
UNIT 2 ROLE OF SERVICES IN ECONOMY

Objectives

After going through this unit you should be able to:

- explain the International scenario regarding service sector and trends in service trade,
- understand how India is also becoming a service economy, employment in service sector, and the emerging national scenario on services, and
- identify key service sectors and discuss their present scenario.

Structure

- 2.1 Introduction
- 2.2 International Scenario
- 2.3 Service Sector in India
- 2.4 Analysis of Specific Service Sectors
- 2.5 Summary
- 2.6 Self Assessment Questions
- 2.7 Appendix : Service Tax in India

2.1 INTRODUCTION

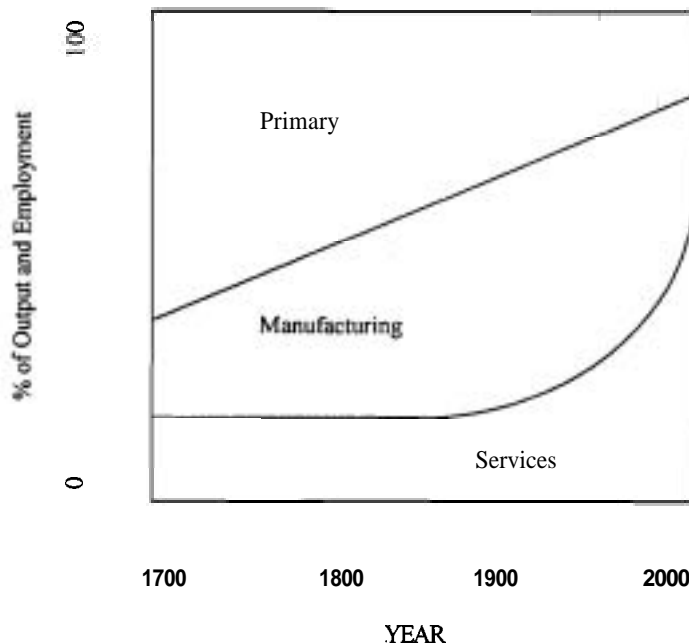
The unit begins with an introduction on how globalization has given a boost to the services sector. Thereafter, the international scenario showing the contribution of services sector, as against agriculture and industry, to the GDP of various countries across the globe, has been described. This section also covers Service sector liberalization, role of WTO and the share of services sector in the world trade. The next section of this unit details the Indian scenario and the growth in specific sectors like, tourism, financial services, telecom services, health services and information technology.

Services are extensively used by people day to day in all aspects of life. From education to entertainment, finance to fast food, travel to telephone, advertisement to amusement parks, market research to maintenance services, and retailing to recreation...and so on. Today services are increasingly being used by corporate as well as household sector. The explosive growth in this sector started in the 20th century, especially after the end of World War II. Due to large scale destruction during the war lot of economic activities, had to be carried out to bring the war torn economies back to strength. This resulted in a number of new projects fuelling the demand for financial services.

Today households as well as firms are demanding more services as well as services of increasing quality and sophistication. There are number of reasons for this growth in service sector which have been discussed in the previous unit (Unit 1). In addition to these factors, globalization has resulted in growth of service sector as well. Globalization of economies has led to an increased demand for communication, travel and information services. This has been fuelled by the rapid changes brought by new information technology, Globalization has also made increased and new demands on legal and other professional services. Also, increased specialization has led to greater reliance on specialist service providers at international level e.g., advertising and market research.

It is quite obvious from Figure 2.1 that while the role of agriculture has been reducing in the economies of industrial societies, that of service sector has been increasing at a fast pace. As the economies shift from developing to developed stage they will show more and more shift towards services.

Figure 2.1: The growing importance of service sector in industrial societies



Source J. Geruhuny and I. Miles, The New Service Economy, London, 1983.

In US economy, the fastest growing segment is services. The economies of other developed countries are also dominated by services. This trend of growing dominance of services has been so strong that some people term it as the Second Industrial Revolution.

At times it is argued that growth in services is at the expense of manufacturing sector of the economy. However, it is not true. In fact services and manufacturing are positively linked to each other. Micheal Porter in his book, 'The Competitive Advantage of Nations' identified three distinct links between manufacturing and services as explained below:

i) Buyer/supplier relationship: Many service industries have come into existence through the de-integration of service activities by manufacturing firms. An automobile manufacturer may outsource number of service activities like transportation, warehousing, marketing research, legal services, education and training of its employees, information processing etc. Service industries depend a lot on manufacturing firms for a significant share of their sales.

ii) Services tied to the sale of manufactured goods: Sale of a wide variety of manufactured goods creates demand for associated services. The sale of consumer durables require ongoing need for servicing, sale of computers leads to demand for training services and after sales services, exports of any manufactured goods would require sale of insurance, financial services and transportation services.

iii) Manufactured goods tied to the sale of services: This link is reverse of the previous one. The sale of certain services leads to demand for manufactured goods, for example sale of engineering or management consulting from a nation can lead to demand for equipment and other associated manufactured goods from that nation. Also provision of a service requires a lot of manufactured goods.

