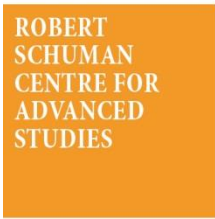




European
University
Institute



ROBERT
SCHUMAN
CENTRE FOR
ADVANCED
STUDIES

RSCAS POLICY PAPERS

RSCAS PP 2015/08
Robert Schuman Centre for Advanced Studies
Global Governance Programme

International Public Procurement:
From Scant Facts to Hard Data

Lucian Cernat and Zornitsa Kutlina-Dimitrova

European University Institute
Robert Schuman Centre for Advanced Studies
Global Governance Programme

**International Public Procurement:
From Scant Facts to Hard Data**

Lucian Cernat and Zornitsa Kutlina-Dimitrova

RSCAS Policy Paper 2015/08

This text may be downloaded only for personal research purposes. Additional reproduction for other purposes, whether in hard copies or electronically, requires the consent of the author(s), editor(s). If cited or quoted, reference should be made to the full name of the author(s), editor(s), the title, the working paper, or other series, the year and the publisher.

ISSN 1830-1541

© Lucian Cernat and Zornitsa Kutlina-Dimitrova, 2015

Printed in Italy, October 2015

European University Institute

Badia Fiesolana

I – 50014 San Domenico di Fiesole (FI)

Italy

www.eui.eu/RSCAS/Publications/

www.eui.eu

cadmus.eui.eu

Robert Schuman Centre for Advanced Studies

The Robert Schuman Centre for Advanced Studies (RSCAS), created in 1992 and directed by Professor Brigid Laffan, aims to develop inter-disciplinary and comparative research and to promote work on the major issues facing the process of integration and European society.

The Centre is home to a large post-doctoral programme and hosts major research programmes and projects, and a range of working groups and *ad hoc* initiatives. The research agenda is organised around a set of core themes and is continuously evolving, reflecting the changing agenda of European integration and the expanding membership of the European Union.

Details of the research of the Centre can be found on:

<http://www.eui.eu/RSCAS/Research/>

Research publications take the form of Working Papers, Policy Papers, Distinguished Lectures and books. Most of these are also available on the RSCAS website:

<http://www.eui.eu/RSCAS/Publications/>

The **Policy Paper Series** of the Robert Schuman Centre for Advanced Studies complements its Working Papers Series. This series aims to disseminate the views of a person or a group on a particular policy matter, specifically in the field of European integration.

The European University Institute and the Robert Schuman Centre for Advanced Studies are not responsible for the proposals and opinions expressed by the author(s).

The aim of the Robert Schuman Centre for Advanced Studies is to contribute to the public debate by offering views and opinions on matters of general interest.

The Global Governance Programme at the EUI

The EUI and the RSCAS are not responsible for the opinion expressed by the author(s).

The Global Governance Programme is one of the flagship programmes of the Robert Schuman Centre for Advanced Studies at the European University Institute (EUI). It aims to: build a community of outstanding professors and scholars, produce high quality research and, engage with the world of practice through policy dialogue. At the Global Governance Programme, established and early career scholars research, write on and discuss, within and beyond academia, issues of global governance, focussing on four broad and interdisciplinary areas: European, Transnational and Global Governance; Global Economics; Europe in the World; and Cultural Pluralism.

The Programme also aims to contribute to the fostering of present and future generations of policy and decision makers through its unique executive training programme, the Academy of Global Governance, where theory and “real world” experience meet. At the Academy, executives, policy makers, diplomats, officials, private sector professionals and academics, have the opportunity to meet, share views and debate with leading academics, top-level officials, heads of international organisations and senior executives, on topical issues relating to governance.

For more information: <http://globalgovernanceprogramme.eui.eu>

Abstract

Public procurement is a negotiating area gaining in importance at multilateral and bilateral level, as evidenced by a brief review of procurement provisions in existing trade agreements. The size of procurement spending stands in most developed economies at double-digit percentage points of GDP. However, despite the size and importance of these markets, the factual information available to trade negotiators remains scarce. Although public procurement patterns (e.g. size of procurement markets, composition of procurement spending and level of government procurement) can be derived from traditional national accounts statistics, these figures fall short of capturing the international dimension of public procurement. Hence, the paper puts forward a basic conceptual framework for data collection on public procurement that would best serve the future negotiating agenda in this area.

