Working Paper No. 1/2016-DEA

सत्यमेव जयते

INDIA’S SERVICES SECTOR: PERFORMANCE, SOME ISSUES AND SUGGESTIONS

Dr. H.A.C. Prasad

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S.S.Singh

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Department of Economic Affairs
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Disclaimer and Acknowledgements

The views expressed in this paper are those of the authors and do not necessarily reflect the views of the Ministry of Finance or Government of India.

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EXECUTIVE SUMMARY AND CONCLUSION

Executive Summary and Conclusion

Executive Summary

This paper examines the performance of India's services sector; the recent policy reforms in some important services sectors; issues and suggestions in services sector and in particular the four important services sectors, namely, tourism, shipping & port services, IT including software and superspeciality healthcare including medical tourism.

India's Services Sector Performance:

The performance of India's services sector has been mixed. While services growth was good at 10.3 per cent in 2014-15 and estimated to grow at a marginally lower rate of 9.2 per cent in 2015-16, there was a major slowdown on the export front eroding the cushion provided by net services to trade balance. In the first half of 2015-16, services export growth, import growth and net services growth were 0.7 per cent, 4.2 per cent and (-) 3.1 per cent respectively. Internationally also, services trade performance has been dismal with services export and import growths moving to negative territory in Q_1 and Q_2 of 2015 for World and many services trading countries, as in the aftermath of global financial crisis.

Sector-wise performance of services exports shows that business and software services exports had a reasonably high growth of 6.3 per cent and 5.8 per cent respectively in H1 2015-16, while travel (4.1 per cent) and financial services (2.0 per cent) have positive growth rates. But transportation (-17.0 per cent) has negative growth rate reflecting the world trade and growth situation.

India's IT-BPM services sector export growth is estimated at 10.2 per cent for 2015-16. But India's tourism sector growth decelerated with Foreign Tourist Arrival (FTA) growth at 4.4 per cent and Foreign Exchange Earnings (FEE) growth at -2.8 per cent in 2015. The Baltic Dry Index which is a freight index and a good proxy for the robustness of trade and also an indicator or shipping services, which had fallen from a peak of 11793 on 20th May 2008 to a low of 663 on December 8, 2008 has fallen to the lowest level of 297 on 5 February 2016 which is even lower than that in Dec 8, 2008. In the case of major ports, while capacity addition has been increasing since 2011-12, capacity utilization has been falling.

Recent Policy Reforms:

Recently, the Government has undertaken FDI related reforms in many services sectors. Policy reforms were also undertaken in some of the major service sectors like tourism and ports and IT including software. In the tourism sector, e-tourist visa (eTV) facility has been extended to a total of 113 countries and at 16 airports.

In shipping sector, recognizing the need to encourage the growth of Indian tonnage, several policy initiatives were taken which include allowing Indian shipping companies to acquire ships abroad and flag them in the country of their convenience, allowing access to cheaper finance abroad; exemption from customs and central excise duty leviable on bunker fuels used in Indian flag containers for transportation of export and import items and on empty container between two or more ports in India; and elimination of registration requirement of ship repair units (SRUs) with the Director General of Shipping.

In the Maritime Agenda, a target of 3130 million tonnes (MT) port capacity has been set for the year 2020 with around Rs. 2,96,000 crore investment. More than 50 per cent of this capacity is to be created in the non-major ports. FDI up to 100 per cent under automatic route is permitted for construction and maintenance of ports. In 2013-14, 16 public private partnership (PPP) projects were awarded at an estimated cost of Rs. 18,640.8 crore for capacity addition of 159.7 MT in the major ports comprising construction of berths and terminals and mechanization of existing berths. Other initiatives in the Port Sector include the Sagarmala Project, improving port connectivity, a new scheme for coastal berths, incentives to green major ports, green channel clearance of coastal cargo, setting up 2 new major ports and delegation of powers to major ports.

In the case of IT sector, its cross-sectoral impact is critical for India's growth and development. The Government has recognised its potential, and the Information Technology sector is undoubtedly a key pillar in various flagship initiatives like Digital India, Make in India, Skill India, and Start-up India.

Issues and Suggestions

General: Some general issues common to all services include the following. Firstly, there is relatively higher appreciation of the Real Effective Exchange Rate (REER) for India compared to China and the high depreciation in many countries like Brazil, Malaysia, Mexico, S. Africa and Thailand which affects the export competitiveness of India in both goods and services. Secondly, domestic regulations and trade restrictiveness are pointers to our policy responses. The score of OECD's Services Trade Restrictiveness Index (STRI) is above average in 21 out of 22 sectors for India. The least restricted sectors are road transport (establishment only), storage and warehousing (logistics) and freight forwarding (logistics), while the most restricted sectors are rail freight transport, legal services and accounting services. With the recent reforms related to Railways sector, the STRI scores are likely to change further. Thirdly, the Mega Free Trade Agreements (FTAs) like the Trans-Pacific Partnership (TPP), ASEAN Economic Community (AEC), the proposed Trans-Atlantic Trade and Investment Partnership (TTIP) between US and EU are a new challenge for India both in merchandise trade and services trade. These mega FTAs, erode existing preferences for Indian products in established traditional markets benefiting the partners to these agreements and also lead to the development of a rules architecture which will place greater burden of compliance on India's manufacturing and services standards for access to these markets. All these have happened when India's own FTAs with different countries benefit its partners more affecting India's domestic sector, particularly, the agricultural sector. Fourthly, there is plenty of scope for Disinvestment in many services PSUs both under Central and State Governments. Fifthly, there are credit related issues like need for collateral free soft loans for services and the need for start-up capital which has been recognized by the Government which has unveiled an action plan recently. Sixthly, there are some tax, trade policy and investment related issues, like the condition of payment in foreign exchange for Domestic Tariff Area (DTA) sales; insistence on environmental clearance by customs department for re-imports for repair service, refurnishing, reconditioning, return samples and re-imports for R&D purpose; and the issue of speeding up passing of Bankruptcy laws which can speed up closure of failed firms and starting of new firms. Seventhly, there is the need for designating a department as nodal department for services which can deal with all issues related to services on a regular basis and also coordinate with all concerned departments and ministries at the central and state levels.

Sector specific Issues

Tourism: Some important issues in Tourism Sector are the following.

Need for improvements in the e-tourist visa and ordinary visa which includes the need to extend eTV visa window to 180 days instead of 30 days before the tour at present; need for multiple entry eTV instead of single entry eTV at present; extension of duration of stay to 60 days under eTV instead of the 30 days at present; making available biometric facility in major ports to help cruise passengers get eTV; need for proper display at eTV counters; increasing the counters for eTV tourists to avoid delays; extending eTV facility for medical tourists; and streamlining the biometric process in overseas missions by having more biometric locations.

Tax Issues which include issues like the place of provision clause in service tax resulting in tourism services not being treated as export of service and being taxed; need for lower GST for tourism related services as in many OECD countries; and import duty exemption for equipment and accessories for adventure tourism.

Finance and Investment related issues which include positioning India as a convention centre by creating a global fund; examining the possibility of giving special incentives like tax free bonds and income tax exemptions on profits used in reinvestment in tourism sector; development of tourism infrastructure on PPP basis and by channelizing CSR spends into India's heritage development; support for SMEs in tourism sector with the help of venture capital funds and extending the MUDRA Yojana to SMEs in tourism sector; setting up India Haats in major cities/towns with miniature cultural India by channelizing CSR spending or under PPP mode.

Besides the above, there are other issues like the need for a national cruise strategy; making railways more tourist friendly with cleanliness & hygiene, e-booking with special quotas for foreign visitors; introducing smart cards for e-payments across all tolls in India and national permit for tourist vehicles; considering global parameters while deciding CRZ norms and organizing India tourism fairs in Indian embassies abroad.

Shipping and Port Services: Some important issues in this sector are the following:-

Need for cheaper finance and longer tenure for funds in the light of the fact that Indian ships are ageing and need to be replaced and asset prices are serendipitously low. Atleast the issue of longer tenure for loans to shipping sector could be addressed urgently. An institutional mechanism can also help shipping sector in acquiring assets at the right time.

Terms of shipment imports CIF which makes it difficult to ascertain the freight element and helps sellers to keep control over transportation and support to their own nationality or companies. Though the government's policy states that all contracts by PSUs and government controlled ships need to be on an FOB basis for imports, items like fertilisers are imported on CIF basis as foreign manufacturing companies are unwilling to sell directly to designated agencies like STC which do not pre-book. Of late, countries like Saudi Arabia sell at small discount provided India buys on CIF basis. This is to help their own transportation and needs to be examined carefully.

Other issues include the need to address the high capital costs issues and import of sub-standard machines in maintenance dredging; allowing pre-payment of ECB for shipping companies to help borrow, for purpose of fresh acquisition of a suitable asset; allowing opening of a joint ESCROW account for purchase of asset which is denied at present; making India a bunkering hub by allowing 'Nil' duty on bunkers for all segments of coastal shipping and not just for containers as is being done at present; exploring the possibility of creating an Indian Production & Indemnity (P&I) company; restoring the exemption from withholding taxes on interest payments on ECB loans taken by shipping companies; issue of refinancing through ECB funds which is not permitted at present for shipping sector; addressing port infrastructure; and examining the relatively higher port services prices in India.

IT including Software

Issues in this sector include visa issues like the impact of Grassley-Durbin Reform Bill (if passed in US Congress) on H1B visas and even L1 visas and the visa fee hikes in US; need to be competitive and focus on high end software products; need to promote our own domestic 'Apps'; comprehensive approach to start-ups and innovation which is now being done with Start-up Action Plan and Atal Innovation Mission; clarity under proposed GST given the dual levies of VAT and service tax; e-commerce taxation issue; difficulty in the getting payments for government work which is outstanding to the extent of Rs.3,000 crores and above; extending the 200 per cent weighted deduction on R&D expenditure in IT industry on the lines of R&D incentives to IT sector in UK and many other countries; extending Services Exports from India Scheme (SEIS) to IT sector in the light of proposed phasing out of SEZ benefits and phased out STPI exemptions; uniformity in exchange rate calculations for different tax calculations; addressing pending issues related to transfer pricing; streamlining exit route for STPs and need for providing relief and rehabilitation for both workers and firms in Chennai by considering measures like waiver of customs duty, tax relief etc with sunset clauses.

Healthcare Services Exports and Medical Tourism

India has a great potential for Medical Tourism with comparatively low costs for superspeciality medical care and 'no waiting time' unlike in advanced countries. However, India has been fragmented in its approach, where individual hospitals have been promoting themselves as the hospital destinations. Our Asian neighbours have taken many initiatives to promote medical tourism, some of which can be emulated by India. Some suggestion in this sector include promoting medical tourism in India's Brand India Campaign; rapid immigration clearances for medical tourists; enhanced basic infrastructure for medical tourists in airports; streamlining the medical visa process and also extending eTV to medical tourists; promoting geriatric healthcare by also leveraging on our expertise in Ayurveda, Yoga and Unani; getting international accredition for Indian hospitals; addressing the exchange risk factor for medical tourists who have to deposit foreign currency during admission in hospitals and get the refund after billing during which time exchange rates could have changed; and promoting telemedicine.

Conclusion

The services sector is like an unchartered sea with plenty of opportunities. While an attempt has been made here to see the performance and problems in some important services, the other services are equally important. A targeted policy of quickly addressing the issues in major and potential services can result in higher dividends in the form of higher services growth and services exports which in turn can help in pulling the economy to higher growth levels.

CHAPTER 1

INDIA’S SERVICES SECTOR PERFORMANCE

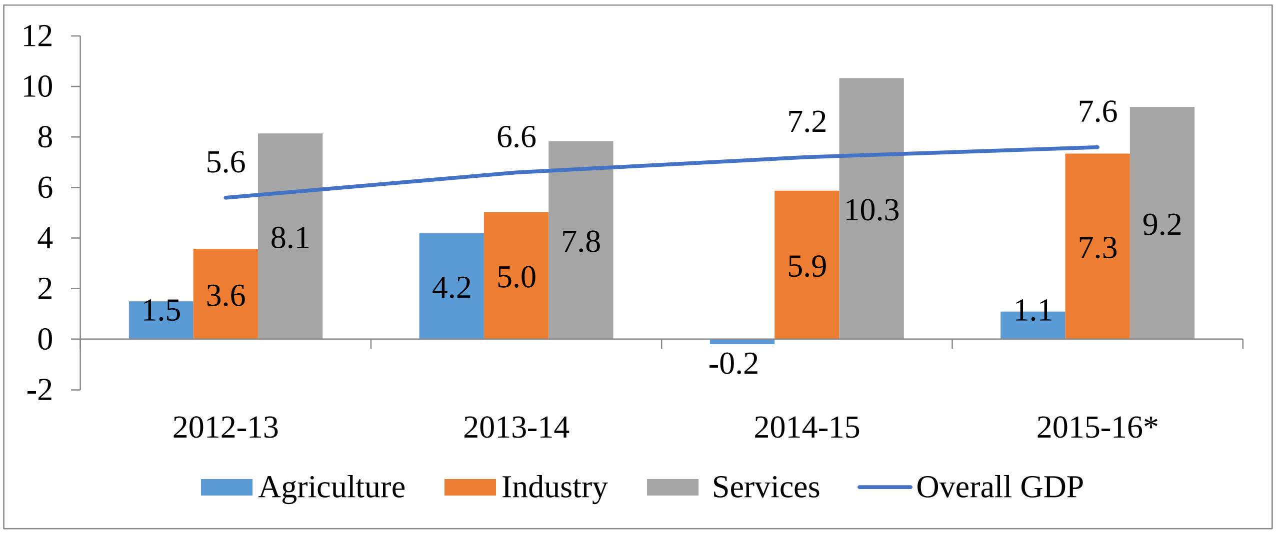
Chapter 1 - India's Services Sector Performance

India's services sector performance shows a mixed picture. While it is performing well in terms of GDP/GVA despite some slowdown, on the export front there is a major slowdown.