2.2 INTERNATIONAL SCENARIO

The tremendous growth of service sector has resulted in its increased importance to the world economies. As early as in 1948, US service sector contributed 54% of GDP, and with the increasing trend in the use of services it now generates 80% of the GDP.

Table 2.1: Sectoral Distribution of GDP (in %), 2002 (Estimates)

Country	G D P		
	Services	Industry	Agriculture
Denmark	71	26	3
France	71	26	3
Germany	68	31	1
India	50	25	25
South Korea	54	41.6	4.4
Russia	59.6	34.6	5.8
Nigeria	35	20	45
Switzerland	64	34	2
U.S.A	80	18	12
Taiwan	67	31	2

Source: The World Fact Book 2003, www.cia.gov

Service sector dominates the economies of other developed nations as well. As countries develop, the role of agriculture in the economy declines and that of services rises. Highly developed countries all have more than 50% of GDP and employment derived from services. A particular characteristic of the development of service employment over time is that it is less sensitive to business cycle fluctuations than other types of employment.

The service sector comprises 80% of US employment, up from 55% in 1950. Most of the absolute growth in number of jobs in US in recent years is in service sector. According to University of Michigan study, a 1/3rd cut in global barriers to trade in services would increase US annual income by \$150 billion (\$ 2,100 per American family of four). Total elimination of barriers in services would raise US annual income gain by over \$ 450 billion (\$ 6,380 per family of four). Apart from US, leaders of major global service industry associations representing the EU, Australia, Hong Kong, and Japan called for urgent progress in the multilateral liberalization of trade in services.

Trade in services also benefits developing countries greatly. The infrastructure of modern and growing economies and the gains made from liberalizing trade in services and agriculture are enhanced with open service sectors. The benefits of a modern services sector reverberate across an entire economy, touching

every product, idea and consumer. Modernizing services can help developing **countries** jump start the economic growth necessary for reducing poverty. The service sector is the fastest growing part of the economy in many developing countries, with the World Bank reporting that services account for 54 per cent of their GDP.

In the OECD countries, services account for 69% of economic output, while **agriculture** accounts for 2.1%. Even in low income countries, services account for an average of nearly 50% of GDP, with agriculture representing 23%. More than **half** of all global flows of foreign direct investment are now in the services sector. This investment is normally in the form of investment in local **companies**, often with local partners. Access to modern services (financial, professional and infrastructure services, for example) is essential to growth and development in any country. WTO commitments are **vital** to attracting this investment. While the value of trade in services is well below that of **merchandise** trade, services account for a larger portion of virtually all the world's economies; liberalization of services trade is therefore clearly in the interest of developing countries. (Source: <http://www.esf.be/>)

Service Sector — Role of WTO

WTO's 134 trade ministers met in Seattle Summit (1999). The broad objective of ~~the~~ summit was to expand private markets by removing barriers to the global movement of goods, services, and capital, with a **major** focus on public services. The WTO hopes to open the public **funding** streams which pay for **public** services for commercial exploitation. US and European governments use the WTO to promote the commercial interests of their transnational corporations, which they see as the source of economic prosperity.

As profits in manufacturing industry are falling, the corporate lobby is targeting the **proportion** of gross domestic product that governments spend on public **services**. In many European countries, governments are spending more than 15 **per** cent of GDP, in health and education alone. The WTO is devising the **international** laws and regulatory **frameworks** which will enable to open up public funding pools and public services to the market. For example, The General Agreement on Trade in Services (GATS) opens up service provision, like **education** and health care, to direct foreign competition and ownership.

In addition to GATS, the WTO has two other devices crucial to opening up public services and their funding pools.

I. Procurement Reform

WTO devised it to supply the legal and regulatory framework within which public bodies contract for goods, services, and investment **funds**. Procurement reform is a primary mechanism for opening up public services to international competition. European Commission proposals focus to unlock 'new potential markets' by extending private firms' involvement with public services and by creating contracting rules to ensure 'acceptable returns for investors'.

2. Disputes Settlement Procedure

The WTO disputes settlement procedure allows one member state to challenge the **domestic** laws of another and provides a mechanism for changing the ways in which governments regulate and subsidize public services. The US is **committed** to making mandatory a disputes system which outlaws subsidies and regulations which are not market-friendly.

The next unit of this block discusses the issues related to international trade in **services**, the WTO, and India in detail.

Leading Exporters and Importers in commercial services

Besides the US most of the West European countries as well as Mediterranean countries are net exporters of services. Germany, Japan,, most of the South East Asian countries, and Canada are net importers. The Third World countries are net service importers too. As per 1999 figure India ranked 25th in exports of commercial services valued at U.S.\$ 13.9 billion and ranked 21st in imports, valued at U.S.\$ 17.2 billion. Table 2.2 and Table 2.3 give details of international trade in services. You may visit the WTO website to find out further details on the regional shares in world trade in services.

