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Deepening the EU's Single Market for Services

by Christian Ebeke, Jan-Martin Frie, and Louise Rabier

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Deepening the EU's Single Market for Services[1]

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Abstract

The services sector is increasingly important for the euro area economy, but productivity growth in the sector has stalled over the past two decades. Remaining barriers to cross-border trade in services within the EU Single Market contribute to this weak performance. Our empirical analysis suggests that slow progress in tackling these barriers is associated with political economy factors such as weak government support in parliaments, low government efficiency and high markups. To remove the cross-border restrictions on services trade, we suggest combining incentives such as financial support, technical assistance and improved communication on barriers with more effective enforcement.

JEL Classification Numbers: F15, K23, L8, O52, P35

Keywords: Euro Area, European Union, Productivity, Services

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CONTENTS

I. Introduction

The services sector is important for the euro area economy.[2] First, the euro area services sector is large in terms of value-added and employment share. Importantly, its share in employment is increasing and this trend is set to continue (Fig. 1). Second, the services sector is deeply interlinked with the manufacturing sector (Fig. 2 and Miroudot and Cadestin, 2017).

However, productivity growth in the services sector is falling behind. Since 2000, real labor productivity in the services sector has remained virtually flat in the euro area (0.1 percent per year average growth), while increasing by 30 percent in the U.S. (Fig. 3).[3] Moreover, hourly labor productivity in the services sector is only 71 percent of that in the manufacturing sector. Within services, however, there is large dispersion in productivity, with the information and communication technology (ICT) sector being the most productive sector, while other sectors clearly lag behind, including professional services (Fig. 5 & 6). Higher productivity growth overall is critical to ensuring solid long-term growth rates and improved living standards for its citizens, amid pressing demographic challenges.

The decline in total factor productivity (TFP) explains the bulk of the decoupling with the U.S. (Fig. 7). According to the KLEMS growth accounting decomposition, available for a sample of eight euro area countries, there has been on average a 0.9 percentage points gap each year between labor productivity growth in the euro area and in the U.S. between 2001 and 2014.[4] TFP growth differentials explain the largest share of the productivity gap (0.7 percentage points). Lower ICT investment in the euro area explains 0.1 percentage points of the gap.[5]

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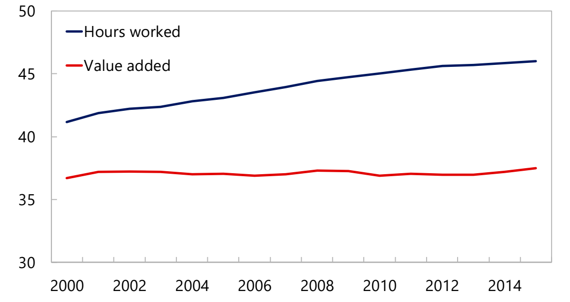
[2] The focus of this study is on nonfinancial and nonreal estate market services, which we refer to as "services," including wholesale and retail trade, transportation, accommodation and food services, information and communication, professional services, arts, entertainment, and other market services (Sections G, H, I, J, M, N, R, S from the NACE Rev 2.). Financial and real estate services are excluded because of difficulties in productivity measurement. Nonmarket services are also excluded.

[3] Figures 3 and 4 show that services productivity stalled in all major euro area economies relative to the U.S., although to a lesser extent in Germany (15 percent growth over the period) and France (10 percent growth over the period). While Italian services productivity keeps decreasing, the Spanish picked up after the crisis and is now back to its 2000 level. Italian productivity performed poorly in all services relative to the euro area average, and the largest decline in Italian productivity comes from the professional services sector (-30 percent over the period).

[4] AT, BE, DE, ES, FI, FR, IT, NL.

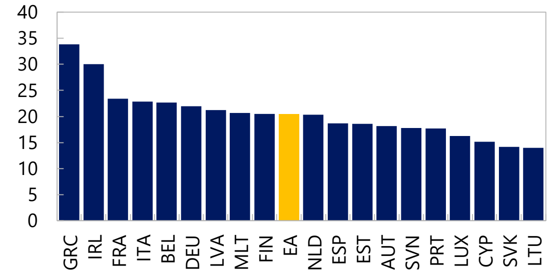
[5] The productivity gap *vis-à-vis* the U.S. has been 2.4 percentage points per year in professional services, of which 2.1 percentage points are due to declining TFP; in the information and communication sector, the gap has been 2.3 percentage points, of which 1.0 percentage point is due to TFP, and 0.8 to lagging ICT capital investment.

Figure 1. Euro area market services share
As a percent of total employment and value added



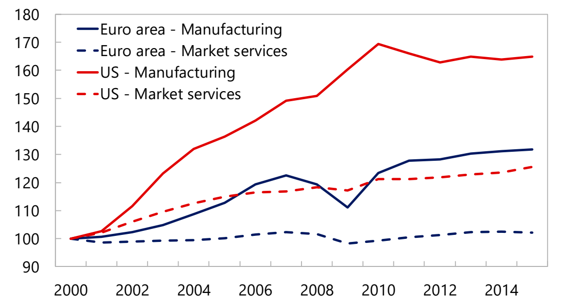
Source: EU KLEMS, IMF staff estimates.

