EUROPEAN SEMESTER THEMATIC FACTSHEET

SERVICES

1. INTRODUCTION

The services sector is the main contributor to growth and employment in the EU, accounting for about two thirds of both EU employment and value added[1]. Figure 1 depicts the value added share of market services (NACE sectors G to N) in Member States as well as the average value added share in the EU28 in 2014. Luxembourg (70%), Cyprus (62%), United Kingdom (60%) and Greece (55.6%) are among the countries with the highest value added generated by market services. On the other extreme are the Czech Republic (42.6%) and Hungary (44%) and to a lesser extent Germany (48.5%) when compared to other MS and the EU.

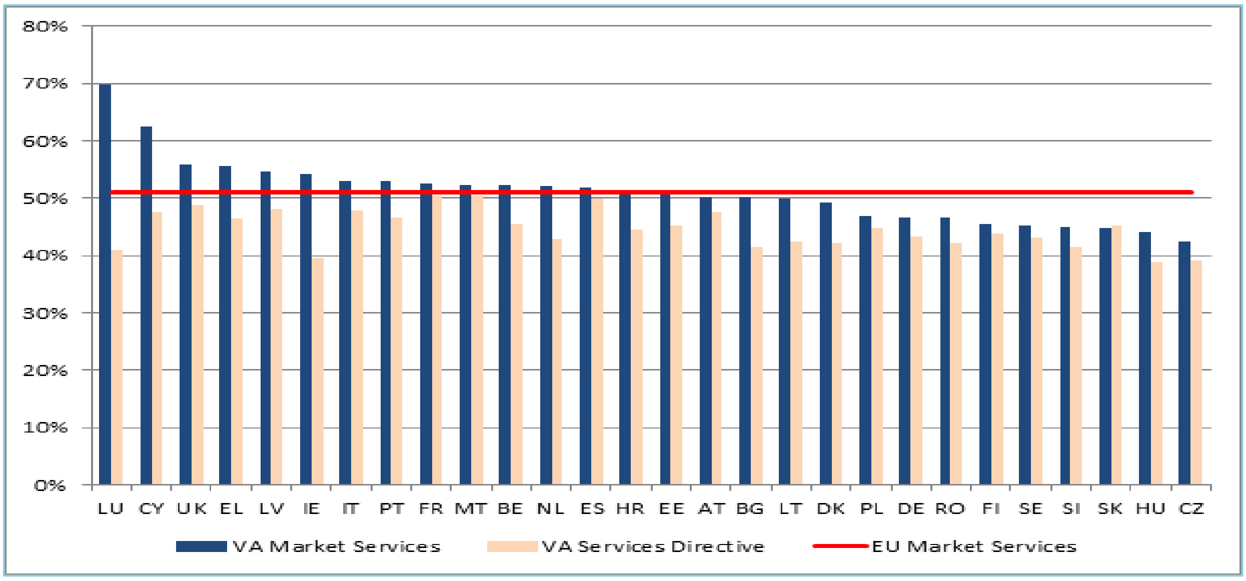
The Services Directive, approved in 2006, provides a horizontal framework which covers 46% of EU GDP (including business services, wholesale and retail and construction). The share of total value added stemming from services covered by the Services Directive varies among Member States, from around 50% in France, the UK, Latvia, Cyprus, Italy, and Austria, to approximately 40% in Ireland, Hungary and Czech Republic.

While value added share provides an output-based measure on the importance of a particular sector in the economy, employment share provides further information from the input side. Figure 2 displays the 2014 aggregate employment share of market services as well sectors covered by the Services Directive (measured as persons employed), which shows considerable variation across countries. Around 45% of EU employment is generated by the sectors covered by the Services Directive, with Member States' shares spanning from close to 50% in Luxembourg to around 29% in Romania. In particular, the activities covered by the Services Directive made up more than 52% of employment in the UK, the Netherlands, Malta and Cyprus and less than 39% in Poland, Bulgaria, Hungary and Ireland.

Due to the nature of service provision, the sector has strong interlinkages also to other economic sectors, such as manufacturing. The interlinkages, or mutual dependencies, are visible in two ways. Firstly, they are important as services industries are customers or users of other sectors' inputs (backward linkages). Secondly, services industries also serve as suppliers or inputs into the production process of other sectors (forward linkages). The increasing forward and backward linkages are part of the trend of blurring borders between services and manufacturing, sometimes known as servitisation or servicification.

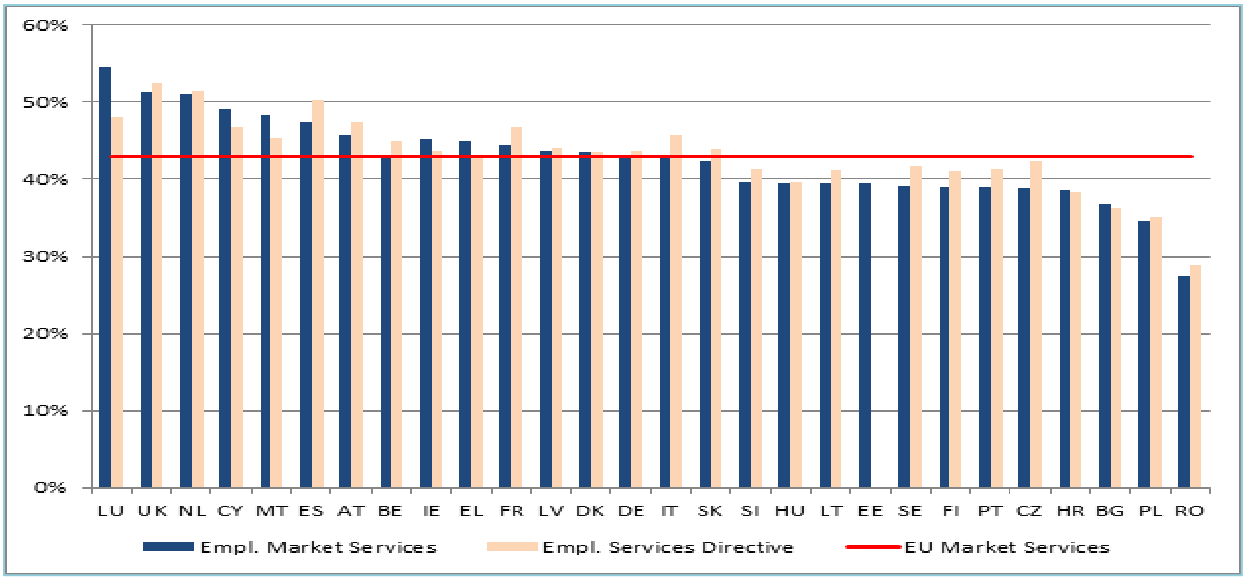
[1] Measured as gross value added (GVA), here used as an approximation of gross domestic product (GDP). The relationship between GVA and GPD is: GVA + taxes on products – subsidies on products = GDP.

