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Theory and Operation of a Modern National Economy

Developing Service: what learn about trends in the developed countries

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A quarter of a century passed since the seminal work of Daniel Bell described what was considered a consistent vision of the future of our society. Unfortunately, the emphasis given by the author regarding to the employment aspect in the so called “post-industrial” society obscured his equally rich insights about the role of the innovation and the knowledge in inducing this kind of transformation on the economy. And, most important, the interpretations of his work misguide the debate about the role of the services in the new *paradigm* of production that was made possible by the new technologies available with the development of the microelectronic. By these interpretations, the services sector will dominate the economy, not only by the generation of a majority of the employment, but even by responding for the push on the economic growth.

Although “services” have become the magic word used to suggest that a new era of economics has begun, the transformations occurred during the last two decades suggest that researchers have to be more cautions about the naive view that avoids to look to the new created failures of the market, specially with the linkage among the

economies promoted by what has been called globalization. The radical transformation of the production and the competition are generating new opportunities of profits but are deepening the gap between riches and pours everywhere and demanding new kinds of regulations in strategic activities, that might be performed by the government.

Another important aspect to consider, nowadays, is the role of the information and the transformation that make it possible by the new ways of communication. Though then, even in the shantytowns of the poorest countries there are notable transformations in the expectation of the population – and this includes not only what they could expect about their jobs and the products that are available in the market, but what are considered as rights and duties of the citizens. This means that to keep democracy and market, both desirable aspects of our lives, an effort has to be done to understand how the transition to this “new world” is affecting different groups of the population and different economy. Only by doing this, it will be possible to rethink the role of the economic policy enforced by the governments in all levels, and achieve their major goal – increase productivity and compensate, or at least diminish the negative impacts of this period of economic transition.

The main objective of this text is to give an overall look of what is happening in the economy during the last decade, specially in the industrialized economies, focusing in how services are used to improve competitiveness and, as a consequence, creating new opportunities of work. The main argument is that improving the competitiveness of the economy is the ability of make strategic choices that increase productivity of the economic activities, allowing to preserve employment and, by doing this, making possible the gradual transition from a low skill and low paid structure of employment to a high skill and high wage structure.

To achieve this goal, this paper will summarize part of the large number of studies that have been done to understand the role of services in the dynamic of the economy,

and will show some of the results got in the industrialized economies, with a special attention to the role that is attributed to new services that is considered strategic to enhance competitiveness. As many of these activities are equally demanded by companies in other economies, as the Brazilian economy, it seems reasonable to think that the experience of the industrialized economy could be useful to this economy.

I – Understanding Services

The services have been growing faster than that the overall economy during the last two decades in the industrialized economies, although during the 90's this trend of expansion is smoothing. As a result of this, the share of this sector in the Gross Domestic Product has increased sharply and accounted for approximately 70% of GDP, with the exception of the Japanese economy where this sector recently reached 60% of GDP, and the Korean economy where this share still remains close to the 50% of GDP. In all these economies, during the same period, the share of manufacturing value added to GDP declined, representing an average of 20% of GDP.

Sectorial Contribution do GDP OECD - Selected Countries and Brazil 1987-1997

	% of GDP							
	Agriculture		Industry				Services ¹	
	1987	1997	Total		Manufacturing		1987	1997
France	3.5	2.3	29.6	26.2	21.4	19.3	66.9	71.5
Germany	1.4 ^e	1.1	34.6 ^{e,k}	29.1 ^k	28.9 ^{e,k}	23.6 ^k	64.0 ^{e,k}	69.9 ^k
Italy	4.1	2.6	34.1	30.5	23.4	20.1	61.9	66.9
Japan	2.8	1.9 ^a	40.4	37.9 ^a	28.1	24.3 ^a	56.8	60.2 ^a
Korea	10.1	5.7	42.6	42.9	31.4	25.7	47.2	51.4
Mexico	7.3 ^g	5.6 ^a	29.5 ^g	26.1 ^a	21.9 ^g	19.8 ^a	63.3 ^g	68.4 ^a
Spain	5.5	3.5 ^c	35.3	25.6 ^c	25.0	17.8 ^c	59.3	70.9 ^c
United Kingdom	1.7	1.7 ^d	32.2 ^m	27.5 ^{d,m}	21.0 ^m	18.8 ^{d,m}	66.1 ^m	70.8 ^{d,m}
United States	1.8 ^a	2.0	29.7 ⁿ	26.8 ^{a,n}	19.8	18.2 ^a	68.3 ^{a,p}	71.4 ^{a,n,p}
Brazil	10.2 ^h	7.6	41.0 ^h	33.3	...	...	48.9 ^h	59.1
São Paulo	3.5 ^h	4.7	44.5 ^h	36.4	...	...	52.0 ^h	58.9

Sources: National Accounts: 1984-96; 1985-1997, OECD, Paris 1998 e 1999; São Paulo -1998, Fundação Seade, 1999.

Notes: ... = not available; 1 - Includes import duties and others adjustments and excludes imputed bank; a - 1996; b - 1993; c - 1994; d - 1995; e - 1991; f - 1992; g - 1988; h - 1980; j - sewage services included under industry; k - publishing included under services; m - repair services of consumer durables other than clothing included under services; n - sanitary and similar services included under industry; p - includes government enterprises.

The cause of the rapid increase in output of the service sector stills remains an *incognito* to the researchers. There is some explanation that try to understand the shift to the services in the economy, but every one captures only part of the process. As indicated in large study sponsored by the Economic Council of Canada – ECC, there are four main explanation for this event: “first, that the consumer demand for services has increased faster than for goods; second, that labor productivity growth has been slower in service than in goods; third, that goods producers are now simply contracting out for services that were formerly produced in house; and fourth, that there has been strong growth in the intermediate demand for services as input to the production process” (ECC, 1991). After a careful exam of these aspects, the study arguments that, although each one of these explanations provides some increase in service activity, taken together, they cannot provide a convincing explanation of the growth in the overall service sector.