Keywords

Government procurement statistics; international trade; trade agreements

1. Introduction*

Public procurement is a major component of public spending, with a sizable impact on total demand of any domestic economy. Public procurement expenditures represent about one third of total government expenditures in OECD countries. In 2013, in GDP terms, government procurement expenditures as measured in national accounts amount to an average of almost 14% of GDP in the European Union and to more than 10% of GDP in the US.¹ But the actual public procurement spending is in reality higher as these national accounts aggregates do not include procurement spending of public utilities providers. For example, in the EU the total public procurement spending (including utilities) accounted for €2.4 trillion, corresponding to nearly 19% of EU GDP in 2011.²

Around the world, historically, public procurement contracts have to a large extent benefitted domestic companies, thus ensuring a safe market for local suppliers of goods and services. This preference for domestic producers, the so called ‘home bias’, raises serious efficiency considerations. It can significantly distort trade flows and international specialisation, particularly in sectors characterized by a large share of public consumption in total demand and in sectors affected by monopolistic competition.³ Moreover, domestic preferences in government procurement such as ‘buy national’ provisions may alter international companies’ outsourcing choices and significantly affect production decisions along global value chains. Empirical evidence of the presence of this home bias is provided in a series of studies.⁴ The combination of large share of government expenditures in GDP and the ‘home bias’ characteristics makes public procurement one of the few fields in which liberalisation efforts at international level have substantial untapped potential, and thus an area of growing importance in international negotiations.

Liberalisation efforts in the area of government procurement at multilateral level started as early as 1979 leading to the adoption of the plurilateral Government Procurement Agreement (GPA) under the aegis of the WTO. However, only a small set of countries undertook binding commitments to open their procurement markets for foreign goods and service suppliers. In recent years, the importance of liberalizing public procurement markets was recognized not only as part of the GPA negotiations but also in a bilateral/regional context. A growing number of recent free trade agreements (FTAs) contain legally binding public procurement provisions with various degrees of liberalization ambition.

Despite gradual improvements in the openness level of public procurement markets for GPA members and many FTA partners, a large number of WTO members are not part of the GPA. It is still fair to say that by and large public procurement markets around the world are yet to become part of future liberalisation rounds.

There are many intrinsic and political economy reasons why public procurement (alongside other economic activities) is less prone to internationalisation. However, unlike other negotiating areas where sometimes progress is difficult, public procurement negotiations are fraught with an additional difficulty: the lack of often basic comparable information that renders the negotiating process even more complex (e.g. market size, cross-border share of foreign companies participation and geographical breakdown, a clear taxonomy of barriers and their restrictiveness level). The lack of such

* The opinions expressed in this article are the authors’ own and do not necessarily reflect the views and opinions of the European Commission. The authors would like to thank Desislava Borisova for data analysis of the WTO list of all RTAs and to their colleagues in DG TRADE for comments and fruitful discussions.

¹ See OECD statistics, available at: <http://stats.oecd.org/>, web access 5 December 2014.

² See also the EU official submission to the WTO reported under Article XIX:5 of the GPA agreement, available online at http://www.wto.org/english/tratop_e/gproc_e/notnat_e.htm#statPro.

³ See Trionfetti, F. (2000).

⁴ See Shingal, A. (2015), Shingal, A. (2011), Brühlhart, M. and Trionfetti, F. (2001).

basic statistics negatively affects also the implementation and monitoring efforts of existing agreements.

Given the importance of having hard data on public procurement and a common analytical base, one of the main aims of this chapter is to suggest ways on how to deal with this lack of sound analytical framework that is needed for successful procurement negotiations and implementation efforts. The paper goes further and argues that negotiating partners need to frontload this analytical infrastructure as part of their current and future negotiating agenda. It also puts forward an empirically-driven conceptual approach on how to structure and adapt this future data collection efforts in order to identify existing barriers to international public procurement with a view to address them in future negotiations.

The rest of the paper is organized as follows: Section 2 takes account of the importance of government procurement provisions at the multilateral and EU level inter alia by reviewing the public procurement disciplines found in the RTAs announced to the WTO. Using national accounts statistics, section 3 describes public procurement patterns in terms of size of procurement markets, composition of procurement spending and level of government procurement. Section 4 puts forward a basic conceptual framework for future data collection on public procurement that would best serve the future negotiating agenda in this area. Finally, section 5 concludes and identifies a straightforward set of priorities for this important policy area.

2. Internationalisation of public procurement

2.1 Multilateral dimension of public procurement

At multilateral level government procurement is negotiated under the aegis of the WTO. Liberalisation efforts in this area started in 1979, when the so-called “Tokyo Round Code on Government Procurement” was signed. More than a decade later, in 1987, the agreement was amended and in 1994 joint efforts of the negotiating countries led to the “Agreement on Government Procurement”, which was signed on the same date as the agreement establishing the WTO. Further liberalisation efforts in the area of government procurement in a plurilateral context led to the entry into force of the revised GPA on 6 April 2014. The "GPA II" is characterized by an extended scope, as a number of additional government entities has now been included. The coverage of the revised GPA has been enlarged as well by adding new services and public procurement activities. The gains from the extended GPA are assessed to be ranging from US\$ 80 to 100 billion annually.⁵

The GPA also involves provisions on collection and submission of statistical data on government procurement by the GPA Member States, pursuant to Article XIX:5. This data reporting requirement is supposed to cover the number of contracts awarded and a breakdown of the award value by government entities and type of contract i.e. works, services and supplies.⁶ In addition, the GPA data submissions by members should provide information on cross-border purchases and the country of origin of the purchased goods and services.⁷

⁵ WTO (2014a), Annual Report 2014, Geneva.