Figure 1 – Value added share (%) of market services, 2014[2]



Source: Own calculations based on Eurostat

Figure 2 – Employment share (%) of market services, 2014[3]



Source: Own calculations based on Eurostat

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[2] Market services defined as: G-I: Wholesale and retail trade; transport, accommodation and food service activities, K_L: Financial and insurance activities; real estate activities, J: Information and communication, M_N: Professional, scientific and technical activities; administrative and support service activities. Sectors covered by the Services Directive are retail and wholesale trade, construction, business/professional services, real estate, tourism and some entertainment services. At this level of disaggregation data are available for 2013, except for ES and PL where latest data available refer to 2012. Based on 'Nace Rev. 2 – Statistical classification of economic activities in the European Community', Eurostat, Luxembourg, 2008.

[3] See footnote 2.

Demand spillovers (backward linkages) generated by services sectors are large and for selected sectors of a similar order of magnitude of the spillovers generated by manufacturing. These backward linkages show the total production generated, directly and indirectly, to satisfy one euro of final demand for services.

The range of the value of multipliers for services in the EU27 is 1.6 (real estate) to 2.5 (air transport) and are important for the priority sectors of construction (2.3), business services (1.9) and retail services (1.8)[4].

The role of services as intermediate inputs into the production of all goods and services produced in the economy is analysed by calculating forward linkages. The value of a services industry's forward linkages is an indication of how much of its production contributes to the production of other industries.

It includes both services' share as direct inputs into the production of other goods and services, as well as indirect inputs via other industries (feedback effect).

The larger this *feedback effect*, the larger the spillovers generated by well-functioning services sectors as efficiency gains are transmitted to the rest of the economy via their role in the production process.

For EU27 the share (%) of the various services sectors in the total value of intermediate inputs used in the economy stand at: Business services (5.5), wholesale trade (3.0), retail trade (2.3), construction (2.2) and hotels and restaurants (1.3). In particular the former thus constitute key inputs into other parts of the economy[5].

Given the importance of the performance and functioning of the EU services market for the overall EU economy, a well-functioning services market is a key component in the Commission's focus on boosting job, growth and investment, while ensuring a deeper and fairer internal market.

Despite previous attempts to lower the barriers to the cross-border provision of services, obstacles remain mainly as a result of diverging national rules and procedures.

Such obstacles stifle economic growth while leading to an inefficient allocation of resources across/within EU economies, lower competitive pressures and less cross-border trade. Removing such obstacles would provide both services providers and customers with greater opportunities to make full use of the potential of the internal market.

In the 2015 Digital Single Market Strategy (DSM) and the Single Market Strategy (SMS), the Commission announced initiatives aimed at removing obstacles hampering the growth in the EU services market, be it on-line or off-line. These initiatives include:

- *Collaborative economy:* A June 2016 Commission communication providing legal guidance and orientation to public authorities, market operators and interested citizens for the balanced and sustainable development of the collaborative economy.
- *Geo-blocking:* A May 2016 Commission proposal for a regulation seeking to clarify the grounds on which access to a service can be denied depending on residence or nationality, providing increased certainty to customers and companies alike.
- *European Services e-card:* A forthcoming legislative proposal introducing a European services e-card facilitating the provision of services in the single market.
- *Notification procedure:* A forthcoming legislative proposal aimed at strengthening the procedure under the Services Directive, whereby the Member States notify changes in national services rules.
- *Proportionality tests:* An initiative to improve the assessment of proportionality of national regulatory measures.

[4] Source: World Input-Output Database (WIOD) (www.wiod.org).
[5] Source: WIOD (www.wiod.org).

- *Reform guidance:* A guidance for regulation of professional services at national level[6].
- *Retail:* Commission initiative setting out best practices for facilitating retail establishment and reducing operational restrictions in the Single Market.

This note is structured as follows. Section 1 provides an overview of economic input (value added) and output (employment) indicators highlighting the importance of the services sector for the EU wide economy. Section 2 contains performance indicators which summarise the policy challenges facing the services sector. Section 3 identifies policy levers to address these challenges. Section 4 provides good policy examples used by Member States to address challenges.

2. POLICY CHALLENGES

Despite the importance of the EU services sector overall, a number of challenges continue to face EU services provision to the detriment of the sector's growth potential.

These challenges include slow productivity growth, inefficient resource allocation, low competitive pressure and cross-border services integration.

2.1. Slow productivity growth

Despite some improvements in labour productivity per person employed in 2008 to 2013 in some countries (notably those that joined the EU in 2004), labour productivity growth in the EU services sector has been outperformed by other economic sectors, including manufacturing[7].

OECD data[8] shows average annual labour productivity growth (2001-2013) in manufacturing of 2,6%, whereas most service sectors experienced growth below 1% or even decline over this period.

Also, when comparing to average annual labour productivity growth in the US, research[9] estimates that EU services over the period 2007-2010 underperformed in several sectors such as construction (-3,45% vs. 2,55%), IT services (-0,72% vs. 4,24%) and retail (2,02% vs. 2,94%). Reducing this productivity growth gap is key for the competitiveness of the European services sectors and the growth and jobs it can create.

Figure 3 compares labour productivity growth in the EU across market services and the manufacturing sector in two periods of time. Since the crisis labour productivity in the manufacturing sector has grown at higher rates in comparison with the services sector.

It is important to note that business services displayed a negative labour productivity growth during the first years of the crisis. Even if during the adjustment years (2012-2014) their productivity has recovered, it still grew at a slow pace.