This study suggests a fifth possibility related to the “manufacturing matters” argument. This argument shows that the goods and services are very dependent on one another, that the expansion on goods industries results in an expansion of service, and that the expansion of service output results in an increase in demand for goods. The expansion of goods proportionately requires in this case more services as inputs, and this interdependence of goods and services, and particularly the fact that the increase in goods production requires the expansion of the service sector, may account for the increase in the overall proportion that services make up in GNP. Although this seems a good explanation, there are some aspects that are not quite convincing, as remember Melvin (1995), specially because the correlation between the behavior of the production of goods and the services did not show as strong as expected. In the recession period of the 80’s, for instance, the fall in the output of goods did not induce a larger fall in the output of services. However, by using this last explanation one can understand the rise of part of

these heterogeneous sector (specially telecommunication, transportation, trade, business services, for example) that are considered key elements to enhance the competitiveness of the economies.

As Cohen and Zysman (1987) emphatically argued by discussing the competitiveness of the American economy, having in mind that the production of services still remained dependent of the industrial-lies, it is important to understand how the new forms of production are changing the way services and goods are becoming complementary. By doing this could by possible understand how this complementary allowed to increase productivity and decreased costs as prices. The authors argument was built considering that when the industrial economy surpasses agricultural economy, that never means that a country that is producing manufactured goods left to produce primary goods, all the contrary, that means a larger amount of investments (by spreading the use of machinery, better seeds, and other procedures) and the reallocation of the most important factor – labor – that was needed to develop new industries. In the case of the role of the aggregations of activities that is called service the same argument is valid. For then, the potentialities demonstred by the new technologies (microelectronic, communication and information process) enhance the direct linkage among a substantial core of service employment that is tightly tied to manufacturing, but by the contrary “if a economy lose the mastery and control of manufacturing, the high paying service jobs that are directly linked to manufacturing will, in a few short rounds of product process innovation, seem to wither away” (Cohen & Zysman, 1987).

This new perspective of understanding the transformations in the economy suggested the necessity of a more accurate definition of what services are, because, in reality, we want to understand what the strategic approach of some of the new way of increase productivity is.

Defining services: the difficulty is still there

How to define service is relatively old problem that still remains like that although many attempts done in this direction (Riddlle, D. 1986, and Delaunay and Gadrey, 1991). The heterogeneity of activities that are classified under this section is a clear obstacle to the ability of differentiating goods and services, and to achieve a comprehensive classification of activities.

The main characteristic that is used to differentiate these activities remains the distinctions between tangibility and intangibility (that means the possibility of touch the product that one was buying or not). Although others aspects have being considered as equally important, specially the storability and the transferability. Usually if the product of the activity has these three characteristics, it is considered as a good and otherwise a service. In that case, service still is perceived as a negative definition.

The recent attempts to elaborate more abroad definitions try to introduce the relationship between producers and consumers, suggesting that in the case of services the direct contact is necessary (Gadrey, 1992). The new technologies, in this case, are somehow changing this perception, by allowing the virtual communication between the agents.

Others, as Melvin (1995) discuss the confusing cause by the poor discrimination between the intermediation activity and the thing being intermediated. For instance, the output of the transportation of a certain good (say furniture) between cities is not the good but the activity *per se*. Nonetheless some industry have a lot of problems in making this kind of discrimination and are unable to declare the value added of his different activities, bank activities still have a lot of problem to have his "production" measured.

Showed the difficulties caused by the lake of definition of what are services, the option of many researchers was directed in building operative ways to analyze different services

(Griliches, 1992 and Inman, 1985), and others try to propose changes in the classification distinguishing the services by the functions associates to each activity. The figure below summarized a large group of attempts of accomplish this goal.

The results, although interesting and suggestive, indicate the large road that might be accomplished to understand the differentiation between activities, and seem to avoid important aspect of the measurement of services, like the auxiliary activities that are doing *in house* by the companies, that are not present in the accountability that is used by the companies, and by this way underestimate the amount of service that are produced.

Summary of Alternate Classification Systems
<p>Production-based Classification</p> <p>Fisher-Clack (1935/1940)</p> <ul style="list-style-type: none"> • Primary (agriculture, mining) • Secondary (manufacturing) • Tertiary (residual) <p>Sabolo (1975)</p> <ul style="list-style-type: none"> • Primary (agriculture, stock raising, fisheries) • Non- primary • High use of capital and skills (transport, mining, manufacturing) • Low use of capital and skills (trade) • High use of skills, low use of capital (finance) <p>Fuchs (1968)</p> <ul style="list-style-type: none"> • Agriculture • Industry (mining, manufacturing, transportation, utilities) • Services (commerce, business, government) <p>Consumption-based Classification (service portion)</p> <p>Singer (1981)</p> <ul style="list-style-type: none"> • Production services • Collective consumption • Individual consumption <p>Function-based Classification (service portion)</p> <p>Foot and Hatt (1953)</p> <ul style="list-style-type: none"> • Tertiary (restaurants, hotels, repair and maintenance, laundry) • Quarternary (transportation, communication, commerce, finance) • Quinary (health, education, recreation) <p>Katouzian (1970)</p> <ul style="list-style-type: none"> • Complementary services (finance, transportation, commerce) • New services (health, education, entertainment) • Old services (Domestic) <p>Browning and Singelmann (1975)</p> <ul style="list-style-type: none"> • Distributive services (transportation, communication, commerce) • Producer services (finance, professional) • Social services (health, education, defense) • Personal services (domestic, hotels, restaurants, leisure) <p>U.S. Census Bureau</p> <ul style="list-style-type: none"> • Transportation, communication, utilities • Wholesale and retail trade • Finance, insurance and real state • Service (personal and business)

Source: Riddle, D. 1986

Another aspect that are not considered by these classification is the discrimination of a large number of new services that are been developed to allow the process of contracting out of the firms, specially the conglomerates, in their attempt to focus their production of goods or services in core activities, aiming to reduce variable and fix costs. Although there were few primary researches in this field, the results are insufficient to allow the construction of a new classification, allowing the analyst of service to use certain terms with very little accuracy.

