merchandise shipments to U.S. maritime services abroad in 1981:

Item	Value (1,000 U.S. dollars
Third-country shipments-------------	95,000
Host-country shipments--------------	2,500

The largest portion of these shipments accounts for spare parts, equipment, and foodstuffs needed in connection with service to foreign parts, and less than half of the third-country shipment value was attributable to foreign bulk carriers acquired to support U.S. shipping operations abroad. Specific examples, cited by industry sources, where the entry of U.S. services into foreign markets has benefited the economies of the host-country include employment of crew members as a result of manning agreements and agent services to manage U.S. shipping activity locally.

International Service Trade Barriers

Industrial sources feel that major restrictive measures impeding foreign operations or international trade are still prevalent. In fact, they stress that many countries, particularly non-OECD countries, have moved toward more, rather than less restrictive business practices in international maritime services. Such practices include commercial cargo preference schemes, currency exchange and repatriation constraints, and restriction on use of certain equipment such as containers and barges. They point out that the effect of these practices is to competitively disadvantage U.S. companies; for example, tobacco shipped to Japan from North Carolina is handled by Japanese vessels due to certain restrictions on container size.

The existing barriers identified by maritime industry sources as of greatest concern are noted in table 8 and in the following discussion.

1. Cargo preference or waiver systems generally include the UNCTAD code of conduct for liner conferences and unilateral cargo allocations or waivers by certain countries, discussed earlier, which calls for a 40-40-20 cargo split. Industry sources stressed that cargo preference schemes are widespread and adversely affect the ability of U.S. carriers to compete. For example, they point out that foreign governments will often employ a "Presidential Decree" which will effectively make all cargo entering a port to be under government control and therefore requiring shipment by a national carrier.

Concurrent with the UNCTAD liner code, industry reports a trend toward unilateral protective measures employed by countries to reserve a substantial portion of their own cargoes for their own ships. Taiwan, for example, was noted to have a 100-percent "preference" that includes cargo trade associated with all government-financed programs and all government monopolies including tobacco and liquor. In the Philippines, industry representatives point out that "Presidential Decree 1466" requires all import cargo "funded or supported" by the government to be shipped by Philippine flag ships.

2. Closed conferences have already been singled out in previous discussion as being particularly onerous to U.S. companies. One large U.S. liner company complained that it faced closed conferences in trade between Western Europe and the Middle East as well as trade between the Far East and India (that is, in the cross trading of cargoes between these two areas). These conferences are believed to account for a significant share of the total international cargo trade in 1981.

3. Government subsidies to national lines are endemic to the world maritime industry, and in many cases, industry sources point out that direct government subsidies to their national lines put U.S. shippers at a disadvantage. In France, for example, COFACE, the government-backed French Export Insurance Company, is reported to issue export credit insurance guarantees to shippers. Once a shipper is covered by COFACE, he is obligated to make all shipments covered by the policy on French-flag vessels. Taiwan, as another example, in addition to giving direct subsidies to its national lines provides them with preferential treatment in such competitive areas as berthing and fuel allocation. Philippine-flag lines pay no income tax on revenues in the Philippines, whereas other shippers must pay a 2.5 percent income tax.

4. Direct government restrictions against U.S. shippers. Brazil, South Africa, Japan, Italy and France are some of the major countries, according to industry sources, that have laws directly affecting U.S. shippers. Japan, for example, has restrictions on container sizes. Under such Japanese container restrictions, equipment cannot economically be transported to inland destinations; instead, goods must be unloaded at the port facility. In Italy, U.S. carriers are required to bond all inbound nonnationalized cargo (i.e., cargo not cleared by customs at the port of entry) for inland transport, but the national Italian line is not required to do so. This Italian restriction results in an added cost to U.S. shippers of at least $50 per container.

Table 8.--Trade barriers to international services in the maritime transportation industry 1/

Category and barrier	Number of responses	Percent of total respondents
Right of establishment	4	50
Restrictive employment regulations (e.g. local labor requirement)	2	
Credit, investment, or financial activity restrictions	2	
Administrative/ownership restrictions	1	
Entry of service personnel and specialized tools	1	
Citizenship/residency requirements	1	
Restrictive government/business regulations	1	
Special deposit requirement for foreign companies	1	
Trade in goods	1	13
Local purchase requirements	1	
Restricting entry of equipment or supply	1	
Trade in services	4	50
Restrictive government/business regulations and administrative procedures	1	
Restriction related to resident firm preference (fixed percentage of service must be provided by domestic resident companies)	3	
Operating/ownership restrictions	2	
Prohibition on services offered by nonresident companies	2	
Technical issues	1	13
Governmental paper requirement for importing	1	
Licensing	1	13
Licensing restrictions (e.g., quotas)	1	
Government procurement	3	38
Preference given to national firms	1	
Shipment restricted to National flag carriers partially or completely	3	
Customs valuation	1	13
Discriminatory tariffs and customs procedures	1	
Subsidies/countervailing duties	2	25
Tax benefits (e.g., rebate or tax breaks)	2	
Direct financial aid to local firm by government	1	
Preferential financing arrangements	2	
Standards/certification	1	13
Local labor or material requirements	1	

See footnote at end of table.