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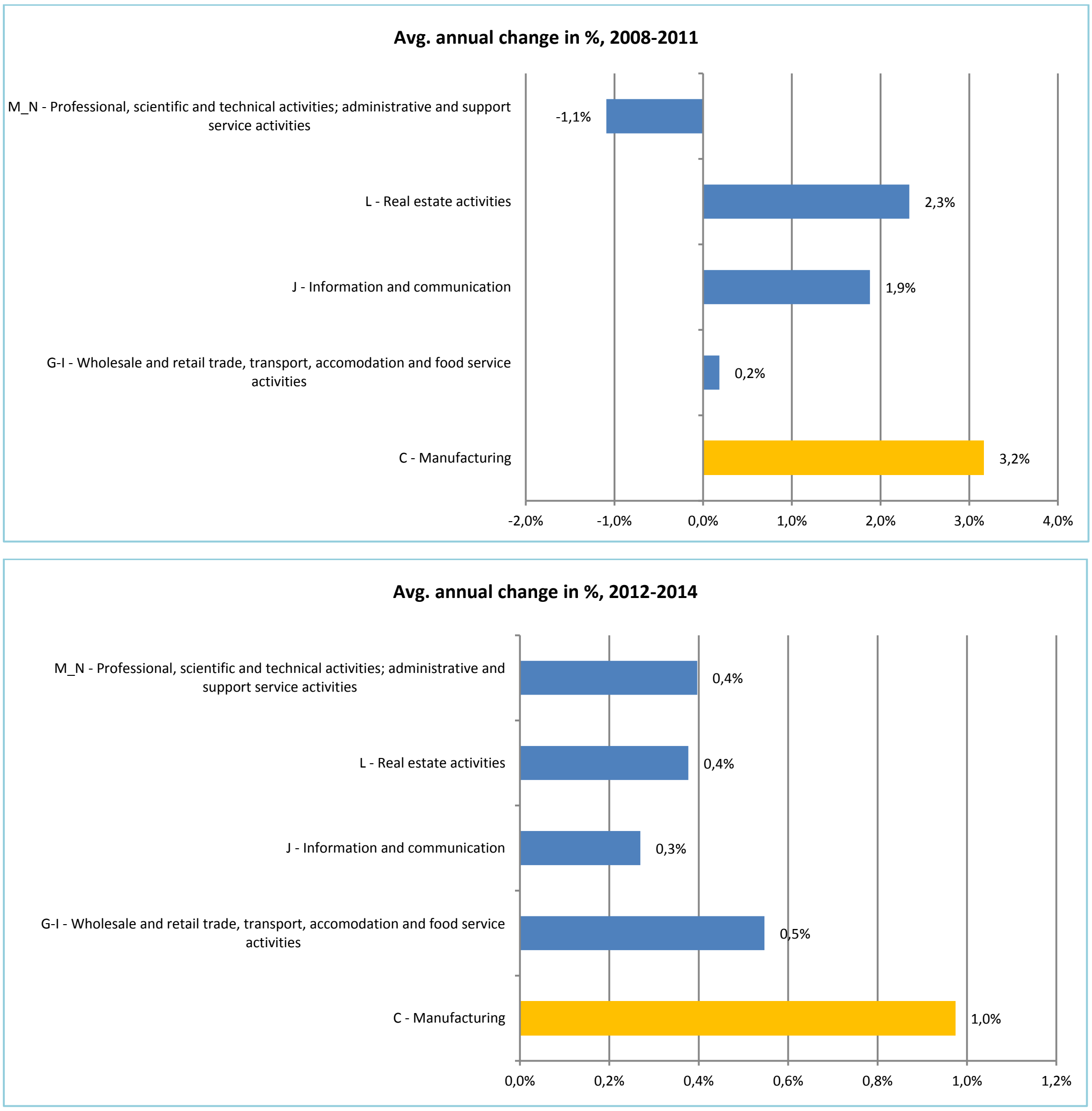
6 For further discussion, see the European Semester thematic factsheet on regulated professions.

7 See Commission SWD(2015) 203, 'Report on Single Market Integration and Competitiveness in the EU and its Member States', accompanying the Communication COM(2015) 550, 'Upgrading the Single Market: more opportunities for people and business'.

8 See OECD statistics on Productivity and ULC by main economic activity (http://stats.oecd.org/Index.aspx?DataSetCode=PDBI_I4).

9 Source: WIOD (www.wiod.org).

Figure 3 – Sectoral productivity growth since the crisis in market services



Source: Commission services' calculations based on Eurostat

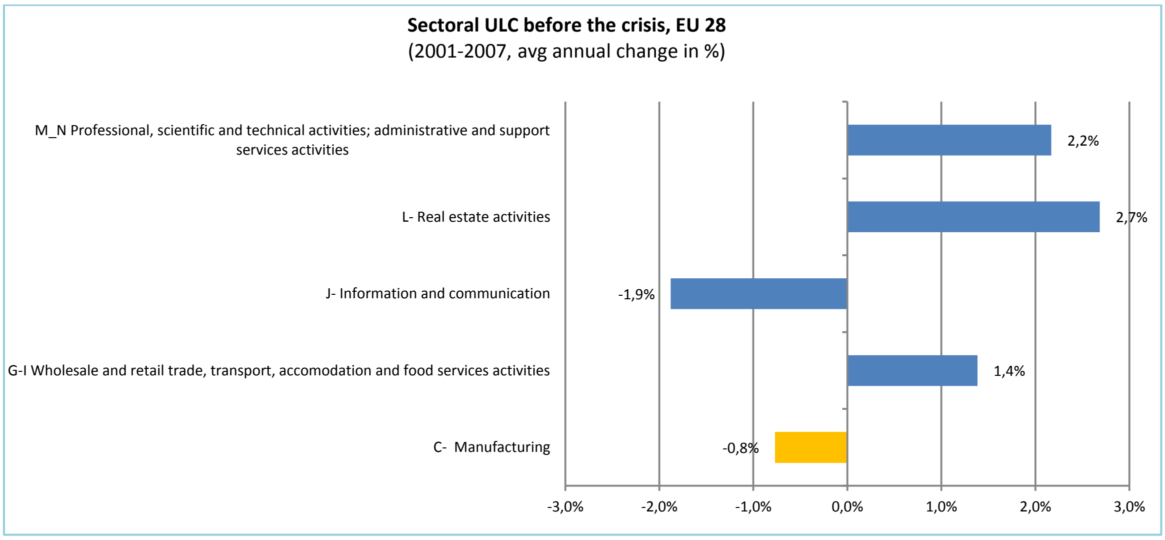
In terms of the relation between labour productivity developments and labour compensation, recent evidence[10] shows that labour productivity in market services has only outpaced labour compensation in countries such as Portugal, Spain, Cyprus and Greece[11], which have experienced strong market pressures and which have been undergoing major competitiveness adjustments. Figure 4 compares Unit labour costs (ULC) at sectoral level, before and during the crisis.