Figure 2.Euro area share of services in manufacturing input in 2014
(Domestic and imported services)



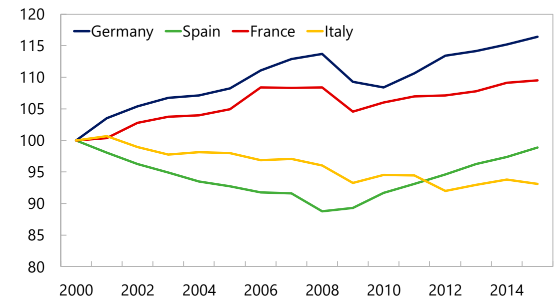
Source: OECD based on WIOD data.

Figure 3. Labour productivity
(Real value added per hour worked, 2000=100)



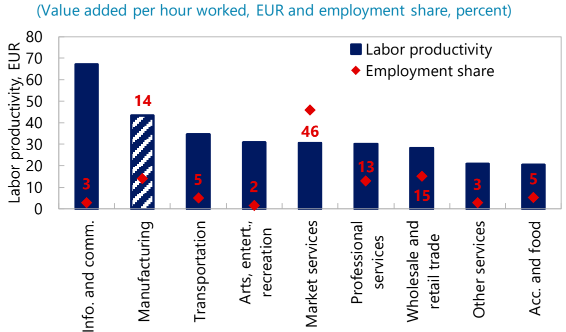
Source: EU KLEMS, IMF staff estimates.

Figure 4. Market services labour productivity
(Real value added per hour worked, 2000=100)



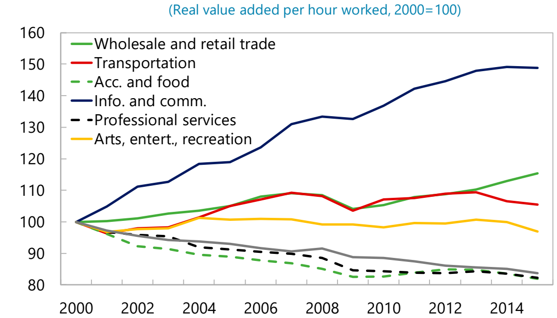
Source: EU KLEMS, IMF staff estimates.

Figure 5. Nominal labour productivity, euro area, selected sectors, 2015
(Value added per hour worked, EUR and employment share, percent)



Source: EU KLEMS, IMF staff estimates.

Figure 6. Euro area market services labour productivity
(Real value added per hour worked, 2000=100)



Source: EU KLEMS, IMF staff estimates.

Cross-border trade in services is relatively low compared to that in goods, although this partly reflects the lower tradability of some services.[6] Traditional cross-border trade in services is less than 10 percent of GDP, compared to more than 20 percent of GDP for goods (Fig. 8).[7] This partly reflects intrinsic characteristics of services that limit their tradability, such as their less standardized nature or the fact that they need to be delivered on site (Sorbe et al., 2018). Low cross-border trade could also reflect that the services sector is dominated by micro firms (see Garicano et al., 2016 for evidence on the French economy), which have more limited capacity to engage in cross-border trade (Fig. 9). Equally, the large share of

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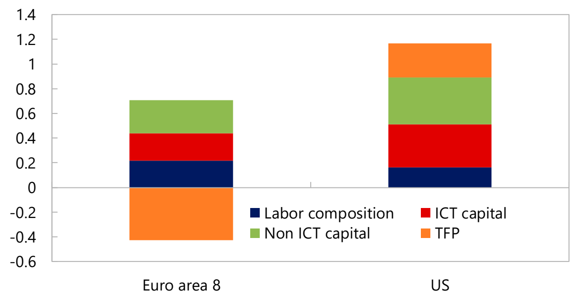
[6] See Scott Marcus et al. (2019).

[7] According to Aussilloux et al. (2011), such a low level of intra-EU trade in services would be consistent with non-tariff barriers between 20 and 40 percent in tariff equivalents.

micro firms, is likely to negatively weigh on productivity growth reflecting limited economies of scale.

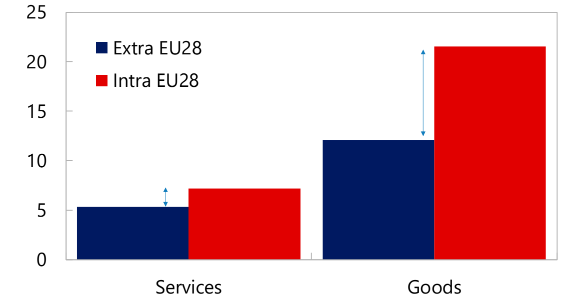
Given the barriers to services trade, the main mode of providing cross-border services has been through FDI (Fig. 10). Intra-EU FDI in the services sector (about 2 percent of GDP) plays a more important role than in goods markets (0.5 percent of GDP). This may further increase the gap between large companies that have enough capacity to establish themselves cross border, and smaller ones which cannot seize cross-border opportunities.