Table 8.--Trade barriers to international services in the maritime transportation industry 1/--Continued

Category and barrier	Number of responses	Percent of total respondents
Foreign exchange controls	2	25
Restrictions on remittances	2	
Convertibility limitations	2	
Delays in obtaining foreign exchange permit	1	

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 8 of 37 firms surveyed; respondents represent about 20 percent of the foreign revenue of the estimated 37 major firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

5. Absence or inadequacy of Treaties of Friendship, Commerce and Navigation (FCN) create problems when countries implement cargo reservation laws or waiver systems, or refuse extraterritoriality applications of U.S. antitrust laws. U.S. industry representatives suggested, for example, that existing FCNs, particularly in those instances where governments have State-owned trading companies or State subsidized industries, do not adequately provide U.S. carriers with equal access to shipment of cargoes as provided to foreign shippers in the U.S. market. Industry sources expressed the need for clarification of U.S. antitrust laws to enable U.S. carriers to participate in major ocean liner conferences which set rates and capacity. In fact, they emphasize that the United States is the only country to have applied domestic antitrust laws to international liner shipping. Further, foreign "blocking" statues were also cited as obstacles to getting the data necessary to enforce U.S. laws, particularly antitrust laws. Industry sources assert that many countries, such as Great Britain which have such statutes will virtually prevent executives of their maritime industry from cooperating with the U.S. Department of Justice.

6. Obstacles related to cargo liability determination, particularly applicable in the Philippines and Guatemala have been mentioned by U.S. industry representatives. In the Philippines, for example, when cargo is discharged into the customs area, it is technically under the control and responsibility of the port operator, who frequently disclaims any financial liability over cargo which is lost or damaged.

7. The UNCTAD Convention on the Multimodal Transport of Goods, the industry stresses, has the potential for providing any contracting nation the opportunity to implement a web of regulations which will be more restrictive than any currently faced by the U.S. maritime industry. Specifically, the Convention which is reportedly scheduled to be put into force in 3 to 4 years, calls for the creation of Multimodal Transport Operators (MTO) that would be licensed and regulated by contracting governments. These MTOs could subject

U.S. shippers to increased costs and further inhibit their ability to do business on a purely commercial, competitive basis.

In short, the industry believes that international service trade barriers have a detrimental effect on the U.S. maritime industry in conducting foreign business, particularly in the area of cross trading and with the origination of trade from the developing countries. Respondents to the Commission's questionnaire indicate that revenues would increase provided trade barriers were reduced. The number of responses to a question to determine the economic effects of international barriers to U.S. services trade and associated product exports in maritime transportation service activities abroad, was as shown in the following tabulation:

Question	Number of responses 1/	Percent of total respondents
What effect, if any would reduction or removal of service trade barriers have upon your receivables, billings, or revenues in current or potential country markets?:		
Increase	4	50
Decrease	0	0
No effect	1	13
What effect, if any, would reduction or removal of service trade barriers have upon potential U.S. products exports in current or potential country markets?:		
Increase	1	13
Decrease	1	13
No effect	2	25

1/ Data are for questionnaire respondents only. The total number of respondents in this service industry was 8 of 37 firms surveyed; respondents represent about 20 percent of the foreign revenue of the estimated 37 major firms believed to be operating internationally in 1981.

Respondents, indicating that reduction or removal of trade barriers would have a positive effect on foreign revenues, reported that trade would increase from 10 to 30 percent in the Middle East and Far East, Europe, and Latin America (table 9). Two industry respondents indicated a 10 to 20 percent increase in product trade would result from reduction or removal of trade barriers (table 10).

Table 9.--Estimated changes in revenues absent trade barriers to international business of maritime transportation service firms, by areas 1/

Area and direction of change	Number of responses	Percentage change							
		10	20	30	40	50	60	80	Other
Middle East:									
Increase	2	1		1					
Decrease									
Far East:									
Increase	2	1		1					
Decrease									
Latin America:									
Increase	2		1	1					
Decrease									
Europe:									
Increase	1		1						
Decrease									
Africa:									
Increase	1								1(100)
Decrease									
Canada:									
Increase	-								
Decrease									
Mexico:									
Increase	1			1					
Decrease									
Other:									
Increase	-								
Decrease									

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 8 of 37 firms surveyed. Respondents represent about 20 percent of the foreign revenues of the estimated 37 firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 10.--Estimated changes in U.S. merchandise exports absent trade barriers to international business of maritime transportation service firms, by types 1/

Type and direction of change	Number of responses	Percentage change 10	20	30	40	50	60	80
Machinery and equipment:								
Increase	2	1	1					
Decrease								
Agricultural, animal and vegetable products:								
Increase	1	1						
Decrease								

1/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 8 of 37 firms surveyed. Respondents represent about 20 percent of the foreign revenues of the estimated 37 firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Conditions of Competition in Current and Potential Service Markets

U.S. oceanborne foreign trade to virtually every major port in the world and 145 countries, is conducted essentially by the three types of shipping services. These services provided by the 522 U.S. active flag ships, are conducted along 65 U.S. foreign trade routes and areas. The number of trade routes is expanding with the growth of trade between the United States and the developing nations.

The following lists several measures that have been cited by representatives of the U.S. maritime services industry as important influences affecting its international competitive position.

(1) U.S. operating subsidies - These subsidies offset all or part of the large difference between the cost of operating U.S. ships and the ships of other countries.

(2) U.S. construction subsidies - Offset all or part of the significant difference between the cost of building a ship in domestic shipyards and building it in a foreign shipyard.

(3) Noneconomic operations - Use of foreign merchant fleets to accomplish political ends by charging substantially reduced rates.