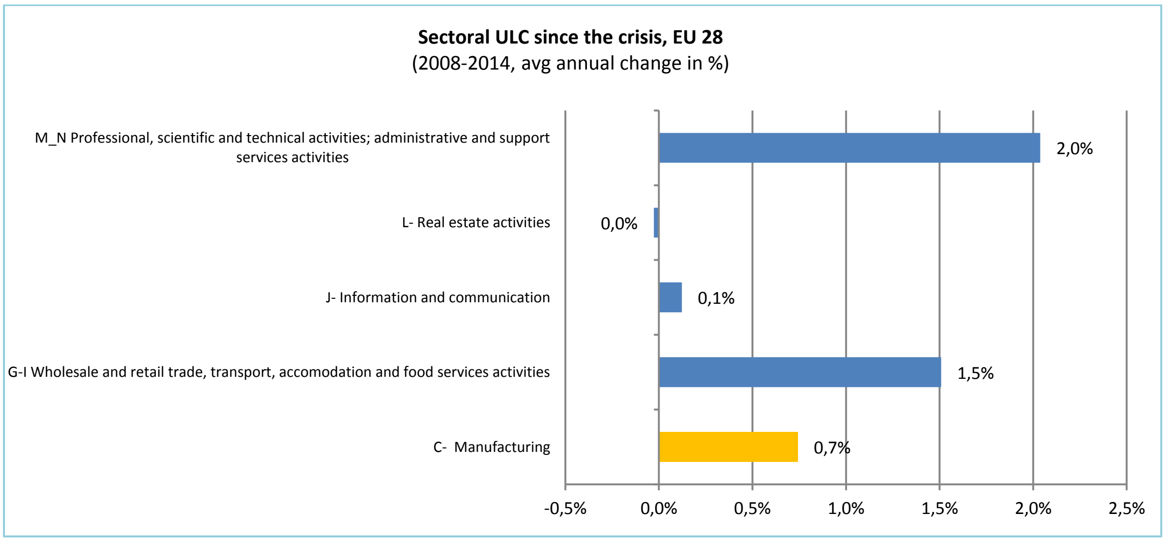
The figure shows that in the period before the crisis wage compensation were growing faster than labour productivity. Indeed, losses of competitiveness in the pre-crisis were driven by large unit labour costs increases in the services sectors (mainly business services, real estate activities and wholesale and retail activities). And since the crisis, some services sectors still show some resistance to adjustment, this is particularly the case of business services and retail.

10 'Quarterly Report on the Euro Area', Volume 14, No 2, European Commission, 2015.

11 Though the strong wage adjustment in Greece has not been accompanied by improvements in labour productivity in services.

Figure 4 – Sectoral ULC before and during the crisis, EU28 (average annual change in %)





Source: Commission services' calculations based on Eurostat

2.2. Inefficient allocation of resources

Services sectors are in general - and also when comparing to manufacturing - not showing an efficient flow of resources to their most competitive firms. This is illustrated by the allocative efficient index (AE)[12] which captures the extent to which more productive firms have higher market shares[13]. An analysis across Member States comparing AE for manufacturing sector with professional services shows that the manufacturing sector displays a positive relation between labour productivity and market share of companies (see Figure 5). The interpretation is the following. For example, in the Belgium manufacturing sector, the actual allocation of resources implies a 23% higher productivity (compared with a theoretical benchmark where all resources would be allocated uniformly across firms). For professional services, the allocative efficiency is typically negative, implying that firms with relatively low productivity have above-average market shares.

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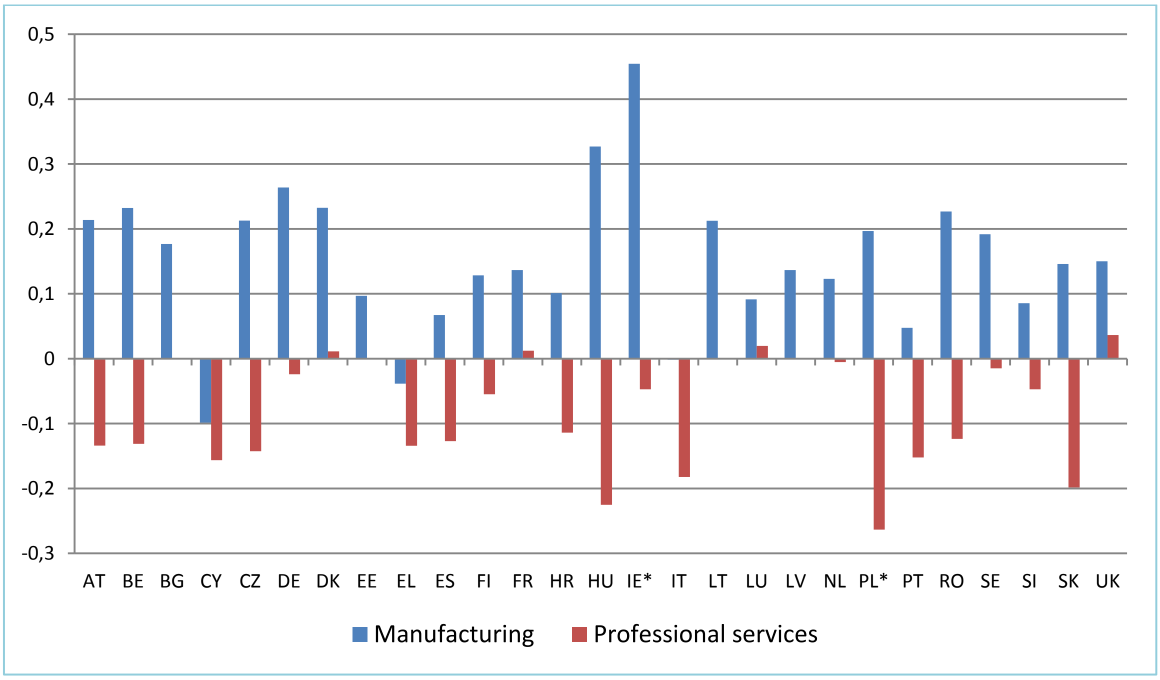
12 'Product Market Review 2013 – Financing the real economy'; European economy 8/2013, European Commission.