⁶ This requirement applies only for procurement covered by the GPA agreement. Note that obligations may differ across GPA annexes.

⁷ The revised GPA has amended the obligation to provide cross-border statistics to the extent that such statistics is available.

Despite these GPA provisions the process of data collection and submission has not functioned well, as also acknowledged by the WTO Secretariat.⁸ For instance, there are GPA countries that have never submitted a statistical report (such as Israel and Iceland) or countries for which the latest report submitted dates a few years back, as in the case of the US to 2008.

Even more important, in an international context, is the fact that the cross-border dimension of the submitted data is scarce. Looking at the GPA members who have submitted a statistical report, only two of them have provided information on cross-border procurement purchases in recent years: Japan and Chinese Taipei. There is information on the cross-border dimension of government procurement submitted by the EU, Switzerland and Korea but it dates back to 2007 and 2003, respectively. Apart from the fact that information on cross-border procurement expenditure is outdated, even where such information is available it covers in general only few countries of origin. In the case of Japan, for example, a breakdown is provided for government procurement purchases from five countries and the rest of the world. The most complete information on the origin of the goods and services purchased by governments abroad is submitted by Korea and includes cross-border procurement from 14 countries and the rest of the world in 2003.

The fact that the data on cross-border government procurement is so scarce makes any attempt to analyse the economic impact of liberalisation efforts in this area an ambitious challenge. This applies not only to an economic impact assessment of market opening in public procurement at multilateral level but also to identifying economic benefits of public procurement provisions in bilateral FTAs.

The latter is crucial also because there is a trend showing an increased importance of government procurement provisions in regional trade agreements (RTAs). Analysing all RTAs announced to the WTO in terms of stand-alone public procurement provisions (a chapter or an article for example) shows that, until the year 2000, out of all agreements announced to WTO only 17 had separate legal provision on procurement.⁹ Since the year 2000 until today the amount of agreements with a stand-alone procurement article or chapter almost quadrupled, reaching 88 FTAs. This shows that negotiating countries are aware of the importance and untapped potential of cross-border procurement markets and are willing to increase market opening and/or improve transparency provisions.

2.2 Government procurement in EU's FTAs

Since 1970 the EU has announced 40 FTAs to the WTO, out of which 36 have already entered into force.^{10 11} Analysing these FTAs against the background of having a separate chapter or article on government procurement shows that until 2000 none of 13 RTAs signed had an stand-alone chapter or article on public procurement.¹² Since 2000 however, out of the 24 EU FTAs 13 had a separate public procurement provision; this corresponds to a share of 54%. Out of these 13 EU FTAs containing

⁸ see WTO (2014b), Statistics reports under Article XIX:5 of the GPA, http://www.wto.org/english/tratop_e/gproc_e/gpstat_e.htm, web access on 8 December 2014.

⁹ For this analysis the WTO list of all RTAs was used. All agreements are available at <http://rtais.wto.org/UI/PublicAllRTAList.aspx>. Thereof the agreements on Custom Unions were excluded. Web access on 8 December 2014.

¹⁰ See WTO (2014), List of all RTAs, last updated on: Thursday, December 4, 2014, Web access on 8 December 2014 at <http://rtais.wto.org/UI/PublicAllRTAList.aspx>.

¹¹ The four EU agreements which have been negotiated but are yet to be notified are: Canada, Singapore, SADC and West Africa. They have been included in the data analysis of this sub-section.

¹² The agreements between the EU and Israel and the EU and Korea were not considered as having a separate public procurement provision as both are members of the GPA and the procurement provision mentioned in the FTA refers to the GPA.

separate public procurement provisions 9 have dedicated a chapter on public procurement and the remaining 4 contain a stand-alone article on government procurement.¹³

This growing trend shows that the importance of bilateral negotiations in the area of public procurement has increased substantially and has yet to play a major role in upcoming EU trade negotiations, as this is a key negotiating area in the Transatlantic Trade and Investment Partnership with the US (TTIP).

3. Characteristic of public procurement markets

This section aims at quantifying the size, the composition and the level of government procurement. The data source used for this purpose is EUROSTAT and OECD national accounts statistics. The advantage of using national accounts lies in the cross-country comparability of the data, as national statistical authorities follow the same methodology by collecting and reporting the data.¹⁴ However as already mentioned these public procurement aggregates do not include procurement spending of state-owned corporations, such as state-owned utilities and therefore the sizes of the market is underestimated in countries where utilities providers are state-owned. Public procurement as measured by the OECD and in this section comprises of intermediate consumption (e.g. government expenditures on IT systems or stationary), social transfers in kind via market producers (e.g. medical expenses ultimately refunded by national social security systems) and gross fixed capital formation (infrastructure expenditures on building new roads for example).^{15 16} The data covers the most recent year 2012 for which data for almost all OECD and all EU Member States is available.