Figure 7. Average annual labor productivity growth, market services, 2001-2014 (Contributions to growth, %)



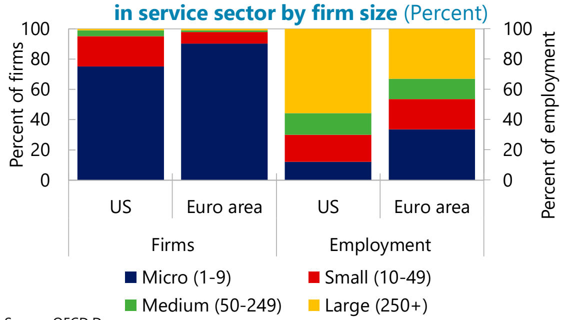
Source: EU KLEMS, IMF staff estimates.

Figure 8. Trade openness
(% of GDP, 2017)



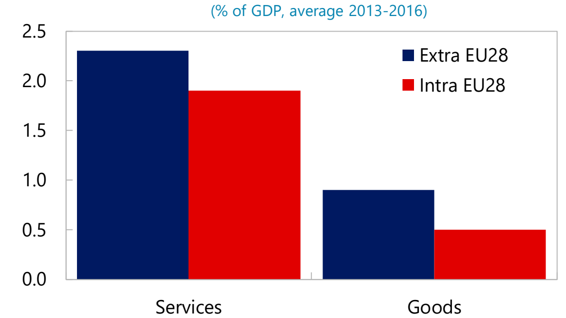
Source: Eurostat, IMF staff estimates.

Figure 9. Firm and employment distribution in service sector by firm size (Percent)



Source: OECD Dynemp.

Figure 10. FDI flows openness
(% of GDP, average 2013-2016)



Source: Eurostat, IMF staff estimates.

Barriers to cross-border service trade in the EU contribute to the sub-par performance of the internal market for services. Several recent studies have identified cross-border barriers as a critical impediment to openness and to firm growth, healthy job creation, productivity and welfare gains (Bourlès et al., 2010; Egert and Gal, 2016; Canton and Thum-Thyssen, 2015).[8] Previous estimates suggest that an ambitious implementation of the 2006 EU Services Directive (see Box 1) could boost EU GDP by almost 2 percent.[9]

In this paper, we identify the factors that stand in the way of reducing the barriers to cross-border service trade in the euro area. We review the literature on the impediments to deeper services sector integration and carry out several empirical investigations. The main

[8] These studies have detailed the link between stricter product market services regulation and lower productivity on the one hand and higher markups on the other hand. The CSES (2012)'s study found that regulation and economic performance indicators (productivity, turnover, size) are negatively or not significantly correlated.

[9] See Monteagudo (2012) and Copenhagen Economics (2018).

contributions of the paper are twofold. First, we take advantage of the newly released Organisation for Economic Co-operation and Development (OECD) dataset on intra-EU service trade restrictiveness to investigate the level of the barriers and their economic as well as political drivers. Second, we rely extensively on the qualitative arguments from the literature, to formally test in various specifications the main arguments as to why service trade liberalization is stalling despite various EU initiatives to that end.

Our empirical results show that political economy factors (a government's support in parliament and years left in the office) affect the likelihood of a euro area country reducing services trade restrictions. We also show that services trade liberalization is less likely in sectors where markups are higher, but similarly, higher government efficiency helps overcome this bottleneck by prioritizing reforms in sectors where they are the most pressing. Finally, we do not validate the argument often used that service sector reform systematically reduce service quality *ex post*. Our results suggest that countries could achieve similar levels of consumer satisfaction with fewer regulations.

II. Progress and Challenges Since the EU's 2006 Service Directive

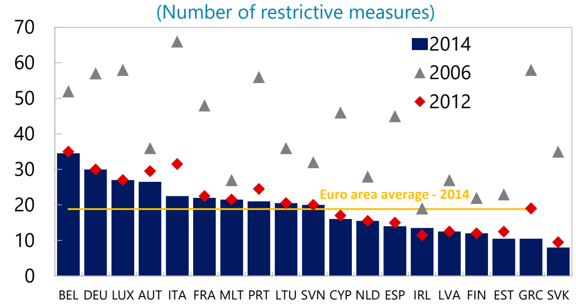
A. Progress in Implementing the Services Directive

The 2006 Services Directive aimed at facilitating the cross-border provision of services within the EU. It was introduced to reduce regulatory barriers to the provision of services across borders (trade) as well as to the establishment of a firm in another EU country (FDI). Moreover, it aimed to simplify administrative procedures and foster administrative cooperation between EU countries (see Box 1). The Directive covers services representing some 45 percent of EU GDP.

While the Directive has helped reduce discriminatory cross-border barriers to trade and FDI, important implementation gaps remain.[10] Based on the European Commission's assessment, significant progress was made to reduce the gap between the legal requirements of the Directive and the actual legal framework in the first years after its implementation in 2006. However, subsequently, progress has been limited, leaving many EU countries with considerable implementation gaps (Fig. 11).

Fig. 11. Services Directive remaining restrictions

(Number of restrictive measures)



Source: European Commission and IMF staff calculations. Partially abolished measures count for 0.5.