Services GVA

The services sector growth accelerated to 10.3 per cent in 2014-15 from 7.8 per cent in the previous year. This growth acceleration was mainly due to higher growth in services sub-sectors like 'trade, repair, hotels & restaurants' (10.7 per cent), 'financial services' (7.9 per cent), 'public administration and defence' (9.8 per cent), and 'other services' (11.4 per cent). In 2015-16, as per the advance estimates, the services sector accounting for 53.3 per cent of India's Gross Value Added (GVA) at basic prices (current prices), grew by 9.2 per cent (constant prices) marginally lower than in 2014-15. This is mainly due to the deceleration in the growth of the combined category of 'public administration, defence and other services' to 6.9 per cent from 10.7 per cent registered in 2014-15.

Figure 1: Sector-wise GVA and Overall GDP Growth at Basic Price (per cent)



Source: Based on CSO data, *Note:* * Advance Estimates

The quarterly estimates of services sector growth during 2014-15 show a fluctuating trend from Q1 to Q4. The growth rate of services sector during Q1 to Q3 of 2015-16 was at 9.0 per cent, 9.4 per cent and 9.4 per cent respectively compared to 8.6 percent, 10.7 per cent and 12.9 per cent respectively recorded in the same period of previous year. Among the major broad categories of services, the combined growth of 'trade, hotel, transport, communication and services related to broadcasting' achieved the highest growth rate at 10.1 per cent during Q3 of 2015-16 followed by 'financial, real estate & professional services' with growth rate at 9.9 per cent.

The growth prospects of services sector is promising as also indicated by some other estimates like the the Nikkei/Markit Services PMI for India which rose to 54.3 in January 2016 from 53.6 in December 2015, the highest reading since June 2014.

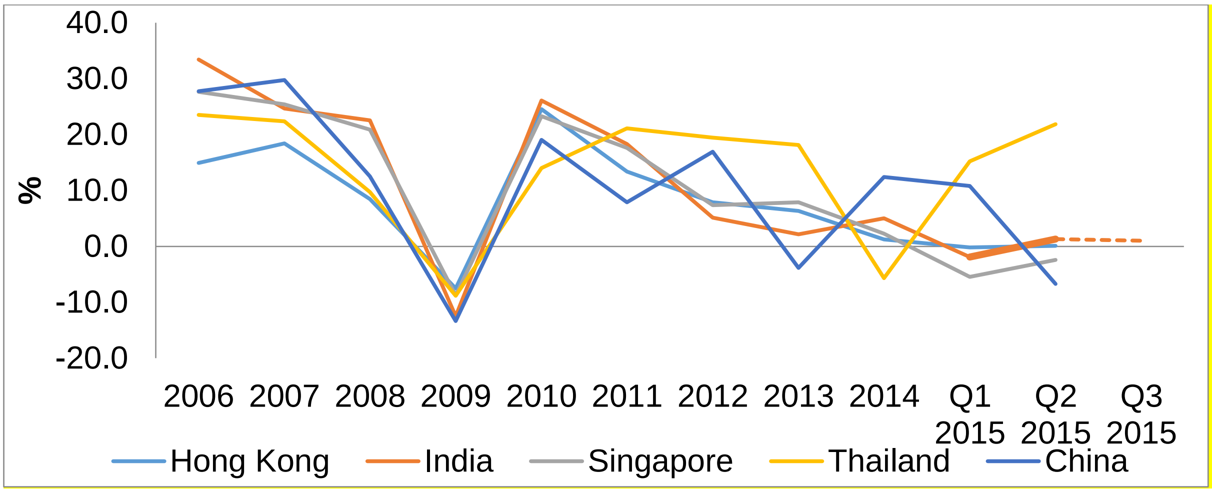
Services Trade Performance of India and World

After the negative growth in the aftermath of the global financial crisis, services export and import growths have again moved to negative territory in Q1 of 2015 for India, World and many important services trading countries as per WTO data.

Services Exports

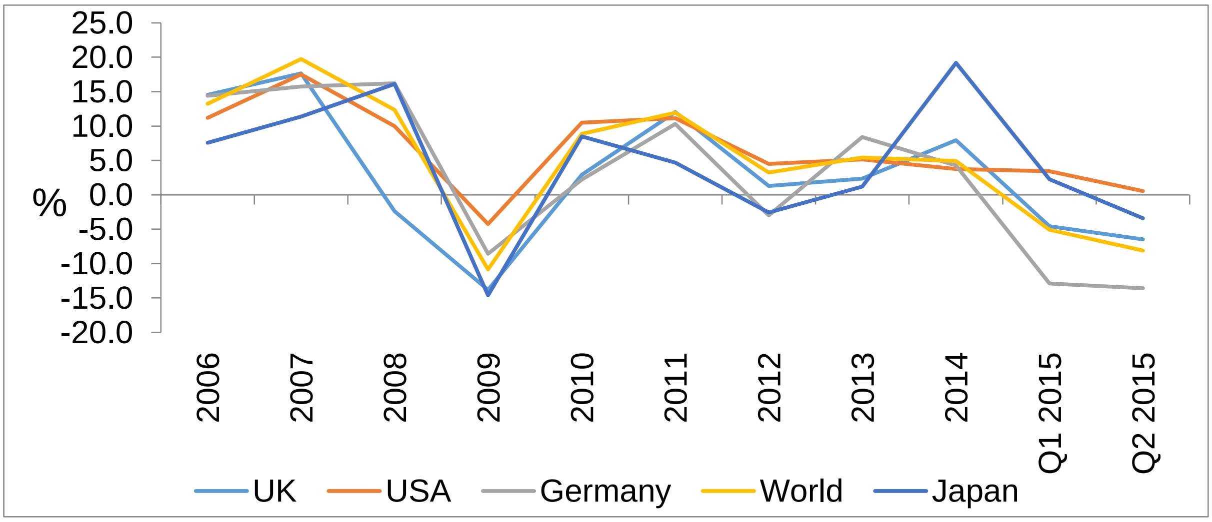
In 2009, following the global financial crisis, world services export growth had turned negative at (–) 10.9 percent. It was also negative for all major service exporters in 2009. In both Q1 and Q2 of 2015 it was negative at (-) 5.1 per cent and (-) 8.1 per cent respectively for World. It was also negative for Germany (-12.9 per cent and -13.6 per cent), Hong Kong (-0.3 per cent and 0.1 per cent), India (-1.9 per cent and 1.3 per cent), Singapore (-5.5 per cent and -2.4 per cent) and UK (-4.5 per cent and -6.5 per cent). In countries like Thailand it is positive (15.1 per cent and 21.8 per cent) due to base effect. (Figure 1 & 2).

Figure 2: Services Export Growth: India, China and South East Asian Countries



Source: Based on WTO data, Note: Dotted portion (Q3 2015) for India is based on RBI data

Figure 3: Services Export Growth: World and Some Developed Countries

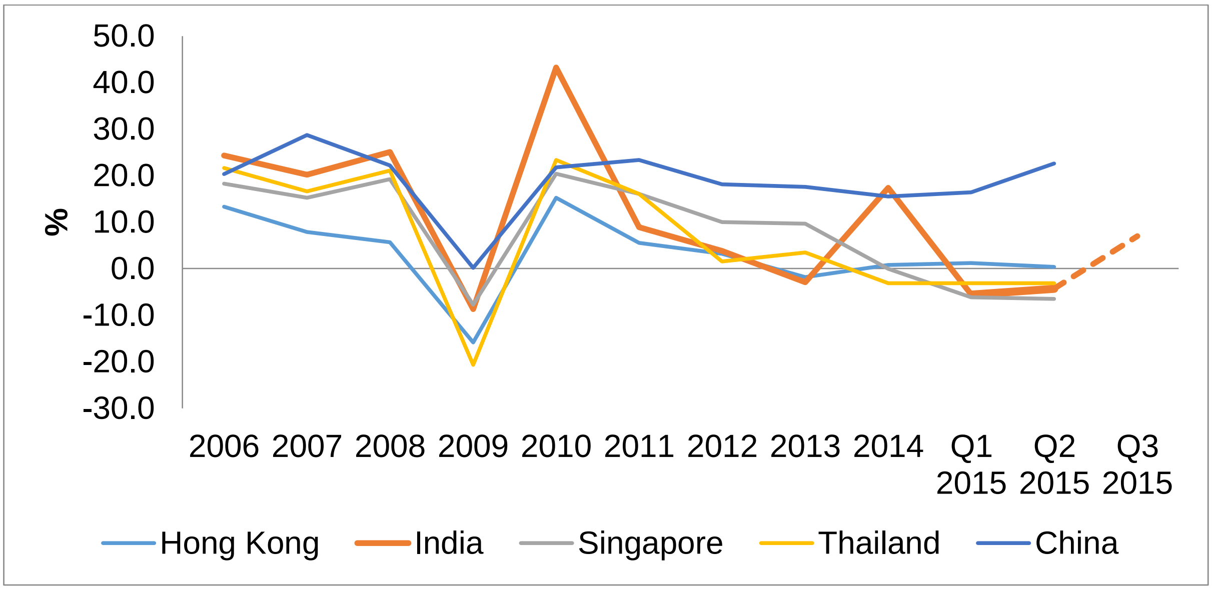


Source: Based on WTO data.

Services Imports

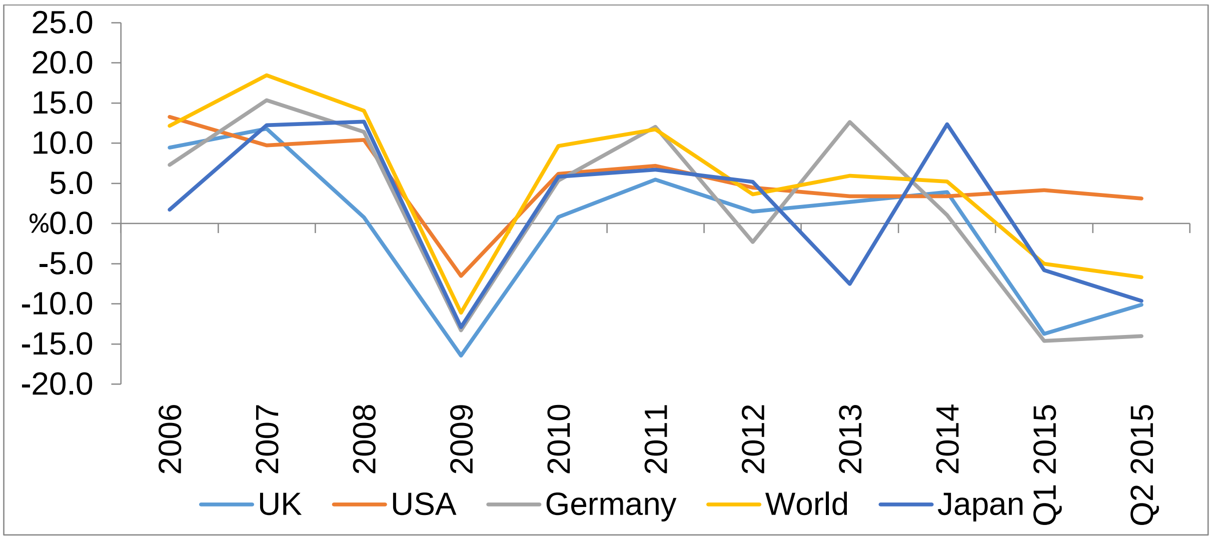
The situation is almost similar in the case of services imports. (Figure 3 & 4). However in September 2015 for India, there is a pick-up in services import growth (20.8 per cent).

Figure 4: Services Import Growth: India, China and South East Asian Countries



Source: Based on WTO data, Note: Dotted portion (Q3 2015) for India is based on RBI data.

Figure 5: Services Import Growth: World and Some Developed Countries



Source: Based on WTO data.

In comparison to services, merchandise export growth figures show a steeper fall than services export growth both in 2009 and 2015 Q1. Unlike services export growth, in the case of merchandise exports, negative growth has started since Q4 2014 in all the major trading countries except China which also shows a deceleration in export growth. Merchandise import growth figures are also almost similar except that all major countries including China have registered negative growth in Q1 2015.

India’s Trade in Services

- The tremendous rise in India’s services exports in recent years has been clearly corroborated by latest data from WTO. From US$ 16.8 bn in 2001, India’s services exports increased to US$ 155.6 bn (7.5 per cent of GDP) in 2014, making the country the eighth largest services exporter in the world.
- The increasing comparative advantage of India in the global economy, particularly in the services sector, can be seen from the fact that the share of India’s services exports in global services exports at 3.15 per cent in 2014, is nearly double the share of India’s merchandise exports in global merchandise exports at 1.7 per cent.
- After witnessing high growth during 2002-03 to 2008-09 with a CAGR of 31.2 per cent, and a pick up and good growth in 2010-11 and 2011-12 in the aftermath of the global financial crisis, export growth of services decelerated in 2012-13 to 2.4 per cent and then increased to 4.0 per cent in 2013-14. In 2014-15 services exports further decelerated to 2.6 per cent from 4 per cent in 2013-14 to US$ 155.5 billion. Services imports which grew by 1.6 per cent increased to US$ 79.7 billion resulting in net services of US$ 75.7 billion with 3.7 per cent growth. In Q1 2015-16 services exports grew by only 0.4 percent and in Q2 2015-16 by 1 per cent. In the first half of 2015-16, services export growth, import growth and net services growth were 0.7 per cent, 4.2 per cent and (-) 3.1 per cent respectively. In October 2015, services exports, services imports and net services grew by 9.9 per cent, 18.0 per cent and 2.0 per cent respectively. But in november 2015 both services exports and imports growth were negative at (-) 3.6 per cent and (-) 7.6 per cent respectively with net services growth at 0.2 per cent. Thus the cushion provided to India’s trade balance by net services is no longer there in 2015-16. (Table 1).

- Net transfers (a proxy for labour services exports) growth has however become negative in both Q1and Q2 of 2015-16. This has not happened even in the aftermath of global financial crisis of 2008. Lower oil prices and relative lower spending could be the reason for the fall in growth of remittances inflows represented by private transfers inflow at -2.3 per cent in H1 2015-16.