3.1 Size of procurement markets based on national accounts data

In 2012 the size of the government procurement market ranged from nearly 23% of GDP in the Netherlands to 8% in Switzerland (Figure 1). Public procurement expenditures in GDP terms are particularly high in Finland (18%), Sweden (16%), Japan (16%) and Denmark and France (15%). In the US, government procurement spending accounts for nearly 11% and in Canada for 14% of GDP.

In 2012 the average procurement spending in the Euro-area stands at almost 14% and for the sample of countries presented in this section at 15% (Figure 1). This shows the significant importance of public procurement entities as buyers of goods and services in an economy. Converted in absolute values the size of these public procurement markets accounts for nearly €1.8 trillion in the EU, nearly €1.3 trillion in the Euro-area and \$1.7 trillion in the US in 2012. If there was any doubt, the magnitude of these figures also shows the importance of achieving cost-efficiency in government spending. For example in the EU, policy measures which would help achieving savings on procurement expenditures of 10 percent would result in an efficiency gain of almost 1.4% of GDP, the equivalent of around €180 billion.

In this respect an interesting analysis shows that the expected procurement cost decrease as the number of bidders for a contract increase and especially so if the number of bidders reaches 5-6.¹⁷ Consequently, policy measures which would foster international competition on government procurement markets, increase transparency of tendering procedures and insure non-discrimination

¹³ For this analysis 'Titles' in RTAs are considered as Chapters.

¹⁴ See, OECD (2013).

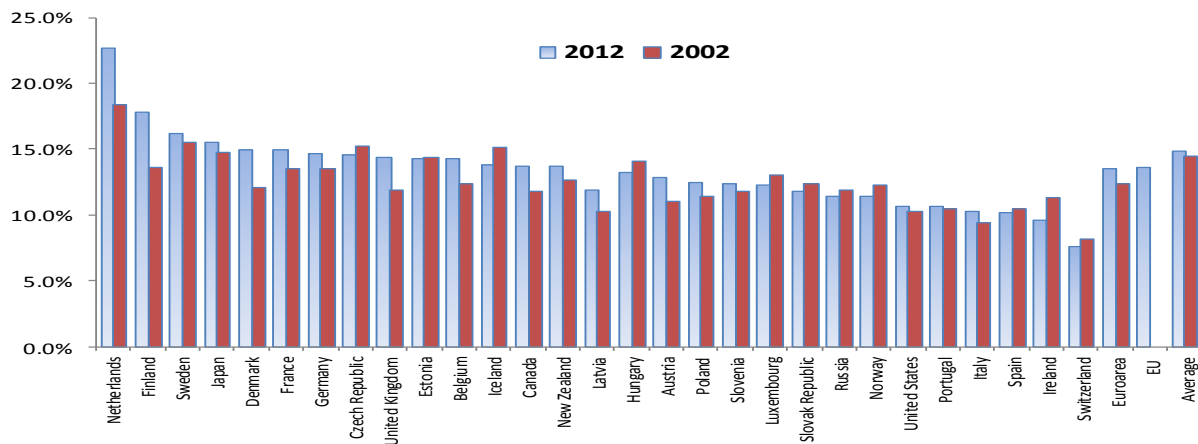
¹⁵ Note that government procurement as accounted for in national accounts may be overestimated as the above mentioned categories may include non-procurement government expenditures, OECD (2011).

¹⁶ The public procurement data analysed in this section does include total procurement spending at all levels: central, state and local. It does not however include expenditures of state-own corporations, such as state-owned utilities provides.

¹⁷ See, McAfee, R. and McMillan, J. (1989).

among bidders would induce cost savings with significant impact in terms of magnitude on the entire economy.

Figure 1: Public procurement in % of GDP in 2012 and 2002



Source: EUROSTAT, OECD National Account Statistics, own calculations, web access 5 December 2014. *No complete data on Australia, Chile and Turkey. There is no data for the EU for the year 2002.

Compared to 2002 procurement spending in relation to GDP increased in the Euro-area by 9% and in respect to the average of the country sample included in Figure 1 by 3%. Government purchases increased the strongest in Finland by 31% and in Netherlands and Denmark by 24%. There are few countries however in which procurement spending decreased in the 10 years period considered here. The strongest decrease took place in Ireland (15%) and Iceland (8%).