[10] See Mustili and Pelkmans (2013), World Bank (2016), Monteagudo et al. (2012; 2014), and Fernández Corugedo and Pérez Ruiz (2014).

Box 1. The 2006 Services Directive and Complementary Legislation

The Directive 2006/123/EC on Services in the Internal Market ("the Services Directive") covers a wide range of services and is best understood as a 'horizontal' directive, that is, it applies to a wide range of sectors. The services that are not covered include among others, financial services, network industries and transport services. These are covered by separate pieces of legislation.

The main objective of the Directive was to eliminate remaining regulatory barriers to the cross-border supply of services (either through trade or FDI), whilst also simplifying administrative procedures and fostering administrative cooperation between EU member states. The Directive did not aim to replace national regimes. Instead, it introduced a set of prohibitions and principles that EU Member States need to respect when regulating services at the national level.

A key element of the directive is an explicit catalogue of regulatory restrictions imposed that EU countries are not allowed to put in place (Mustili and Pelkmans, 2013). Such forbidden practices are generally of discriminatory nature such as, the requirement that the firm's headquarters be located in the country and involvement of (domestic) competitors in the process of granting authorization to operate.

The directive also outlines principles that EU member states need to respect when evoking public interests to justify regulatory measures: they must be transparent, undergo a necessity as well as a proportionality test, and not directly or indirectly discriminate against non-nationals (Fiorini and Hoekman, 2018). Public interests include among others consumer protection, safeguarding the sound administration of justice, and the preservation of national historical and artistic heritage (Hook Tangaza, 2016).

An important complementary legislation is the Professional Qualifications Directive (2005/36/EC later amended Directive 2013/55) which pre-dates the Services Directive and covers the mutual recognition of professional qualifications and other closely linked requirements under national legislation restricting access to a profession.[1] Its relevance is underlined by the fact that about 22 percent of the EU work force (or 50 million people) need some kind of prior authorization to access and exercise their profession (Adamis-Császár et al., 2019). In 2018, this directive was again strengthened with a complementing, 'proportionality directive' which aims to improve the analytical framework for regulatory impact analysis of EU countries (see Box A1 in Appendix on legislative initiatives under the Juncker administration).

1/ The Directive applies to all regulated professions except those governed by specific regulatory pieces (such as lawyers, commercial agents, sailors, statutory auditors, insurance intermediaries, aircraft controllers). It enables automatic recognition of qualification for those professions where the minimum training requirements are harmonized at EU level, such as a wide range of health professionals (for example nurses, midwifes, doctors); sets up a general system of recognition for other regulated professions such as teachers, translators and real estate agents; and offers recognition on the basis of professional experience for certain professional activities (for example carpenters, upholsterers and beauticians).

Due to incomplete implementation, the Directive has only been partially effective, according to the European Commission.[11] The Commission finds that service providers still face significant administrative burden and costs when going cross border. Also, it finds that the system of administrative cooperation between EU countries is currently not working in practice, and that countries continue to impose their domestic requirements on service providers with little regard to the regulatory framework already imposed on the service provider in their home country. Similarly, while the Professional Qualifications Directive has improved the process of recognition of professional qualifications between EU countries,

[11] See European Commission (2017).

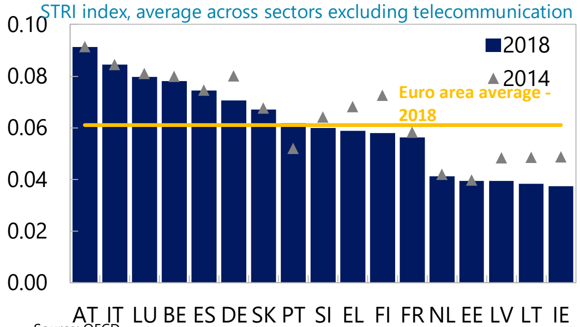
there seems to be remaining issues with its implementation and the general recognition process remains cumbersome and lengthy.[12]

Newly compiled OECD data provides additional insights on the importance of the remaining barriers to cross-border trade in the EU's service sector. [13] The OECD has compiled data on EU-specific barriers to the cross-border provision of services, summarized in an index called the Services Trade Restrictiveness Indicator (STRI).[14] The index confirms previous restrictiveness indicators by the European Commission.[15] It shows that while barriers have been lowered (Fig. 12), their level remains high in some key sectors such as professional services (accounting, legal services, architecture) as well as in air transport (due to an exemption of air carriers' alliances from competition law) (Fig. 13).

On average, the most significant barriers are those related to foreign entry, regulatory opacity, and lack of competition (Fig. 14). Barriers to the movement of people as well as other discriminations appear largely resorbed within the EU. Countries with the highest regulation level include Austria, Italy, Luxembourg, Belgium, and Spain (Fig. 15). Lower regulations include the U.K. and Ireland, as well as some Eastern (Lithuania, Latvia, and Estonia) and Nordic countries (Sweden, Denmark, and Netherlands).