Table 1: Growth Rate of Services Trade

Year / Item	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	H1 2015-16	Q1 2015-16	Q2 2015	October 2015 *	November 2015*
Services Exports	33.3	28.0	22.4	17.3	-9.4	29.8	14.2	2.4	4.0	2.6	0.7	0.4	1.0	9.9	-3.6
Services Imports	24.0	28.5	16.2	1.1	15.3	34.2	-2.9	3.2	-2.8	1.6	4.2	1.6	7.0	18.0	-7.6
Net Services	**50.2**	**27.2**	**31.8**	**38.8**	**-33.2**	**22.4**	**45.4**	**1.3**	**12.4**	**3.7**	**-3.1**	**-1.0**	**-5.1**	**2.0**	**0.2**
Net Transfers	**18.8**	**21.8**	**39.5**	**6.8**	**16.2**	**2.1**	**19.5**	**0.8**	**1.9**	**0.4**	**-1.3**	**-1.8**	**-0.8**	**--**	**--**

Source: Based on RBI BoP Data, Note: * Preliminary data

Sector wise growth rate of India's services trade

Sector-wise performance of services exports (Table 2) shows that business and software services exports had a modest growth of 6.3 per cent and 5.8 per cent respectively in H1 2015-16, while Travel (4.1 per cent) and financial services (2.0 per cent) have positive growth rates. But transportation (-17.0 per cent) has negative growth rate reflecting the world trade and growth situation.

Sector wise, India's services imports show negative growth in financial, travel & transportation services in H1 2015-16, whereas in business services there is high positive growth.

Table 2: Sub-sector wise growth rate of services Exports and Imports

Year / Item	Exports Growth (per cent)							Imports Growth (per cent)						
	2011-12	2012-13	2013-14	2014-15	H1 2015-16	Q1 2015-16	Q2 2015-16	2011-12	2012-13	2013-14	2014-15	H1 2015-16	Q1 2015-16	Q2 2015-16
Travel	16.9	-2.5	-0.4	13.5	4.1	7.9	0.9	24.8	-14.1	-0.1	29.6	-1.2	0.2	-2.5
Transportation	28.0	-5.0	0.3	0.6	-17.0	-13.1	-20.9	18.0	-9.6	-0.1	9.4	-0.9	5.0	-6.6
Software Services	17.2	5.9	5.4	5.3	5.8	4.6	7.0	30.3	-42.8	88.2	5.0	6.2	30.3	-11.0
Business Services	7.7	9.8	0.1	-0.2	6.3	10.3	2.4	-3.3	13.3	-10.4	1.7	13.2	15.8	10.8
Financial Services	-8.3	-17.1	34.4	-14.9	2.0	-18.6	25.9	6.7	-42.0	25.5	-38.4	-27.1	-45.0	2.7

Source: Based on RBI Data

IT-BPM (software) export growth

NASSCOM has estimated revenue growth of IT-BPM sector excluding e-commerce and hardware at 9.2 per for 2015-16 (Table 3). Of this, export growth is estimated at 10.2 per cent. Domestic growth of IT and BPM excluding e-commerce and hardware is 8.3 per cent. If e-commerce is excluded it is 2.9 per cent and if hardware is also excluded it is 4.8 per cent. The main contributor to growth in the IT-BPM domestic sector is e-commerce contributing 75 per cent to growth in 2015-16.

Table 3: Overall Performance of the IT-BPM Sector

	Values (US$ billion)			Growth (Per cent)	
	2013-14	2014-15	2015-16^{E}	2014-15	2015-16^{E}
Total IT and BPM Revenues	**130.0**	**146.0**	**160.0**	**12.3**	**9.6**
Excluding Hardware	117.0	132.0	146.0	12.8	10.6
Excluding eCommerce	119.0	132.0	143.0	10.9	8.3
Excluding eCommerce and Hardware	106.0	119.0	130.0	12.3	9.2
Total Exports	**87.0**	**98.0**	**108.0**	**12.6**	**10.2**
Excluding Hardware	86.6	97.6	107.6	12.7	10.2
Total Domestic	**42.0**	**48.0**	**52.0**	**14.3**	**8.3**
Excluding Hardware	29.0	35.0	39.0	20.7	11.4
Excluding eCommerce	32.0	34.0	35.0	6.3	2.9
Excluding eCommerce and Hardware	19.0	21.0	22.0	10.5	4.8

Source: NASSCOM, Note: E-estimated

Tourism Sector

The United Nation's World Tourism Organization (UNWTO) report (2014) shows that international tourist arrivals reached 1.2 billion in 2015, a 4.0 per cent increase over the previous year and for 2016 the forecast is also a 4 per cent increase.

India's tourism export growth (Table 4) was in double digits in 2014 in terms of growth of foreign tourist arrivals (FTA) and nearly so in terms of foreign exchange earnings (FEE) in dollar terms. But in 2015 growth has decelerated to 4.4 per cent for FTA, and became negative at -2.8 per cent for FEE indicating not just lower growth in numbers but a fall in tourism receipts which may be due to lower spending by tourists or increase in share of low spending tourists in arrivals.

Table 4: Tourism Growth in India

Year	Value		Growth Rate	
	FTA (lakh)	FEE (US$ billion)	FTA	FEE (US$)
2012	65.8	17.7	--	--
2013	69.7	18.4	5.9	4.0
2014	76.8	20.2	10.2	9.7
2015	**80.16**	**19.7**	**4.4**	**-2.8**

Source: Based on Monthly Press releases of Ministry of Tourism, Note: FTA - Foreign Tourist Arrivals, FEE - Foreign Exchange Earnings

Shipping and Port Services

I) Shipping

Shipping is an important indicator of both commodity and services trade of any country. Around 95 per cent of India's trade by volume and 68 per cent in terms of value is transported by sea. As on 30 November 2015, India had a fleet strength of 1246 ships with gross tonnage (GT) of 10.45 million, with the public-sector Shipping Corporation of India (SCI) having the largest share of around 36 per cent.

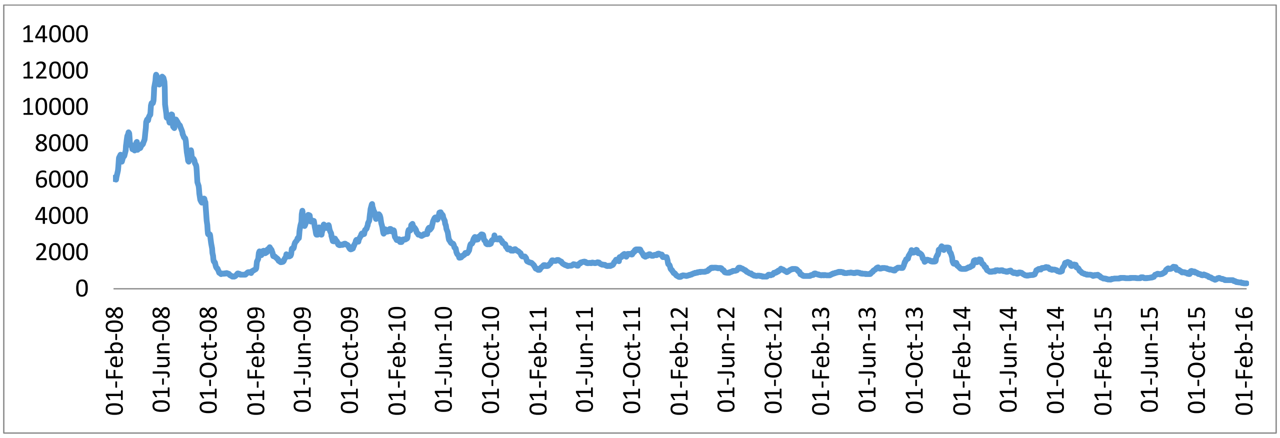
Of this, around 369 ships with 8.94 million GT cater to India's overseas trade and the rest to coastal trade. Despite having one of the largest merchant shipping fleets among developing countries, India's share in total world deadweight tonnage (DWT) is only 0.9 per cent as on 1 July 2015. As per UNCTAD, India with 11.7 million twenty-foot equivalent units of container (TEUs) and a world share of 1.7 per cent ranked 9th among developing countries in terms of container ship operations.

The shipping sector has been plagued by economic hardships since 2008. In 2014, all segments of shipping saw intermittent spikes but there was no secular uptrend in any of them. There could be further dampening of shipping freight rates as deliveries of new ships are slated in 2016.

The Baltic Dry Index which is a freight index and a good proxy for the robustness of trade and also an indicator or shipping services, had fallen from a peak of 11793 on 20th May 2008 to a low of 663 on December 8, 2008. Though it picked up in the following years, it has not really come anywhere near the earlier level. Instead, it fell to the lowest level of

290 on 10 February 2016 (which is even lower than that on Dec 8, 2008) which shows that the international trade and shipping situation is still fragile. (Figure 6).

Figure 6 : Baltic Dry Index [BDI]Close



Source: Based on data accessed from http://in.investing.com/indices/baltic-dry

II) Port Services

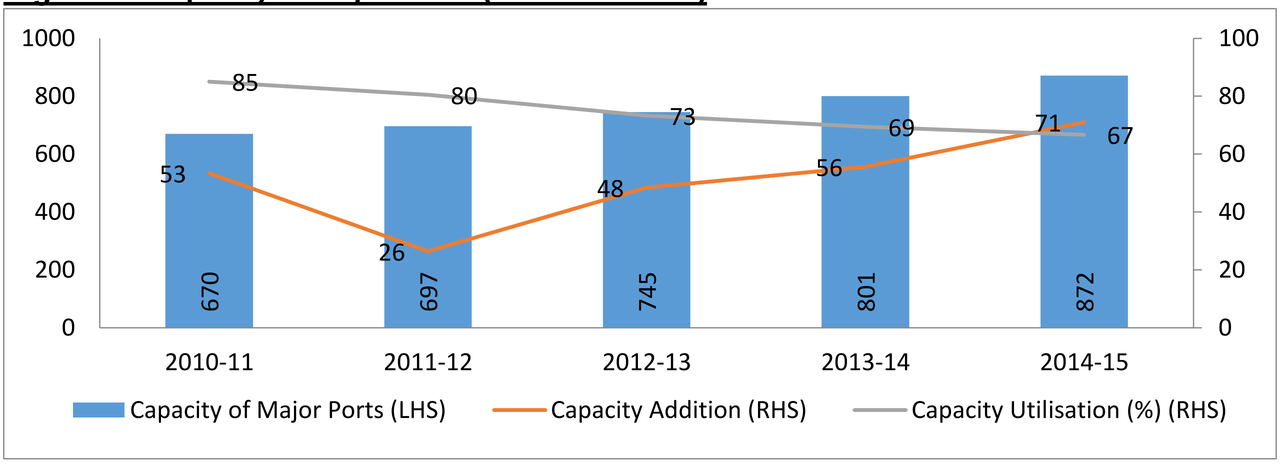
The cargo traffic of Indian ports increased by 4.5 per cent in 2013-14 and by 6.8 per cent in (April-December) 2014-15. The traffic handled in major ports grew by 4.1 per cent to 299.6 million tonnes in April-September 2015 from 287.7 million tonnes in April-September 2014 (Table 5). Capacity addition has been increasing since 2011-12, but capacity utilisation has been falling (Figure 7).

Table 5 : Cargo Handled at Indian Ports (Million Tonnes)

	Major Ports	Non-Major Ports	All Ports
2011-12	560.2	353.7	913.9
2012-13	545.8	387.9	933.8
2013-14	555.5	417.0	972.5
2014-15	581.3	471.2	1052.5
H1 2014-15*	287.7	NA	287.7
H1 2015-16*	299.6	NA	299.6

Source: Based on Indian Ports Association (IPA) and Ministry of Shipping

Figure 7: Capacity at Major Ports (Million Tonnes)



Source: Computed from Data from IPA and Ministry of Shipping

CHAPTER 2
SOME RECENT POLICY REFORMS RELATED TO SERVICES SECTOR

Chapter 2 - Some Recent Policy Reforms related to Services Sector

There are some policy reforms which apply to all or many services sectors like the FDI reforms. Recently the Government has introduced FDI related reforms and liberalisation touching upon 15 major sectors of the economy which include many of services related sectors like broadcasting sector, civil aviation, construction development sector, cash and carry wholesale trading / wholesale trading (including sourcing from MSEs), single brand retail trading, duty free shops and private sector banking.

There are also some sector specific measures. Here the measures for the three important services sectors covered in this paper are given

Tourism

One of the important policy measures in tourism sector is the easing of the visa regime through the execution of tourist visa on arrival enabled by electronic travel authorization (ETA). The Government of India launched e-Tourist Visa (eTV) facility on November 27, 2014 and this facility was further extended to 36 more countries and 7 more Indian airports (Ahmedabad, Amritsar, Gaya, Jaipur, Lucknow, Tirchy, Varanasi) from August 15, 2015. The new countries included in e-TV scheme are Andorra, Argentina, Armenia, Aruba, Belgium, Bolivia, Colombia, Cuba, East Timor, Guatemala, Hungary, Ireland, Jamaica, Malta, Malaysia, Mongolia, Monaco, Mozambique, Netherland, Panama, Peru, Poland, Portugal, Seychelles, Slovenia, Spain,St. Lucia, St Vincent & the Grenadines, Suriname, Sweden, Taiwan., Tanzania, Turks & Caicos Island, United Kingdom, Uruguay, and Venezuela. With these additions, the total count of countries under the scheme is 113 and the total number of designated airports is 16. Though the growth in total foreign tourist arrivals (FTAs) has decelerated to 4.4 per cent in 2015, a total of 4,45,300 tourists arrived on eTV as compared to 39,046 in 2014 registering a growth of 1040.4per cent . This is probably due to tourists shifting to eTV from ordinary visas. It is expected that the substantial addition of countries and airports will give a big boost to tourism industry in the country.