Table 2.2: World exports of commercial services by category, 2002

(Billion dollars and percentage)

	Value	Share		Annual percentage change			
	2002	1995	2002	1995-00	2000	2001	2002
All commercial services	1570	100.0	100.0	4	6	0	6
Transportation	350	25.2	22.3	3	7	-1	4
Travel	480	33.7	30.6	3	4	-2	4
Other commercial services	740	41.1	47.0	6	7	2	9

Source: WTO

Table 2.3: Leading exporters and importers of other commercial services, 2002

(\$ bn and percentage)

	Value	Share in world exports/imports		Annual percentage change			
	2002	1995	2002	1995-00	2000	2001	2002
Exporters							
United States	141.2	16.0	19.1	11	5	4	6
United Kingdom	84.1	8.2	11.4	13	5	-1	15
Germany	54.7	7.7	7.4	3	-3	4	20
Japan	37.4	7.8	5.1	1	16	-8	3
France	34.3	7.2	4.6	-3	1	2	9
Netherlands	28.7	4.1	3.9	1	-3	21	11
Ireland	23.4	...	3.2	...	...	...	23
Italy	23.4	4.4	3.2	-2	-5	20	2
Hong Kong, China	21.1	2.5	2.9	10	17	0	5
Belgium	19.8	...	2.7	...	...	...	...
Spain	19.0	1.7	2.6	12	8	15	15
Canada	18.7	2.5	2.5	11	9	-2	-5
India	18.1	0.5	2.4	41	38	28	12
Austria	17.8	3.0	2.4	3	8	6	0
Singapore	17.2	3.5	2.3	-1	14	2	6
Above 15	560.0	...	75.7	...	...	...	...
Importers							
United States	86.2	8.5	12.5	13	12	8	11
Germany	65.3	10.6	9.5	5	-2	8	-1

Japan	48.4	10.6	7.0	0	-4	-1	1
United Kingdom	34.9	4.4	5.1	10	8	-4	8
Ireland	34.8	...	5.1	...	...	...	14
Italy	30.9	5.7	4.5	0	1	14	5
France	30.6	5.9	4.4	-2	-6	10	16
Netherlands	30.0	4.2	4.3	5	7	10	9
Spain	21.7	2.4	3.2	10	2	10	14
Austria	21.4	2.9	3.1	6	5	5	12
Canada	21.0	3.2	3.1	8	6	2	-4
China	17.1	2.5	2.5	2	1	12	24
Belgium	17.0	...	2.5	...	...	...	...
Korea, Republic of	15.4	2.0	2.2	10	26	-6	9
Sweden	12.4	1.5	1.8	11	7	6	0
Above 15	485.0	...	70.7	...	...	...	...

Source: WTO

The composition of service exports is very different from country to country. Michael Porter, in his work "The Competitive Advantages of Nations" has suggested that nations exhibit strikingly different patterns of national competitive advantages in services as they do in manufactured goods. Table 2.4 shows pattern of international leadership in different service industries.

Table 2.4: Estimated leading positions of National Competitive Advantage in International Service Industries

Country	Leading Position in Industry
USA	Fast Food, Education and Training, Health Care Services and Hospital Management, Hotels, Car. Rental, Accounting, Advertising, Commercial Banking, Money Management, Information, Trading, Entertainment
U.K.	Specialty Stores, Auctioneering, Advertising, Trading, Money Management
Switzerland	Trading, Commercial Banking, Money Management
Italy	Design Services
Germany	Money Management

Source: Adapted from 'The Competitive Advantage of Nations', Michael Porter, 1990, p 225.

For a greater number of developed countries services industries have grown to a level of definite competitiveness in international trade whereas their competitive advantage in merchandise has started to recede. However, for most developing countries service industries are at various stages of development ranging from low to intermediate. For most of these countries service sectors are recognized as strategic to their development and consequently, are subjected to intensive regulations. Ranging from architecture to telecommunications, financial to health services and beyond, services today are the largest and most dynamic component of both developed and developing country economies.

2.3 SERVICE SECTOR IN INDIA

The service sector is also assuming increasing importance in Indian economy. In line with the global trend, the services sector in India is growing rapidly. In 2002, India's service exports are recorded \$ 20.70 bn, as against \$ 4.60 bn in 1990, a growth of 350%.