(4) Trade-in allowances - Excessive credits for old vessels when replaced by nationally built ships of foreign countries.

(5) Official low-interest loans - Loans granted to foreign merchant fleets at low interest for purchasing of new ships.

(6) Interest subsidies - Foreign governments are alleged to pay all or part of interest on loans.

(7) Official loan guarantees - Foreign governments are reported to guarantee loans made by private institutions.

(8) Accelerated depreciation - For tax purposes, industry sources indicate that foreign ship operators are permitted to writeoff the cost of ships and related equipment over a period shorter than the normal expected useful life.

The U.S. maritime industry does not enjoy a competitive edge in the world market. In addition to the factors mentioned above, industry sources cite a variety of economic developments and barriers that have a definite effect on U.S. shipping companies entering, or attempting to enter, the world market.

The U.S. industry has experienced cost increases in labor, materials, fuel, and capital. The average annual payroll for a U.S. ship, for example, is $3 million, compared with about $1.3 million for an Italian ship. As might be expected, the price of fuel has increased tenfold in the past decade, to where it now accounts for 50 to 60 percent of a ship's operating cost as opposed to 20 to 30 percent before 1973. Moreover, the price of fuel can vary by up to 45 percent depending on where it is loaded. Companies therefore, encourage shipmasters to find the cheapest sources of fuel. Other methods used by U.S. companies to reduce costs have included reduction in the manning level since 1970, by about 30 percent. Such reduction has been brought about by increasing automation. A disadvantage of this is that some members of U.S. crews have guaranteed annual wages whether they go to sea or not.

Currently, the U.S. merchant marine faces higher construction and operating costs than most other nations. These higher costs, however, are offset by construction and operating differential subsidies so that U.S. liners can generally compete with foreign operations. In 1981, the United States paid an average of $1.8 million in subsidies for each of 165 ships. It is possible for some U.S. liner companies to compete on the basis of service and utilization of the latest cargo carrying technology, but of the nine existing major U.S.-flag liner companies, for example, only one does not receive government subsidies. Moreover, such subsidies do not directly apply to the building of tankers and bulk carriers which industry sources contend is a detriment to the competitive posture of the U.S. industry.

Recent international developments cited by industry sources may also affect the future competitive position of the U.S. maritime industry. Developing countries in mid-1981 were instrumental in the passage of a resolution by the United Nations Conference on Trade and Development (UNCTAD) calling for the elimination of flags of convenience and tighter control over the shipowner by country of registry. Although the resolution has little impact to date, shipowners in the United States are concerned because it would lessen their flexibility in the reduction of high crew costs.

Another major issue cited by industry sources was growing nationalist policies within UNCTAD which, in the long run, could deeply affect the U.S. maritime industry. Specifically, in 1978 developing countries successfully urged UNCTAD to adopt a resolution giving every country the right to reserve 40 percent of its liner cargoes for its own fleet. Another 40 percent was reserved for the fleets of the recipients of the cargoes and the remainder left for third-nation "cross traders." The resolution which to date has been ratified by 51 countries representing about 20 percent of the world liner fleet, would place the U.S. maritime industry at a severe disadvantage. Cross trading is currently dominated by European carriers and many countries don't allow shipments from their ports by third flag vessels.

Finally, efforts by the U.S. maritime industry to be competitive in the world market are hampered, according to industry sources, by the presence of the principal categories of obstacles or barriers discussed earlier. Industry sources have expressed broad concern about the restrictive policies of foreign governments which are designed to nurture and protect their own merchant fleets, while enabling them to enjoy almost unrestricted access to the transporting of U.S. cargoes. This situation provides foreign carriers with a competitive advantage to "draw-off" foreign commerce of the United States. Over time, the U.S.-fleet carriers are accounting for a less substantial portion of this country's foreign commerce. In 1979, for example, industry sources point out that U.S.-flag vessels carried only 27.5 percent of U.S. liner trade, a reduction in 3 years from 30.9 percent, representing an 11 percent decline in market share.

Questionnaire responses support the current competitive difficulties facing the U.S. industry. The basic reason given by those few respondents providing insights on the competitive environment is that lower prices account for competing firms' success in world maritime transportation service (table 11). Data in table 12 show that of the competitive strengths identified by U.S. maritime transportation service firms in foreign markets, superior quality of service was designated to be the most important competitive factor.

Table 11.--Likely reasons 1/ for competing firms' success in world maritime transportation service markets, by base countries of firms 2/

Base country	Lower price	Technology expertise	Preferential financing	Experience in the market or service	Superior quality association	Political or regional bias	Government support	U.S. restrictions
Netherlands	3							
United Kingdom	3							
Other	3							
Total	9							

1/ The importance of each reason is indicated by the number of times each was designated, based on 3 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 8 of 37 firms surveyed; respondents represent about 20 percent of the foreign revenues of the estimated 37 major maritime firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 12.--Likely reasons 1/ for the competitive strength of U.S. maritime transportation service firms in foreign service markets 2/

Service market	Lower price	Technology lead	Financial strength	Experience in the market or service	Superior quality association	Other
Far East:						
Taiwan	1		1	1	2	1
Europe:						
Ireland					1	1
Africa:						
Egypt					1	1
Total	1		1	1	4	3

1/ The importance of each reason is indicated by the number of times each was designed, based on 2 responses.