13 Approximating market shares with the employment of the firms in a size class.

Figure 5 – Allocative efficiency, 2013 (%). Manufacturing and professional services



Source: ECFIN's calculation based on Eurostat. Data for MT are not available. Data are also missing for BG, EE, LT and LV for professional services.
** Data for IE and PL relate to 2012.*

Other service sectors (including retail, construction and accommodation and food services) too have negative allocative efficiency index values, showing that there is an inverse relation between productivity and market share of services companies. This sub-optimal resource allocation constrains the productivity of these sectors and hampers their competitiveness.

2.3. Low competitive pressure

There are several channels through which competition can drive productivity. For example by ensuring that over time less productive firms are replaced by productive new ones, or by creating incentives for firms to invest in the reduction of costs and in innovative new products that boosts productivity. Two indicators that can be used as proxies for competition forces are market churn rates[14] and gross operating rates[15].

Churn rates and profit rates disaggregated by service sectors vary significantly between Member States and services sectors. Large differences in churn rates or profit rates between Member States hint at varying degrees of competitive pressure. A more integrated market would be expected to see a convergence of these indicators between Member States.

The link between churn rates, profit rates and allocative efficiency is also important to highlight. In a study on the effect of regulatory barriers on four regulated professions (legal, accounting, architectural and engineering) it has been shown with econometric modelling that the entry and exit of firms have a significant effect on the profit rates and allocative efficiency for the professional services sector[16].

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[14] Market churn rates are defined as the sum of birth and death rates expressed as percentage of the total number of active firms in an industry.

[15] The gross operating rate is defined as the ratio of gross operating surplus to turnover and is a proxy for profits.

[16] E. Canton, D. Ciriaci and I. Solera, 'The Economic Impact of Professional Services Liberalisation', European Economy. Economic Papers. 533, DG ECFIN, European Commission, September 2014.

A reduction of the regulatory barriers in the sectors has been shown to increase sector-specific churn rates, which in turn increase allocative efficiency and decrease profitability – substantiating the theoretical assumption that more dynamic markets put stronger competitive pressure on profit rates while contributing to a more efficient use of production factors.

2.4. Cross-border services integration

Trade integration can be used as a measurement of the extent to which business are able to access potential customers in other Member States. At 6%, the trade integration[17] of services across the EU lags considerably behind that of goods (22%).

Cross-border investments[18] in services stands at 11% and is also disproportionately low compared to goods (17%).

While some of the differences are due to the lower tradability of services, the figures indicate that service providers are unable to make full use of the potential offered by the Single market.

3. POLICY LEVERS TO ADDRESS THE POLICY CHALLENGES

The challenges described above are to a significant extent a result of the regulatory and administrative policies of the EU Member States.

Resolving these challenges will unlock a significant number of positive effects. A number of policy levers can be pursued to advance the modernisation of services regulations across the EU.

3.1. Potential policy levers

3.1.1. Country-specific recommendations

Economic evidence shows that there is a significant scope for services reforms beyond the minimum legal requirements of the Services Directive. To reap the full potential benefits offered by the Services Directive, numerous Country-specific Recommendations (CSRs) have been adopted by Council to ensure more dynamic and competitive services markets. In 2016, Council approved recommendations in the area of services addressed to ten different Member States. CSRs serve the aim of achieving an EU services market with fewer barriers for providing and receiving services, in particular in areas where the acquis does not categorically outlaw certain practices and leaves it up to Member States to assess the justification and proportionality of national regulation.

3.1.2. New targeted EU-level policy initiatives

As described in section 1, the Commission is committed to putting forward new initiatives aimed at improving the functioning of the EU services market in priority areas. Initiatives promoting the balanced development of the collaborative economy, ensuring that consumers have access to goods and services without being unjustifiably discriminated, reducing the barriers in cross-border provision with the help of the European services e-card, making the notification procedure under the Services Directive more efficient, introduce proportionality tests for regulatory measures and provide reform guidance for regulation of professional services and for particular sectors (retail) all serve to make it easier for services providers and recipients to make use of the internal market for services.

3.1.3. Enforcement and implementation

Enforcement of the existing requirements under the Services Directive remains an important instrument in achieving that the full potential of the services market liberalisation is realised.

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17 Defined by the average of intra-EU imports and export divided by GDP (2012, EU-27). (Source: Eurostat).

18 Share of value added generated by enterprises controlled by another EU Member State – secondary establishment. Nace Rev. 2 service sectors included are D-J, L-N and S95 (source: Eurostat). No data is available on cross-border provision without prior establishment.

In its 2012 Communication[19], the Commission announced a zero tolerance policy with respect to Member States not complying with the Services Directive. In 2013, the Commission initiated structured dialogues with Member States in 16 cases related to the Services Directive and in 2014 there were 17 new cases.

In June 2015 the Commission launched six infringement procedures in order to address excessive and unjustified obstacles relating to the use of legal form and shareholding requirements for regulated professions. In November 2016 decisions on a package of 10 cases concerning key sectors in the scope of the Services Directive were adopted.

The Commission also initiated structured dialogues with ten Member States over the performance of their Points of Single Contact and the electronic procedures they must offer under the Services Directive to allow services providers to complete administrative procedures online.