Table 2.5: World Service Exports and India's Share

Year	Total world service exports \$ bn	India's service exports in \$ bn	India's share in world services exports
1990	807.01	4.60	0.57
1991	844.83	4.90	0.58
1992	960.79	4.90	0.51
1993	943.40	5.00	0.53
1994	1052.63	6.00	0.57
1995	1192.99	6.80	0.57
1996	1250.00	7.00	0.56
1997	1313.43	8.80	0.67
1998	1321.43	11.10	0.84
1999	1333.33	13.20	0.99
2000	1435.00	17.60	1.20
2001	1460.00	20.40	1.40
2002	1540.00	20.70	1.30

Source: WTO

The share of services in the country's GDP was 56.1% in 2002-03 (RE), up from the 51.5% recorded in 1998-99 and 36% in 1980-81. In contrast, the industrial sector's share in GDP has declined from 25.38 per cent to 21.8 per cent in 1990-91 and 2002-03 respectively. The agricultural sector's share has fallen from 30.93 per cent to 22.1 per cent in the respective years. The growth in the services sector has averaged 8.5 per cent during the period 1994-2000. Dr. Manmohan Singh, the then Union Finance Minister, in his budget speech for the year 1994-95 introduced the new concept of Service Tax. The number of services being taxed has increased from 3 in 1994-95 to 51 in 2002-03. The corresponding increase in revenues from services tax has been from Rs. 410 crores to 4,125 crores. The details of service tax in India have been given in Appendix at the end of this unit.

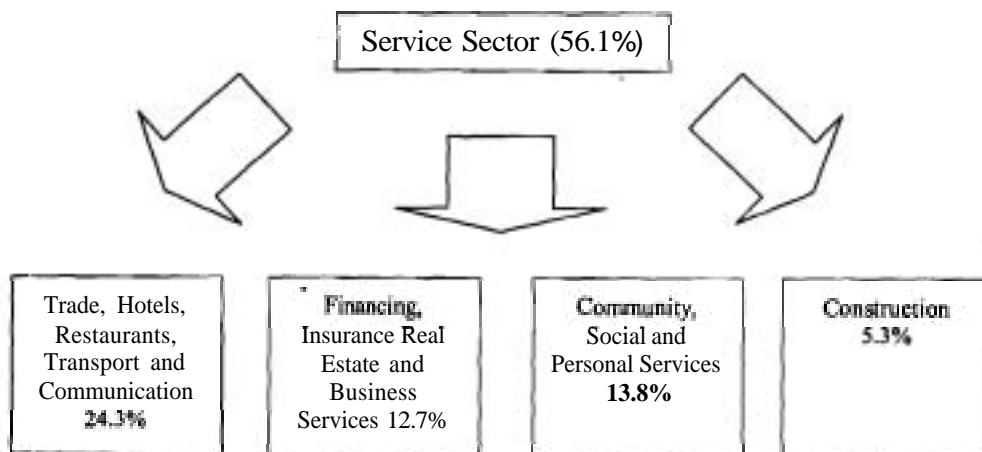
The rise in the service sector's share in GDP marks a structural shift in the Indian economy and takes it closer to the fundamentals of a developed economy. If the service sector bypasses the industrial sector, economic growth can be distorted. Service sector growth must be supported by proportionate growth of the industrial sector; otherwise the service sector growth will not be sustainable.

It is true that, in India, the service sector's contribution in GDP has sharply risen and that of industry has fallen. But, it is equally true that the industrial sector too has grown, and grown quite impressively through the 1990s (except in 1998-99). Three times between 1993-94 and 1998-99, industry surpassed the

growth rate of GDP. Thus, the service sector has grown at a higher rate than industry which too has grown more or less in tandem. The rise of the service sector therefore does not distort the economy.

The service sector is further subdivided into several groupings. Figure 2.2 gives the major groupings and their relative share in Indian economy.

Figure 2.2: Service Share by Sub-sectors
% of GDP, 2002-03 (Revised Estimates)



Source: RBI Annual Report 2002-03

Employment in Indian Service Sector

Exhibit 2.1

Services Sector : The growth Engine

Indians eat out more than ever. They take their clothes to dry cleaners, their cars to mechanics, their dogs to veterinarians. They go to beauty salons for hair cuts. For home they hire maids, gardeners, plumbers, electricians, interior decorators and architects. Outside the home, school teachers, police officers and public servants contribute to their daily lives. Lawyers, accountants, stock brokers and insurance agents help keep finances and personal affairs in order. To maintain their health and well being they turn to doctors, nurses and dentists. All this – and more – is India's service economy.

One in every two Indians earns his livelihood by providing services. An INDIA TODAY – ORG MARG poll shows that a majority of middle class families want their children to work in the services sector.

Source: Rohit Saran, Growth Engine, India Today, February 19, 2001

The importance of service sector in Indian economy can be further gauged by the fact that the majority of new employment in the organized sector has come in the service sector only. According to economic survey, from 1993-94 to 1999-2000, the financial, insurance, real estate and business services sector, employment increased to over 46 lakh from 33 lakhs in this period. In the hotel and restaurant sector employment increased to 3.75 crore from 2.68 crore and in the transport, storage and communication services sector, it increased to 1.36 crore from 98 lakh. India is a signatory to the General Agreement on Trade in Services, and is actively engaged in seeking full opportunities for free movement of "natural persons" on a temporary basis as non-residents across borders to enable it to supply services globally. India should explore all possibilities to export services which might solve its economic problems, including unemployment and poverty.