2/ Data are for questionnaire respondents only. The total number of questionnaire respondents in this service industry was 8 of 37 firms; respondents represent about 20 percent of the foreign revenues of the estimated 37 major maritime firms believed to be operating internationally in 1981.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

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APPENDIX

UNITED STATES INTERNATIONAL TRADE COMMISSION
Washington, D.C.

(332-132)

THE RELATIONSHIP OF EXPORTS IN SELECTED U.S. SERVICE INDUSTRIES TO U.S. MERCHANDISE EXPORTS

AGENCY: United States International Trade Commission

ACTION: In accordance with the provisions of section 332(b) of the Tariff Act of 1930 (19 U.S.C. 1332(b)), the Commission has instituted, on its own motion, investigation No. 332-132 for the purpose of gathering and presenting information on the relationship between the exports of selected U.S. service industries and U.S. merchandise exports. Specifically, the Commission will investigate the level of product exports generated by selected service industries, to include air transportation, computer services, construction and engineering, educational services, equipment leasing services, financial services, franchising, health services, hotel and motel services, telecommunications, and transportation and related services; the implications of international service trade barriers to U.S. goods-producing industries; and the nature of product movements in international markets and foreign shipments of merchandise attributed to existing U.S. services trade.

EFFECTIVE DATE: September 16, 1981

FOR FURTHER INFORMATION CONTACT: Mr. Larry Brookhart (telephone 202-523-0275), Office of Industries, U.S. International Trade Commission, Washington, D.C. 20436.

WRITTEN SUBMISSIONS: While there are no public hearings currently scheduled for this study, parties wishing hearings may so request. Written submissions from interested parties are invited. Commercial or financial information which a party desires the Commission to treat as confidential must be submitted on separate sheets of paper, each clearly marked "Confidential Business Information" at the top. All submissions requesting confidential treatment must conform with the requirements of section 201.6 of the Commission's Rules of Practice and Procedure (19 CFR 201.6). All written submissions, except for confidential business information, will be made available for inspection by interested persons. To be assured of consideration by the Commission in this study, written statements should be submitted at the earliest practicable date, but no later than March 15, 1982. All submissions and other correspondence related to this investigation should be addressed to the Secretary, United States International Trade Commission, 701 E Street NW., Washington, D.C. 20436.

By order of the Commission.

Kenneth R. Mason
Secretary

Issued: September 21, 1981

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Washington, D.C. 20436
by
April 19, 1982 OMB approval number: 3117-0109
Expiration date: 1/31/83

SERVICE INDUSTRIES QUESTIONNAIRE

The information requested in this questionnaire is for use by the United States International Trade Commission in connection with its study No. 332-132 under section 332(b) of the Tariff Act of 1930, notice of which was published in the Federal Register of September 30, 1981. The principal area of concern in this study is the volume of export trade by the U.S. service sector, the level and type of merchandise trade related to trade in services, and the economic impact of non-tariff measures in services. The information is needed to supplement data available to the Commission from other sources and is requested under the authority of section 333(a) of the Tariff Act of 1930, as amended (19 U.S.C. 1333(a)).

You are requested to fill in all blanks on the questionnaire and return the completed questionnaire to the United States International Trade Commission, 701 E Street NW., Washington, D.C. 20436, as soon as possible, but no later than April 19, 1982. Use the enclosed postpaid envelope to return the completed questionnaire.

The commercial and financial data furnished in response to Sections A. through C. will be treated as confidential business information by the Commission. The confidential information supplied by you in this questionnaire, or in connection therewith, will not be published in a manner that will reveal the individual operations of your firm.

Name and address of reporting firm:

____

____

____

If the reporting firm is wholly or partly owned by another firm, indicate the name and address of the parent firm and the extent of ownership:

____

____

Information needed for any further clarification of data provided in the questionnaire.

____
Date

____
Area Code & Telephone No.

____
Name & Title of Company Official (Please type)

If you have any questions concerning the questionnaire, please contact Mr. William Cunningham (202-724-0980) or Mr. Larry Brookhart (202-523-0275) of the Commission's staff. Correspondence may be sent to the above address or via "mailgram" to TWX number 710-822-9507.

General Instructions

1. If the answer to any question is "none," so indicate, rather than leave the space blank.

2. If information is not readily available from your records in exactly the form requested, furnish estimates, designated as such by the letter "E." Any necessary comments or explanations should be supplied in the space provided or on separate sheets attached to the appropriate page of this questionnaire.

3. This report should cover all foreign and domestic service establishments managed and operated by the company as noted on page 1 (name of reporting firm) regardless of who owns the business or profession.

4. For the period(s) specified, report all receivables, billings, or revenues for all services rendered even though payment may be received at a later date.

5. To facilitate response, a firm operating more than one establishment in one country should combine the data for all establishments in a single report.

6. Country codes in alphabetical order by regions are provided on page 5 of this questionnaire. Please use these codes for country designations where specifically requested in the questionnaire.

DEFINITIONS

For the purpose of this questionnaire, the following definitions apply:

1. Firm.--An individual proprietorship, partnership, joint venture, franchised or licensed operation, association, corporation, including any subsidiary corporation, business trust, cooperative, trustees in bankruptcy or receivers under decree of any court, owning or controlling one or more establishments as defined below.

2. Establishment.--A facility engaged in providing services to foreign or domestic markets; it embraces foreign affiliates, regional offices, branches, subsidiaries, joint-ventures, or franchised or licensed operations.

3. Services.--The term "services" encompasses economic activities in which the principal outputs are not manufactured goods, and overseas investments which are necessary for the export and sale of such services.