Accepting this kind of limitation of definition and classification, still it is possible to indicate the more dynamic activities in services. On the last decade the branch of services that are expanded more output and employment are Finance, Insurance, and Real State and Business Services¹. In the main OECD countries, this group of service represents, in average 20% of GDP, quite similar to the average share represented by the manufacturing industry. As is known, this is the group of services that has experienced a great transformation, specially with the incorporation in its routine activities of communication and informational new technologies, and by rationalizing methods of work (banks are the main case, but not the only one) what increased productivity and output².

There is no similar increase in others activities, and when there is a positive result seam less expressive. Except for Spain there is a decrease of share in the group of Wholesales and Retail Trade, Restaurants and Hotels to the most important OECD countries. If considered the share of Community, Social and Personal Services³ or even in

¹ Financial Institutions, Insurance, Real State and Business Services, including machinery and equipment rental and leasing, compose this group of services.

² In Brazilian economy is quite remarkable the increase of the share of this activities (Finance and Business Service) on GDP, although still highly concentrate in the city of São Paulo, and with a relative low impact on employment, because of the rationalization of the activities and the business cycles.

³ Motion picture and other entertainment services; amusement and recreational services; repair services; laundries, laundry services, and cleaning and dyeing plants; domestic services; miscellaneous personal

Services Produced by Government⁴ most of the countries has experienced a decrease of activities, and that results in the reduction of their share in the product⁵.

**Contribution to GDP of different types of Services
OECD - Select Countries
1987-97**

	Wholesale and Retail, Trade, Restaurants And Hotel - I		Transportation, Storage and Communication - II		Finance, Insurance Real State and Business Services – III		Community, Social and Personal Services -IV		% of GDP Producers of Government Services - V	
	1987	1997	1987	1997	1987	1997	1987	1997	1987	1997
	France	14.9	14.7	6.0	5.7	20.4	22.9	5.2 ^t	6.2 ^t	16.4 ^t	17.4^{t}
Germany	...	...	5.4 ^g	5.0	11.3 ^{g,p}	14.0 ^p	...	...	11.1 ^g	10.8
Italy	19.1 ^c	18.4 ^c	5.6	6.5	22.5 ^r	27.0 ^r	0.8 ^r	1.0 ^r	12.2	12.2
Japan	13.5 ^a	11.1 ^{ab}	6.7	6.7 ^b	16.6 ^q	17.9 ^{b,q}	16.4 ^{a,q}	19.7 ^{a,b,q}	8.1	8.0 ^b
Korea	14.3	11.3	7.1	7.3	12.2	17.6	5.4	7.1	6.7	8.3
Mexico	23.3 ^k	19.7 ^b	8.7 ^k	9.3 ^b	10.0 ^k	15.9 ^b	10.5 ^k	12.5 ^b	4.1 ^k	5.0 ^b
Spain	20.1	22.6 ^e	5.5	5.7 ^e	16.7	17.6 ^e	5.7	0.9 ^e	11.4	12.8 ^e
United Kingdom	11.7 ^h	12.5 ^{f,h}	7.1	7.3 ^f	18.8	22.3 ^f	4.9 ^h	9.6 ^{f,h}	12.6	9.7 ^f
United States	16.9	16.8 ^b	6.3	5.9 ^b	25.5	28.6 ^b	9.8 ^v	11.5 ^{b,v}	11.8	11.4 ^b

Sources: National Accounts: 1984-96; 1985-1997, OECD, Paris 1998 e 1999; São Paulo -1998, Fundação Seade, 1999.

Notes: ... = not available; 1 - Includes others producers; a - Restaurants and hotels are included in IV; b - 1996; c - Recovery and repair services include in Wholesales and retail trade; d - 1993; e - 1994; f - 1995; g - 1991; h - Repair services of consumer durables other than clothing included in wholesale and retail trade; j - 1992; k - 1988; m - 1985; n - real estate and business services included in IV; p - business services and real estate except dwellings included in IV; q - business services included in IV; r - community, social and personal services included in III; s - excludes sewerage services; t - other producers included in V; u - educational services included in V; v - excludes sanitary and similar services.

The employment created by the service activity is even more expressive than that the share of output of this sector. Although the difficulties to compare data, the areas where there is happening a net increase is concentrated show different movements in the different countries. The main increase of the share of employment appears to be in the area where the improvement of productivity will suggest a reduction of occupations:

services; private educational services, private health services; private welfare institutions; business, professional and labor associations compose this group of services.

⁴ Public administration and defense; public educational services; public research and scientific institutes; public medical, dental, other health and veterinary services; public welfare institutions; libraries, public museums botanical and zoological gardens, and others cultural services not elsewhere classified mainly form this group of services.

Finance, Insurance, Real State and Business Services. This group of activities aggregates jobs with high skill and relative low skill, but usually has a better average of wages than others groups, except Health and Public Administration.

In France, the two most important group of service to create employment, in the last decade, was the Government Services and the Wholesale and Retail, Trade, Restaurant and hotel. In Italy, United Kingdom and United States, on the contrary was Finance, Insurance, Real State and Business Service and Community, Social and Personal Services.

