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Service Sector: India's Road to Economic Growth

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Abstract:

Service sector also known as tertiary sector is essential for economic growth in any economy including India. It has emerged as the largest and fastest-growing sector in the global economy in the last two decades. The tremendous performance of Indian economy is attributable in a considerable manner to the spectacular dynamism shown by services sector. Rising urbanization, privatization and demand for services bring boom in Indian service sector. This sector continues to be a star performer and by contributing 59 per cent of GDP, it is enjoying first place among all sectors in Indian economy. In employment providing, this sector is occupying second place, next only to agriculture. Keeping in above backdrop, the present study makes an analysis of service sector in Indian economy. The study confirms that service sector has achieved tremendous growth over the year in Indian economy. To maintain and accelerate the growth & contributions of this sector & to develop it as a true engine of economic growth, there is logic & rationale of complementary investments in physical infrastructure as well as in human capital.

Keywords: Service Sector, GDP, Employment, Growth, Challenges

1. Introduction:

The service sector covers a wide range of activities from the most sophisticated in the field of Information and Communication Technology to simple services pursued by the informal sector workers. Service may be defined as a type of economic activity that is intangible & is not stored and does not result in ownership.

Among fast growing developing countries, India is distinctive for the role of the service sector. The sector, has emerged as one of the largest and fastest-growing sectors not just in the country but in the global landscape; subsequently, its contribution towards global output and employment has been substantial.

During FY 2014–15, the sector is projected to grow at a healthy 5.6 per cent, according to National Council of Applied Economic Research (NCAER).

1.1. Constituents of Indian Service Sector

Service sector can be classified into four broad categories, viz. a) trade, hotels, and restaurants; b) transport, storage, and communication; c) financing, insurance, real estate, and business services; and d) community, social, and personal services. The following table shows the broad grouping of activities which can be considered to form part of the service sector

Service Sub-sectors	Activities Included
1. Trade, Hotels & Restaurants	
1.1 Trade	Wholesale & retail trade in commodities both produced at home (including exports) and imported purchase & selling agent, brokers and auctioneers.
1.2 Hotels & Restaurants	Service rendered by hotel & other lodging places, restaurant, cafes & other such places.
2. Transport, Storage & Communication	
2.1 Railways	
2.2 Transport by other means	Road, water, air transport & service incidental to transport.
2.3 Storage	Agricultural storage for agri produce, foodgrains, fertilizers, manure, etc. ; Industrial storage for industrial goods, import cargo, and excisable cargo; inland container depots (ICDs)/container freight stations (CFSs) for facilitating import/export trade; and special warehouses for cold and temperature controlled storage.
2.4 Communication	Postal, money order, telegrams, telephones, overseas communication services.
3. Financing, Insurance, Real Estate and Business Services	
3.1 Banking & Insurance	Banks, banking department of RBI, Post office saving bank, NBFI, employees PF & Life insurance, postal life & non life insurance
3.2 Real Estate, Ownership of Dwellings and Business Services	Business services include accounting, software development, data processing services, business and management consultancy, architectural, engineering and other technical consultancy, advertisement and other business services
4. Community, Social and Personal services	
4.1 Public Administration & Defense	
4.2 Other Services	Personal Services: Domestic laundry, barber, beauty shops, tailoring and others. Community Services: Education, research, scientific medical, health, religious & other community services. Others: Recreation, entertainment, radio, television, broadcast, sanitary services.

Source: CSO

Figure 1: Constituents of Indian Service Sector

2. Contribution of the Services Sector to India’s GDP

The contribution of the services sector in GDP has increased from 30.3 per cent in 1950-51 to 38 per cent in 1980-81 and further to 59 per cent in 2011-12. However, in 1980-81, the service sector has overtaken the agriculture on the basis of GDP share and since then it became the primary contributor of GDP. Similarly, industry sector whose share in GDP has remained in the range of 16 to 28 per cent over the years got second rank in terms of its contributions. The entire decline in share of agriculture has been balanced by an increase in share of the services sector. Thus, the resilience of the economy to shocks owe to the services sector which has the largest share and most consistent growth performance. The changes in relative shares of agriculture, industry & service sectors in GDP over the years is shown in the following figure