4. Merchandise Exports.--This term used in Section B. and C. of the questionnaire refers to exports of products solely used in connection with your firm's international establishments and/or operations.

Purpose of Service Industries Study

The Commission's study will examine the relationship between selected U.S. service activities abroad and U.S. merchandise exports. This study will also attempt to evaluate the impact of international barriers to U.S. services trade. Further, the study will examine significant areas where host country merchandise shipments and third country exports have resulted from the entry of U.S. service industries into international markets.

The selected service industries to be examined in this study include air transportation, communication services, consulting and management services, computer and data processing services, construction and engineering services, educational services, equipment leasing services, financial services, franchising, health services, hotel and motel services, insurance services, maritime transportation, and motion picture services.

INDIVIDUAL FIRM DATA WILL NOT BE REPORTED BY THE U.S. INTERNATIONAL TRADE COMMISSION

Section A.--Company Classification and Scope of Operations

1. Please classify your organization by checking the service industry category or categories which best describe your principal and secondary activities in foreign markets--indicate percentages based on total receivables, billings, or revenue during 1981:

			%				%
a	/_/	Air Transportation	___	i	/_/	Franchising (Type)__________	___
b	/_/	Communication Services	___				
c	/_/	Computer and Data Processing Services	___	j	/_/	Health Services	___
d	/_/	Construction and Engineering Services	___	k	/_/	Hotel-Motel Services	___
e	/_/	Consulting and Management Services	___	l	/_/	Insurance Services	___
f	/_/	Educational Services	___	m	/_/	Maritime Transportation	___
g	/_/	Equipment Leasing and Rental Services	___	n	/_/	Motion Pictures Services	___
h	/_/	Financial Services	___	o	/_/	Other (specify) ____________________	___
						Total	100%

NOTE: PLEASE ANSWER THE REMAINDER OF THE QUESTIONNAIRE BASED ON THE PRINCIPAL SERVICE ACTIVITY WITH THE LARGEST PERCENTAGE DESIGNATED IN 1. ABOVE.

2. What organizational structures do you use in conducting your foreign business operations? (Please check as many as applicable).

a /_/ Foreign affiliate b /_/ Joint venture c /_/ Licensing

d /_/ Subsidiary or branch e /_/ Franchising f /_/ Other (Specify)____

3. Describe the specific services offered in foreign markets by your organization.

____
____
____
____
____
____

4. Provide ESTIMATES of the following information on your firm's foreign and domestic operations in calendar years 1980-82:

	Source	Calendar year	Foreign	Domestic	Total
a	Total value of receivables, billings, or revenues 1/ (US $1,000)	1980 E			
		1981 E			
		1982 E			
b	No. of establishments (see definition)	1980 E			
		1981 E			
		1982 E			
c	Investment in physical assets 2/ of foreign affiliates (US $1,000)	1980 E			
		1981 E			
		1982 E			

1/ Exclude value of any merchandise exports.
2/ Include the undepreciated book value of land, plant and equipment.

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5. Of total receivables, billings or revenues (excluding value of merchandise exports) provided in question 4, state ESTIMATES for the percentage allocation to the following regions in calendar years 1980-82:

(Estimated percent of total receivables, billings, or revenues)

Calendar year	Middle East	Far East	Latin America 1/	Europe	Africa	Canada	Mexico	Other	Total
1980 E----									100
1981 E----									100
1982 E----									100

1/ Central and South America (excluding Mexico).

6. Circle your 3 principal country markets in each region for 1981:

Middle East	Far East	Central and S. America (excluding Mexico)	Europe	Africa	Other
01 Afghanistan	17 Australia	33 Argentina	50 Austria	62 Algeria	_____
02 Bahrain	18 Bangladesh	34 Bolivia	51 Belgium	63 Botswana	_____
03 Iran	19 Burma	35 Brazil	52 W. Germany	64 Cameroon	_____
04 Iraq	20 China(P.R.C.)	36 Chile	53 Greece	65 Egypt	
05 Israel	21 Taiwan	37 Colombia	54 France	66 Ethiopia	
06 Jordan	22 India	38 Costa Rica	55 Ireland	67 Ghana	
07 Kuwait	23 Indonesia	39 Ecuador	56 Italy	68 Guinea	
08 Lebanon	24 Japan	40 El Salvador	57 Netherlands	69 Ivory Coast	
09 Oman	25 S. Korea	41 Guatemala	58 Portugal	70 Kenya	
10 Pakistan	26 Malaysia	42 Honduras	59 Spain	71 Liberia	
11 Qatar	27 New Zealand	44 Nicaragua	60 United Kingdom	72 Libya	
12 Saudi Arabia	28 Pacific Islands	45 Panama	61 U.S.S.R.	73 Morocco	
13 Syria	29 Papria-New Guinea	46 Paraguay		74 Nigeria	
14 Turkey	30 Philippines	47 Peru		75 Somalia	
15 U.A.E.	31 Thailand	48 Uruguay		76 S. Africa	
16 N. Yemen	32 Vietnam	49 Venezuela		77 Sudan	
				78 Tanzania	
				79 Tunisa	
				80 Uganda	
				81 Zaire	
				82 Zambia	
				83 Zimbabwe	

North America and Mexico

43 Mexico

84 Canada

INDIVIDUAL FIRM DATA WILL NOT BE REPORTED BY THE U.S. INTERNATIONAL TRADE COMMISSION

Section B.--Relationship of U.S. Service Activity in Foreign Markets to Merchandise Trade

U.S. Merchandise Exports

1. Do you believe that U.S. products might be used as a result of the services your firm provides abroad?

/_/ YES /_/ NO (If "no," proceed to question 7 on page 11)

Comment: ______________________________

2. Are U.S. products (or U.S. manufacturers) specified or recommended in the course of providing your service in foreign markets?