**Contribution to Employment of different types of Services
OECD - Select Countries
1987-97**

	% of Total Employment									
	Wholesale and Retail, Trade, Restaurant, hotel - I		Transportation, Storage and Communication – II		Finance, Insurance Real State and Business Services – III		Community, Social and Personal Services -IV		Producers of Government Services – V	
	1987	1997	1987	1997	1987	1997	1987	1997	1987	1997
France	17.3	17.7	5.8	5.7	11.5	9.3	6.1	7.4	25.4 ^p	28.4 ^p
Germany	...	...	6.0 ^e	5.4	2.7 ^{e,h}	3.0 ^h	...	...	15.9 ^e	15.3
Italy	21.5 ^b	22.0 ^b	6.3	6.2	13.4 ^j	16.7 ^j	2.6 ^j	3.4 ^j	15.5	15.8
Japan	18.0 ^d	16.7 ^{ad}	5.5	5.7 ^a	4.6	4.6 ^a	22.0 ^d	26.3 ^{a,d}	6.4	6.0 ^a
Korea	...	...	...	...	...	...	...	...	...	...
Mexico	...	...	...	...	...	...	...	...	...	...
Spain	22.0 ^b	23.4 ^{b,f}	5.8	5.8 ^f	4.6	2.3 ^f	9.0	3.8 ^f	13.8	16.7 ^c
United Kingdom	19.7	19.6 ^g	5.8	5.6 ^g	10.3	11.9 ^g	9.6	11.8 ^g	21.5 ^q	16.9 ^{g,q}
United States	22.9	22.7 ^a	4.2	4.4 ^a	14.1	15.9 ^a	15.1 ^m	18.1 ^{a,m}	14.5	13.4 ^a

Sources: National Accounts: 1984-96; 1985-1997, OECD, Paris 1998 e 1999; São Paulo -1998, Fundação Seade, 1999.

Notes: ... = not available; 1 - Includes others producers; a - 1996; b -recovery and repair services included in wholesale and retail trade; c - 1995; d - Restaurants and hotels are included in IV; e - 1991; f - 1994; g - 1990; h - business services included in IV; j - community, social and personal services included in III - 1992; k - educational services included in V; m - excluding sanitary and similar services; p - others producers included in V; q - industries of general government included under V.

This kind of result, in certain way, have been used to oppose two different approach of economic policy, and definition of the role of the government supporting the private sector activities. On one side the government provides jobs, in average, higher skill and better paid, in general creating opportunities for women and young people. This

⁵ To the Brazilian economy, Community, Social and Personal Services remains the most important group source of new employment, especially domestic services and non-paid employment in urban and rural

attempt focus in the ability of counterbalance the imbalance of wealth and access to public goods – as education, health and security – among the resident population, generate by the high paid activities in finance and some of the business services.

On the other side, the expansion of private activities with high salaries enhance the gap of wealth and access to public goods, even if there is the expansion of the share of employment in Community, social and personal services, where usually are concentrated the low skill and low wage jobs. This results appears to be linked on different economic trend of the overall economy, in special on the United States that have experienced a long period of continuous growth⁶.

A recent study of detail data about employment in United State suggests that “contrary to common assumptions, there was a significant decline in the number of domestic, cleaning and food service jobs in the United States during the 1980’s. Two-thirds of the jobs created in the United States in the period 1990-95 have been in sectors where wages are above average. The most dramatic increase in employment has occurred in industrial services, medical services and financial occupations. (Cohen, 1998)

And comparing this situation to the case of France – an opposite situation - the author concludes, “the gradual disappearance of unskilled jobs is directly linked to the tertiarization the French economy experienced in the 1970’s and the 1980’s. This is clear from the results of a study conducted by Dominique Goux and Eric Maurin of the French National Institute of Statistics. According to Goux and Maurin, the falling demand for unskilled labor in France in the 1980s is not mysterious at all: it is essentially due to the evolution of employment toward a structure that is not unlike the structure that prevailed in

activities.

⁶ Is basic having in mind that the weigh and the size of the economies used in this comparison are strongly different. The United States represents 35.3% of the Gross Domestic Product created in OECD counties. France and Italy, only 5.4% each. This is important because characterize economic differences in the ability of generate dynamic push inside the country, and induce different needs and role to the government.

the United States approximately a decade earlier".(Cohen, 1998). These results seem to indicate that, although with differences the trend is similar in the different countries that are enhance the competitiveness of the economy by developing new kind of services.

As sid before, the aggregation of different types of services could shadow important aspects of the transformation of activities and employment in services. The main problem regards the difficulties to show which kind of linkage bound manufacturing firms and services, that is the reason why studies that try to indicate which are the purchases of services by the companies in others industry became part of the agenda for research on the services. (Fuchs, 1985)

As showed in the case of OECD counties (Sassen and Orloff, 1997), the linkage is changing with the increase of the role of new informational services and the enhance of the process of *contracting out* not only traditional services, but new activities developed to solve specific problems. For these countries, the major problems related with communications, transportation and others basic infrastructure facilities are solved, almost the opposite situation that happens in the others countries, specially the less industrialized and the poorest.⁷

On OECD's countries, among the services which have grown in importance in recent years and have become an integral part of the business infrastructure for firms in general and for manufacturing firms in particular are a little-known, and as yet insufficiently researched, group of strategic business services. These services are proving to be key elements for firm-level competitiveness and an important source of growth and dynamism

⁷ Selected indicator on communications and information show the differences among high-income countries and, for instance Latin America and Caribbean countries. On the first group of countries, per 1.000 people, there is 286 daily news paper, 1,3000 radios, 664 television sets, 552 telephone main lines, 188 mobile telephones, 269.4 personal computers and, per 10.000 people, 470.1 internet hosts. On the second group, to the same indicator the results are: 71, 414, 263, 110, 26, 31.6, and 9.64. World Development Report 1999/2000.

in their own right, as was recognized in the 1999 OECD Ministerial Council Meeting when new services were identified as one of the driving long-term growth factors.