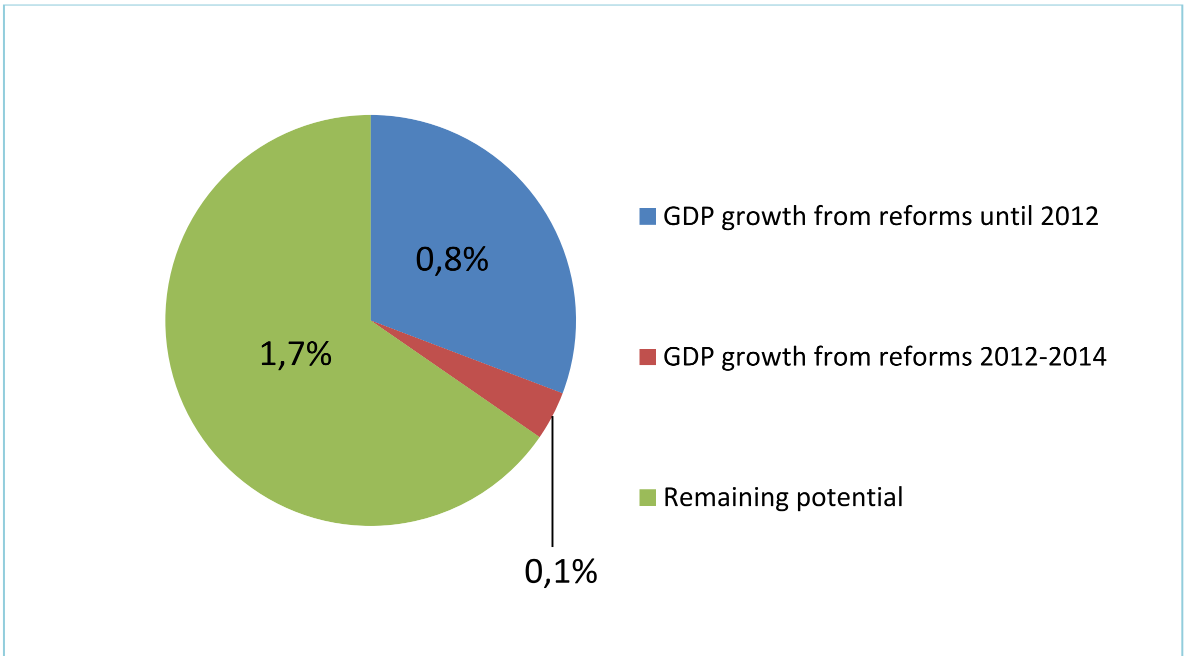
3.2. Beneficial effects of addressing identified challenges

Following the adoption of the Services Directive in 2006, Member States undertook substantial reform efforts adopting more than thousand laws in order to abolish existing barriers. In 2012 a Commission assessment found that the reforms undertaken up to that point would yield a 0.8% GDP increase over the coming year[20].

The assessment also found that if Member States would pursue a more ambitious implementation (where Member States would reach the average of the 5 least restrictive Member States) the additional growth potential was estimated at 1.8% of EU GDP.

Considering this significant untapped growth potential, the Commission, the European Parliament and the Council in 2012 all called for a more ambitious implementation of the Services Directive.

Figure 6 – Estimated EU level GDP impact from services reforms



Source: European Commission SWD(2015) 202, 'A Single Market Strategy for Europe – Analysis and Evidence'

[19] European Commission COM (2012) 261, 'A Partnership for new growth in services 2012-2015'.
[20] J. Monteagudo, A. Rutkowski and D. Lorenzani 'The economic impact of the Services Directive: A first assessment following implementation', European Commission economic paper 456, 2012.

In an updated assessment in 2015, estimating the impact of reform efforts during 2012-2014, it was found that only a fraction (0.1%) of the 1.8% GDP potential has been realised (illustrated in Figure 6). These results are not surprising as reform effort during this period has been uneven, with reforms mainly having taken place in Member States subject to financial assistance programmes or implementing comprehensive national reform programmes[21].

According to the World Bank study published in the fall of 2016, limiting service sector restrictions to the level of the three least regulated Member States (the UK, Denmark and Sweden) would increase productivity of firms that operate in services and manufacturing by up to 5.3% within two years of implementation[22].

The successful removal of identified barriers would give rise to a number of positive effects:

A more competitive services sector. Increased competitive pressures following a reduction in market barriers leads to more firms entering and exiting the market, thereby driving up overall productivity. This is supported by 2014 Commission study[23] which assessed the economic impact of national reforms lowering regulatory burden for selected regulated professions. The study shows that reducing regulatory barriers in such professions by 1 point[24] increases churn rates[25] on average by 1.75%, leading to a better allocation of resources, as a result of which allocative efficiency is increased by 5.7%. A related Commission assessment from 2015 of the barrier for key business services found that a reduction of the current barrier level would increase the number of companies providing such services by up to 18%[26]. This means that reducing regulatory restrictiveness opens up markets to competition, which leads to a more dynamic and productive services sector[27].

Positive spill-over effects, including to the manufacturing sector. Services are increasingly interconnected with other sectors of the economy both as user of input from other sectors (*backward linkages*) and as input for the production process in other sectors (*forward linkages*). Many services companies are fully integrated in the European value chain as they use inputs produced by other parts of the economy and provide inputs to other sectors. A productivity increase in one service sector will therefore have considerable multiplication effects across the economy[28]. As the manufacturing industry is an important consumer of business services, increased competition and productivity gains in business services would entail important benefits for the manufacturing industry. This is supported by research by IMF which quantifies the impact of these multiplication effects[29]. The study shows in

[21] European Commission SWD(2015) 202, 'A Single Market Strategy for Europe – Analysis and Evidence'.

[22] 'Growth, jobs and integration: Services to the rescue', World Bank EU Regular Economic Report, Fall 2016. (http://pubdocs.worldbank.org/en/930531475587494592/EU-RER-3-Services-to-the-Rescue.pdf).

[23] 'The economic impact of the professional services liberalisation', Economic Paper 533/2014, European Commission.

[24] Professional Services regulation measured by the OECD PMR indicator, an index developed by the OECD which quantifies the level of restrictiveness per Member State and sector (from 0 to 6 with a low value corresponding to a light regulatory burden) (source: https://www.oecd.org/eco/growth/indicatorsofproductmarketregulationhomepage.htm).

[25] See note 14 for the definition of market churn rates.

[26] European Commission SWD(2015) 202, 'A Single Market Strategy for Europe – Analysis and Evidence'.

[27] See also 'Market Reforms at work in Italy, Spain, Portugal and Greece'; European Economy 5/2014, European Commission.

[28] For a more detailed analysis of the role of services sectors in international value chains see 'International value chains intra- and extra-EU', background study for the 2014 annual single market integration report, European Commission, 2013.

[29] See E. Fernández Corugedo and E. Pérez Ruiz, 'The EU Services Directive: Gains from Further Liberalization', IMF Working Paper, 2014. The results in this study are based on

particular that increasing the total factor productivity in the other business activities sector (mainly including business services) would lead to significant economy-wide spill-overs. Also in retail and wholesale, acting as distribution channels for manufacturing, efficiency can boost demand with a positive effect on manufacturing value chains.

