

THE ROLE OF THE SERVICE SECTOR IN THE INDIAN ECONOMY

Dr.D.Amutha

Associate Professor of Economics, St.Mary's College (Autonomous), Tuticorin

Email: amuthajoe@gmail.com

And

Dr.M.Juliet

Asst. Professor of Economics, St.Mary's College (Autonomous), Tuticorin

Abstract

Service sector also recognized as tertiary or residual sector is indispensable for economic development in any economy including India. It has developed as the main and fastest-growing sector in the global economy in the last three decades. The present study makes an analysis of service sector in Indian economy. The paper also makes an analysis of Indian services sector through examining its growth and contributions in the economy. The paper also highlights reform measures that will enable the services sector to not only to grow at a fast pace but also create quality employment and attract investment. The study confirms that services sector have grown at the significant rate in comparison to other sectors. Its growth rate is found to be higher than growth of overall GDP. Rising share of this sector in GDP over covers the poor performance of agriculture sector. As a service sub-sector, trade is dominant all in terms of its contribution in Indian GDP. The employment percentage in service sector as well as in industry sector is rising while in agriculture, it is falling continuously. A large proportion of Indian population is still engaged in agriculture sector and the next largest employer is service sector where trade, hotels & restaurants and community, social & personal services are the significant generator of employment. Thus, service sector which is dominant in terms of its growth & shares serves as an engine of growth for Indian economy. It is important for a developing country like India with a large and young population to generate quality employment and move up the value chain. India needs private investments in key infrastructure services such as transport, energy and telecommunications.

Key words: services sector, Gross Domestic Product, economic growth, tertiary sector, employment elasticities.

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Introduction

Service sector also recognized as tertiary or residual sector is indispensable for economic development in any economy including India. It has developed as the main and fastest-growing sector in the global economy in the last three decades. The rising part of the services sector in the gross domestic product (GDP) of India indicates the importance of the sector to the economy (GOI 2012). The services sector accounted for about 30 per cent of total GDP of India in 1950s; its share in GDP increased to 38 per cent in the 1980s, then to 43 per cent in the 1990s and finally to about 56.5 per cent in 2012-13 (GOI 2013). Thus, the services sector currently accounts for more than half of India's GDP.

While the share of the services in GDP increased from 34 per cent in 1970s to 54 per cent in 2010-11, the corresponding share of services sector employment in total employment changed from 15 per cent in 1972-73 to only about 26.67 per cent per cent in 2009-10. As a consequence, a large proportion of workers remain in rural agriculture. Among others, this has led to a situation of a large gap in productivity between agricultural workers and workers in the services sector (Papola and Sahu 2012).

Service sector employment is associated with informal sector not only due to the relatively large proportion on unprotected jobs, but also due to the fact that a large proportion domestic workers are accounted for as services sector workers (Jonakin 2006). Unlike the output of agriculture, mining or manufacturing which are material and tangible, the output of the services sector such as teaching, cleaning, selling, curing and entertaining have no physical form and therefore are immaterial or intangible (Noon 2003). The present study makes an analysis of

service sector in Indian economy. The paper also makes an analysis of Indian services sector through examining its growth and contributions in the economy.

Development and structure of services sector GDP in India

Within the services sector, however, there is a wide variation in the growth performance of different sub-sectors. Between 1950-51 and 1965-66, the services that grew at a rate faster than the average growth rate for the entire services sector are: Public administration (6.37 per cent), Banking (6.8 per cent), Insurance (6.8 per cent), Road transport (6.06 per cent) and Trade (5.2 per cent).

Other sub-sectors that were relatively smaller in size and had smaller base values and experienced higher growth rates during this period were: Education (8 per cent), Water transport (6.15 per cent), Air transport (9.64 per cent) Health (5 per cent) and Communications (7 per cent). The services sub-sectors that experienced lower than average growth in the period from 1950-51 to 1965-66 belonged to the category of Personal services (2.33 per cent) and to Dwellings and business services (2.45 per cent). Within personal services the low growth services were Domestic services (1.8 per cent), Laundry, dyeing & dry cleaning (4.18 per cent), Barber & beauty shops (1.32 per cent) and Tailoring (1.87 per cent). Within business services the low growth services were Dwellings (2.34) real estate (3.72) and legal services (0.25).