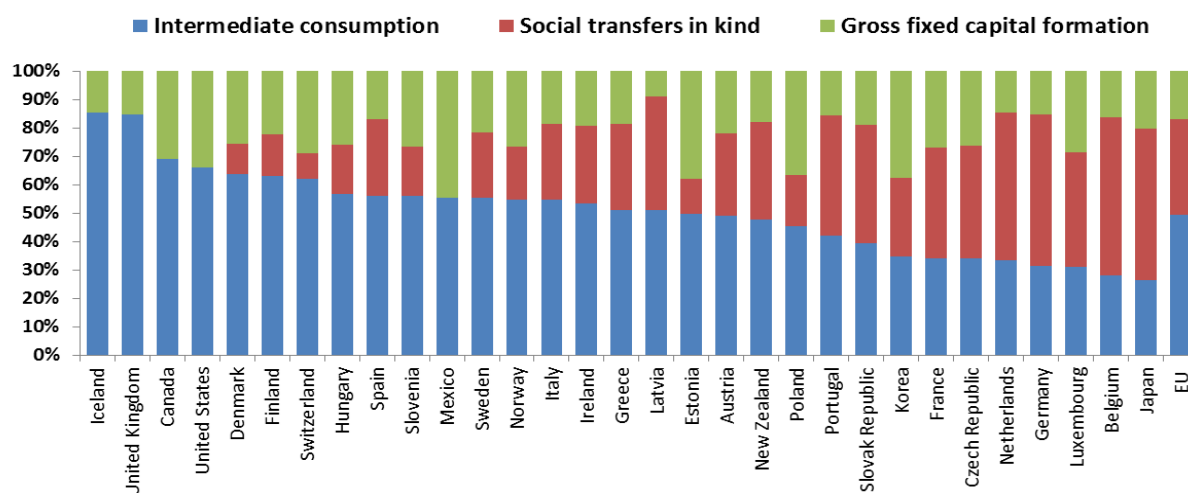
Finally, government procurement purchases account for considerable amount not only of GDP but also of total government expenditure. In OECD countries, the share of public procurement expenditure in total government expenditure amounts to around 30%.¹⁸

3.2 Composition of public procurement

Comparable cross-country data about government procurement expenditures on aggregate categories is of great importance for assessing the spending by broad categories. Figure 2 provides information on the composition of the three government procurement aggregates: intermediate consumption, gross fixed capital formation and social transfers in kind among the country sample.

In general, intermediate consumption i.e. government purchases of goods and services is the most important government procurement expenditure (Figure 2). Looking at the average of the countries included in the sample, intermediate consumption accounts for 50% of total procurement purchases and for 49% in the EU. Intermediate consumption expenditures as a share of total procurement expenditures however vary widely across the countries considered here. In Iceland and the UK, procurement of goods and services accounts for 85% of total expenditures (Figure 2). Canada and the United States are other examples of countries with high intermediate consumption expenditures shares of 69% and 66% respectively.

¹⁸ See, OECD (2013).

Figure 2: Public procurement composition by category, 2012

Source: EUROSTAT, OECD National Account Statistics, own calculations, web access 5 December 2014. *No complete data on Australia, Chile and Turkey.

On the other side of the spectrum, intermediate consumption accounts for only 26% in Japan, 28% in Belgium, 31% in Germany and Luxemburg.

The second most important component of public procurement spending is social transfers in kind via market producers. Calculating a simple average of the countries included in Figure 2 shows that 26% of total procurement is spent on social transfers. For the EU as a whole the proportion of social transfers is higher and stand at 34% in 2012, reflecting the larger weight of the European social system as compared to the average of the countries considered here. Also in terms of this category of procurement expenditures there are substantial differences across countries. Spending on social transfers through market producer is practically non-existent in the United Kingdom, Iceland, the US, Canada and Mexico. At the same time government purchases of goods and services produced by companies and offered to households (e.g. medical care or special equipment) reaches 56% in Belgium, 54% in Japan, 53% in Germany and 52% in the Netherlands (Figure 2).

The third public procurement component discussed in this section is government spending on gross fixed capital formation.¹⁹ The data presented in Figure 2 shows that it is an important component of public procurement expenditures. Calculating a simple average of fixed capital formation expenditures of the countries presented in Figure 2 points to a share of 24% in total public procurement spending and of 17% in the EU.

The countries with the highest spending on gross fixed capital formation in 2012 are Mexico (44%), Estonia and Korea (38%) and Poland (37%). This may be an indication that these countries were in the process of building up and extending infrastructural capacities. Latvia, the Netherlands, Germany, Iceland and the United Kingdom on the other hand are the countries in which government procurement of fixed assets as a share of total procurement is particularly low as it stands at 9% and 15%, respectively (Figure 2).