The OECD's Industry Committee sponsored an analytical study⁸ based on a group of five strategic business services believed to be essential for business processes, firm competitiveness and growth: computer software and information processing services, R&D and technical testing services, marketing services, business organization services (comprising management advise and labor recruitment services) and human resource development services. Other important business services, such as engineering consulting, were not included. Although there is an incomplete information, the turnover for these selected strategic business services reported by 19 countries amounted to approximately USD 1.1 trillion in 1995. (OECD, 1999)

Computer services generated the largest share of turnover in the total, accounting for approximately 32%. The second largest category of business services in turnover terms was business organization services (USD 290 billion), Marketing services (USD 242 billion), R&D and technical testing services amounted to USD 192 billion, management advise services (USD 158 billion) and labor recruitment services (USD 108 billion).

The information collected shows that the growth of these business services, by whatever measurement, has been robust in general and in many cases spectacular in recent years, even in those years when overall economic growth was slow or absent, in Finland, United Kingdom, France (for strategic business services expanded by 19% between 1993 and 1995). According to this study, in the United States, the growth in turnover for these activities was estimated at 50% between 1990 and 1995. In Japan,

⁸ This part of the paper is based on the large work released in 1999 by the OECD relatively to the Strategic Business Service.

increased by 28% between 1989 and 1994, and in Canada, 23% for the period 1993-95. Nonetheless their share in GDP still is above 3%.

The drive of this growth have been the outsourcing, that means shifting the firm's value-added functions or activities to external suppliers, affecting activities such as R&D and design, human resources, management and production operations and marketing, seems to be a major drive. This strategy is motivated by various objectives: decrease the concentration of firm and management resources on core activities, increase specialization of outsource functions, cost reduction, but includes also reducing and controlling operating costs, improving company focus, gaining access to world-class capabilities, freeing up internal resources for other purposes, gaining access to resources not available internally, accelerating benefits from reengineering, improving efficiency of functions which are difficult to manage, making capital available for other purposes, reducing or sharing risks, providing a cash infusion (The Outsourcing Institute, 1998).

Surveys in the United States by The Outsourcing Institute (1997) showed that companies which outsource services, usually the biggest, are also financially more stable than the average, and affect manufacturers account for nearly two-thirds of all outsourcing, information services companies (telecommunications and technology companies). There are indications that a similar process is appearing in Europe, the most active markets been in France, Italy and the United Kingdom.

In Japan, outsourcing is generally expected to continue growing on information services (software and hardware supply, system operation and maintenance), labor recruitment/provision of personnel, vocational education and job training, personnel management, human resources, R&D, planning, design, management advise and marketing, as well as professional services (legal, accounting and taxation advise), security, etc. Future demand in Japan for strategic business services (in descending order)

was expected in: information services, logistics, business assistance services (advise), training, advertising/marketing, professional services (MITI, 1995).

The same Japanese survey showed that the following functions are most likely to be outsourced from the business sector: job training, information systems, production processes, accountancy and tax, R&D (MITI, 1997). The motives given by users are: promotion of specialization in areas such as expanding the information network, improving human resource functions and employment-related benefits for workers, performance evaluation (65%); cost saving in areas such as responding to business fluctuations and restructuring (50%); improving business efficiency in areas such as concentrating on core activities, diversification of risk, improving flexibility, accelerating new business formation (36%).

A number of broad trends have recently been seen in outsourcing, all of which are reshaping strategic business service firms and industries. Outsourcing firms are increasing multi-sourcing arrangements, with closer relationships between service purchasers and service suppliers and greater involvement of service suppliers in core functions at the heart of business processes. This is likely to favor large international firms offering a range of strategic services. Outsourcing is moving well beyond information technology and data processing, as demonstrated by a very rapid growth in logistics, human resources, and back-office operations. Large service suppliers, such as the international accounting and consulting firms, are stepping in from their traditional bases to provide new services and new bundles of strategic services.

Compare with Brazilian situation is possible to find many similarities. Even in Brazil, where the process of reorganization of the industrial activities remains incomplete and almost unknown in some sector, the informational services are the most important service that is introduced in the purchase of industrial firms. The process of contracting out

other kind of services, although different attempts improved by the largest firms, still remain restrict to an auxiliary or secondary tasks. In a study done in the State of São Paulo, with almost 33.000 companies, in 1996 it was possible to understand part of the logic of the contracting out services by companies in multiple industries – manufacturing, building, commerce and finance enterprises.

The majority of the firms contract out traditional services, like accountability and lawyers, but only the big one contract out partially new services. In some cases, they start to produce in-house during the period of transition to new process of production. It is important to remember that except for the traditional services contracting out, great part of the firms still are familiar or small, and did not use this new service with the regularity that make corporations establish entire departments or even secondary firms (Montagner et alli, 1999).

In the case of Brazil, there is a relatively concentrate utilization of contracting out – the manufacturing industry, large supermarkets and banks and others finance companies. The companies in these sectors are large and tend to follow the patterns of their competitors in the international market. Nonetheless, the small utilization of the contracting out in new services could be associated with the difficulties of finding, in the national market, companies that can provide specific services without compromise key information about the capability of the competition of the firm. In many cases, the Brazilian companies made the option for contract employees for developed in-house services, as in other countries.