Figure 12. Intra EEA Services trade restrictions

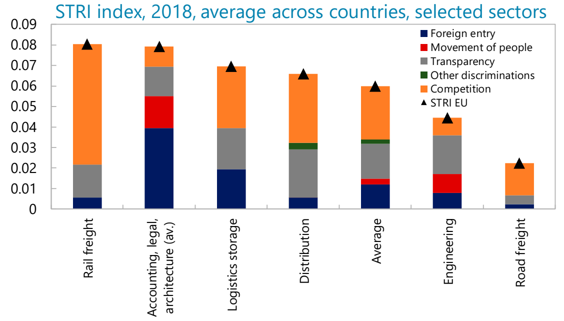
STRI index, average across sectors excluding telecommunication



Source: OECD.

Figure 13. Intra EEA Services trade restrictions

STRI index, 2018, average across countries, selected sectors



Source: OECD.

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[12] Particularly the automatic recognition procedure, which is available for those professions where the minimum training requirements are harmonized at EU level seems to work well. For instance, the mobility of health professionals has been greatly improved. For general nurses, 75 percent of recognition decisions are automatic. (Adamis-Császár et al., 2019).

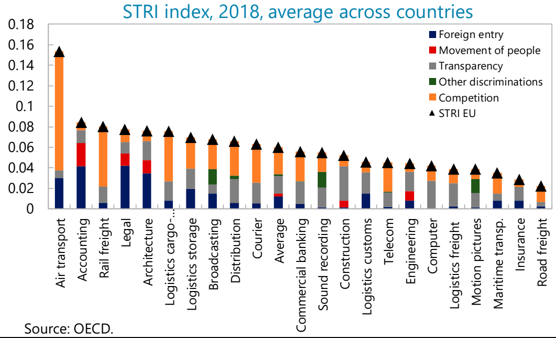
[13] Restrictiveness indicators are not perfect and should be taken with caution and systematically complemented with detailed case studies as to evaluate the proportionality of regulations.

[14] The OECD STRI measures restrictions faced by foreign firms in a market due to: i/ foreign entry; ii/ the movement of people; iii/ barriers to competition; iv/ regulatory transparency; and v/ other discriminatory measures. The index describes *de jure* restrictions and includes EU-level legislation as well as national-level legislation and does not take into account differences neither in implementations of EU directives or transposition delays.

[15] European Commission's restrictiveness indicators include a database on barriers before and after the implementation of the Services Directive and a more recent "Restrictiveness indicator" for a subset of regulated professions.

Figure 14. Intra EEA Services trade restrictions

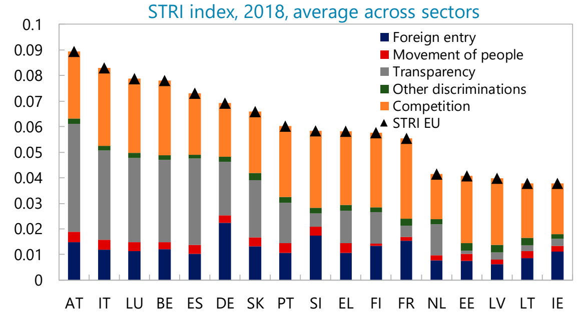
STRI index, 2018, average across countries



Source: OECD.

Figure 15. Intra EEA Services trade restrictions

STRI index, 2018, average across sectors



Source: OECD.

B. Literature Survey: What is Holding Back Services Sector Reforms?

In order to identify the hurdles to the liberalization of cross-border trade in services in the euro area, we review the literature with respects to barriers to wider services reform and explanations for the slow implementation of the Services Directive.[16]

- Political-economy factors have been conjectured to play a key role. The proximity of national elections or an absence of a strong majority in the parliament are tested as limiting the appetite for service sector reforms, although empirical studies find mixed results (Høj et al., 2006; Da Silva et al., 2017). The importance of vested interests, exacerbated by the "fear" of social dumping also tends to limit the appetite for cross-border service sector liberalization (Hook Tangaza, 2016; Høj et al., 2006; Draghi, 2017). Equally, EU member states with higher taxation rates may fear that increased mobility of service providers could see their tax base erode.[17]

- In some EU countries, there is also a fundamental belief that cross-border service sector liberalization is detrimental to the quality of services provided. As a result, some countries have kept barriers in place or introduced new ones by evoking the public interest motive (Adamis-Császár et al., 2019; Hook Tangaza, 2016; Pelkmans, 2019). In reality, the empirical evidence gathered from case studies on this issue appears rather mixed and not definitive (European Commission, 2019a).

- Another challenge is the large number of decision-makers and other players involved, such as national, regional and local levels of government, professional bodies, regulators or supervisors (Pelkmans, 2019). In addition, professional associations sometimes have

[16] The scope, complexity and principle-based nature of the Directive (rather than substantive harmonization) contribute to its low implementation (Pelkmans, 2019). Others argue that while some countries have removed barriers at a legislative level, these have not always been reflected at an operational level (Hook Tangaza, 2016), suggesting an implementation in letter rather than in spirit. The World Bank (2016) highlights the lack of implementation of the agreed steps by EU countries.