3.3 Public procurement patterns at government levels

Gaining knowledge about public procurement expenditures per level of government is of great importance in the framework of negotiating international commitments in bilateral and multilateral

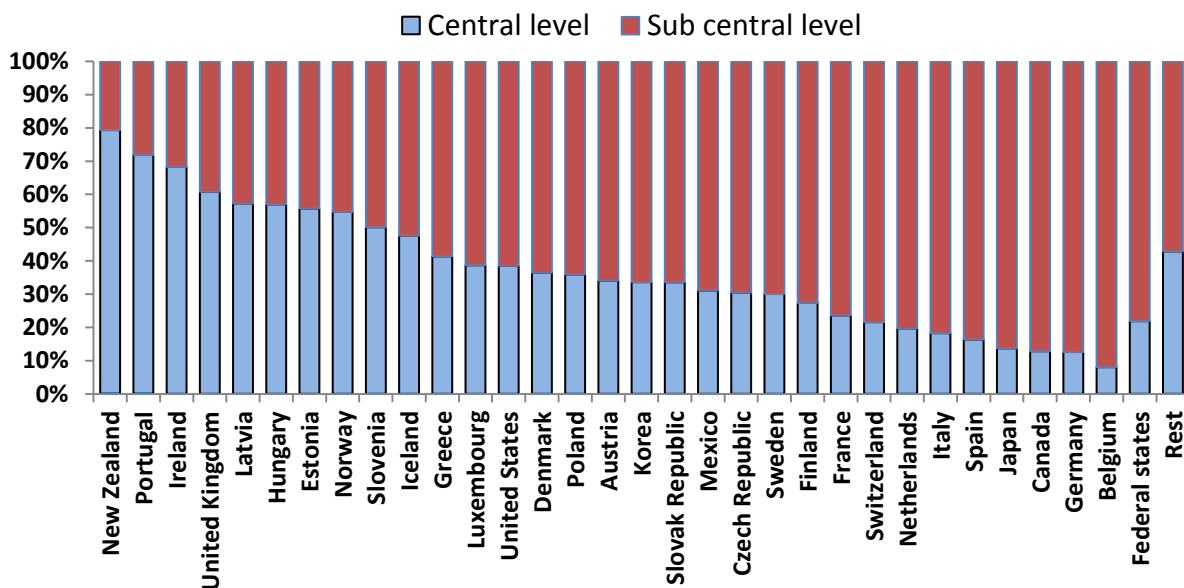
¹⁹ Gross fixed capital formation is the annual acquisition of capital less the sales of fixed assets.

agreements, as this gives an indication of the size of the public procurement market at central, state and local level. In this respect Figure 3 depicts the share of central level procurement in relation to general government (total) procurement and as a residual the share of sub-central level procurement.

The breakdown of public procurement by level of government reveals vast differences between the countries considered here (see, Figure 3). Central level procurement ranges from 80% in New Zealand to merely 8% in Belgium. Central government expenditures account for 72% of the public procurement budget in Portugal, 68% in Ireland and 61% in the United Kingdom. On the other hand, sub-central public authorities represent 87% of the public procurement expenditures in Germany and Canada and 86% in Japan.

The reason for this immense gap lies to a large extent in the legal and regulatory architecture of the countries considered here. Figure 3 shows that in general federal states have significantly larger sub-central level procurement compared to the rest of the countries. Indeed, local and state procurement of federal states like Belgium, Germany, Canada, Spain, Switzerland, Mexico and the United States account on average for 78% of total national public procurement, whereas the average for the rest of the countries lies at 57%. The spending at central level of non-federal countries is more than twice as high as the central level spending of federal countries. Nonetheless, some non-federal states such as Japan, Italy and the Netherlands also have high spending ratios at sub-central level.

Figure 3: Public procurement expenditures per level of government, 2012



Source: EUROSTAT, OECD National Account Statistics, own calculations, web access 5 December 2014. *No complete data on Australia, Chile and Turkey.

4. International public procurement: modalities of delivery

The previous section has illustrated the existing statistical information on public procurement that can be derived from national accounts and data on overall public spending, essentially across OECD countries. Based on this standard source of data, one can derive a handful of useful indicators, e.g. public procurement market size, distribution of spending between central and sub-central level, expenditure patterns, etc.

However, these national account figures do not provide information on cross-border public procurement. The reason for this is the fact that many countries do not systematically make available such figures across various agencies, levels of government and type of contracts. In a number of economies such information nevertheless exists. One of the best known examples is the EU Tender Electronics Daily (TED) database. The TED database is part of the e-procurement system across Europe that allows for the electronic publication of public tenders and awards for services, public works, and supplies as well as for other types of public contracts and projects (e.g. projects financed by the European Investment Bank, EBRD, and also external aid projects).^{20 21} The TED structure contains very important information for international public procurement negotiations: it identifies the administrative level of the contracting authority (central versus sub-central) and the service or product sought based on the so-called Common Procurement Vocabulary (CPV), a common and recognised classification. It also contains the country and address of the contractor, the number of offers received, the final value of the award, the type of procedure, and the award criteria.²²

While this is a major enhancement in terms of the cross-border dimension compared to public procurement statistics derived from national accounts, there is scope for considerable improvement. In order to identify the most important missing elements that would be needed in an international negotiation on public procurement (and its subsequent monitoring and implementation) one has to consider the complexity of today's global economy and to draw inspiration from the way in which goods and services are delivered across the border in a non-public procurement context.