Sectoral growth rate

Road transport continued to increase in share accounting for 5.8 per cent in 1965-66 and 7.4 per cent in 1979-80. Similarly, the share of air transport increased from 0.2 per cent to 0.6 per cent (an almost trebling of its share) and storage from 0.2 per cent to 0.4 per cent. The Banking and insurance sector also increased its share with Banks' share in services increasing from 1.7 per cent to 2.5 per cent and that of non-life insurance increasing from 0.9 per cent to 1.3 per cent. The growth of the public sector led services continued in this period.

While the share of education services remained unchanged that of medical services increased from 2.1 per cent to 2.6 per cent, that of public sector communications increased from 0.7 per cent to 0.9 per cent and finally public administration from 12.4 per cent to 14.7 per cent. In the period from 1950 to 1966, Trade, Dwellings, Public administration, Education services, Road transport, Railways and Banks together contributed to about 80 per cent of the overall services sector growth. The average annual growth rate of the services sector from 1980-81 to 1995-96 was about 6.5 per cent. The services sector growth further increased to 7.7 per cent in

the period from 1996-97 to 2004-05 and finally to 10.3 per cent in the most recent period from 2004- 05 to 2009-10.

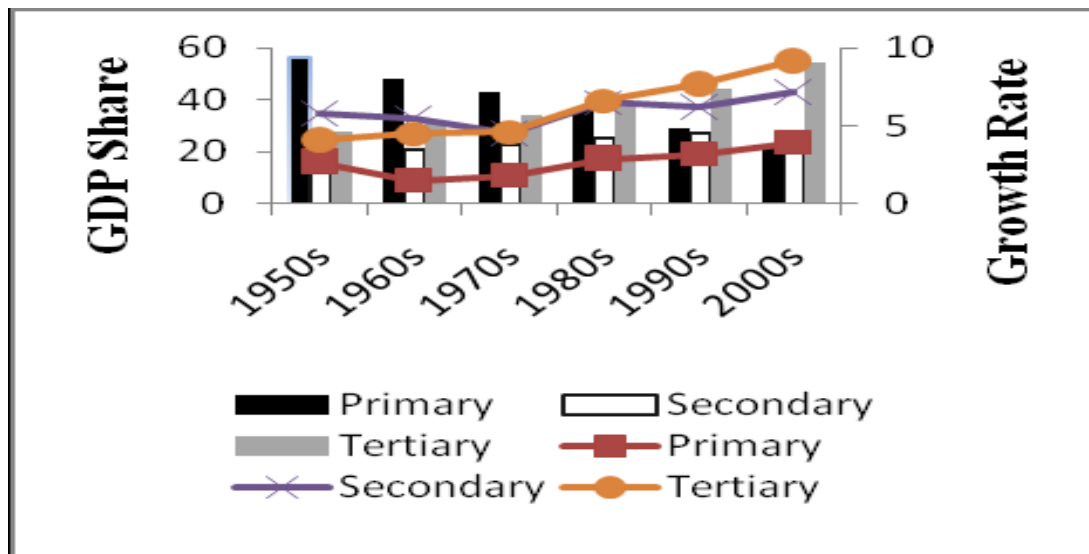
Sectoral shares in GDP, 1950-2016 (per cent of GDP)

Year	Agriculture	Industry	Services
1950	58	15	28
1980	38	24	38
1990	33	27	41
2000	24	27	49
2003-04	22	26	53
2004-05	20	26	54
2005-06	20	26	54
2006-07	19	27	55
2010-11	21	30	59
2015-16	23	32	63

Source: Central Statistical Organisation

The data presented by CSO also speaks of the phenomenal shift in the service growth which has crossed more than half contribution in terms of percentage share in the GDP.

Average GDP share (%) & trend growth rate (% p. a)



Sectoral Composition of GDP Growth

The contribution of services sector to GDP share has increased rapidly since the post liberalization period, that is, since 1990s. So also, the growth of services has been higher than

secondary sector since 1990s. There appears to be convergence in the trend growth rates of the two sectors in 1980s thereafter services registering a higher growth than the secondary sector. The GDP share of services jumped from 44% in 1990 to 54% in 2000 and 67% in 2016. The trend growth rate also increased phenomenally from 7.7% in 1990 to 9.2% in 2000 and 16.34% in 2016. The figure shows a comparison in the change of GDP shares of different sectors and their trend growth rate since 1950s.