As is known pure cross-border trade⁹ in business services remains difficult and usually means a foreign direct investment rather than pure cross-border trade. The

⁹ That means the provision of a service via a business letter, a business report, a telephone conversation, computer-to-computer transfer of electronic information via telecommunication or similar means.

reasons are a combinations of technological, economic and regulatory factors. Much of the process of production in business services remains embedded in the direct relationship between clients and producers (examples are the time spend by the systems analysts and programming manager who produce customized software with their clients). If quality is important, service and local tastes and customs has become a formidable competitive weapon, business service producers simply need a local based operation; besides there are regulatory reasons that make the pure cross-border trade not possible.

Other important difference that affects the use of services are the small and medium enterprises (SME) in Brazil, and as in other countries there are a clear necessity of building new form of production that allow them to incorporate this new services (management, consult, marketing, R&D, etc) to improve the competitiveness of the economy. This bring the focus of this paper to another aspect, that was neglected in the recent past: the role of the cities and the possible differentiation that seams to be observed among the specialists.

Cohen and Zysman (1987) argument that even when the manufacturing sector may have ceased to be a dominant sector in major cities, it remains the source of the economic dynamic. Indeed, several scholars have argued that the producers services could not exit without manufacturing. This position creates an important debate where there are at least two others positions – Drennan (1992), a leading analyst of the producer services sector in New York City, argues that a strong finance and producer services sector is possible in New York, notwithstanding decline in its industrial base, and that these sectors are so strongly integrated into the world markets that an articulation with the larger region becomes secondary.

Sassen (1991), by other way, shows that although manufacturing feeds the growth of the producer services sector, it does so whether located in the area in question,

somewhere else or overseas for the global-level firms. Thus, whether a manufacturing plant is located offshore or within a country, it may be quite irrelevant as long as it is a part of a multinational corporation likely to buy the services from those top-level firms. Secondly, the territorial dispersal of plants, especially international, actually raises the demand for producer services. To Sassen the major forces shaping economic space are telematics and globalization. Both aspects have been inducing the formation of new “centralities” at the inter-urban level, namely New York, London, Tokyo, Paris, Frankfurt, Zurich, Amsterdam, Los Angeles, Sydney, Hong Kong, and includes also cities such São Paulo and Mexico City.

“The intensity of the transactions among these cities, particularly through the financial markets, trade services, and investments, has increased sharply, and so have the orders of magnitude involved. And this has been enhance the inequality in the concentration of strategic resources and activities between this cities and others in their respective countries” (Sassen, 1998a).

These situations are different, but suggest to the researchers that the major trend of the producer services is an unexpected concentration in the central cities, because of the agglomeration economies and highly innovative environment that are offered. It is becoming clear that, in this case, the key relationship is not the one that concerns the professional and the client, but rather the professional and other high-skill professional that could help to solve a problem using all sort of expertise (legal and economic consulting, communication, advertising, designers, printers, public relations, etc).

These kind of necessities are the reason why the author indicates that for this kind of service the agglomeration in the cities is crucial rather than a suburban office park, although theory suggests that could be different, with high skilled professionals working in their home on the suburban areas to avoid traffic, pollution and others nasty aspects of the

living in the big agglomerations. According to Sassen, the dispersion of the factories would make indispensable the increase of the conventional infrastructure to support the use of telematic, informational, what means more airports (international networks) but also more trains and cars (regional or metropolitan networks).

This hypothetical, although reasonable, development point to how the concentration of expertise and infrastructure articulate two others aspects concern the service sector: the reconfiguration of the state and the consumption in the cities.

As Calabrese and Burgelman (1999) point out there are few consensus about the new shape of the state, especially because the concentration of power in the national level have been shaken in support of the local power and the global power, nonetheless still is the national level the space that can enforce legal regimes, one of the most important tools to allow contracts, which means business, and this has much more to do with reshape this level of government and the capability of coordination creating a new type of order.

One major aspect of this process, specially in the less developed countries, in the privatization process the state became the owner of a lot of enterprises. There is a large group of works showing the benefits of the privatization of state enterprise all over the world (see web site of World Bank). The main argument that is clear is the necessity of increase competitiveness in areas where the new technologies multiply the use of old structures (communication, electrical energy distribution are good examples) or literally introduces a substitute (wireless phones and traditional telephone). In this case the private sector can contribute with its experience, improving productivity and reducing costs and prices. One important aspect is the possibility of learn with the bad experience avoiding the persistence in the lake of rules.

The major aspect on this subject seems to be able to create regulatory agencies and enforce the rules that might protect the citizens and at same time the economic

environment of the abuses of power of corporation that acted globally. Another issue is the enhance of the ability of provide the incentives that could guarantee the preservation and the growth of the infrastructure required by the economy, an activity that involves high levels of coordination and enforcement.

On the other hand, still remains important the role of some economic policy to support the development of some activities, as enhance the role of regulatory agency to avoid monopoly and abuse of economic power of private companies; in the case of some key services that contribute to the increase of productivity and competitiveness of the national economies, is possible even endorse others approach, as described in the recent study produced by OECD (1999). Business services and, indirectly, industry are covered in a comprehensive policy framework with the following objectives: i) productivity improvement; ii) promotion of employment possibilities; iii) improved competition (outsourcing); iv) promotion of industrial co-operation; v) promotion of the supply of and the demand for business services; vi) modernization of public administration.

Three main policy actions and a number of concrete measures will undertake the implementation of these objectives:

- Facilitate decision making by creating a comprehensive theoretical and analytical basis for continuous monitoring of the situation of business services in order to ensure the necessary background for decision-makers at the enterprise, public administration and political level. To this end, there is a strong need to improve statistical data on business services and information on how they contribute to competitiveness and job creation. Important measures undertaken include: together with Eurostat, statistical pilot projects on the supply of various services; working towards the creation of an organizational framework or observatory for the continuous collection of data; monitoring and analysis of all services adding value to industry complemented by a

quantitative, statistical project by Eurostat on the demand for business services; a project to get better knowledge of the productivity and competitiveness of the business services sector. In the short to medium term, these actions will gradually lead to a better balance between data and information collection in manufacturing and in services.