When looking at the international public procurement transactions through this new lens, several important additional elements become apparent, if one wants to capture the various ways in which 'home bias' and discriminatory policies hamper the internationalization of public procurement.

The first dimension that needs to be taken into account when trying to generate statistics relevant for international public procurement negotiations is the "value-added" dimension reflecting the existence of global supply chains.²³ The second important element that needs to be considered are the so called "modes of supply", a concept already widely used in services negotiations.²⁴ Like in the case of services trade, public procurement purchases (irrespective of the type of contract i.e. works, supplies, etc) can take place under different modalities. Think of an infrastructure project involving either setting up a new 4G mobile telecom network, or a new power grid, a railway upgrade or simply a new building. In all these cases foreign companies can participate through various channels and ways of bidding, either directly from abroad or through local subsidiaries. In doing so, they will use a combination of domestic and imported goods and services needed for the public project. Alternatively, foreign companies can be subcontractors or merely suppliers of certain parts and/or intermediate services to a domestic company that will carry out the project.

Thus, one can differentiate between three key dimensions that comprise of an international component in public procurement: (i) the nationality of the firm, (ii) the location of the bidding firm (e.g. located abroad or domestic subsidiary of a foreign firm), and (iii) the purchase of foreign value-added along the supply chain, irrespective of the location and nationality of the companies winning the

²⁰ The TED database covers not only EU Member States but also EEA countries and Switzerland.

²¹ A recent paper by Kutlina-Dimitrova, Z and Lakatos, C. (2014) analyses the determinants of direct cross-border public procurement by using inter alia TED data.

²² A growing number of countries, both developed and developing, have started to adopt comprehensive e-procurement systems covering similar types of data (or parts thereof) as the TED system.

²³ See for instance the EU-sponsored World Input-Output Database (WIOD), the OECD-WTO Trade in Value Added (TiVA) database and the associated literature for a comprehensive set of international trade in value-added indicators for both goods and services.

²⁴ A recent paper argues that 'modes of supplies' have to be considered also in other trade areas (e.g. custom valuation) as there is large amount of services traded embodied into goods, see Cernat, L. and Kutlina-Dimitrova, Z. (2014).

public tender. Based on these key dimensions one can distinguish 3 main modalities of international public procurement of goods and services:

- **Direct cross-border international procurement:** a foreign company submitting a bid and winning "from abroad". This mode is conceptually similar to the traditional mode 1 for services trade.
- **Commercial presence procurement:** a domestic subsidiary of a foreign company wins "locally" the public contract. This mode is conceptually similar to mode 3 for services trade.
- **"Value-added" indirect international procurement:** a foreign company participates indirectly with parts and components (goods and services) without necessarily being part of the winning bid. In this case the foreign company may supply goods and services to a domestic company winning the bid or to another foreign company that received the public contract.

Equipped with this simple set of international procurement modalities one can make better sense of the scant data currently available. Take the TED data for instance analysed in Kutlina-Dimitrova and Lakatos (2014). This data only covers the direct cross-border public procurement contracts and does not distinguish specifically the international procurement through commercial presence, e.g. the public contracts won across EU by domestic subsidiaries of foreign firms in Europe. Similarly, neither does the TED database (nor probably any other similar e-procurement platforms in other countries) capture the "value-added" international procurement, since there is not a systematic assessment of the foreign value-added content in the final basket of goods and services purchased by public authorities. Therefore, the very few papers that tried to quantify the foreign penetration of public procurement markets severely underestimate the actual openness, since they capture essentially one mode of supply and only a part of the total international procurement.

The existing anecdotal evidence and the various case studies carried out in the past seem to suggest convincingly that, for a number of reasons, the value of commercial presence public procurement would be significantly higher than the one for direct cross-border procurement.²⁵ On the one hand, commercial presence public procurement may be less subject to discriminatory restrictions against foreign participation, whenever national treatment is granted to foreign affiliates (like in the case of the EU procurement markets). On the other hand, there are good objective reasons why commercial presence would be the preferred way of bidding, since given the complex technical nature of certain procurement contracts, both contracting authorities and prospective companies value proximity and local presence.

Value-added indirect procurement contracts also have certain specific characteristics. First, the GPA distinguishes clearly between companies and their goods and services provided under public procurement contracts. Therefore, the existing disciplines create a different set of rules when one looks at the products and services delivered, as opposed to a "company-based" approach. Similarly, domestic public procurement legislation subjects such value-added international participation to different rules than the foreign companies themselves. For instance, a particular procurement contract may be only open to domestic companies but it may put no restrictions on the purchase of key components (steel or high-tech equipment) from foreign firms or on minimum local value-added. Conversely, government procurement provisions may be very liberal vis-a-vis foreign companies but at the same time there might be strong discriminatory value-added 'buy local' restrictions on imported intermediate goods and services.