Table 2.6: Employment in organized sector by industry division

(Figure in '000)

For the year ending ~ a r c B1,	2001	1991	1981	1971
Total	27790	26734	22879	17473
Agriculture etc.	1433	1447	1321	1074
Mining and quarrying	954	1099	948	586
Manufacturing	6443	6333	6047	4761
Electricity, gas and water etc	987	945	718	481
Construction	1138	1222	1161	1019
Services	16835	15689	12684	9552

Source: Statistical Outline of India, 2003-04, Tata Services Limited p.167

Table 2.6 gives statistics of employment in organized sector in India. The higher growth of employment in service sector is partly because with the growth of economy and technological developments, a smaller proportion of work force is needed by the manufacturing sector. Total employment in the organized sector in the last 30 years has increased by around 59%, the increase in employment in service sector in the corresponding period has been around 76%. With the changing pattern of Indian economy, a shift in employment pattern is bound to happen.

2.4 ANALYSIS OF SPECIFIC SERVICE SECTORS

The fact that the service sector now accounts for more than half the **GDP** probably marks a watershed in the evolution of the Indian economy. India's high capabilities in Information Technology, and its booming IT software exports which now account for 2% of the **GDP**, are well known. India's health services, manned by highly qualified and experienced personnel, super-specialty hospitals specializing in both modern and traditional Indian medical systems like **Ayurveda**, Unani, and nature-cure supported by state-of-the-art equipment, are attracting patients from across the world, and constitute a significant segment of India's services sector.

Education is another field which is not only a huge segment of the services sector within the country, but also a foreign exchange earner by way of **NRIs** and foreign students enrolled in major medical, technological and other institutions in India, and also export of manpower even to the western world.

The entertainment industry, particularly films and TV, which happen to be among the fastest growing in the world. Indian films are popular across West Asia, Afghanistan, Central Asia, Russia and in South East Asia and are now penetrating the **Western** world. India, the second largest scientific and technical manpower in the world, has been providing varied consultancy and other services to the world.

There is immense scope for India to undertake project and management consultancy, repair and maintenance work pre-publishing services, and **R&D** in various disciplines, and interested parties from across the world are welcome to tap these and other capabilities available in abundance in the country. The tourism industry in the country is well equipped, and also fast growing to offer

tounsts with diverse interests and means, all the services needed to make **their** visit memorable. India, as a subcontinent with varied geographical, climatic, ethnic, cultural, religious and social strands intertwined, India is a one-stop destination for any tourist wanting a kaleidoscopic experience of life in its entirety. We will now discuss some of the prominent service sectors in brief. **The** last two blocks of this course are devoted to **sectoral** applications of services marketing concepts discussed in the first three blocks.

Hospitality and Tourism

Tourism has become the world's largest employer and this sector is one of the world's largest economic forces with more than 200 trillion dollar yearly. This sector is today second largest foreign exchange earner for India. A record **2.3** million tourists made their way from various parts of the world to India in calendar 2003, registering a rise of 15.3 percent over 2002, while as many as 4.5 million Indians traveled abroad accounting for a rough 30 percent **growth**.

The number of government approved hotels increased from 348 in 1980 to **1,490** in 2002 bringing in a corresponding increase in number of hotel rooms available from 21,581 to 80,936. Table 2.7 gives the details of foreign tourist **arrival** in India and earnings from tourism.

Table 2.7: Foreign Tourist Arrivals and Earnings from Tourism

Year	Foreign Tourist Arrivals (Million)	Earnings (US\$ Billion)
1980	0.80	1.40
1990	1.71	1.51
1996	2.29	2.96
2001	2.54	3.04

Source: Statistical outline of India 2003-2004 , TSL, p.98

Marketing issues specific to Hospitality and Tourism services and detailed data regarding this sector will be covered in Unit 12.

Financial Services

The role of financial services in stimulating and sustaining economic growth is **well** known. A distinct feature of Indian Financial System is the dominance of public sector institutions in practically all areas like banking, term lending and **insurance**. At the end of March 2002, 97 commercial banks, 196 Regional rural **banks**, 52 scheduled urban co-operative banks and 16 scheduled state co-operative banks were operating.

One of the most important segments of the financial system is commercial banking. The saving deposits with the commercial banks have shown a steady rise **from** Rs. 101,861 crores in 1995-96 to Rs. 279,107 crores in 2001-02.