- To create an internal market for business services. Any business service lawfully provided in the country of establishment should be freely available to clients in other member states, without the need to verify in each instance whether it is compatible with regulatory, administrative, professional provisions or other barriers in the client country. However, many national barriers still exist; their removal would lead to reduced compliance costs and increased competition within and outside the internal market, stimulating more efficient provision of business services. In order provide this, a review of existing national barriers is under way with a view to assessing their justifiability or proportionality. Mutual recognition of provisions will be sought and new European Union legislation proposed.
- To improve the environment in which business services and their clients work, by using existing Community policy instruments to enhance competitiveness. Policy instruments due to be developed include standardization and certification of qualifications, SME policy, R&D, training, public procurement, competition policy, structural policy, GATS, and the Information Society and electronic commerce.

The European Commission has developed a broad approach to business services policy, and presented a comprehensive policy framework for business services covering productivity improvement, employment, competition, industrial co-operation, and promotion of services and modernization of public administration.

According to this study the governmental competition and regulatory policy have two kinds of effect on the demand for business services. First, increasing competition will in many cases increase pressures on firms to reorganize their activities to use assets more productively and increase productivity and performance. To the extent that this is accompanied by decreased size and increased outsourcing, it will increase demand for marketed business services. Similarly, liberalization, and elimination or limitation of monopoly power in areas such as utilities and infrastructure provision may also lead to greater demand for such services. As unit size diminishes, former monopolies are obliged to shed non-core functions, outsource various business services and undertake extensive training in the new competitive environment. A further source of demand for strategic business services, for example, for marketing and advertising services, is likely to come from the liberalization of broadcasting and the media associated with the advent of new technologies.

Recent trends on trading services

Services are traded internationally through four main channels, not all of which are measured well in current trade statistics; this is notably the case for the third category below, often referred to as foreign affiliate trade in services (FATS):

- *Cross-border supply* (supply of services from the territory of one country into the territory of another country).
- *Consumption abroad* (supply of services in the territory of one country to a service consumer of another country).
- *Commercial presence* (supply of services by a services supplier of one country through commercial presence in the territory of another country).

- *Presence of natural persons* (supply of services by a service supplier of one country through the presence of natural persons of that country in the territory of another country).

The international trade has been growing during the last decade, mainly among the countries of OECD, that in many cases are small economies that produced complementary goods. Although trade in service represents a small part of the total trade (one quarter of merchandise exports or imports, more than three quarter done among countries with high-income countries), the situation is clearly different and is connect to some particular aspects.

When the data are look is clear that Germany and Japan present a negative result mainly because of the travel abroad of part of the population. The results are quite opposite in the case of Spain and United States that attract tourism all over the world.

Trade in Services - Total
OECD - Select Countries
1996

	billion USD								
	Total services			Transport		Travel		Other services	
	Net	Credit	Debit	Net	Credit	Net	Credit	Net	Credit
France	16.3	83.5	67.3	-0.5	20.2	10.6	28.4	6.1	35.0
Germany	-43.5	85.0	128.5	-5.0	19.8	-33.4	17.5	-5.1	47.7
Italy	2.0	70.0	68.0	-8.5	15.1	14.2	30.0	-3.7	24.9
Japan	-62.3	67.0	130.0	-12.0	21.6	-33.0	4.1	-17.3	42.0
Korea	-6.2	23.4	29.6	-1.5	8.8	-2.6	4.9	-2.1	9.8
Mexico	0.1	10.9	10.8	-2.8	1.4	3.5	6.9	-0.7	2.6
Spain	19.8	44.3	24.5	-0.2	6.8	22.6	27.5	-2.6	10.0
United Kingdom	11.2	81.7	70.5	-0.7	17.9	-6.1	20.0	18.0	43.8
United States	84.7	236.7	152.0	3.3	46.5	30.8	80.2	50.7	110.0
G7	1.6	654.0	652.4	-25.8	146.8	-19.4	188.8	46.7	318.4
OECD	46.5	1028.4	978.3	-15.2	243.0	14.2	313.8	47.4	468.0
Total									

Sources - National Accounts OECD, Paris 1999. Services: statistics on International Transactions 1987-1996. Paris OECD/Eurostat, Paris 1999.

According to OECD study, trade in commercial services is considerably less than merchandise trade. In 1997, world exports of all commercial services were valued at USD 1.3 trillion, amounting to only 20% of merchandise and commercial services exports combined. This compares with an average share of services in GDP for most countries in the region of 60%-70%.

The explanation of the shortfall of this kind of trade still remains the local presence of the producer of the service. "The nature of service provision is such that services have a large component of person-to-person interaction, often involving tacit information, which can only be provided through local presence. Small firm size is another. Service suppliers are predominantly small firms, and are therefore less globalizes and less disposed than large-scale manufacturing or agricultural operations to export high-volume homogeneous products. Product differentiation and cultural preferences are other reasons. Because of the customized nature of services, the geographical proximity of suppliers and clients is often important. Finally, there are barriers to the supply of services by foreign firms, such as restrictions on local establishment and operations in some areas" (OECD,1999).

However, trade in commercial services has been growing faster than merchandise trade, with exports of commercial services growing at 8% a year in the 1990-97 period while merchandise exports grew at 7%. Within commercial services, "other commercial services" were the most dynamic, and within this group, strategic business services such as computer and information services appear to have had the highest growth in trade. This high growth can be explained by a number of factors including: very rapid growth demand for these services; the growth of international outsourcing, particularly by manufacturing firms; the rapid globalization of manufacturing, often resulting in services providers establishing an international presence abroad alongside major manufacturing clients; and the growing size of some strategic business service suppliers in consulting, personnel

supply and advertising, increasingly the result of mergers and acquisitions, which facilitates their globalization. The liberalization of trade and investment in services also serves to encourage the international expansion of service supply.