[17] Global corporate tax competition has gained increasing attention but remains largely unaddressed (Keen et al., 2019). The European Commission's proposal for a Common Consolidated Corporate Tax Base (CCCTB) in the EU represents an attempt to limit corporate tax competition at the regional level.

an ambiguous role, by combining regulatory and representational responsibilities, which may also complicate the reform process (Hook Tangaza, 2016, Høj et al., 2006).

III. Econometric Investigations

We now focus on investigating empirically the barriers to services sector reforms in the euro area. First, we model explicitly the drivers of reforms. Second, we investigate the relationship between services sector reform and quality of services.

A. What Drives Within-EU Services Trade Liberalization?

We first estimate an econometric model for the probability of reforms that liberalize services trade. Services trade liberalization is measured as a decrease in the within-EU Services Trade Restrictiveness Indicator observed at the sector-country level, over the total 2014–18 period. We estimate the probability of reform liberalization as a function of the initial level of restrictions, and various macroeconomic control variables capturing at the country level the economic cycle, the influence of financial assistance programs with conditionality (EFSF/ESM program dummy[18]), government effectiveness—as measured by World Bank's Worldwide Governance Indicators[19] (WGI)—and political capital of governments (years left into office and government support in parliament, with data from the Gothenburg University's Quality of Government Dataset).

More formally the model takes the following form:

$$\mathbb{1}_{services\ reforms_{k,c}} = \beta euSTRI_{k,c,t0} + \theta Z_{c,t0} + \sigma_k + \epsilon_{k,c}, \quad (1)$$

where k denotes the sector, c the country and Z the set of explanatory factors listed above.

The dependent is a dummy variable which equals one if the OECD's within-EU service trade restrictiveness measures at the sector-country level has been reduced over the 2014–18 period.[20] The *linear probability model*, in line with literature (Høj et al., 2006, Da Silva et al., 2017), controls for sector-specific dummies to capture unobservable sectoral heterogeneity which makes a reduction in the level of regulation more or less likely.[21] This

[18] Countries included in the panel: Cyprus, Greece, Hungary, Ireland, Latvia, Portugal, and Spain.

[19] Government effectiveness captures perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies.

[20] Out of the 478 observations available, there were 194 occurrences of reduction in the STRI, 255 of stability and 29 of increase in restrictiveness (which are counted as 0 in the dummy variable). See also Table A1 in the Annex.

[21] Results are robust to alternative definitions of the dependent variable such as continuous variable or thresholds, available upon request.

model has the advantage of being very simple. Smaller values of R-squared are usual in panel data models.

The results suggest that political factors and good governance play a key role in services trade liberalization (see Table 1). We find that government effectiveness increases the likelihood of reform. Reforms are also more likely to be driven by governments that have stronger support in their parliaments and are in the beginning of mandates. Countries with a financial assistance program have been more likely to conduct liberalizing reforms (confirming findings by the European Commission, 2015). The initial level of regulation coefficient is insignificant, pointing towards an absence of convergence in restrictiveness over the period.

We then investigate in more detail whether the quality of governance helps prioritizing reforms at the sectoral level. We hypothesize that incumbent firms in overly protected sectors oppose reforms, and test whether the quality of governance helps targeting reforms in those protected sectors. We approximate undue regulations by one of their outcomes, high markup rates (see for example Thum-Tysen and Canton, 2017). The main difference with the previous estimation is thus the inclusion of country-sector-level measures of markups μ (approximated by a ratio of gross operating surplus to sales or Lerner index, computed with BACH data and we use initial values of the sectoral markups in the regressions to reduce the potential reverse causality bias).[22] Given the correlation between the sectoral level of markups and regulation, the initial value of STRI is excluded. The model now takes the following form:

$$\mathbb{1}_{services\ reforms_{k,c}} = \theta_1 \mu_{k,c,t0} + \theta_2\left(\mu_{k,c,t0} * government\ effectiveness_{c,t0}\right) + \theta Z_{c,t0} + \sigma_k + \epsilon_{k,c}, (2)$$

Table 1. Equation 2 Estimation Results

	$\mathbb{1}_{services\ reforms_{k,c}}$
Government support in parliament in 2014	0.00829*
	(1.92)
Years left into office in 2014	0.0427**
	(2.32)
Government efficiency in 2014	0.383***
	(6.78)
Financial assistance program between 2009 and 2013	0.148*
	(1.82)
Output gap in 2014	-0.0251**
	(-2.48)
Initial level of regulation	-1.065
	(-0.99)
Constant	-0.682**
	(-2.46)
Sector fixed effect	Yes
N	436
R^2	0. 158

t statistics in parentheses
* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

[22] STRI sectoral nomenclature is more detailed than financial data are. The match is thus imperfect.

The estimation results suggest that higher sectoral markups lower the likelihood of reform, but that government efficiency helps liberalizing those sectors with higher markups (Table 2). The number of sectors analyzed in this section is smaller due to data availability.