In the Budget 2014-15, the government announced several measures for boosting tourism like streamlining of some service tax bottlenecks and focused effort for the development of a global-scale buddhist circuit and cleaning of the Ganga along with creation of world class amenities to enhance the spiritual experience along the holy river. The following new schemes were launched pursuant to the Budget 2014-15 announcements: 1) Swadesh Darshan for integrated Development of Tourist Circuits around specific Themes. 2) National Mission on Pilgrimage Rejuvenation and Spiritual Augmentation Drive (PRASAD) to beautify and improve the amenities and infrastructure at pilgrimage centres of all faiths.

Shipping and Ports

I) Shipping

Recognizing the need to encourage the growth of Indian tonnage, several policy initiatives were taken. Some are given below.

Seafarers' taxation: In the finance bill of 2015, a major relief was given to Indian seafarers working on Indian ships while on EXIM trades; wherein the stay of Indian seafarers in Indian waters while on an Indian ship and enroute to a foreign port will be counted as days stayed abroad for purposes of calculating income tax. This benefit was given with retrospective effect of 2014-15. Being more than 182 days/year out of India, gives an Indian a tax free NRI status. With this benefit, the Government has corrected a longstanding anomaly in the tax legislation applicable to the seafarers working on Indian ships.

India Controlled Tonnage: The Director General of Shipping vide its circular No. 10 of 2014 dated July 23, 2014 permitted Indian shipping companies to directly flag their ships outside India and not through a subsidiary. Income from such vessels under the foreign flag would accrue directly in the books of the Indian company. The advantages are the following:-

- Such a facilitative regime would open doors for increasing tonnage directly under the Indian control but not necessarily Indian flag.
- Such vessels will be owned by an Indian company and will therefore be an Indian asset located outside India. Indian firms would capture revenues directly from assets and not dividend income.
- There would be no loss to the Indian exchequer since taxation flows come from the owner (residence of the taxable entity) and not flag.
- Increased employment, training slots for seafarers, access to Indian controlled ships in national emergency which is not available to ships owned under a subsidiary.

There are also additional commercial benefits of India controlled tonnage as given below:-

- As this will add to India's tonnage, Indian cargo will be able to bargain for competitive rates.
- Positive impact on Indian shipping in coastal trade as higher content of Indian trade will be retained for Indian ships and Indian companies will carry more Indian cargo on the coast.
- It will increase footprint of Indian shipping abroad as Indian companies will have the ability to cater to specialized projects/customer requirements which cannot be fulfilled currently and leads to flagging out.

Cabotage: Cabotage has been relaxed for special vessels such as RO-RO, hybrid RO-RO, RO-Pax, Pure Car Carriers, Pure Car & Truck Carriers, LNG Vessels, Over Dimensional Cargo, and Project Cargo Carriers for 5 years up to 2nd September 2020. This move protects Indian tonnage and yet ensures that tonnage which is not available in India is welcomed into India to aid growth of coastal transportation. It is important to see how many such foreign flag vessels would actually take advantage of this relaxation.

Duty free bunkers for coastal container carriage: A notification dated September 17, 2015 has extended the benefit of customs and central excise duty free bunkers to container ships carrying a mix of coastal and EXIM cargo, as also empties. Earlier, this exemption was restricted to ships carrying EXIM coastal containers only. This is a major benefit to container shipping companies in India.

Incentive for shipbuilding and ship-repair Industry: The government has recently approved incentives to promote domestic shipbuilding industry. These include financial assistance to domestic shipyards for any vessel built by them subsequent to its delivery and grant of right of first refusal for Indian shipyards for government purchases. The government has addressed the problem of inverted duty structure in ship manufacturing. Inputs used in ship manufacturing and repair have been exempted from customs and central excise duties with effect from the 24th of November, 2015. Prior to this exemption, while ships could be imported at almost negligible rates of basic customs duty (BCD) and nil rates of countervailing duty (CVD), the inputs used in ship manufacturing and repair attracted normal rates of BCD and CVD. This put the Indian shipyards, which are built for the domestic market, at a cost disadvantage. Correction of this inverted duty structure was therefore necessary.

Jal Marg Vikas Project: The Budget 2014-15, states that a project on the river Ganga called 'Jal Marg Vikas' (National Waterways-I) would be developed between Allahabad and Haldia to cover a distance of 1,620 kms, which would enable commercial navigation of at least 1,500 tonne vessels and that the project would be completed over a period of six years at an estimated cost of Rs.4,200 crore. The Project's objective is to provide an environment friendly, fuel efficient and cost-effective alternative mode of transportation, especially for bulk goods, hazardous goods, captive cargo and over dimensional cargo. Government has commissioned three expert studies to assess the interventions required to achieve greater clarity on the entire project and its impact. The project includes construction of terminals, jetties, river training and conservancy works, modern automated information system, navigation aids, etc. The construction of the project is expected to commence from March, 2016.

Others

These include allowing access to cheaper finance abroad and elimination of registration requirement of ship repair units (SRUs) with the Director General of Shipping.

II) Ports:

In the Maritime Agenda, a target of 3130 million tonnes (MT) port capacity has been set for the year 2020 with around Rs. 2,96,000 crore investment. More than 50 per cent of this capacity is to be created in the non-major ports. FDI up to 100 per cent under automatic route is permitted for construction and maintenance of ports. In 2013-14, 16 public private partnership (PPP) projects were awarded at an estimated cost of Rs. 18,640.8 crore for capacity addition of 159.7 MT in the major ports comprising construction of berths and terminals and mechanization of existing berths. Some other policy initiatives related to ports are the following.

Sagarmala project: "Sagarmala Project" has been launched with an objective of modernizing the ports along India's coastline and achieving rapid expansion of port capacity and development of inland and coastal navigation. The initiative aims at supporting port-led development through appropriate policy and institutional interventions, port infrastructure enhancement, including modernization and setting up of new ports, and efficient evacuation to and from hinterland. An allocation of Rs. 200 crore has been made during the year 2015-16 for implementation of the project. The work under Sagarmala project is to be done in close collaboration with the maritime state governments.

Improving port connectivity: The Cabinet has given approval to create a Special Purpose Vehicle (SPV) to focus on providing efficient evacuation systems in major ports and to improve their connectivity. The SPV would undertake the following Projects:

– Last mile connectivity to major ports
– Modernization of evacuation infrastructure in ports
– To operate and manage internal port railway system
– To raise financial resources for funding port related railway projects

Coastal berths**:** In order to promote & encourage coastal shipping, a new scheme for coastal berths has also been approved by the government and necessary guidelines issued to all the ports.

Incentive to make major ports green: A new incentive scheme has been evolved to encourage major ports to become green ports. Under the scheme, green projects such as waste water treatment, renewable energy generation, use of bio-diesel and provision of shore power would be supported up to 50 per cent of the project cost. Each major port would be given a financial grant of up to Rs.25 crores for undertaking these initiatives. Nine major ports have given a commitment to generate at least 150 MW of renewable energy through solar and wind power in the next five years. This includes 25 MW generation by Jawaharlal Nehru Port and 20 MW each by Paradip Port, Kamarajar Port and Kandla Port.

Green channel clearance for coastal cargo: In order to ensure faster clearance of cargo, the government has introduced green channel clearance system for coastal cargo in major ports.

New major ports: The government has decided to take steps for setting up of 2 new major ports in Andhra Pradesh and West Bengal at Durgarajapatnam and Sagar respectively. The two Ports will be developed in PPP mode.

Oil pollution cess: Government has approved a new central scheme for providing assistance to the ports handling crude oil and POL for combating oil pollution and mitigation measures. Financial assistance under the Scheme would be given in the form of grant-in-aid up to 50 per cent of the total cost of the procurement of pollution response (PR) equipment/material.

Delegation of powers to major ports: The Government has issued orders on 11/2/2015 for enhancement of the financial powers delegated to major port trust boards as also chairman, deputy Chairman and heads of departments in the port trusts. The enhanced delegation is expected to speed up decision making in the port trusts in general. Keeping in view the need for simplifying and rationalizing the delegated powers, the earlier distinction between plan and non-plan expenditure and category I and II ports as also new and replacement works have been done away with. The powers for sanctioning and incurring expenditure on capital works have been enhanced from Rs. 50/Rs.100 crore for new/replacement works to Rs.200 crore for all capital works, facilitating speedy decision making.

Developing 78 lighthouses as tourism centers: The Ministry of Shipping, along with the Directorate General of Lighthouses and Lightships (DGLL) has drawn up an ambitious programme to develop 78 lighthouses in the country as centres of tourism in the first phase under Public Private Partnership (PPP).

IT Sector

The cross sectoral impact of the IT sector has never been so critical for India's growth and development agenda. The government recognizes its potential, and the Information Technology sector is undoubtedly a key pillar in various flagship initiatives like Digital India, Make in India, Skill India and Start-up India.

The 'Digital India' programme with the vision to transform India into a digitally empowered society and knowledge economy was launched on 1 July 2015. Digital India is an umbrella programme that covers multiple government ministries and departments. The vision of Digital India is centred on three key areas, viz., (i) Infrastructure as a utility to every citizen (ii) Governance and services on demand and (iii) Digital empowerment of citizens. Digital India aims to provide the much needed thrust to the following nine pillars of growth areas which include broadband highways, universal access to mobile connectivity, public internet access programme, e-Governance – reforming government through technology, e-Kranti (NeGP 2.0) – electronic delivery of services, information for all, electronics manufacturing with net zero Imports target, IT for jobs and early harvest programmes.

CHAPTER 3
ISSUES AND SUGGESTIONS

Chapter 3 - Issues and Suggestions

While the data and methodology issues related to services prices and production indices which we have been mentioning in earlier papers are still important, there are also many other issues. Some are the following:-

I **General Issues:** Here some issues which are common to all services are given.

a) Exchange Rate

While the recent data of China's slowdown is a dampener, the recent devaluation of Yuan and the resultant competitive devaluations/depreciation is another phenomenon to be watched carefully. While India's depreciation (February 10, 2015 over March 2015) in nominal terms at 7.79 per cent is higher than that of China's at 6.51 per cent, there are many countries with higher depreciation levels. This could affect both services and merchandise exports of India. Taking the latest month-wise data available only in BIS database, REER (which indicates export competitiveness as it also includes relative inflation), has appreciated for India while it has depreciated for China. There are also many countries like Brazil, Malaysia, Mexico, S. Africa, and Thailand with high depreciation (Table 6).

Table 6: Nominal Exchange Rate, NEER and REER (per cent)

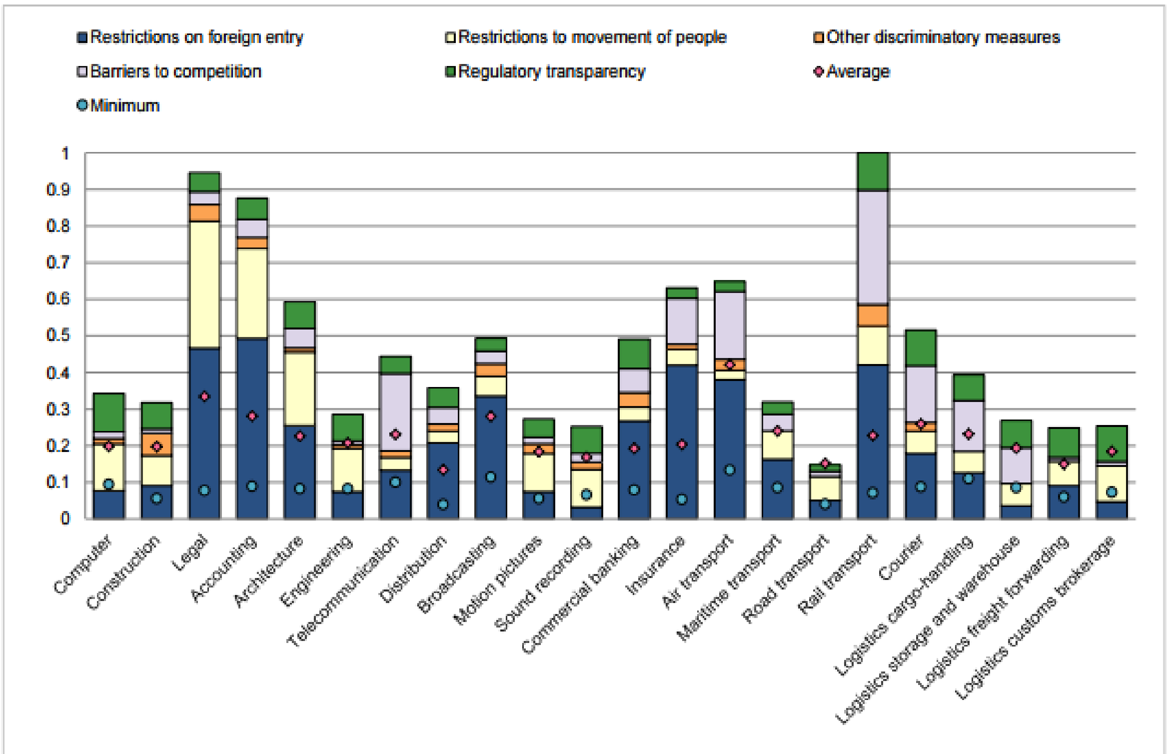
Currency/Country	Nominal February 10, 2016 Over March end 2015	NEER December 2015 over March 2015	REER December 2015 over March 2015
Japanese Yen/Japan	4.67	2.7	2.1
Australian Dollar/Australia	-7.62	-3.3	-2.8
Brazilian Real/Brazil	-16.35	-14.7	-10.9
Chilean Peso/Chile	-12.38	-6.6	-4.9
Chinese Yuan/China	-6.51	-0.1	-0.2
Indian Rupee/India	**-7.79**	**-3.4**	**0.5**
Indonesian Rupia/Indonesia	-3.35	-2.2	0.9
Korean Won/South Korea	-8.12	-1.8	-1.9
Malaysian Ringgit/Malaysia	-10.68	-11.4	-8.9
Mexican Peso/Mexico	-18.84	-8.9	-7.9
Russian Ruble/Russia	-27.09	-11.8	-7.8
Singapore Dollar/Singapore	-1.25	1.5	-0.4
South African Rand/South Africa	-23.08	-17.7	-15.9
Thai Baht/Thailand	-7.97	-6.2	-7.6

Note: Appreciation (+) / Depreciation (-)
Source: Calculated from IMF for Nominal and from BIS for NEER and REER

b) Domestic Regulations (DR) and Trade Restrictiveness (TR) :

Policy reforms would depend on how we tackle DR & TR. OCED Services Trade Restrictiveness Indices (STRIs) for the 34 OECD countries and eight major emerging economies provides a comprehensive portrait of services trade restrictions. India's score on the STRI index in the 22 sectors is presented below along with the average and the lowest score among the 42 countries included in the STRI database for each sector (Figure 7).