/_/ YES /_/ NO

Comment: ______________________________

3. Are U.S. merchandise exports believed to be directly generated as a result of your service activities in foreign markets?

A. /_/ YES /_/ NO (If "NO", proceed to question 4 on page 7).

B. If "YES," what is the total ESTIMATED value of U.S. merchandise exports generated by your foreign service activities for calendar years 1980-82?

Calendar year	Value of U.S. merchandise exports (US $1,000)
1980 E-----------	
1981 E-----------	
1982 E-----------	

PROCEED TO QUESTION 5 ON PAGE 7

4. (Answer only if you checked "no" to question 3 on page 6)

   Based on product needs required to implement the services your firm provided in 1981, it is estimated that ____% of total receivables, billings or revenues, and/or US $(1,000) __________ per year is a reasonable gauge of U.S. merchandise exports which could accrue from your foreign service activities.

5. Would you consider calendar year 1981 to be typical of the volume and regional activity in merchandise trade resulting from your service activities abroad?

/__/ YES /__/ NO

Comment:____

____

____

____

6. Identify on the following pages the major U.S. manufacturing sectors, (as applicable), key product categories, and regional markets affected by U.S. merchandise exports believed to be generated in 1981 by your foreign service activities.

   Note: The sectors are listed to identify the key manufacturing category for the product exports that may be related to your company's trade in services. Please provide ESTIMATED DATA and check the sector(s) and the accompanying product groups only as they apply to exports believed to be generated in conducting your foreign operations.

Note: This section tailored to each service industry.

Air Transportation Services

	U.S. Manufacturing Sector and Products (check as applicable)	1981: Value of U.S. product exports used in providing your services 1/ (U.S. $1,000)	Middle East	Far East	Central and South America (exclude Mexico)	Europe	Africa	Canada	Mexico	Other (Specify)	Total
			Percent of U.S. product exports allocated by region								
01	Total (enter amount from question 3.B. or 4.)										100
02	/_7 Machinery and Equipment										100
a	/_7 Telephone and telegraph apparatus										100
b	/_7 Aircraft and parts										100
c	/_7 Air traffic control systems										100
d	/_7 Airport/aircraft support and maintenance equipment										100
e	/_7 Food service equipment										100
f	/_7 Data processing (computing) equipment										100
g	/_7 Materials handling equipment										100
h	/_7 Office machinery & equipment										100
i	/_7 ______________										100
j	/_7 ______________										100
03	/_7 Agricultural, Animal and Vegetable Products										100
a	/_7 Processed food										100
b	/_7 Soft drinks										100
c	/_7 Alcoholic beverages										100
d	/_7 ______________										100
e	/_7 ______________										100

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Note: This section tailored to each service industry.

Air Transportation Services--Continued

U.S. Manufacturing Sector and Products (check as applicable)	Value of U.S. product exports used in providing your services 1/ U.S. $1,000	Middle East	Far East	Central and South America (exclude Mexico)	Europe	Africa	Canada	Mexico	Other (Specify)	Total
		1981 — Percent of U.S. product exports allocated by region								
04 /_7 Forest Products										100
a /_7 Paper products										100
b /_7 Industrial paperboard & packaging										100
c /_7 Printed matter										100
d /_7 ____________										100
e /_7 ____________										100
05 /_7 Textiles, Apparel, and Footwear										100
a /_7 Institutional linens										100
b /_7 Fabric and carpet										100
c /_7 Employee uniforms & apparel										100
d /_7 Shoes										100
e /_7 ____________										100
f /_7 ____________										100
06 /_7 Chemicals and Related Products										100
a /_7 Plastic food and beverages containers										100
b /_7 Cleaning compounds										100
c /_7 Petroleum products										100
d /_7 Pneumatic tires										100
e /_7 Soaps and detergents										100
f /_7 ____________										100
/_7										100

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Note: This section tailored to each service industry.

Air Transportation Services--Continued

U.S. Manufacturing Sector and Products (check as applicable)	Value of U.S. product exports used in providing your services 1/ U.S. $1,000	1981 Middle East	Far East	Central and South America (exclude Mexico)	Europe	Africa	Canada	Mexico	Other (Specify)	Total
		Percent of U.S. product exports allocated by region								
07 /_7 Minerals and Metals										100
a /_7 Glass and ceramic tableware										100
b /_7 Flatware (utensils										100
c /_7 ________										100
d /_7 ________										100
08 /_7 Miscellaneous Manufactures										100
a /_7 Furniture and fixtures										100
b /_7 ________										100
c /_7 ________										100

1/ Exclude the value of cargo shipments provided for customers and not related to your firm's international service operations.

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Host Country or Third Country Shipments

7. Do you believe that foreign-manufactured products might be used as a result of the services your firm provides abroad?

/_/ YES /_/ NO (If "no" proceed to Section C on page 12)

COMMENT:____

____

8. Do you specify or recommend products (or manufacturers) of the host country or other countries in major country markets in which you are performing a service?