Table 2. Equation 3 Estimation Results

	$\mathbb{1}_{services\ reforms_{k,c}}$
Lerner index (in 2014)	-0.0227**
	(-2.13)
Lerner index * Government efficiency (in 2014)	0.0147**
	(2.16)
Government efficiency (in 2014)	-0.215
	(-1.64)
Financial assistance program between 2009 and 2013	0.324**
	(2.19)
Output gap (in 2014)	0.0778***
	(3.92)
Constant	0.742***
	(2.86)
Sector fixed effect	Yes
N	195
R^2	0.247

t statistics in parentheses
* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

B. Services Sector Reforms and Quality: Is There a Link?

The need to ensure a certain quality of services is often used as an argument for restrictions, though there is no clear evidence that liberalization leads to lower quality. Article 15 of the Services Directive allows countries to put restrictions in place if judged necessary to protect the public interest. This article has been used to justify regulation to preserve a decent level of service quality which will benefit consumers. However, a recent case study by the European Commission (2019a) found no clear link between services sector reform on a broad spectrum of service quality dimensions.

We take a further look at the correlation between services sector regulation and perceived consumer satisfaction. We exploit the variations in the OECD's index of within-EU services trade restrictiveness and variations from the European Commission's Market Performance Index (MPI) which approximates consumer satisfaction in various countries and sectors in a sample of euro area countries between 2015 and 2017.[23] More formally, the relation looks as follows:

$$MPI_{kc,t} = \rho_1\ euSTRI_{kc,t} + \sigma_{kt} + \mu_c + \epsilon_{kc,t}, (3)$$

[23] The MPI synthetizes a survey on consumers' perception of comparability, trust, problems, expectations, and choice in different markets for services (and goods). Sectors included in the following section include: broadcasting, courier, distribution, and air transport. The analysis is robust to the exclusion of air transport whose STRI is very high.

Box 2. Reform of the Polish Legal Profession

The law profession in Poland was very restricted and admission was largely arbitrary. Successive rounds of reform have made it easier to enter. For instance, in 2013 access to the profession of advocate and legal advisor by other legal professionals was facilitated by extending the exemptions from the bar training and professional examination to professionals with experience in other legal professions.

Furthermore, reforms have substantially reduced the scope of exclusive reserved activities of advocates and legal advisors, and opened them up to other legal professions, thus increasing supply and competition. Also, the scope of rights of legal advisors was widened. Since 2015 legal advisors are authorized to defend a party in criminal and fiscal crime cases, which means their scope of rights has become equal to advocates.

Finally, the role of professional organizations in admission to the profession of legal advisor and advocate has been drastically revamped. The exams used to be entirely in the hands *of self-governed professional organizations and the decisions of the examination boards were non-contestable. Recruitment was highly selective, subject to diverse and unclear rules* (European Commission 2019a). In 2009, the exams were standardized and put under the supervision of the Ministry of Justice.

The reforms enabled a two-fold increase in the number of legal professionals, while no decrease in quality occurred. The increase in supply of lawyers was badly needed in order to avoid a significant increase in prices as demand surged on the back of rapidly increasing income of Polish households. This successful reform episode should encourage Poland to engage in further reforms, as the Polish legal sector exhibits one of the highest STRI scores, particularly with respects to barriers to foreign entry.

or alternatively in a dynamic form:

$$\Delta MPI_{kc} = \rho_2\, \Delta euSTRI_{kc} + \sigma_k + \mu_c + \epsilon_{kc}, \quad (4)$$

We do not find evidence of a systematic relationship between services sector regulations and service quality as measured by consumer satisfaction, although the analysis is only illustrative given the limited data availability and the absence of cleaner identification strategy. The analysis does not show any statistically significant correlation between service sector regulations and service quality (Table 3)[24]. Anecdotal evidences also provide some support this finding (for example Box 2 on the reform of the Polish legal profession).

[24] The high explanatory power of country fixed effects in the difference specification likely reflects country-specific factors affecting consumer satisfaction, such as economy-wide economic activity or labor-market reforms.

Table 3. Correlation Between STRI-EU and Consumer Satisfaction							
	Y	Y	Ln(1+Y)	Ln(1+Y)	D.Y	D.Y	D.Y
STRI EU	-1.774	2.119	-0.0181	0.0226			
	(-0.50)	(0.67)	(-0.41)	(0.57)			
Change in STRI EU					2.119 (0.67)	-4.255 (-1.03)	0.276 (0.09)
Constant	80.70***	80.52***	4.401***	4.399***	0.306*	0.275	0.144
	(258.72)	(292.59)	(1138.71)	(1265.03)	(1.79)	(0.89)	(0.34)
Fixed effects	Country-Sector	Country-Sector-Year	Country-Sector	Country-Sector-Year	-	Country	Sector
N	280	280	280	280	140	140	140
R^2	0.000	0.022	0.000	0.016	0.000	0.511	0.021

IV. Policy Discussions

This paper has shown that there is scope to further deepen the Single Market for services. Despite several EU initiatives since the 2006 Service Directive, unduly restrictive regulations on services trade remain in key sectors such as professional services. Our empirical analysis suggests that the slow progress in tackling services trade restrictions in the euro area reflects political economy factors and that there could be room to eliminate restrictions without compromising service quality.