Figure 7: OECD Services Trade Restrictiveness Index (STRI)



Source: OECD STRI Country Report-India

The STRI can help India identify obstacles to broadening its competitiveness in services and services-intensive manufacturing sector. The OECD trade in value added database and the STRI together can help in assessing regulatory bottlenecks and regulatory spillovers that may hinder the objectives of attracting more manufacturers through the "Make in India" initiative. India has a STRI score above average in all sectors except road freight. The sectors with the lowest STRI scores in India are road transport (establishment only), storage and warehousing (logistics) and freight forwarding (logistics). These three sectors follow the automatic route up to 100 per cent equity share. No sector-specific restrictions apply at the national level in road transport and for logistics there is a commercial presence requirement for freight forwarding and a major state-owned enterprise in storage and warehousing.

The sectors with the highest STRI scores are rail freight transport, legal services and accounting services. Rail freight transport is on the list of prohibited sectors. As per OECD report, it is not open to private investment, let alone foreign investment.

Transit rights are also limited rendering the sector closed to foreign trade and investment. However, recently steps have been taken by the government to allow FDI in some areas of railways with certain conditions though railway operations other than permitted activities is still in the prohibited sectors list. Many areas in railway infrastructure are open to private sector participation and 100 per cent FDI under the automatic route. They include the construction, operation and maintenance of the following (i) Suburban corridor projects through PPP, (ii) High speed train projects, (iii) Dedicated freight lines, (iv) Rolling stock including train sets, and locomotives/coaches manufacturing and maintenance facilities, (v) Railway Electrification, (vi) Signaling systems, (vii) Freight terminals, (viii) Passenger terminals, (ix) Infrastructure in industrial park pertaining to railway line/sidings including electrified railway lines and connectivities to main railway line and (x) Mass Rapid Transport Systems. With these changes STRI scores may have to be changed further by OECD, which has possibly not taken note of these developments in its 2015 STRI country report of India.

Legal services, both national and international law, are reserved for licensed Indian lawyers. Indian nationality or citizenship is required for obtaining a full license. Only fully licenced lawyers (advocates) may form and own law firms. Corporations are not permitted in the sector and lawyers may not enter into partnerships or otherwise associate with other professions or foreign lawyers. The only opportunity for foreign legal services providers to do business in India is through business visits to provide legal advice to their clients (fly-in-fly out).

Auditors and chartered accountants are regulated professions. To obtain a license degrees from Indian higher education institutions or institutions in countries with which India has a mutual recognition agreement are required. Only licenced auditors or chartered accountants may form and own accounting or auditing firms. Auditing corporations or commercial associations with other professionals are not permitted. Foreign auditors or accountants may provide services in India on a short-term basis through limited licensing.

c) <u>Mega Free Trade Agreements (FTAs) :</u>

This is a new concern for us both in merchandise trade and services trade. The Trans-Pacific Partnership (TPP) was reached on 5 October 2015 among 12 nations: Australia, Brunei, Chile, Canada, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the US and Vietnam, which comprise 40 per cent of the world's gross domestic product (GDP). In addition to greater market access for goods and services, the areas of negotiations covered by TPP include intellectual property rights, foreign investment, competition policy, environment, labour, state-owned enterprises, e-commerce, competitiveness and supply chains, government procurement, technical barriers to trade, transparency in healthcare technology and pharmaceuticals, and regulatory coherence.

The establishment of the ASEAN Economic Community (AEC) in 2015, which excludes India and China, is a major milestone in the regional economic integration agenda in ASEAN, offering opportunities in the form of a huge market of US$2.6 trillion and over 622 million people. In 2014, AEC was collectively the third largest economy in Asia and the seventh largest in the world. If the proposed Trans-Atlantic Trade and Investment Partnership (TTIP) between US and EU materializes then we may be affected further.

In this situation, to adequately benefit from international markets, other countries such as India will have to improve their capacities both for developing policies and the capabilities of their producers to upgrade standards in line with the higher requirements. The Peterson Institute for International Economics (PIIE) in a report released in September 2015 stated that if China and the rest of the Asia-Pacific Economic Cooperation (APEC) forum join a second stage of the TPP that continues to exclude India, India's annual losses would be $45 billion in exports and $30 billion in annual income. However, many analysts claim such projections are exaggerated. India is not in a position to undertake obligations finalized under TPP with respect to intellectual property rights (IPRs).

There are two concerns. First, mega FTAs will erode existing preferences for Indian products in established traditional markets benefiting the partners to these agreements. Second, they are likely to develop a rules architecture which will place greater burden of compliance on India's manufacturing and services standards for access to the markets of the participating countries.

Another view is that even the existing FTAs signed by India benefit the partners more than India, affecting India's domestic sector, particularly, the agricultural sector.

d) <u>Disinvestment:</u>

There is plenty of scope for disinvestment in services PSUs under both central and state governments which was mentioned in our earlier paper (2010). Speeding up disinvestment in some services-sector PSUs like Shipping Corporation of India (SCI), RITES, Engineers India Ltd., Engineering Projects India Ltd. could not only provide revenue for the government but also speed up the growth of these services. Some of these companies need to be listed. In the case of companies like SCI, we may have to wait till the shipping & trade situation picks up.

e) <u>Credit Related:</u> The issues here include the following:

- 'Collateral free' soft loans to support the sector's cash needs and possibility of considering even export or business orders as collateral for credit-worthy service firms as the services are intangible and low asset base of services firms do not offer the best collaterals for debt.
- Need for start-up capital. The Government has recognized this need and has recently unveiled 'Start-up India' and 'Stand-up India' programmes.

f) <u>Tax, Trade Policy and Investment Related</u>: Some issues are the following:-

- <u>Issue of DTA sales</u>: In para 6.08(b) of FTP 2015-20, wherein EOUs are permitted to sell 50 per cent of the FOB value of exports, the clause is mentioned as follows: "For services, including software units, sale in DTA in any mode, including on line data communication, shall also be permissible up to 50 per cent of FOB value of exports and / or 50 per cent of foreign exchange earned, where payment of such services is received in foreign exchange." Thus the payment from DTA sales is to be received in Foreign Exchange. This goes against the very purpose of granting approval for DTA sale entitlement which is to allow the Indian exporters to get additional income by supplying the products/ services in the domestic market. Domestic customers cannot be asked to buy Forex and remit it for the billings. Also the customers may turn away with these type of conditions. Also RBI may not grant permission to remit foreign currency to clients for the rupee invoices. So suitable solution to para 6.08(b) of FTP is needed.

- <u>Issues of re-imports for repair services, refurnishing, reconditioning; return samples; and re-imports for R&D purpose</u>: When such goods are imported, the customs department insists on obtaining clearance/approval from the Ministry of Environment, Forests and Climate Change (MoEF&CC), with a notion that the imported goods are in the nature of hazardous waste or e-waste. This process of obtaining approval takes about three to four months and in a worst-case scenario even a year, which severely affects the importer as they are not able to meet their obligations towards their foreign customer/supplier. This also results in incurrence of huge demurrage charges, as the goods have to be stored in the customs premises for an unduly long period of time. The foreign customers/suppliers may also initiate proceedings against the Indian importers for inordinate delay which may result in loss of business and cancellation of orders/contracts. The concerned Committee under the MoEF&CC meets at New Delhi only once a month and there are many such imports across the country awaiting the clearance of the committee. Presently, import of hazardous waste and e-waste is subjected to clearance under the Environment Protection Act, 1986 and the Rules framed thereunder. However, this has been applied even in case of import of used goods received on repair and return basis or refurbished goods meant for R&D purposes in India by importers including EOUs. In some places, the problem is compounded, as for example, on the strength of Circular No.27/2011-Cus., dated 4.7.2011, issued by the Central Board of Excise and Customs (CBEC), the Bangalore Customs has issued a Public Notice No.14/2015, dated 14.8.2015. As per the said Circular and Public Notice, the customs department insists on getting a no objection certificate/clearance from the MoEF&CC in terms of Hazardous Waste (Management, Handling and Transboundary Movement) Rules, 2008 and E-Waste (Management and Handling) Rules, 2011 even to cases where goods are imported for reconditioning or repair or R&D purposes etc. This poses serious difficulties to Indian importers especially EOUs, who are supposed to fulfill their export/contractual obligations in a time bound manner. While review of the circular No. 27/2011-Cus, dated 4.7.2011, issued by the Board is needed, as an interim measure, suitable instructions for Fast Track Clearance for genuine importers can be issued and the process of giving environment clearance could be decentralized by setting up clearance committee in major port cities.

- <u>Issue of speeding up the Bankruptcy laws</u>: This law can speed up closure of failed firms and starting of new firms. The government has introduced the Insolvency and bankruptcy Bill 2015 in the Lok Sabha which has now been referred for further scrutiny to a joint parliamentary committee.

g) **Need for a Nodal Department for Services:** The need for a nodal department to deal with all issues related to services has long been felt as some services are dealt by some departments and for some others there is no specific department. The Department of Commerce has been trying to deal with the different areas of services and even taking initiatives like forming an Inter-Ministerial committee, Global Exhibition on Services and a Services Conclave. But most of the efforts are trade related. The Department of Economic Affairs has also been coming up with policy related papers at regular intervals on services and has been dealing with services related issues in the Economic Survey and Budget. However, there is a need to designate a department as nodal department for services which can deal with all issues related to services on a regular basis and also coordinate with all concerned departments and ministries at the central and state levels. This can help in facilitating the service providers in different services and different parts of the country.

II- Sector Specific Issues: In this paper we have focused on four major services sectors, namely tourism, shipping & port services, IT including software and healthcare services including medical tourism. Some important issues in these four sectors are given below.

1. **Tourism**

Tourism sector which can lead to higher and inclusive growth is a goldmine of opportunity and not really tapped. India's share in world tourism inflows was only 0.7 per cent in 2014 (rank 41), while that of China was 4.9 per cent. Interestingly, the share in world tourism expenditure of India is relatively higher at 1.6 per cent (rank 15) implying that foreign tourists spend relatively more in India. Some issues in this sector are the following:-

a) Need for improvements in e-Tourist visa and ordinary visa

- The window for e-Tourist visa application is now open 30 days before the tour. This needs to be increased as all airlines ask upfront payment for making any travel booking and last minute booking is costly. This will remove the uncertainty for foreign visitors in getting visa as they plan well in advance including applying for leave. Hotels and Tour operators also need confirmations and guaranteed payments well in advance. So the e-tourist visa window could be made open for 180 days. This can be done without much difficulty.
- E-tourist visas are single entry visas. As a result the e-tourist visa excludes many travellers who combine their trips to India with other neighbouring countries and are part of some package tours. So the e-tourist visa needs to have the option for multiple entry. Exceptions to any country for security reasons can be made if necessary.
- Duration of stay under e-tourist visa is only 30 days. Since some visitors may like to spend more than 30 days and some of the package tours including to our neighbouring countries last for more than 30 days, the duration of stay could be increased to 60 days.
- There is no biometric facility at Indian seaports where big cruise ships come with 2000 to 3500 tourists at a time. In major ports where cruise tourists arrive, biometric facility could be made available which can help cruise passengers to get eTV and return if necessary from some other airport or seaport.

- There is delay to bio-metric process at airport for e-tourist visa holders. This is due to many reasons like lack of proper display for eTV holders counter at the immigration hall resulting in tourists standing in normal queue and then being told by officers to go to the dedicated counters, biometric machines being defective, lack of adequate counters for e-tourist visitors, etc. This has resulted in taking hours for a tourist to come out of immigration and find the baggage removed from the belt and kept elsewhere. This is tiresome particularly for group tourists. So, there is a need to streamline the process, increase the counters for e-tourist visa holders and also have biometric machines even in normal visa counters which become free quickly and can be used for e-tourist visa holders.

- E-Tourist visa is not given for tourists visiting India for medical purpose. There is a need to consider giving such visas, given India's potential as a medical tourism destination.

- Biometric process for non e-TV visa is done in Indian missions overseas. This involves travel cost & time and sometimes hotel stay. This process needs to be streamlined by having more biometric locations.

b) Tax Issues

- Issue of Service Tax on Exports: Exports are not taxed. By this logic, tourism exporting units (hotels & resorts, tour operators, tour rent a cab, travel agents, convention centers and other tourism service providers) which are earning in foreign exchange should not be taxed. The definition for export of services given by the Department of Commerce in its Foreign Trade Policy is on the lines of the WTO definition and also covers the consumption abroad mode i.e. supply of a service from India to service consumer(s) of any other country (mode 2). However, as per service tax rule 6A the provision of any service provided or agreed to be provided shall be treated as export of service when a) the provider of service is located in the taxable territory, b) the recipient of the service is located outside India, c) the service is not a service specified in the section 66 D of the Act (service tax negative list which does not include tourism services), d) the place of provision of the service is outside India, e) the payment of such services has been received by the provider of service in convertible foreign exchange, and f) the provider of service and recipient of service are not merely establishments of a distinct person. Thus due to the place of provision clause, tourism services are not treated as export of service and are taxed. This anomaly needs to be rectified.