Benefits for consumers. National reforms reducing barriers and integrating the single market for services entail considerable economic benefits for consumers. Firstly, stronger competition leads on average to lower prices. The above mentioned European Commission study shows that reducing regulatory barriers in selected highly regulated professions moderates the observed larger-than-average profits caused by lack of competition. The observed effect of competition-friendly reforms undertaken in Member States supports this notion, e.g. reforms in the Spanish business services sector have seen decreased margins from 28% to 18% over the past 15 years, leading to increased purchasing power for consumers[30]. Overall consumption levels will also increase, given that firms will set prices closer to competitive levels. Secondly, a more competitive and integrated services market will offer consumers on average more choice and better quality of services. E.g. an analysis of the effect of deregulating tourist guides and notaries in Poland found no negative impact on the quality of services provided (while it did find evidence of new and cheaper services[31]). Furthermore, evidence shows that consumers evaluate more integrated markets as better performing markets[32]. In addition, the Product Market Regulation Indicator (OECD) shows negative correlations with the extent that markets meet consumers' expectations, which suggests that in countries in which there are less barriers to competition and entrepreneurship, consumers' satisfaction is somewhat higher[33].

4. CROSS-EXAMINATION OF POLICIES: STATE OF PLAY

4.1. Persistent barriers in the services markets

Even though Member States have complied with the obligations relating to the transposition of the Services Directive, providers in several service sectors still face a wide array of barriers when they want to establish in another Member State or provide services on a temporary cross-border basis.

Taking the example of business services, the largest services sector falling under the Services Directive, accounting for almost 12% of both EU GDP and employment, the administrative and regulatory burden varies significantly between Member States. Figure 7 shows the overall restrictions in four key professions forming part of business services – accountants, architects, engineers and lawyers, based on a study of barriers in business services performed in 2015[34].

the impact of further liberalisation on the French economy.

[30] 'The effects of reforms of regulatory requirements to access professions: country-based case studies', DG GROW, European Commission, 2015 (http://ec.europa.eu/growth/tools-databases/newsroom/cf/itemdetail.cfm?item_id=8525&lang=en).

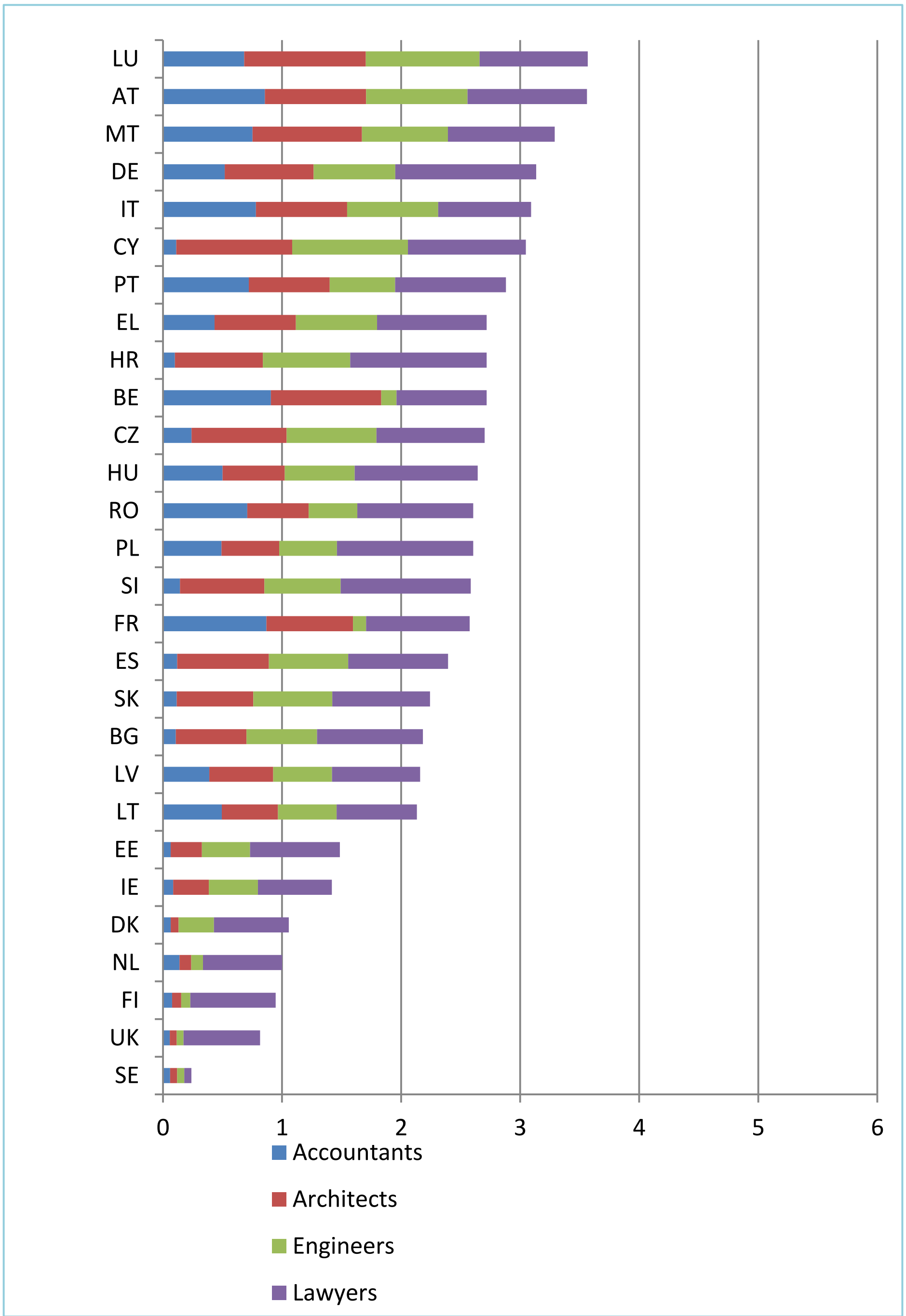
[31] M. Rojek and M. Rosior 'The effects of reforms liberalising professional requirements in Poland', report funded by European Commission, Warsaw, 2016.

[32] The Consumer Markets Scoreboard results show consistently a strong negative correlation between the variance in Market Performance Index (MPI) registered between countries and the actual MPI scores on aggregate level.