These results have practical policy implications at the EU level. Progress could be achieved by combining incentives with effective enforcement, to reduce the potential for political backlash in EU countries. The EU should also aim to support its member states in increasing government efficiency. Equally, it should tackle the underlying structural barriers to freedom of movement, establishment and trade in services, such as divergent education and training requirements as well as legal form, shareholding and insurance requirements.

- Incentives:
    - Continued focus on services-sector reform in the Country-Specific Recommendations (CSRs) is important. The proposed Reform Delivery Tool could further incentivize countries, including by providing financial support to offset any costs associated with reforms.
    - The Technical Support Instrument and the Convergence Facility can increase government efficiency by offering technical assistance that can improve policy formulation, implementation and overall quality of civil services.
    - The European Commission can increase transparency and improve policy formulation by challenging the justification put forward by countries for a given restriction under the Services Directive. The proposed proportionality directive is a welcome initiative and should make it more binding for EU member states to reflect and justify restrictive regulation in the field of professional services.

- Recently created National Productivity Boards could help by guaranteeing effective public communication of the reforms, including by showcasing examples of EU best practices.

- More EU-wide transparency and comparable data could help to highlight the long-term costs of inaction as well as the benefits of reform, creating transparency about the beneficiaries and losers of the status quo.

- A larger role for national competition authorities in evaluating whether a regulation is in line with public interest could help if national competition authorities are less influenced by political pressure than national ministries.

- Addressing divergent education and training requirements within the EU would also help facilitate the provision of services in a truly internal market for services.

• Enforcement: Formal infringement proceedings against EU countries inadequate implementation of the Services Directive remain an important enforcement instrument. The use of enforcement tools to date has been limited—the European Court of Auditors (2016) argues that it has been insufficient. The recent stepping up of infringement procedures with respect to, among others, the Services Directive and the Professional Qualification Directive appears appropriate.

V. APPENDIX

Table A1. Descriptive Statistics

	N	Mean	Median	St.Dev
Dummy if liberalizing reform in services between 2014 and 2018	478	.41	0	.49
Financial assistance programme post-2009	478	.26	0	.44
Lerner index (EBITDA/Sales, 2014)	186	14.85	11.67	12.63
Government support (Seats share of parties in government, 2014)	476	56.14	54.83	8.1
Years left in current term (2014)	435	1.66	2	1.21
Government effectiveness (2014)	478	1.24	1.16	.47
Concentration (2014)	160	.55	.56	.22
Output gap (2014)	457	-3.76	-2.86	3.32
STRI EU (2014)	478	.06	.06	.03

Note: EU-28 countries.

Box A1. Initiatives of the 2014–19 European Commission

Early on during the 2014–19 European Commission a 'Single Market Strategy' was published (2015), where the internal market for services featured prominently.

In 2017 the Commission put forward two horizontal services initiatives under the Services Directive. The proposals for an e-card for service providers (COM/2016/0824) aimed to set up a simplified electronic procedure for administrative formalities required to provide services abroad (European Commission, 2017). The proposal was met with significant resistance as NGOs and labour unions felt it would facilitate social dumping and dubious practices (Pelkmans, 2019) and rejected by the European Parliament in March 2018. Similarly, no agreement could be reached so far on the proposal for a new form of notification (COM(2016)821), which would tighten existing notification requirements and introduce a 3-months prior notification of planned services laws, a practice that is standards in technical legislation on goods for a long time (Pelkmans, 2019).

In the field of professional qualifications and services, the 2014–19 European Commission has taken a number of non-legislative initiatives that aim to increase transparency and peer pressure (for example COM (2016)820 and SWD(2016)436 of Jan. 10, 2017 on reform recommendations in professional services). The Commission has expressed doubts about the effectiveness of the 'Reviews and Mutual Evaluation' and is seeking other ways to proceed (including infringement cases, proportionality assessments, the European semester) (Pelkmans, 2019). For instance, a proportionality directive (2018/958) passed, which aims to make it more binding for EU member states to reflect and justify restrictive regulation in the field of professional services. The Commission had earlier found significant issues with how EU countries approach occupational regulation (Adamis-Császár et al., 2019).

Equally, the 2014–19 European Commission has taken several steps to increase coordination and introduce some harmonization in the field of employment and social policy (European Commission, 2019b). These steps can help to address fears over social dumping and reduce resistance to further services liberalization.[1]

An important initiative in the light of the (need for) digitization of the European economy is the Digital Single Market. The Digital Single Market consists of legislative and non-legislative initiatives aimed at facilitating cross-border electronic commerce and digitize the European economy (Scott Marcus et al., 2019). Key initiatives include the General Data Protection Regulation (2018), regulation on free flow of non-personal data (2018), the regulation addressing unjustified geo-blocking (2018) and the European Electronic Communications Code (2018).

1/ Another aspect that may gain in political relevance is the scale of emigration from the Eastern EU member states, which may have slowed growth and income convergence in the sending countries, albeit not for the EU as a whole (Atoyan et al., 2016). To the extent that intra-EU mobility might be perceived as a net loss by these countries, resistance to further services liberalization, which will likely increase the mobility of professionals and hence potentially emigration, might increase.

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