With the opening of the banking sector to the foreign competition, and liberalized regulatory norms followed by RBI, the private banks have been using **technological** advances in every sphere of banking to up the performance **levels**. With an emphasis on retail finance and growing use of new technologies, **Indian** banks have repositioned themselves as universal finance solution provider with capabilities ranging from investment banking to project financing, and **export** financing on the corporate side, and from providing loans to selling

Table 2.8: Saving Deposits with Commercial Banks (Rs. Crores)

Year	Indian Banks	Foreign Banks	Total
1995-96	99347	2514	101861
1996-97	112570	2875	115445
1997-98	136770	3194	139964
1998-99	160889	3836	164725
1999-00	187173	4727	191900
2000-01	217452	5530	222982
2001-02	272119	6988	279107

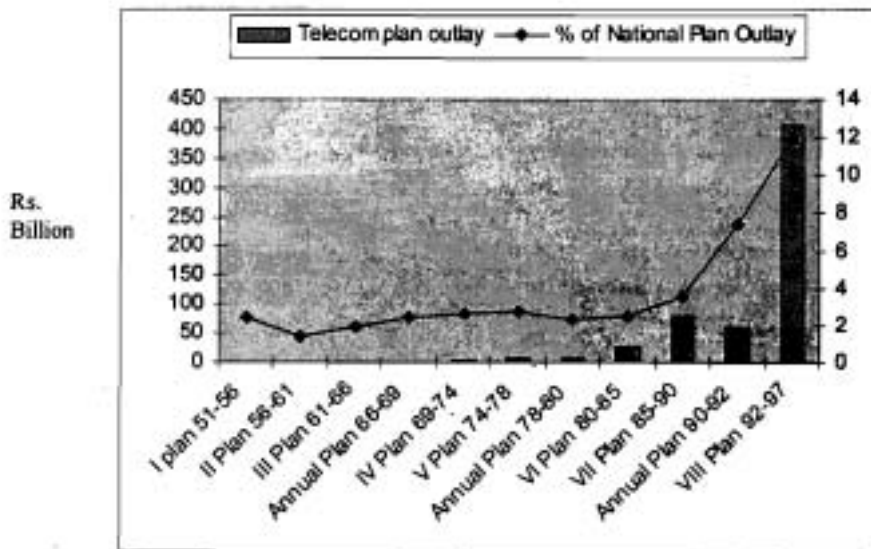
Source. India infoline.com

insurance and mutual funds on the retail side. More details about the financial services sector will be taken up in Unit 11.

Telecommunication Services

Telecommunication sector has witnessed a total transformation throughout the world in the last two decades due to rapid technological advances. Today, an advanced telecom system is a necessity for a nation's manufacturing as well as service industries. Consider for example, the growing use of telecom in services like banking, retailing, trading, health, education and transportation. At the **beginning** of the seventh five year plan in 1985, the then government decided to focus on improving the telecommunication sector and constituted the Telecommunication Board and the Department of Telecommunication (DOT) within the Ministry of Commerce to oversee operations, maintenance and development of telecom services. The emphasis on this sector increased further with liberalization initiative taken by government in the **current** decade. The plan outlay for telecom sector, which was 2.5 per cent of national plan outlay during the sixth plan, was increased substantially to 11.9 per cent in the eighth plan amounting to a whopping Rs. 406 billion. The outlays on communication (including IT) during tenth plan was Rs. 990 billion.

Figure 2.3: Investment in Telecom in Plan Periods



The number of fixed lines has increased from 5.8 million in 1991-92 to 42.58 million (Fixed including WLL-F) in 2003-04. Mobile telephony has brought about a **revolution** in Indian telecom sector. During the year 2003-04 it witnessed a **growth** of 160% over 2002-03. The growth of fixed and mobile subscribers during 2003-2004 is shown below in Table 2.9.

Table 2.9: Fixed and Mobile Subscribers (in Million) in India

Service	March 2003	March 2004	% growth during the year
Fixed including WLL(F)	41.48	42.58	3
Mobile including Cellular and WLL(M)	13.00	33.58	160
Gross Total	54.48	76.16	40

Source: TRAI

You will study the details of telecommunication sector and the marketing issues **related** to it in Unit 17 of this course.

Health Services

According to The economic Times healthcare 2001-02 report, India's healthcare **industry** grew by 13 per cent per **annum** over the last decade and is currently growing at 17 percent annually. Presently the industry size is \$18 billion. According to the report, India can reach a size of \$ 40 billion by 2005-06. The growth is being propelled by an increasingly affluent and more consumer oriented middle class population of 100 million, who are **seeking** and willing to pay for a higher standard of healthcare. During 1990 to 1996, the middle and **higher** income group has **increased** from 14% to 20%.

Table 2.10: Health Services in India during last four decades

(Figure in '000)

	1996/97	1992	1991	1981	1971	1961
Hospitals	15.1	13.7	11.2	6.8	3.9	3.1
Hospital Beds	870	835	810	569	349	230
Doctors	484	411	394	269	151	84
Primary Health	22.4	20.7	20.4	5.7	5.1	2.6
Nurses	566	385	340	154	81	36

Source: Statistical Outline of India 2000-2001, TSL, P. 212

However, a number of changes in the last few years like more consumer awareness, increasing purchasing powers and especially setting up of corporate hospitals with huge capital investment has led to more **competition** and marketing efforts. With the growing population and other factors cited above, the health services are going to increase at a fast pace with more participation **coming** from the private sector. In Unit 13 we will be **taking** up details related to the health services sector.