/_/ YES /_/ NO

COMMENT:____

____

9. Provide your best ESTIMATE of the total value of host country merchandise shipments and third country exports that you believe were generated from your services provided abroad in 1981:

Host country shipments (1981) $US (1,000)__________
Foreign sourced merchandise exports (1981) $US (1,000)__________

10. Identify, for calendar year 1981, significant examples where the entry of your U.S. service industry into foreign markets has benefited the host country or third country (i.e., cite examples where your service activities abroad have stimulated local economies or trade other than exports from the United States):

Example: As a result of a services contract for construction design plans for port facilities in European countries, approximately $50 million in computer equipment, systems software, and machinery and equipment were provided by the host countries of Italy and France; and $10 million of similar equipment was imported from Japan.

Please cite 3 examples, if possible, and use separate sheets if needed or if you wish to cite more examples.

a. ____

____

____

b. ____

____

____

c. ____

____

____

Section C.--International Service Trade Barriers and Conditions of Competition

1. The following is a listing of possible foreign impediments, barriers,and discriminatory practices related to U.S. service industry operations abroad.

Trade Barriers (circle the applicable category and letter(s) for those important trade barriers that you encounter in current or potential country markets)

01 - Restrictive Actions Related to Right of Establishment

a. Restrictive employment regulations (e.g. local labor requirement)
b. Credit, investment or financial activity restrictions
c. Administrative/ownership restrictions
d. Entry of service personnel and specialized tools
e. Citizenship/residency requirements
f. Restrictive government/business regulations
g. Limiting number of establishments
h. Grandfather clause requiring practice before specified date
i. Reinsurance based on local assets
j. Special deposit requirement for foreign companies
k. Commission terms less favorable than national companies
l. Other (Specify)_____________

02 - Restrictive Actions Related to Trade in Goods

a. Restrictive regulations or administrative procedure
b. Local purchase requirements
c. Restricting entry of equipment or supply
d. Other (Specify)_____________
e. Other (Specify)_____________

03 - Restrictive Actions Related to Trade in Services

a. Restrictive government/business regulations and administrative procedures
b. Restriction related to resident firm preference (fixed % of service must be provided by domestic resident companies)
c. Employment related restrictions on non-nationals
d. Operating/ownership restrictions
e. Discriminatory taxation
f. Prohibition on services offered by non-resident companies
g. Other (Specify)_____________
h. Other (Specify)_____________

04 - Technical Issues

a. Lack of security control
b. Privacy restrictions
c. Contract enforcement problems
d. Strict responsibility requirements for handling consumer complaints
e. Time limitations on franchise agreements
f. Discriminatory bilateral agreements
g. Governmental paper requirement for importing
h. Discriminatory standards requirements
i. Other (Specify)_____________

05 - Restrictions related to Licensing

a. Licensing procedures
b. Licensing restrictions (e.g., quotas)
c. Refusal to license or renew
d. Other (Specify)_____________
e. Other (Specify)_____________

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Trade Barriers (circle the applicable category and letter(s) for those important trade barriers that you encounter in current or potential country markets)--Continued

06 - Restrictive action related to Commercial Counterfeiting

a. Inadequate patent or trademark enforcement
b. Unclear definitions of trademark, patent, imported goods, or counterfeit goods
c. Other (Specify)_____
d. Other (Specify)_____

07 - Restrictive Actions Related to Government Procurement

a. Preference given to national firms
b. Governmental import or distribution monopoly
c. Prohibition of foreign services contracts (bilateral or multilateral)
d. Shipment restricted to National flag carriers partially or completely
e. Other (Specify)_____
f. Other (Specify)_____

08 - Restrictive Actions Related to Customs Valuation

a. Discrimination in customs valuation between computer and data processing services transmitted through a tele-communications system or transferred through physical software products.
b. Discriminatory tariffs and customs procedures
c. Other (Specify)_____
d. Other (Specify)_____

09 - Restrictive Actions Related to Subsidies/Countervailing Duties

a. Tax benefits (e.g., rebate or tax breaks)
b. Insurance paid by government for local firm (e.g., inflation insurance)
c. Direct financial aid to local firm by government.
d. Preferential financing arrangements
e. Other (Specify)_____
f. Other (Specify)_____

10 - Technical Barriers (Standards/Certification)

a. Health and safety requirements
b. Origin declaration
c. Local labor or material requirements
d. Other (Specify)_____
e. Other (Specify)_____

11 - Professional Qualification Restrictions

a. Professional license required to practice
b. Other (Specify)_____
c. Other (Specify)_____

12 - Foreign Exchange Controls

a. Restrictions on remittances
b. Convertability limitations
c. Delays in obtaining foreign exchange permit
d. Other (Specify)_____
e. Other (Specify)_____

PROCEED TO QUESTION 2 ON PAGE 14

2. What effect, if any, would reduction (or removal) of service trade barriers (specified in the previous question) have upon your receivables, billings or revenues, and potential U.S. product exports in current or potential country markets?