Therefore, two clear conclusions come out from this conceptual taxonomy of different modalities of international procurement. First, any statistical indicators capturing openness in public procurement needs to reflect the fact that foreign companies, as well as their goods and services can become part of public contracts abroad under different modalities of international procurement. Incomplete data and

²⁵ Ramboll/HTW Huhr (2011).

definitive conclusions drawn based on only a subset of procurement modalities may lead to wrong political perceptions and policy priorities.

Second, having such a comprehensive and structured approach to public procurement data collection by modalities of delivery (both under the new GPA statistical work programme and as part of bilateral trade negotiations) would allow a more informed debate about the different nature of restrictions and barriers affecting each procurement mode of supply, and facilitate the implementation of existing rules. Some countries may be more restrictive on one mode or the other. Other countries may have an interest in trying to liberalize one mode or the other in a particular negotiation, once more systematic data collection enables identification of the nature of the procurement market restrictions and the value of international procurement flows for each mode of supply.

5. Challenges and looking ahead

The current paper tried to argue in favour of a rather straight forward point: the internationalisation of public procurement should be a key priority for trade negotiators, given the significant size of public procurement markets and the high level of restrictions that still persist, despite decades of attempts to arrive at binding commitments and less discriminatory policies.

However, this task is made even more difficult by the absence of a suitable factual basis for negotiations. In the absence of hard data and clear indicators that measure existing international procurement flows, the ‘home bias’ tendency and pronounced offensive interests may hamper progress on new more liberal procurement rules as well as monitoring and implementation of existing procurement provisions.

Comparable and commonly accepted figures based on a solid methodology are also needed to build consensus for new prospective members to understand what are the benefits from participating in future public procurement negotiations.

All these tasks remain daunting but not impossible. For some modalities of international procurement (e.g. value-added indirect participation) the figures would have to rely on estimates, as opposed to other modalities of delivery (direct cross-border or commercial presence) where the actual data can be collected during the procurement process.

A first step would be to agree on an international procurement data collection methodology that all WTO members would be ready to apply in their domestic procurement legislation. The methodology could be tested and fine-tuned based on some pilot cases, covering countries with different legal systems and level of development. The data collection process in developing countries can be supported by donors and other relevant international organisations (OECD, IMF, World Bank, UN agencies) with benefits also for a number of other domestic policy objectives. As it happened in other trade and investment areas, the policymakers and the academic community could join forces to put the basis for a comparable and consistent data collection process that could eventually put public procurement on the same level of analytical rigor and data availability as in WTO trade negotiations in the goods and services areas.

References

- Brühlhart, M. and F. Trionfetti (2001), *Industrial Specialisation and Public Procurement: Theory and Empirical Evidence*, Journal of Economic Integration, 16, pp 106-127.
- Cernat, L. and Kutlina-Dimitrova, Z. (2014), *Thinking in a box: A 'Mode 5' approach to services trade*, Journal of World Trade, volume 48(6), pp 1109-1127.
- Kutlina-Dimitrova, Z and Lakatos, C. (2014), Determinants of direct cross-border public procurement in EU Member States, Chief Economist Note 2014-2.
- McAfee, R. and McMillan J. (1989), *Government Procurement and International Trade*, Journal of International Economics 26, pp 291-308.
- OECD (2011), Government at a Glance 2011, OECD Publishing, Paris.
- OECD (2011), National Accounts at a Glance 2011, OECD Publishing, Paris.
- OECD (2013), Government at a Glance 2013, OECD Publishing, Paris.
- Ramboll/HTW Huhr (2011), Cross-border procurement above EU thresholds, final report for the European Commission, DG Internal Market and Services, Copenhagen.
- Shingal, A. (2011), *The WTO's Agreement on Government Procurement: Whither Market Access?* World Trade Review, 10(4), pp 1-23.
- Shingal, A. (2015), *Econometric analysis of home bias in government procurement*, Review of International Economics, 23(1), pp 188-219.
- Trionfetti, F. (2000), *Discriminatory Public Procurement and International Trade*, The World Economy, 23, pp 57-76.
- WTO (2014a), Annual Report 2014, Geneva.
- WTO (2014b), Statistics reports under Article XIX:5 of the GPA, http://www.wto.org/english/tratop_e/gproc_e/gpstat_e.htm, web access on 8 December 2014.

Author contacts:

Lucian Cernat and Zornitsa Kutlina-Dimitrova

Lucian Cernat, PhD, is the Chief Economist of DG TRADE of the European Commission.

Zornitsa Kutlina-Dimitrova, PhD, is an economist in the Chief Economist and Trade Analysis Unit of DG TRADE

Email: Lucian.Cernat@ec.europa.eu; Zornitsa.Kutlina-Dimitrova@ec.europa.eu