- Need for lower GST for tourism related services: Internationally, the indirect tax levies in tourism are mostly less than 10 per cent overall while in India they are estimated to be between 18-22 per cent. The GST rate of tourism internationally is about half of the standard GST rate. A 2014 OECD study on the impact of taxes on competitiveness of tourism, has stated that the consumption tax on tourism has been kept low to encourage investment inflow, job creation & overall economic development from tourism in many OECD countries. While consumption tax (VAT/ GST) in many OECD countries was around 15-25 per cent, tourism related sectors like hotels & restaurants were rated at almost 50 per cent of the standard rate (SR) or even less (Table 7).

Table 7: Consumption taxes and reduced rates for hotels & restaurants (as on January 1, 2013)

Country	Standard rate	Reduced rate for tourism-related activities	
		Hotels	Restaurants
Austria	20	10	10
Belgium	21	6	12
Finland	24	10	14
France	19.6	7	7
Germany	19	7	..
Greece	23	6.5	13*
Iceland	25.5	7	7
Ireland	23	9	9
Italy	21	10	10
Luxembourg	15	3	3
Mexico	16	0	..
Netherlands	21	6	6
Norway	25	8	15
Poland	23	8	8
Slovenia	22	9.5	9.5
Spain	21	10	10
Sweden	25	12	12
Switzerland	8	3.8	..

Source: Compiled from OECD : Tourism Trends and Policies, 2014
Note: * Pilot reduced rate for restaurants from 1/8/13 to 31/12/13.

- Even in Asian competitor countries such as Thailand, Malaysia, and Singapore, the total net indirect tax incidence on tourism is estimated to be between 6-9 per cent. GST on tourism sector is zero per cent in Malaysia and Singapore. India is among the countries with the highest indirect tax regime on tourism. Tourism industry feels that a reduction in total indirect tax levies through GST to competitive rates of below 10 per cent can get India a share of at least 10 per cent of the US $ 150 bn. Plus (that is between US $ 15-20 bn.) tourism market which is coming to South & East Asian nations in the next few years.

- The report of the committee headed by Dr. Arvind Subramanian, Chief Economic Adviser has suggested standard GST rate for services in the range of 16.9 per cent to 17.7 per cent under preferred rates and 18.0 to 18.9 per cent under alternative rates. While the committee has recommended rationalization of exemptions, it has also stated that the constitution should not limit the freedom of what rates to levy. However, given the experience of OECD countries, and the priority being given by the present Indian Government to Tourism sector which can lead to higher & inclusive growth, there is a need to examine whether lower GST rates could be levied for Tourism sector.

- Import duty exemption for equipment and accessories for adventure tourism: India has one of most enviable natural resources and natural wonders in the world. Despite these advantages, India has not been able to convert them into competitive economic advantages. In the annual global rankings of adventure tourism development index (ADTI) (2015), India with a rank of 119 among 191 countries in terms of its adventure tourism attractiveness is way below the other BRICS countries. Exemption of import duties or levying low duties on equipment needed for adventure tourism could be considered as it will make Indian companies cost competitive and also provide quality equipment of global standards.

- There is also need to address issues like high luxury tax on hotels by States.

c) Finance and Investment related

- Positioning India as a Meeting / Convention Centre: India currently has less than 0.5 per cent of the world meetings and conventions market. Global conventions create tremendous intellectual goodwill across different industries and the countries that they are held along with tourism market. However, these conventions and meetings have to be bid for much in advance and in a systematic manner. For this, a global bidding fund may have to be created.

- Encouraging Investments in Tourism Sector:
  - Out of an estimated 12.5 million hotel rooms worldwide, India has less than 0.15 million hotel rooms. This has a direct correlation to India's international market share. India gets less than 7million international tourists annually, while China with an estimated 2.5 million rooms has an annual international tourists arrivals of around 55 million plus. To capture the increasing size of the world tourism market and to become a world leader in tourism, the Chinese government is further targeting an increase in its hotel capacity by 3 times to around 7 million hotel rooms through central & provincial government subsidies, support & low cost finance.

  - As per industry estimates, a 100 roomed hotel generates on an average around 150 direct jobs and impacts another estimated 75 indirect jobs around the hotel. 80 per cent of these jobs are estimated to be from the local area & are semi-skilled & unskilled blue collared jobs (i.e. around 180 jobs per 100 rooms). If India is to move towards a respectable global position in tourism, it needs to target a minimum of 0.5 million hotel rooms till 2020. That could create an estimated 63 million additional jobs out of which around 50 million would be skilled & unskilled blue collar from the local area. However, the creation of this additional 0.35 million hotel rooms would require around 1.5 lakh crore at the rate of Rs. 30 lakhs per room. This is a highly capital intensive industry where the breakeven is around 8-10 years on a minimum. To mobilise such large scale funds and to generate investor interest in this sector which will also spur large scale employment, there is a need to examine the possibility of giving special incentives like tax free bonds and income tax exemption on profits used for reinvestment in tourism sector.

- Development of Tourism Infrastructure on PPP basis: In “The Travel & Tourism Competitiveness Report 2015”, of the World Economic Forum, India's natural and cultural resources were rated at a high of 12 worldwide. However the overall rating of India was pulled down to 52 worldwide, due to very poor ratings of 96 on the parameter of prioritisation of travel & tourism and 67 on the parameter of the infrastructure and 109 on tourist service infrastructure. Added to this, India's ranking is low in terms of health and hygiene (106) safety & security (129) and Information and Communication Technology (ICT) readiness (114) which infact is disturbing given India's expertise in ICT. However, in terms of price competitiveness, India is at 8th rank. Thus efforts by the central and state governments to create cultural tourism focused infrastructure and enabling policies can help India to convert its comparative cultural advantages in tourism to competitive global advantages. Each of the cultural sites need to offer an integrated tourism experience which is more than just the monument through a well-designed site management plan on PPP basis. This will create a new class of tourism economy and will also re-ignite the interest of the young Indians in our legacy. Soft tourist infrastructure could be developed around important monuments and cultural heritage sites on a PPP basis by channelising corporate social responsibility (CSR) spends into India's heritage development. This will create new destinations for tourism spending and will also bring back focus on Indian heritage by making it more contemporary. Even the funds under Mahatma Gandhi National Rural Employment Gurantee Act (MGNREGA) scheme can be used for developing Tourism Infrastructure.

- Support for SMEs in Tourism Sector: A lot of India's tourism experiences are developed and enabled by micro, small and medium enterprises throughout the country. If leveraged and developed well, not only will they stimulate high end heritage and adventure tourism into the country leading to valuable foreign exchange, but will also empower and enrich a large population in this micro, small and medium enterprises sector across the country. These SMEs need financial support. Venture capital funds and the recent initiative of MUDRA Yojana could also be extended to the SMEs in tourism sector.

- Setting up India haats on the lines of Delhi haat in major cities/towns to attract tourists: In these haats, there should be miniature-cultural India with different cultural performances which can also provide employment for the artists. This could be done by encouraging private investments in these activities by channelizing CSR spending or under PPP mode.

d) National Cruise Strategy

- The global cruise industry is estimated at US $40 billion with almost 2 million tourists. This is high end tourism which creates high economic output. Unfortunately, India is estimated to get less than 0.1 per cent of the global cruise tourism market. Almost 150 additional high end cruise ships are estimated to bypass India which could touch Indian shores if there is an integrated cruise strategy across all Indian ports. India has an enviable 7000 kilometers of coastal line which needs to be leveraged through a futuristic well planned cruise strategy.

e) Making railways more tourist friendly

- Indian railways has been the lifeline of Indian travel and tourism and accounts for the majority of the one billion visitations. So the condition of railways and railway stations including cleanliness & hygiene needs to be drastically improved.

- E-booking facility with special quotas for foreign visitors against a pre-defined time line and if necessary by payments in foreign currency can be introduced.

- Tourism experience can be enhanced by providing decent waiting rooms and biodegradable toilets in trains. Audio & video facilities as in aero planes could be provided in special trains to major tourist destinations.

f) Others

- Introducing smart card for e-payment across all tolls of India to prevent inter-state border stoppages, which can help in smooth & seamless travel for tourists.

- Introducing a national permit for tourist transport vehicles with a flat annual fee similar to national permit for trucks.

- Increasing baggage allowance on domestic sector in flights for foreign tourists.

- Implementing global parameters in CRZ norms as per vulnerability mapping: India has a 7000 kilometers coastline which can be leveraged for hospitality infrastructure. The Indian coastline can be leveraged for creation of the tourism infrastructure by considering global CRZ norms which consider dynamic mapping of high tide lines instead of a blanket 200 meters from the high tide line as recommended by Dr. Swaminathan Committee. As per coastal Regulation Zone Notification dated 6th January, 2011, an area up to 200 mts. from High Tide Line (HTL) on the landward side in case of seafront and 100 mts. along tidal influenced water bodies or width of the creek whichever is less is to be earmarked as No Development Zone (NDZ). Though the Swaminathan Committee has recommended 200 meters as the NDZ and specifically warned against proliferation of tourism units in this zone if relaxed, it has stated that any modification, if considered must be handled with extreme caution.

- Inclusion & classification of sustainable adventure tourism activities under permissible activities in forest areas in line with global best practices.

- Marketing Indian Tourism: Like trade fairs, India Tourism fairs could be organized in Indian embassies abroad as per a pre-defined calendar.

2. **<u>Shipping and Port Services</u>**

Shipping is another major service sector for India, the potential of which has not been fully tapped. This sector is a very good candidate for India's 'Make in India' programme as it has high linkage effects covering broad areas like ship-building, providing shipping services, ship repairs & maintenance, port services and even closely related to merchandise trade. However, India's shipping sector is not really in a good shape. There has been a sharp decline in the share of Indian ships in the carriage of India's overseas trade from about 40 per cent in the late 1980s to 7.45 per cent in 2014-15. The existing Indian fleet is also ageing, with the average age increasing from 15 years in 1999 to 17.89 years as on 31 December 2015 (42.42 per cent of the fleet is over 20 years old and 12.43 per cent in the 15-19 age group). Thus there is an urgent need to increase India's shipping fleet. While India has progressed well in infrastructure development related to Airports and Metro railways, Ports and Shipping have lagged behind and are the areas for immediate focus. Some issues in the shipping sector are the following:-

a) Need for cheaper finance and longer tenure for funds to shipping sector.

- Indian ships are ageing and need to be replaced. There is a dearth of funding for Indian companies to purchase younger assets. Currently, only three major banks, i.e., EXIM Bank, SBI and ICICI Bank, by and large participate in the funding of shipping assets. The cost of loan funds averages about 13.5 per cent. Comparatively, the competing foreign shipping companies are able to source funds at about 2-3.5 per cent.

- Added to this the tenure of loans available to Indian shipping companies are as short as 7 years while assets have a useful life of 20-25 years. Foreign banks are known to fund for periods as long as 70 per cent of the life of an asset. So this practice needs to be replaced with tenures related to the useful life of an asset.

Whether the above two issues needs to be addressed by considering shipping industry as an Infrastructure sector and included in 5:25 scheme or flexible structuring of long term project loans to infrastructure and core sector industries as desired by the shipping industry or by some other method, the problem is genuine. Since international freight is competitive, this cost differential due to interest and tenure, squeezes operating margins of Indian companies. This impacts profitability as well as cash flows – further impacting internal accruals that could be used to further expand. While lowering interest rates may be gradual depending on domestic inflation and other parameters considered by the RBI, at least the issue of longer tenure could be addressed as it makes a significant difference to cash flows as can be seen in table 9 which gives the per day cost of servicing a loan using different scenarios in terms of interest rate and tenure. While the difference between scenario 1 and 3 with both differing rates and tenures gives a breakeven difference per day of US$1144/day, even the difference between scenario 1 & 2 with only differing tenures gives a break-even difference of US$522 per day.

Table 8: Per day costs for shipping companies under different scenarios

	Prices of asset	Rate of Interest (per cent)	Tenure of loan (years)	Break-even charter higher at 80 per cent of lending
Current scenario 1:	$4,000,000	13	7	6708
Beneficial scenario 2:	$4,000,000	13	12	6186
Beneficial scenario 3:	$4,000,000	6	12	5560

Source: Indian National Shipowners' Association (INSA)

Shipping companies need a steady source of funding through an institutional mechanism to procure long term funds at attractive interest rates on par with international interest costs. This will increase Indian tonnage and make the industry more competitive vis-a-vis foreign shipping companies. For this, there is a need to consider permitting a financial institution to create a dollar denominated shipping fund by raising funds abroad to buy ships. Shipping companies buy assets in dollars and also earn in dollars. Hence there is no reason for currency hedging. This will help provide the industry to competitive funding similar to that available to its peers internationally. Since asset prices are currently serendipitously low, the institutional mechanism is likely to help the shipping sector in acquiring assets at the right time.

b) Terms of Shipment

- The terms of shipment, imports CIF makes it difficult to ascertain the freight element. Sellers invariably like to keep control over transportation and support their own nationality or companies. The central government had taken a decision that all contracts by PSUs and government controlled cargo shall be done on FOB basis. When there is an exception, the concerned PSUs have to approach the Ministry of Shipping for permission. However, this was to be done through Transchart. After Transchart was disbanded in September 2015, shipment terms have again become CIF.
- Crude oil is still imported on FOB basis (except from Iran due to the sanctions). Transporting critical energy cargo on FOB with long term contracts on the national flag provides certainty and surety to the supply chain of the nation. Of late, countries such as Saudi Arabia have offered to sell crude oil at a small discount provided India buys on CIF basis. This is done to support their own national tanker fleet and caution is needed while such deals are finalised.
- Other commodities such as coal and fertilizer are being imported on CIF basis. Fertilisers are imported on CIF basis since foreign manufacturing companies are unwilling to sell directly to the designated agencies like STC which do not pre-book, and therefore is forced to buy from traders who in turn wish to control freight and therefore insist on CIF basis. CIF contracts are always opaque since the freight is not known. Converting a CIF contract to FOB is always difficult since the supplier artificially increases the FOB component in order to show that the freight being offered is the lowest and prohibits Indian shipping companies from again entering the market. Imports FOB permits the buyer to control freight costs and the transporter too, both of which are extremely important for India which is a net importer and FOB contracts can lead to long term cargo contracts with Indian flag shipping companies. This will ensure that freight does not flow out of India with simultaneous growth of Indian tonnage.
- The terms of shipment issue therefore needs to be sorted out carefully taking into consideration the concerns of domestic shipping.