(Check one)

a /_7 increase in service billings

b /_7 decrease in service billings

c /_7 no effect in service billings

(Check one)

a /_7 increase in U.S. product exports

b /_7 decrease in U.S. product exports

c /_7 no effect on U.S. product exports

3. Please provide an ESTIMATE of this percentage change (where appropriate) in your current receivables, billings or revenues (from 1981 data provided in question 4 page 4) for services in key foreign market regions, assuming major impediments to U.S. service market entry were removed:

	Major regional markets	Percentage change (please check one)							
		10	20	30	40	50	60	80	Other
a	Middle East	/_7	/_7	/_7	/_7	/_7	/_7	/_7	____
b	Far East	/_7	/_7	/_7	/_7	/_7	/_7	/_7	____
c	Latin America	/_7	/_7	/_7	/_7	/_7	/_7	/_7	____
d	Europe	/_7	/_7	/_7	/_7	/_7	/_7	/_7	____
e	Africa	/_7	/_7	/_7	/_7	/_7	/_7	/_7	____
f	Canada	/_7	/_7	/_7	/_7	/_7	/_7	/_7	____
g	Mexico	/_7	/_7	/_7	/_7	/_7	/_7	/_7	____
h	Other	/_7	/_7	/_7	/_7	/_7	/_7	/_7	____

4. Assuming the major trade barriers to services were removed in your current or potential country markets, ESTIMATE the percentage change, if any, of U.S. merchandise export sales (from 1981 data provided in question 3.B or 4 on page 6 and 7) that could have resulted from reaching the potential level of services trade:

U.S. Manufacturing Sector (check as applicable)	Percentage change (please check one)							
	10	20	30	40	50	60	80	Other
a /_7 Machinery and Equipment	/_7	/_7	/_7	/_7	/_7	/_7	/_7	
b /_7 Agricultural, Animal and Vegetable Products	/_7	/_7	/_7	/_7	/_7	/_7	/_7	
c /_7 Forest Products	/_7	/_7	/_7	/_7	/_7	/_7	/_7	
d /_7 Textiles, Apparel, and Footwear	/_7	/_7	/_7	/_7	/_7	/_7	/_7	
e /_7 Chemicals and Related Products	/_7	/_7	/_7	/_7	/_7	/_7	/_7	
f /_7 Minerals and Metals	/_7	/_7	/_7	/_7	/_7	/_7	/_7	
g /_7 Miscellaneous Manufactures	/_7	/_7	/_7	/_7	/_7	/_7	/_7	

5. Please describe the conditions of competition in your top 3 CURRENT international service markets; ranked from left to right by US$ value, i.e., highest in market #1:

		Market #1	Market #2	Market #3
AA. Name country (Please use country codes from page 5).	1.	____	____	____
BB. Value (US$1,000) of receivables, billings or revenues excluding merchandise exports) in 1981 in these markets.	1.	____	____	____
CC. How many known firms (domestic and foreign) are actively competing in this market?	1.	____	____	____
DD. Allocate the number of competing firms by geographic scope of operations:				
National firm of market country	1.	____	____	____
Regional firm	2.	____	____	____
Worldwide firm	3.	____	____	____
Other U.S. firms	4.	____	____	____
EE. Number of contracts or business opportunities which you actively pursued and lost to competing firms during 1981.	1.	____	____	____
FF. List the top 3 base countries (use codes from page 5) of competing firms in each market/and the respective number of competing firms based in those countries.	1.	____/____	____/____	____/____
	2.	____/____	____/____	____/____
	3.	____/____	____/____	____/____
GG. Indicate the respective value (US$1,000) of lost contracts or business corresponding to countries in FF above for each market.	1.	____	____	____
	2.	____	____	____
	3.	____	____	____
HH. Indicate the likely reason for the competitive firm's success in bidding for the service for countries in FF above(check those applicable).				
a. Lower price	1.	____	____	____
	2.	____	____	____
	3.	____	____	____
b. Technology expertise	1.	____	____	____
	2.	____	____	____
	3.	____	____	____
c. Preferential financing arrangements	1.	____	____	____
	2.	____	____	____
	3.	____	____	____
d. Greater experience in the market and/or services area.	1.	____	____	____
	2.	____	____	____
	3.	____	____	____
e. Superior quality (associated with the firm or base country).	1.	____	____	____
	2.	____	____	____
	3.	____	____	____

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HH.--Continued

			Market #1	Market #2	Market #3
f.	Political or regional bias.	1.	____	____	____
		2.	____	____	____
		3.	____	____	____
g.	Government subsidized or supported	1.	____	____	____
		2.	____	____	____
		3.	____	____	____
h.	U.S. restriction or regulations imposed on domestic firms.	1.	____	____	____
		2.	____	____	____
		3.	____	____	____
i.	Other (specify) ____________	1.	____	____	____
		2.	____	____	____
		3.	____	____	____

I. Indicate your competitive strengths in countries identified in 5.AA (check applicable items in appropriate country column).

		Market #1	Market #2	Market #3
a.	Lower price	____	____	____
b.	Technology lead	____	____	____
c.	Financial strength	____	____	____
d.	Greater experience in the market and/or service area	____	____	____
e.	Superior quality (associated with your firm or base country)	____	____	____
f.	Other (specify) ____________	____	____	____

_____C3

6. Please describe what you believe would be your firm's competitive strengths in 3 POTENTIAL international service markets:

	Market X	Market Y	Market Z
AA. Name country (Please use country codes from page 5). 1.	________	________	________
BB. Indicate what your competitive strengths would be in countries identified in AA. (check applicable items in appropriate country column).			
a. Lower price	____	____	____
b. Technology lead	____	____	____
c. Financial strength	____	____	____
d. Greater experience in the market and/or services area	____	____	____
e. Superior quality (associated with your firm or base country)	____	____	____
f. Other (Specify) ________	____	____	____

7. Please feel free to make additional comments about your firm's competitive posture in the international service field.