Cross-border outsourcing is becoming a significant source of international trade in strategic services via a number of different models of outsourcing of services provision: through “out-tasking” of functions to a foreign enterprise for performance offshore or through the adoption of worldwide services outsourcing strategies such as accelerated design through “7x24” design operations using interdependent teams in different time zones; reliance on a foreign external enterprise to support a foreign subsidiary, often based on global outsourcing strategies; establishment of a jointly owned subsidiary to provide shared services to affiliates; use of a multinational services enterprise to support a multinational customer’s operations in multiple countries (including the provision of “private label” services to facilitate the rapid creation of foreign business support infrastructures).

Cohen and Zysman argue in 1986 that there was nothing in the statistics of trade that suggested that the United States had either a particular competitive advantage or even a comparative advantage in service. By focusing in built a more competitive economy, the major American conglomerates have found their way on the trade of services. One among many cases, the General Electric is exemplar. In 1980 manufacturing provided 80% of the group’s profits; now three-quarters come from services sold abroad (The Economist, 09/18/1999), an indication of how large part of the activities of many groups are changing their approach of this new market, by coordinate the sell of products with the maintenance and others connected services¹⁰.That shows the possibilities that are open to this new kind of trade.

¹⁰ Brazilian trade on services are certain increasing, presenting a negative result (over US\$ 10 billions in 1997) only partially due to travel and transport as the majority of other countries there large amount of others services that are imported, without equal enhancement of the exportation of services.

Further Considerations

The last two decades was remarkable for so many reasons. New technologies, specially the microelectronics, turned the market of the products up side down and that was accomplished by miniaturizing and enhance of the possibilities of utilization of many products. The transformation on communications and informational services complementary allow to shrink distances and to save time. The combination of these major advances radically modified the way goods and services were produced.

Unlikely of what was thought, the transformation enhances the number of goods considered as part of the basic needs of life, and in a very similar way it increases the needs of services, specially the one that are complementary to the process of production. This complementary aspect between services and goods seams to be the main answer that the specialists are able to get to understand the increase of services.

In the last decade many economies faced a small growth, as a result of the policies of stabilization and budgetary restriction, the growth on this heterogeneous sector is responsible for the enhance of the competitiveness of the production and for the creation of new opportunities of employment, which are eliminated in others sector of activities, specially in the manufacturing industry.

The ability of growth in a sustainable way, providing better and cheaper products, on one side, and jobs with better wages on the other, has been experienced by a small number of countries. Although different approach on the role of the government, the importance of the development of the service sector is clear, specially basic infrastructure and new business services that are developed to support the needs of the production.

Many of these new activities were performed before in-house in the great conglomerates, but the rationalization of the activities put out of the corebusiness many secondary activities - from accountability and marketing to repair and maintenance of

equipment, usually by contracting out these activities. This nonetheless is one part of the story, the other is connected with the use of the information service – that saves time and avoids the immobilization of the capital. A target always actual specially considered the new problems caused by financial speculation and the lack of regulation on the financial sector.

This transformation has many aspects, and it is possible to enumerate some of them and explain what represent nowadays:

- To improve productivity is a target of the economic system, then is necessary to spread new technologies and informational services, building a new paradigm of production;
- This new services are connected and redefine the role of cities as the places where is possible to find high skilled professional working together to solve new problems. The place where factories are settled appears to become less important of the agglomeration of services to induce new investments;
- The process of outsourcing or contracting out demand high skill professional, otherwise the company will produce what is necessary in-house, although with high costs and therefore less competitiveness;
- The contracting out of business services creates the necessity of new code of conduct or at least new rules concerned the use of the knowledge acquired through the work in the most creative companies;
- The potential need of high skill professionals in almost every step of the production enhance the need of high educated workers.

In short, this transition in a more global environment has a high cost. One of the most visible is the transformation of the ability to preserve good jobs, being able to

combine high skill and better salaries. Until now these jobs are few and tend to enhance the gap among riches and pours, in new forms even on the OECD countries.

The Brazilian economy is in some way an exemplar case because of his role in the global economy, due of his large and diversified production of primary and manufactures goods. To build this structure it was necessary the development of infrastructure, a large and well-spread bank system and a sophisticated net of professional in the business services. But in the last two decades the imbalance of public sector and the high inflation were important reasons that blocked the sustainable growth of the Brazilian economy. This situation provoked the deterioration of the infrastructure and the production, with incredible lost of competitiveness of the economy.

During the last five years, as the government was blocked the privatization of part of the basic services has been attempt, as in the others countries, has been quite difficult built the regulatory agencies creating rule that can prove to be strong enough to prevent the abuse of power, but this is the new challenge of the government.

Another problem is the low grade of education of the population. This can be perceived as a sensitive area by producers and to attract new investments, specially because in this particular transition the main trend is that everyone might better prepared in order to play their part in the creation of solutions that makes the economy more productivity.

The results of new researches about the purchase of services by the others sectors of the economy point out, in the case of every economy a very known problem in Brazil, the difficulties of access faced by the small and medium size enterprises. Although this problem is similar in others economies, in the Brazilian case, the macro-economic restriction represented by the high interest rates creates an additional problem of access to credit and new technologies.

All these points leads to the redefinition of the role of the government: from producer to regulator. A big change is now in course and a long pathway is ahead to be taken to enhance competitiveness and remedy what have been called a social debt, this will require changes in structures, and that one are big ones, but are necessary to developed in the Brazilian economy.

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