c) Issue of infrastructure status for maintenance dredging

- The harmonized list of infrastructure sub sectors included capital dredging in 2013 as part of port infrastructure. But maintenance dredging was not included. Both capital and maintenance dredging are essentially the same and involve removal of soil and similar material. Maintenance dredging is an "essential" activity and is required for safe entry and exit of ships. There is also no differentiation in the nature of services rendered by capital dredging and maintenance dredging companies as the equipment is interchangeable, skill set and manpower are indistinguishable and technical know-how is similar. Further, Indian companies have a presence largely in maintenance dredging and not in capital dredging.
- While giving infrastructure status to maintenance dredging may not be feasible as all maintenance related activities will ask for infrastructure status and the purpose

of having the status will be lost, the basic problem in maintenance dredging needs to be addressed. These include high capital cost and the western countries being unwilling to sell dredging machines to their captive market, i.e., India, resulting in India importing sub-standard machines from China.

d) Prepayment of ECB

- Prepayment of ECB is allowed by authorised dealer banks without prior approval of RBI subject to compliance with the stipulated minimum average maturity period as applicable to the loan. Usually request for prepayment within 3,5 or 10 (depending on Track I, Track II or Track III) years is not permitted or needs prior RBI sanction since the stipulated minimum average maturity period is specified accordingly.
- Shipping companies are required to trade in assets depending on market conditions and hence may require to sell an asset well before previously planned date. The shipping company may also need to prepay in order to borrow for the purposes of fresh acquisition of a suitable asset class depending on the market conditions. Besides Indian shipping companies are net foreign exchange earners and therefore there is no country or company exchange risk.
- So there is a need to consider allowing Indian Shipping companies to prepay ECB loans at any time of the period of the loan.

e) Opening a joint escrow a/c for purchase of asset

- Most second hand purchase transactions require a certain percentage of the proposed sale price to be deposited in a joint escrow account held by the buyer and seller in a bank account outside India. Upon successful completion of sale transaction, the amount held in escrow is transferred to the seller. Currently RBI does not permit automatic opening of a joint escrow account of the buyer and seller. The Indian buyer has to await permission from the RBI to do so and the seller is unwilling to wait. This leads to the Indian company losing deals.
- RBI permits remittance of up to US $5 million directly to the seller without prior approval but opening of a joint a/c with the seller is not permitted. RBI could consider at least granting automatic approval to remit up to US $5 million into a joint escrow account of the buyer and the seller in a foreign bank. Permission to hold such an account would provide considerable ease in selling and buying ships.

f) Enhancing competitiveness of Indian shipping companies in coastal trade and making India a bunkering hub

- The operating costs of Indian shipping companies exceed those of foreign flags and in some cases by as much as 40 per cent in case of coastal container vessels (Table 9). Though the government announced tax free fuel for container ships by waiving customs or excise duty on it, in practise this is not working since oil PSUs are not supplying excise duty free bunkers as they find it difficult to separate the excise duty from the selling price. The same high operating cost parameters plague tanker and bulker ships working on the Indian coast. This is also an impediment for modal shift of cargo from roads to coastal shipping despite it being environment friendly. Added to this, costly finance and high bunkering costs makes Indian ships uncompetitive.

Table 9: Comparative Costs of Indian and Foreign Flag Vessels

Cost Head	Details	Foreign vessel as per CSLA	Indian vessel cost as per CSLA	Percent Difference
Charter Hire	Per day	Rs.480,000	Rs.547,200	
	Taxes on salary	Rs.0	Rs.588,000	
	Total for 14 days (A)	Rs.6,720,000	Rs.8,248,800	22.75
Bunkers	Total for 14 days (B)	Rs.13,456,800	Rs.22,914,000	70
Port Costs	Total for 14 days (C)	Rs.3,036,000	Rs.3,036,000	0
Total cost per voyage(A+B+C)		**Rs.23,212,800**	**Rs.34,198,800**	**47**
The difference in cost per TEU paid by an Indian ship-owner for a 2450 TEU ship.		**Rs.4,737**	**Rs.6,979**	**47**

Source: INSA quoting Container Shipping Lines Association.
Note: Cost comparison of foreign and Indian coastal operators on operating parameters of just fuel and tax. 14 per cent differential due to Service tax has not been considered.

- India is missing an opportunity to be a bunkering hub. The target customers for a bunkering hub in India are export-import (Exim) vessels calling India for loading or discharging, regardless of the flag of the ship and numbering around 19, 917 in a year. Currently, all the Exim vessels buy bunkers at khor fakkan / Fujairah in UAE and Singapore. This is because international bunkers in India cost US$409/MT while in Khor Fakkan it costs US$ 255.5/MT and in Singapore it costs US$265.5/MT as on September 30, 2015. Therefore, nobody buys bunkers in India. However, for bunkering, vessels have to divert from the main trade lane to bunker. This leads to additional port costs of this bunkering port and takes anywhere between 16-24 hours which is also a loss for the ship-owner. Because of higher quantum of bunkers on-board, the ship also has to load proportionately lesser cargo on-board which impacts its revenues. When this vessel comes into an Indian port, the waiting time to discharge cargo is 24-48 hours. This time can be ideally used for bunkering. It also improves the ability of a ship to load more cargo, if bunkering can be scheduled in India.

- While the central government imposes customs and excise duties on the bunker fuels supplied by oil companies, each maritime state also imposes local Value Added Tax (VAT) on the sale of bunker fuels. Sale of Fuel Oil, Marine Diesel Oil and Marine Oil Gas is levied VAT at an average rate of 13.5 per cent. High Speed High Flash Diesel is levied 24 per cent VAT. This also adds to the cost of fuel in India.

- Meanwhile, India exports bunkers which are sold at prevailing rates abroad less cost of freight. If oil companies sell in India at the same rates, they would have saved on transportation and the EXIM ships coming to Indian ports would have been the captive customers.

- So, 'Nil' duty on bunkers for all segments of coastal shipping (not just for containers) can be thought of to encourage both bunkering activity and making Indian ships more competitive in coastal trade. This will also encourage an eco-friendly mode of transport.

g) Piracy issue & Protection & Indemnity (P&I) club

Around July 2012, entities like Lloyd's of London & others were forced to implement additional restrictive measures against Iran w.e.f 23rd January 2012. European insurers & re-insurers stopped from indemnifying ships carrying Iranian crude & oil products anywhere in the world resulting in India and China, the two largest crude importers, facing problems. As Europe and the United States began implementing tougher sanctions against Iran, India suffered collateral damage and Indian shipping companies were forced to abandon carriage of Iranian crude on their own vessels since they were unable to obtain P&I Cover for such vessels. Indian maritime firms as well as our own international arms such as ONGC Videsh Limited were the most affected in Asia by the sanctions as the other two biggest buyers China and Japan did not need to rely on European insurers but were able to obtain such covers from their own P&I Clubs. So the need was felt to create an Indian Protection and Indemnity Insurance company.

A related development is that, due to piracy in the Arabian Sea, P&I clubs were charging higher premiums and even when piracy has been checked, the higher premium continues.

So there is a need to explore the possibility of creating an Indian P&I Company, or possibly leveraging the expertise at GIC for this purpose. While Korea and China began their journey towards a National P&I company through strategic tie ups with already established International P&I companies involving transfer of intellectual skills and technology over a period of time, Greece began by writing war risks covers on a mutual basis - something that GIC is already doing. Even more recently, The Standard Club Asia Ltd launched a new Singapore War Risks Mutual Class to provide the first national mutual war risks insurer in Singapore. This company is fully supported by the Singapore Shipping Association and provides among other covers, P&I War, Hull War and other covers underwritten on a mutual basis. India could also think of a strategic collaboration with an international company to launch a Mutual P&I Company.

h) Issue of withholding tax on interest paid on ECB loans taken by Indian shipping companies

- Remittance of interest on ECB loans taken on or before 1-6-2001 did not have to pay withholding tax. However, the provisions were amended and exemption from withholding tax was withdrawn for ECB loans taken on or after 1-6-2001. Thus, presently, the interest paid by Indian shipping companies to foreign lenders on acquisition of ships is subject to withholding tax at the rate of 20 per cent plus surcharge.

- As per the Report of the Expert Committee to Review Indian Shipping 2002 (Rakesh Mohan Committee report), ship acquisition costs of up to 60 – 80 per cent are financed by ECBs. As a rule, lenders require interest payment to be effected net of all Indian taxes. Subsequent to the withdrawal of exemption, interest cost gets enhanced substantially, which is passed on by the lenders to the borrowers.

- Unlike other segments, the burden of withholding tax falls entirely on shipping companies who cannot pass these increased costs to users of their services. Thus, subjecting interest paid on ECB loans to withholding taxes would effectively increase the financing cost to the shipping companies, especially where the payment to non-residents is to be net of taxes, i.e., the taxes are to be borne by the borrower. This also denies Indian shipping companies a level playing field with international competitors. There is a need to consider restoring the exemption from withholding taxes on interest payment by Indian shipping companies to foreign lenders.

i) Issue of refinancing through ECB funds

- Currently, RBI does not permit refinancing through ECB funds. Indian companies in the manufacturing, infrastructure sector and hotel sector (with a total project cost of Rs. 250 crore or more irrespective of geographical location for hotel sector), can avail of ECBs for repayment of outstanding Rupee loans availed of for capital expenditure from the domestic banking system and/or fresh Rupee capital expenditure provided they are consistent foreign exchange earners during the past three financial years and not in the default list/caution list of the Reserve Bank of India. Airline companies registered under the Companies Act, 1956 and possessing scheduled operator permit license from DGCA for passenger transportation are eligible to avail of ECB for working capital. Companies in the power sector are permitted to utilize up to 40 per cent of the fresh ECB raised by them towards refinancing of the Rupee loan/s availed by them from the domestic banking system subject to the condition that at least 60 per cent of the fresh ECB proposed to be raised should be utilized for fresh capital expenditure for infrastructure project(s). The payment for 3G spectrum allocation, initially met out of rupee resources raised domestically from banks by the successful bidders and are still outstanding in telecom operator's books of account is allowed to be refinanced with long-term ECBs. (See: RBI/2015-16/33/Master Circular No. 12/2015-16).

- Indian Shipping companies should be permitted to raise ECB for the purposes of refinancing debts incurred for the acquisition of assets. This will improve the ability of ship owners to optimize leveraging of funds. Often promising assets are available for sale either spot or on distress sale. Such sellers are not willing to wait for buyers to obtain approvals. In such cases, ECB can be used to replace own funds which may be used temporarily to take advantage of an opportunity and thereby unlock the free cash of the company. Then companies will be able to expand freely and easily.

j) Some issues related to Port Services:

- While port infrastructure issues are important, there are also issues like the Indian ports not having the necessary depth or draft, and also issues like the many port charges in India and the port charges in India being considerably higher than in many developed countries.

3. **IT including software**

a) **Visa Issues in IT sector:** Immigration and visa issues, which have long plagued the information technology sector, could come back to hurt Indian IT services companies as the US heads towards Presidential elections in 2016 . Two issues are important here

i) Grassley-Durbin Bill Two US senators (Grassley and Durbin) have recently introduced a bipartisan legislation in the US senate seeking reform of H-1B visa programme and modification of wage requirements. They also called for a sense of urgency against the "abuse of the system" over a scheme they claimed has got away from its original intent.

- The bill would prohibit companies from hiring H-1B employees if they employ more than 50 people and more than 50 per cent of their employees are H-1B and L-1 visa holders.
- This provision would crack down on outsourcing companies that import large numbers of H-1B and L-1 workers for short training periods and then send these workers back to their home country to do the work of Americans.
- The bill would also give the Department of Labour enhanced authority to review, investigate and audit employer compliance as well as to penalise fraudulent or abusive conduct.
- The Grassley-Durbin reform bill proposes for the first time to prioritise the annual allocation of H-1B visas.
- In addition, the bill includes establishment of a wage floor for L-1 workers; authority for the Department of Homeland Security to investigate, audit and enforce compliance with L-1 program requirements; and a change to the definition of "specialized knowledge" to ensure that L-1 visas are reserved only for truly key personnel.