IT and BPO

The Indian IT sector has proved to be the country's fastest growing **segment**, even in troubled times in the globally challenging economic environment of 2001-03. Outsourcing of IT requirements by leading global companies to Indian majors picked up pace during 2002-03, in line with worldwide trends. The software sector logged in a revenue of **Rs.47,500 crore** during 2002-03, a jump of 30% from the previous year. Similarly, offshore project revenues grew by blazing 49%. Indian companies entered in to high value segments such as system integration, package implementation, IT outsourcing, and IT consulting. The revenue contributions by the US market continued to rise on account of the large number of ITES / BPO projects getting outsourced to **India**.

The Indian ITES industry is estimated to grow to Rs. 810 bn in 2008. In India, ITES-BPO segment registered a growth of 59% to reach Rs. 113 **bn** (US \$2.3 billion). The ITES contributed 25% to the total IT Software and Service exports from India during **FY03**. Captive ITES-BPO players have almost doubled their share in Indian software exports, growing by a phenomenal 90% in last financial year. ITES-BPO segment is projected to register a growth of 54% to clock revenues of US \$ 3.6 billion during FY 2003-04. India continues to offer great value proposition for the ITES companies. "Outsourcing to India has helped companies achieve 40-50 per cent cost savings. Companies are also able to generate higher free cash flows due to reduced investments in physical infrastructure, telecom and equipment." (Source: India Infoline)

2.5 SUMMARY

This unit explained the role of services in national economies and their significance in international trade. Services are used by individual as well as corporations. All the developed economies have more than sixty percent of their GDP contributions from the service sector. As the economies develop, the role of agriculture declines and that of service rises. The world exports of commercial services was valued at U.S. \$ 1,570 billion in 2003 with **U.S.A**, U.K. Germany, Japan, France being the leading exporters while **U.S.A**, Germany, Japan, U.K. and Ireland were the leading importers. India's service export stood at U.S. \$ 20.7 billion in 2002. The share of services in India's GDP is more than half and the growth in employment in organized sector has been greater in service sector. The unit also gave you brief details of hospitality and tourism, financial services, telecommunication services, health services and IT sector.

2.6 SELF ASSESSMENT QUESTIONS

1. Discuss the international scenario of role played by services sector in national economies. Do you feel India is following the trend displayed by developed economies in this regard?
2. Explain the trends in international trade in services and identify the key exporting and importing nations?
3. Select any three major service industries in India and explain the trends of growth in them.

SERVICE TAX IN INDIA*

1. INTRODUCTION OF SERVICE TAX IN INDIA

Dr. Manmohan Singh, the then Union Finance Minister, in his Budget speech for the year 1994-95 introduced the new concept of Service Tax and stated that "There is no sound reason for exempting services from taxation, therefore, I propose to make a modest effort in this direction by imposing a tax on services of telephones, non-life insurance and stock brokers."

Service Tax had been levied on the recommendations made in early 1990's by the Tax Reforms Committee headed by Dr. Raja Chelliah. The Committee also recommended charging of tax on services such as advertising, insurance, share **broking** and telecom etc. to begin with on the pattern of advanced economies. The basic objective of Service Tax is broadening the tax base, augmentation of revenue and larger participation of citizens in the economic development of the **nation**.

Bringing services under taxation is not simple as the services are intangible and are provided by large groups of organized as well as unorganized service providers including retailers who are scattered across the country. Further, there are several services, which are of intermediate nature. The low **level** of education of service providers also poses difficulties to both-tax administration and assessees. As stated earlier, service tax was introduced in India for the first time in 1994.

The Finance Acts of 1996, 1997, 1998, 2001, 2002 and 2003 added more services to tax net by way of amendments to Finance Act, 1994. As of 2003, total number of services on which Service Tax is levied has gone **upto** 58 despite withdrawal of certain Services from the tax net or grant of exemptions (Goods Transport Operators, Outdoor Caterers, **Pandal** and Shamiana Contractors, and Mechanized Slaughter Houses).

2. SERVICES COVERED UNDER SERVICE TAX

The provisions relating to Service Tax were brought into force with effect from 1st July 1994. It extends to whole of India except the state of **Jammu & Kashmir**. The services, brought under the tax net in the year 1994-95, are as **below**:

1. Telephone
2. Stockbroker
3. General Insurance

The Finance Act (2) 1996 enlarged the scope of levy of Service Tax covering three more services, viz.,

4. Advertising agencies
5. Courier agencies
6. Radio pager services.

But tax on these services was made applicable from 1st November, 1996.