Contribution of services sub-sectors to India's GDP

In the period from 1980 to 1995-96, among the relatively larger service activities, Road transport (7.3 per cent) Banks (8.8 per cent) and Hotels and restaurants (7 per cent) had growth rates of sectoral GDP higher than the average for services (6.9 per cent). The services that remained relatively large but experienced lower than average growth rates from 2009-10 to 2014-15 were Dwellings (2.6 per cent), Public administration (6.3 per cent) and the Railways (5.1 per cent).

In the 1980s the services sector was in a way dominated by the public sector. Of the top 10 services which together accounted for about 79 per cent of services GDP, services dominated by public sector accounted for over 30 per cent. These are Public administration (14.5 per cent of services GDP), Railways (3.4 per cent), Medical and health services (2.6 per cent), and banks (2.4 per cent). The other services that were partially in the public sector domain are Road transport (14.6 per cent) and Education (6.9 per cent). The non-public sector related services that accounted for major share of services GDP in the 1980s were Trade (22.2 per cent), Dwellings (14.6 per cent) Road transport (7.9 per cent), and Recreation services (2.1 per cent).

In the period from 1950 to 2014-15, two important sub sectors, Trade and Public administration appear to remain stable with regard to their contribution to services sector GDP. The share of Trade changed from 25 per cent to about 26 per cent. Similarly the share of Public administration changed from 9 per cent to 10 per cent. The services that have notable increases in shares in services GDP through the period from 1950 till 2014-15 are Banks (whose GDP increase from about 1.2 per cent in 1950-51 to 8.3 per cent in 2014-15), Road transport (from 4.5 per cent to 8 per cent), Business services (from 0.8 per cent to 7.4 per cent) and Insurance (0.8 to 2.7 per cent). Of these, the share of Business services increased sharply starting from the mid-1990s. Services that experienced a secular decline in the share in services GDP in the period from 1950s till 2014-15 are Dwellings (23.8 per cent to 7.6 per cent), Domestic services (8.4 per

cent to 1.8 per cent) Recreation and entertainment services (5.4 per cent to 0.8 per cent) and Radio and TV (1.0 to 0.015 per cent).

Services sub-sector percentage shares

Year	Construction	Trade, hotels, transport & communication	Finance, insurance, real estate & business services	Community social & personal services
1950-51	13.01	33.28	22.58	31.13
1960-61	15.49	36.25	19.52	28.75
1970-71	16.50	36.25	16.97	29.89
1980-81	14.78	39.09	16.78	29.35
1990-91	12.54	37.57	21.67	28.23
2000-01	10.08	40.59	23.32	26.00
2005-06	11.50	43.19	22.51	22.79
2006-07	11.55	43.78	23.02	21.65
2007-08	11.49	44.42	23.22	20.87
2008-09	11.25	44.29	22.89	21.57
2010-11	13.01	46.22	23.72	22.01
2015-16	16.43	49.55	26.42	24.53

Source:- Nirvikar Singh, —Understanding Service Led Economic Growth India 2010, Business Standard

Among the various service categories i.e. sub services trade, hotel, transportation and communication have grown significantly during the reforms period i.e. after 1991.

Employment in the services sector

The growth of IT and ITES is having social, economic, health, ethical and environmental implications also (Joshixix, 2006b, 2008c). With the exception of one sub-sector of tertiary sector i.e. transport, storage, communication all other sub-sectors of services sector exhibited an increasing trend in employment elasticities and thereby overall elasticity of employment increased from 0.15 to 0.51 (Mitra, 2008).

In 2009-10, Public administration (11.1 per cent), Dwellings (10.5 per cent), Road transport (9 per cent), Education (7.4 per cent), Banks (5.5 per cent) and Business services (5.5 per cent) are the major contributors to services GDP. Other important services accounting for over two per cent of the services GDP are Hotel and restaurants (2.7 per cent), Non- banking

financial institutions (2.7 per cent) and Public sector communications (2.1 per cent). In the period from 2009-10 to 2014-15, employment in the services sector grew at a modest 1.84 per cent per annum.

Retail trade which accounted for about 31.4 per cent and 30.7 per cent of total service sector employment in 2009-10 to 2014-15 respectively is the largest employer of service sector workers in India. The next two services that accounted for relatively large proportion of workers were land transport (14 per cent in 2009-10) and Education (10 per cent in 2009-10). This was followed by Public administration and defence (8.1 per cent), Hotels and restaurants (5.3 per cent) and Wholesale trade and commission trade (4.6 per cent).