[33] Consumer Markets Scoreboard, 12th scoreboard edition 2016, European Union (http://ec.europa.eu/consumers/consumer_evidence/consumer_scoreboards/index_en.htm).

[34] 'Business services – Assessment of barriers and their economic impact', European Commission, 2015 (http://ec.europa.eu/DocsRoom/documents/13328/attachments/1/translations).

Figure 7 – Overall restrictiveness scores per Member State (business services)



Source: 'Business services – Assessment of barriers and their economic impact', European Commission, 2015

This assessment took into account several requirements which service providers need to respect when going cross-border:

- Authorisations required from businesses to offer their services may serve public interest objectives, but must be proportionate to achieving them so as not to restrict competition unduly. Important reforms aiming to abolish authorisations or replacing them by lighter notification or declaration obligations have taken place in many Member States. Yet there is a scope for further reforms in many other Member States and sectors. The Services Directive stipulates that Member States may not duplicate requirements which are equivalent to those to which the provider was already subject in another Member State. This principle however is insufficiently applied in practice, as service providers often face the same requirements as domestic companies, irrespective of the fact that they may already have complied with equivalent or similar requirements in their home country.

- Legal form and shareholding requirements are important obstacles to the freedom of establishment in the business services sector. A peer review on legal form and shareholding showed that these requirements have an impact on both primary and secondary establishment. They limit investment possibilities, reduce choices for business models and may render the creation of multi-disciplinary professional practices and secondary establishment difficult or even impossible. There is a significant diversity in legal form and shareholding requirements across Member States, showing the scope for further proportionality assessments[35].
- Companies offering professional services or construction services experience great difficulties in obtaining legally required professional indemnity insurance cover when seeking to offer their services in another Member State. In most Member States, cross-border insurance cover is not easily available for service providers from other Member States which severely restricts the ability of service providers to either provide services cross-border on a temporary basis or to establish a branch or a subsidiary in another Member State.
- There is still a lack of clarity in national legislation as to the rules that are applicable to businesses providing services cross-border on a temporary basis. This is notably the case where sectoral laws have not been amended to make a clear distinction between requirements applicable to companies seeking to establish and those seeking to provide services cross-border temporarily. As a result of the ensuing uncertainty, authorities often apply authorisation requirements intended for service providers established in a Member State also to businesses providing services cross-border. The resulting disproportionate regulatory requirements can make it de facto very difficult to provide services cross-border. This is particularly the case given that not all Points of Single Contact (PSCs) established by Member States provide information on all applicable rules and allow for the relevant procedures to be completed online.

4.2. Specific barriers in the retail sector

Retail services are key for the EU economy, representing 4.5% of total EU value added and employing 8.6% of the workforce. The sector is particularly important for youth employment with a significant representation of employees in the 15-24 age range. Over 3.5 million companies in the retail sector act as intermediaries between thousands of product suppliers and millions of consumers.

Performance, market conditions and specific barriers differ between physical and on-line retail as well as between different retail sub-sectors.

Brick-and-mortar retail is characterised by cross-border expansion of companies opening physical stores in other Member States. Retailers wanting to establish in other Member States often face regulatory restrictions. Member States impose requirements relating to the size of retail outlets or to their location which may result in market entry barriers for certain store formats or business models and may affect secondary establishment. Such restrictions can have a negative impact on market structure and dynamics[36].

In addition to establishment restrictions, retailers face operational restrictions influencing their day-to-day business activities. As regards such restrictions,

[35] For further discussion, see the European Semester thematic factsheet on regulated professions.

[36] European Commission SWD(2015) 202, 'A Single Market Strategy for Europe – Analysis and Evidence'.

there is a worrying trend in some Member States to introduce measures affecting in particular foreign retailers.

Reforms leading to a reduction of both types of restrictions have been found to increase firm entry and investment in the retail sector[37]. In addition, reducing conduct barriers and barriers to entry in services leads to increased firm-level productivity[38].

Brick and mortar shops dominate mostly in grocery retailing. Given the specificities of this sub-sector, physical presence is likely to play a relatively important role also in the future. Integration will therefore continue to happen to a large extent through establishment across borders. The respect of the free movement of goods and the freedom of establishment is crucial to enable businesses to fully reap the benefits of the Single Market in this area.

Growing at a rate of 22% a year, e-commerce provides opportunities and challenges to traditional retail. It has increased the potential market for retailers and the scope of products available to consumers.

In 2015 19.1% of companies in the retail sector sold online, against 17% for the EU economy as a whole. This share has been steadily increasing since 2010, when it stood at 11.7%. The value of online sales has more than doubled between 2010 and 2015, reaching EUR 209 billion in 2015. However e-commerce is still only a fraction of the retail market. The value of store-based sales in 2015 was over EUR 2,500 billion, 12 times the value of online sales.

E-commerce is changing the market conditions in particular for non-grocery retail. Here integration often happens through cross-border retail sales. What is needed to support this trend are regulatory frameworks friendly to the development of e-commerce which at the same time fairly address both physical and on-line retail.

Date: 22.11.2016

[37] 'The Economic Impact of Selected Structural Reform Measures in Italy, France, Spain and Portugal', Institutional paper 023, European Commission, 2016.
[38] 'Growth, jobs and integration: Services to the rescue', World Bank EU Regular Economic Report, Fall 2016 (http://pubdocs.worldbank.org/en/930531475587494592/EU-RER-3-Services-to-the-Rescue.pdf).

5. USEFUL RESOURCES

- Europa webpage on services: http://ec.europa.eu/growth/single-market/services/services-directive/
- Europa webpage on implementation of the Services Directive: https://ec.europa.eu/growth/single-market/services/services-directive/implementation_en
- Summary of economic analysis regarding the functioning of the EU Single Market for services: http://ec.europa.eu/growth/single-market/services/economic-analysis_en
- Single Market Strategy: https://ec.europa.eu/growth/single-market/strategy_en
- OECD Product Market Regulation indicator: http://www.oecd.org/eco/growth/indicatorsofproductmarketregulationhomepage.htm
- 'Growth, jobs and integration: Services to the rescue', World Bank EU Regular Economic Report, Fall 2016: http://pubdocs.worldbank.org/en/930531475587494592/EU-RER-3-Services-to-the-Rescue.pdf