The Finance Acts of 1997 and 1998 further extended the scope of service tax to cover a larger number of services rendered by the following service providers, from the dates indicated against each of them.

7. Consulting engineers (7th July, 1997)

* www.servicetax.gov.in (part of CBEC website)

8. Custom house agents (15th June, 1997)
9. Steamer agents (15th June, 1997)
10. 'Clearing and forwarding agents (16th July, 1997)
11. Air travel agents — (1st July, 1997)
12. Tour operators (exempted upto 31.3.2000
Notification No.52/98,
8th July, 1998, reintroduced w.e.f.
1.4.2000)
13. Rent-a-Cab Operators (exempted upto 31.3.2000 *Vide*
Notification No.3/99 Dt. 28.2.99,
reintroduced w.e.f. 1.4.2000)
14. Manpower recruitment Agency (1st July, 1997)
15. Mandap Keepers (1st July, 1997)

The services provided by goods transport operators, outdoor caterers and **pandal shamiana** contractors were brought under the **tax** net in the budget 1997-98, but abolished *vide* Notification No.49/98, 2nd June, 1998.

The Service Tax is leviable on the 'gross amount' charged by the service provider from the client, from the dates as notified and indicated above.

Government of India has notified imposition of service Tax on twelve new services in 1998-99 union Budget. These services listed below were notified on 7th October, 1998 and were subjected to levy of Service Tax w.e.f. 16th October, 1998.

16. Architects
17. Interior Decorators
18. Management Consultants
19. Practicing Chartered Accountants
20. Practicing Company Secretaries
21. Practicing Cost Accountants
22. Real Estates **Agents/Consultants**
23. Credit Rating Agencies
24. Private Security Agencies
25. Market Research Agencies
26. Underwriters Agencies

In case of mechanized slaughter houses, since exempted, vide Notification No.58/98 dtd. 07.10.1998, the rate of Service Tax was used to be a specific rate based on per animal slaughtered. In the Finance Act'2001, the levy of service tax has been extended to 14 more services, which are listed below. This levy is effective from 16.07.2001.

27. Scientific and technical **consultancy services**
28. Photography
29. Convention
30. Telegraph
31. Telex
32. Facsimile (fax)
33. Online information and database access or retrieval

34. Video-tape production
35. Sound recording
36. Broadcasting
37. Insurance auxiliary activity
38. Banking and other financial services
39. Port
40. Authorised Service Stations
41. Leased circuits Services

In the Budget **2002-2003**, **10** more services have been added to the tax net which are listed below. This levy is effective **from 16.08.2002**.

42. Auxiliary services to life insurance
43. Cargo handling
44. Storage and warehousing services
45. Event Management
46. Cable operators
47. Beauty parlours
48. Health and fitness centres
49. Fashion designer
50. Rail travel agents.
51. Dry cleaning services.

and these services have been notified on **1-8-2002** and were subject to levy of Service Tax **w.e.f. 16-8-2002**.

In the Budget **2003-04** seven more services along with extension to three existing services have been added to the tax net which are listed below. The levy of service tax on these services is effective from 1st July, 2003.

1. Commercial vocational institute, coaching centres and private tutorials
2. Technical testing and analysis (excluding health and diagnostic testing) technical inspection and certification service.
3. Maintenance and repair services
4. Commission and Installation Services
5. Business auxiliary services, namely business promotion and Support services (excluding on **information** technology services)
6. Internet **café**
7. Franchise Services

The extension to following three service was given in the Budget **2003-04** as aforesaid.

1. Foreign Exchange broking **services**
- i1. **Maxicab** repair services
3. Minor ports (other than major ports)

The rate of Service Tax has also been increased **from 5% to 8%** on all the **taxable** services **w.e.f. 14.5.2003**.

Service Tax is administered by the Central Excise Commissionerates working under the Central Board of Excise and Customs, Department of Revenue,

Ministry of Finance, Government of India. The unique feature of Service Tax is reliance on collection of tax, primarily through voluntary compliance.

3. SERVICE TAX REVENUE

The Service Tax collections have shown a steady rise since its inception in 1994. They have grown almost 10 folds since 1994-95 i.e. Rs. 410 crores (1994-95) to Rs. 4125 crores (2002-03).

The revenue and assessee statistics from the year 1994-95 to 2002-03 are shown in Table 1.

Table 1

Financial year	Revenue Rs. Crores	% Growth	No. of Services taxed	No. of assessees	% Growth
1994-95	410	Base year	3	3,943	Base year
1995-96	846	101	3	4,866	19
1996-97	1022	24	6	13,982	187
1997-98	1515	49	18	45,991	228
1998-99	1787	18	30	1,07,479	133
1999-00	2072	16	27	1,15,495	7.45
2000-01	2540	23	26	1,22,326	5.91
2001-02	3305	26	41	1,87,577	53
2002-03	4125	25	51	2,32,048	24

Source: www.servicetax.gov.in (Part of CBEC website).