This bill, if passed, could affect Indian Software sector.

ii) Issue of visa fee hikes in US: The IT industry continues to battle as mobility Issues continue to pose challenges in developed economies. The recent imposition of supplemental visa fees that so-called 50:50 companies (with at least 50 employees in the U.S. and more than 50 per cent of their employees on visas) have to pay on H-1B and L-1 petitions, would have an impact in the range of US$ 399 - 575 million per year (including H-1B and L-1 new visas and extensions) and if amended petitions for change in locations of these visa holders are included, then the overall impact could be in the range of US$ 758-1083 million per year. In comparison, the earlier figure till September 2015 was in the range of US$ 75-120 million per year. Such market access barriers pose further challenges to the software sector.

b) **Competitiveness Issue of Indian Software**: There is the issue of Indian Software sector losing out in competitiveness from emerging competitors. There is a need to focus on high-end software products. Even in the BPO sector, China, and Philippines have become major competitors. India is facing competition from these countries, besides Malaysia, East European and Latin American countries.

c) **Need to promote our own domestic "Apps**" India has a potential to develop apps unique to India. As stated by an ICRIER study (2014), this potential can be unlocked if network coverage increases, smartphone penetration continues to rise and the 'absorptive capacity' of the Indian population towards new technology grows through schemes that promote digital awareness and literacy. All major players have a role to play in achieving the growth of locally relevant content. Telecom operators have an imperative to increase 3G deployment or leapfrog into newer generation technologies. Original equipment manufacturers and app developers must collaborate to create and ensure that locally relevant apps can run on a variety of mobile devices sold across India. The Government and Reserve Bank of India need to see that the policy framework is favourable by re-evaluating telecom regulation and mobile-payment policies, respectively.

d) **Comprehensive approach to start-ups and entrepreneurship ecosystem**: The technology led start-ups today account for majority of startups in India and globally. In fact with the government leveraging technology for India's development needs, the country would need many of these entities to develop innovative solutions. There are several issues that hamper the growth of start-ups ranging from complex compliance, high incidence of tax and difficulties faced by investors. Policy Priorities for a flourishing start-up ecosystem would require simplified compliances and exemption from tax liabilities for the initial years, encouraging investors not only by simplifying compliances, but also by ensuring time bound processes. Realizing the importance of start-ups, the government has recently unveiled the Start-up Action Plan.

e) **Challenges for software product development**: India has to move to higher levels in software sector i.e. software product development. But there are challenges in this area which include the following. Software product taxation is already plagued by dual levies of VAT and service tax and emerging business models leveraging cloud for delivery can further complicate it. GST is the promised solution for this problem and therefore there is a need to ensure clarity under proposed GST regime. There are also difficulties in realising payments for subscription based business models related to pay per use of hosted software products through credit cards. The issue of collateral also poses difficulties to software product developers.

f) **E-commerce**: Technology enabled businesses like e-commerce are a reality and have been disrupting business models and operations, globally. In India also Ecommerce related taxation, require clarifications as currently, several states are either proposing or have introduced taxation specific to e-commerce transactions which could impact adoption of tech-platforms for businesses.

g) **Difficulty in doing business with Government**: The Industry is a key partner in various flagship initiatives of the government like Digital India, Smart Cities, Skill India, etc. But it has outstanding dues in excess of RS. 3000 crores today attributed to their business with various government entities. This needs to be settled at the earliest as private sector may lose interest in government's initiatives. Smaller firms would be affected more as payment delays affect their cash flows.

h) **R&D Investment**: Incentives to IT Industry for investment in core & non-routine R&D could be given in the light of international best practices and as extended to Bio-tech sector in India which is 200 per cent weighted deduction of R&D expenditure (capital & revenue). Many countries like UK, Canada, Israel, Germany and Ireland consider R&D activities as eligible for R&D benefits. In the UK, development of new software products and systems normally involved the resolution of technological challenges, and enhancements arising out of change in technologies, standards etc. Sample qualifying

R&D activities for the purpose of software product activities in UK are given in Box 1. As stated in the Deloitte document (2014), in UK the R&D benefits are as follows:-

- Large companies:
  - 130 per cent super deduction; or
  - 10 per cent (taxable) credit (from 1 April 2013).
- SMEs: 225 per cent super deduction (200 per cent before 1 April 2012); and
- Cash credits:
  - Cash credits are available for SMEs in loss position, up to 24.75 per cent of the qualifying expenditure, (25 per cent before 1 April 2012).
  - Large companies: Cash credits (subject to a cap) are available for large companies under the new R&D expenditure credit scheme if a company does not have corporate tax liabilities.

R&D benefits, if extended to IT sector as in other countries will help the sector as it will not be at a disadvantage as compared to others.

Box 1: Sample Software product activities qualifying for R&D in UK

1. Development of new technologies, solutions, architecture, customized integration designs, protocols, specialized components and packages.
2. Making noticeable improvements to existing systems – performance, security, scalability and availability.
3. Redesigning existing systems using fundamentally different technologies e.g. redesigning legacy monolithic system into modular / modern service oriented architecture using Java / NET Technologies or re-architecting systems to enable shared access via SaaS, Cloud services.
4. Developing digital applications that may include software such as mobile communications software for delivering multimedia entertainment, video or Internet games that are increasingly interactive and with more realistic graphics or multimedia communications software in support of digital, hi-definition or interactive entertainment.
5. Developing new or improved data processing solutions such as those required in malware detection, security and data warehouse systems which must analyse and interpret large quantities of diverse data.
6. Providing better risk management solutions and analytics to support financial services through the use of simulations and design and incorporation of complex mathematical models.
7. Developing flexible, high quality and scalable engines to manage and automate complex business rules and work-flow.
8. Developing message oriented middleware and information brokers capable of handling asynchronous communications with near real-time or synchronous results.
9. Systems integration work that involves
   a. The unexpected behavior of individual components;
   b. Inadequate or incomplete information about components; and
   c. Unexpected behaviour between or amongst components.

Source: Deloitte https://www2.deloitte.com/content/dam/Deloitte/uk/Documents/tax/deloitte-uk-tax-software-atl-13.pdf

i) **Extension of SEIS scheme benefit to IT including software**: The Services Exports from India Scheme (SEIS) of the Foreign Trade Policy does not include STPI units and IT sector in general. STPI units have been left out, making them uncompetitive in comparison to eligible SEZ units. The sector is expanding with startup and small companies developing innovative software products and solutions. With the proposed phasing out of SEZ benefits and phased out STPI exemptions, the software sector will not have any targeted incentives. The SEIS scheme could be extended to IT sector including software sector.

j) **Uniformity in Exchange rates calculations:** Exchange rate calculations differ for different taxes like service tax, income tax, customs duty, etc. There is a need to examine whether these could be made uniform as a facilitative measure.

k) **Transfer pricing**: In the Finance Act 2015, the threshold for applicability of domestic transfer pricing was raised from Rs.5 crore to Rs.20 crore. However several important legislative changes announced in the budget are awaited. CBDT guidelines on foreign tax credit, reporting norms, transfer pricing rules, rules on the place of effective management are some of them. These issues need to be sorted out quickly. The safe harbor provisions, meant to offer relief to small and medium companies has not really taken off as prescribed margins in the range of 20 - 30 per cent are considered too high by the companies.

l) **Exit Route from STPs**: Exit route from Software Technology Parks (STPs) is very difficult. This needs to be streamlined.

m) **Need for relief and rehabilitation for IT companies in Chennai**: The Chennai floods have led to devastation of many IT firms. Rehabilitation and relief is needed both for workers and the firms. Waiver of customs duty and tax relief could be considered with sunset clauses.

4. <u>Healthcare Services including Medical Tourism</u>

- India has a great potential for export of healthcare services particularly superspeciality healthcare by both consumption abroad mode (medical tourism) and even by cross-border mode (tele-medicine) and commercial presence mode with some major Indian hospitals having set up hospitals abroad. Among these, consumption abroad mode or medical tourism is the most important mode for India.

- The Indian medical value travel industry is presently at a nascent stage, but has emerged as the fastest growing segment of tourism industry despite the global economic downturn. In Asia, India follows Thailand and Singapore in terms of growth in medical tourism. Medical tourists are still a small fraction of the 7 million foreigners who travel to India annually, though there is plenty of scope for expansion with both health and travel being large sectors of the economy.

- As stated in a recent FICCI- KPMG study, global medical tourism is a US$ 10.5 billion industry estimated to grow to US$ 32.5 billion over the next 5 years at a CAGR of 17.9 percent during 2013-19. Medical tourism involves multiple sectors like the hospitality, tourism, transport and logistics, aviation, and healthcare delivery. Medical tourism leverages value from these sectors, and thus help drive growth that is not just restricted to one sector. India has an edge globally in terms of its cost effectiveness for super specialty medical care as can be seen in Table 10.

Table 10: Superspeciality Medical Care: Comparative costs of India and some competitors

PROCEDURES	USA	INDIA	SOUTH KOREA	U.A.E	SINGAPORE	THAILAND
Heart Bypass	$130,000	$8,800	$31,700	$40,900	$18,500	$11,000
Heart Valve Replacement	$160,000	$9,500	$42,000	$50,000	$12,500	$10,000
Hip Replacement	$43,000	$9,200	$10,000	$40,000	$12,000	$12,000
Knee Replacement	$40,000	$8,500	$11,800	$40,200	$13,000	$10,000

Source: Based on KPMG-FICCI (2014) and inputs from Healthcare Service providers

- Another advantage in India is that there are almost no waiting time, as compared to nations like UK, Australia, New Zealand and Canada, where for a non-life threatening condition, a patient may have to wait for over a year in some cases to have surgery performed. The waiting time for critical surgical interventions in countries like UK can be from 6 months to 1 year as there is a huge gap between the number of patients who require treatment and the healthcare infrastructure available, to cater to them.

- However, India has been fragmented in its approach, where individual hospitals have been promoting themselves as the hospital destinations. Our Asian neighbours have taken many initiatives to promote medical tourism, some of which can be emulated by India (Box 2).

Box 2: Initiatives to promote Medical Tourism by some Asian countries

Thailand:

- The Tourism Authority of Thailand (TAT) has a detailed medical tourism website to highlight popular treatment options and reputed hospitals for medical tourists. The TAT promotes medical tourism through online e-marketing campaigns and organizing familiarization tours to major global news agencies for showcasing available medical and wellness treatments.
- Visa for tourists is available on arrival in Thailand. Further, the Government has permitted for patients to be picked up directly from the aircraft and immigration facilitated at the hospital itself in case of emergency cases. The Government has facilitated hospitals to have kiosks for patients to check in at the airport itself.
- A new global advertising campaign called "Thailand Extreme Makeover" from the Tourism Authority of Thailand aims to attract medical tourists via the internet. The campaign is part of the government's aim to promote Thailand as the leading medical tourism country in Asia.

Singapore

- Singapore created ‘Singapore Medicine’ in 2003, a government-industry partnership comprising the country’s Ministry of Health, tourism board, and other stakeholders to promote medical tourism.
- The Singapore government is also promoting medical tourism by signing agreements with the governments of countries such as the UAE and Bahrain.
- The Singapore Tourism Board (STB) works closely with private healthcare providers to strengthen their position in target markets.

Malaysia

- In 2009, the Malaysian government established the Malaysia Healthcare Travel Council (MHTC) to develop the healthcare travel industry and promote Malaysia as a preferred destination for healthcare tourism in the region.
- MHTC works closely with private healthcare players and relevant government agencies to help ensure quality care and ease the entry of medical tourists into Malaysia.
- The government has launched the medical tourism concierge and lounge at the Kuala Lumpur International Airport to provide healthcare service information as well as information on transportation, accommodation, and travel within the country.

Taiwan

- In 2007, the government established the Taiwan Task Force on Medical Travel (TTFMT) to promote the country as a preferred medical travel destination.
- Steps such as e-visa service for Chinese tourists to visit Taiwan for physical check-ups, cosmetic surgery, and anti-ageing treatments, establishing health centres at the airports to provide medical consultation to tourists were taken to enhance medical tourism in the country.

Source: KPMG-FICCI (2014) and Healthcare Service providers

As stated in the FICCI – KPMG study, the leading destinations of medical tourism in India are Andhra Pradesh, Karnataka, New Delhi, Kerala, Tamil Nadu, and Maharashtra. Due to the establishment of some of the earliest medical schools in the southern states of India, healthcare infrastructure available here is of high standards. This has also resulted in the creation of a pool of clinical schools and entrepreneurial skills made available to the medical tourism industry to help facilitate growth at a faster pace than the rest of the states.

Some suggestions to promote Medical Tourism for India are the following:-

- <u>Medical tourism should be a part of Brand India Campaign:</u> Initiatives and platforms like "Incredible India" and "India Brand Equity Foundation", need to be leveraged to promote medical tourism. India should be promoted as a preferred destination for medical tourism via marketing campaigns, road shows, and networking meets. Indian healthcare needs to be positioned at the India pavilion in major trade fairs and shows including foreign missions.

- <u>Enhancing air connectivity, setting information centres and rapid immigration clearance at airports:</u> Air connectivity, rapid immigration and setting up of dedicated information desk for medical tourists across Indian airports as done by some of our Asian neighbours will enhance the patient experience.

- <u>Enhancing Basic Infrastructure at Airports for Medical tourists</u>: There is a need to provide special assistance like ramps, user-friendly lifts, special toilets, wheelchairs, strollers, ambulances and capabilities to handle medical emergencies at airports. Pick-up of patients at the aircraft and allowing immigration clearance at the hospital in case of emergency needs to be considered.

- <u>Promoting India as a healthcare centre for the aged:</u> The fact that India is a home to non-allopathic types of treatment like Ayurveda, Yoga, and Unani can be used in promoting geriatric healthcare.

- <u>Improvement in medical visa process:</u> At present Medical visas (M-visa) are generally issued by the Indian government to medical tourists, for a period of one year. The one year validity of an M-visa can be extended by an additional 12 months in some special cases. Medical cases with heart problem, organ transplants, ophthalmic disorders, and neuro-surgery are given priority. Earlier patients were allowed to visit only three times in a year during this extended time-frame, with a mandatory two-month gap between two entries. However, recent changes in the regulation have now lifted this two-month gap restriction, except for seven countries including China, Pakistan, and Bangladesh. The centre has also allowed granting free medical visas for Maldivian nationals for a period of 90 days. However, the visa application process is highly cumbersome as the patients are asked to report to the Indian embassy personally and furnish bank statements/medical reports, and are even referred to the embassy doctor for a second opinion. There is no special provision given to tourists who come to India to avail wellness facilities.

- <u>Extending eTV to medical tourists</u>**:** Formalities are tedious for medical tourists. There is a need to streamline them and extend e-tourist visas even to medical tourists. The medical tourist visa is three times costlier than the tourist visa and there is a need to consider reducing it.

- International accreditation for Indian hospitals**:** There is also a need to get international accreditation system for Indian institutions along with national standardized accreditation system which will give greater recognition for our medical institutions.

- Addressing exchange rate risk for medical tourists**:** In the case of the foreign patients at the time of admission, the hospital has to collect foreign currency and deposit it in the banks. After treatment, the remaining amount is to be paid in foreign currency to the overseas patients. This involves a huge amount of transaction cost and exchange rate risk. This issue needs to be addressed.

- Promoting telemedicine**:** Telemedicine has good scope in India particularly when patients have to be monitored during their recuperation post-surgery or post-treatment in their home country. But there is shortage of manpower which needs to be addressed.

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