The services where the labour productivity grew the least or was negative in the period from 2009-10 to 2014-15 were storage activities (-4.2 per cent), Radio and TV (-4.1 per cent) Computer related activities (-0.4 per cent). Two important public or state run services also exhibit negative productivity growth, they are, Banking department of RBI (-175.6 per cent) and Employees provident fund (-5.2 per cent).

The top five services with highest labour productivity in 2014-15 were Non-life insurance (₹67,94,000 per worker per year) following by Banks (₹14,59,000 per worker per year), Air Transport (₹11,48,000 per worker per year), Communications (₹10,53,000 per worker per year) and Computer relating services (₹7,87,000 per worker per year).

Indian service sector

Services sector has been a major contributor to India's GDP and growth (Bhattacharya and Mitra 1990). It is the second largest employer after agriculture. India's trade in services have increased overtime and services accounts for the largest share in India's foreign direct investment (FDI) inflows and outflows.

The growth of India's services sector, its contribution to GDP, and its increasing share in trade and investment has drawn global attention. Unlike other countries, where economic growth has led to a shift from agriculture to industries, in India, there has been a shift from agriculture to the services sector. In this respect, some economists (Ansari 1995) consider India as an outlier among South Asian countries and other emerging markets. A modest attempt has been made to discuss the performance of services sector in India and points out the problems/challenges ahead in this sector.

Growth rates of Indian economy during different periods

Year	Growth rate
1960-1980	3.5%
1980-1990	5.4%
1990-2000	4.4%
2000-2009	6.4%
2010-2016	8.6%

Source: CSO

Service sector in India: some issues & challenges

The sustainability of impressive growth of Indian economy has been questioned in the wake of some challenges in the form of lack of social infrastructure, physical infrastructure; IT infrastructure (Joshi, 2008b, 2006a), agricultural and industrial sector reforms, rupee appreciation and US sub-prime crisis, etc. Besides, challenges in the field of IT and ITES like rising labour costs, rapid growth in demand for talented manpower/quality staff, high attrition rate, outsourcing backlash etc are some other limiting factors (Joshi, 2008a, 2006).

The growth of IT and ITES is having social, economic, health, ethical and environmental implications also (Joshi, 2006b, 2008c). Further, delay in the promotion of conducive business environment and good governance will enable us to catch up with the global giants in terms of world –wide presence and scale. It is also important to point out here that the measurement of output, productivity, non-availability of data or availability of data after a time lag are other problems confronted with in case of services.

The problem gets further compounded because of the entry of new species of services (like IT, ITES etc) and lack of development of concepts on the one hand and non-inclusion of unpaid households on the other. Further, quality of each unit of the same service varies from the other. Therefore, it is too difficult to achieve the same level of output in terms of quality as has been pointed out in Cowell (1984). Further, quality improvements stemming from the application of new technologies are extremely hard to measure.

The Indian economic growth has slowed down to 6.9% in 2012 (World Economic Outlook, 2012). Nevertheless, it is projected to grow at 7.3% in 2013, which is higher than the average projected growth rate for emerging and developing economies 6% (World Economic Outlook, 2012). With the rise in GDP and per capita income, the number of people below the poverty line has declined while those in high and middle-income group have increased.

Prospects for Growth in the Services Sector

The contribution of the services sector has increased very rapidly in the India GDP for many foreign consumers have shown interest in the country's service exports. This is due to the fact that India has a large pool of highly skilled, low cost, and educated workers in the country. This has made sure that the services that are available in the country are of the best quality. The foreign companies seeing this have started outsourcing their work to India especially in the area of business services which includes business process outsourcing and information technology services. This has given a major boost to the Services Sector in India, which in its turn has made the sector contribute more to the India GDP.

Conclusion

To sum up, the present paper provides a brief overview of performance, prospects and problems encountered by the services sector in India's economy. India's services sector is burgeoning: a sign of an economy on the high growth path. It has become the mainstay of the growth process and has emerged as the most dynamic sector of the Indian economy, particularly since last one and half decade. The foregoing analysis brings out the fact that in comparison to different countries of the world, the share of service sector in India is not so high.

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