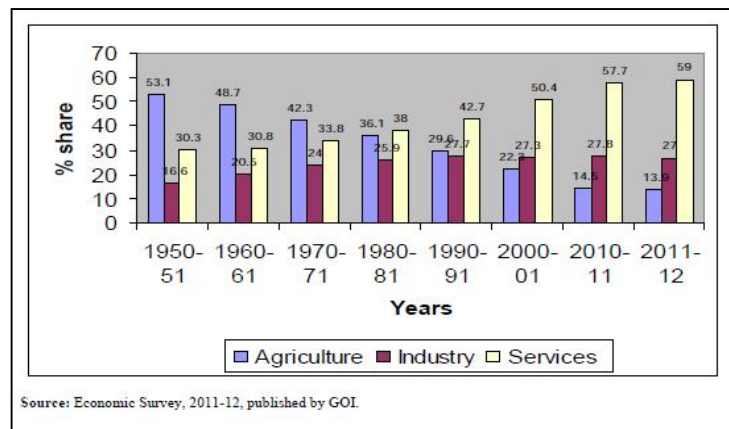


Figure 2: Percentage of Share of Major Service Sectors in GDP of India

The appreciable performance of service sector is due to its some fast growing sub-sectors. Such two broad sub-sectors viz. transport storage and communication; and financing, insurance, real estate and business services, comprising many dynamic services have performed well with growth of 14.7 per cent and 10.4 per cent, respectively in 2010-11. Only community, social and personal services have registered a low growth of 4.5 per cent

Another important sub sector i.e. trade, hotels, and restaurants, whose growth slowed in 2008-09 and has recovered moderately in 2009-10. In the year 2010-11, only communication and banking & insurance have registered a double-digit growth i.e. 27.2 and 14.5 per cent respectively.

Software which has grown at 21 per cent CAGR for the period 2004-05 to 2010-11, is one sector in which India has achieved a remarkable global brand identity. Similarly, tourism - a major item in India’s services, has witnessed significant growth in recent years. Besides these, the potential and growing services include many professional services, infrastructure-related services, and financial services.

Service Sub-sectors /Year-->	2005-06		2008-09		2011-12	
	GDP Growth Rate (%)	% Share in GDP	GDP Growth Rate (%)	% Share in GDP	GDP Growth Rate (%)	% Share in GDP
1. Trade, Hotels & Restaurants	12	16.7	5.7	16.9	6.2	18.0
1.1 Trade	11.6	15.1	6.7	15.3	6.5	16.6
1.2 Hotels & Restaurants	17.4	1.6	-3.3	1.5	2.8	1.5
2. Transport, Storage & Communication	11.8	8.2	10.8	7.8	8.4	7.1
2.1 Railways	7.5	0.9	7.7	0.9	7.5	0.7
2.2 Transport by other means	9.3	5.7	5.3	5.5	8.6	5.4
2.3 Storage	4.7	0.1	14.1	0.1	9.4	0.1
2.4 Communication	23.5	1.6	25.1	1.4	8.3	0.9
3. Financing, Insurance, Real Estate and Business Services	12.6	14.5	12.0	15.9	11.7	16.6
3.1 Banking & Insurance	15.8	5.4	14.0	5.6	13.2	5.7
3.2 Real Estate, Ownership of Dwellings and Business Services	10.6	9.1	10.4	10.3	10.3	10.8
4. Community, Social and Personal services	7.1	13.5	12.5	13.3	6.0	14.0
4.1 Public Administration & Defense	4.3	5.6	19.8	5.8	5.4	6.1
4.2 Other Services	9.1	7.9	7.4	7.5	6.5	7.9
Construction	12.8	7.9	5.3	8.5	5.6	8.2
Total Services*	10.9	52.9	10.0	53.9	8.2	55.7
Total Services#	11.1	60.8	9.4	62.4	7.9	63.9

Source: Economic Survey, 2010-11, 2011-12 published by GOI. *Excluding Construction # Including Construction

Figure 3: Services Sub –Sectors Annual Growth and %age Share in GDP

3. Employment in Service Sector

The service sector in urban India has grown at a rate of (2.5 per cent) as that of all India. A marginal slow down in services growth rate relative to the earlier period (2.6 per cent versus 2.9 per cent) can be attributed to the sharp fall in the growth of trade and hotel industry during 2000s. Business services segment that includes financial, real estate and software services grew the fastest with a growth rate of 3.4 per cent. However, its share in total urban employment went up by less than 2 percentage points.

Industry	1999-2000 over 1993- 94	2009-10 over 1999- 2000	2009-10 over 1993- 94	Share in Total Employment- 2009-10
Agriculture	0.10	-0.10	0.00	52.30
Mining & Quarrying	-2.80	2.70	0.60	0.60
Manufacturing	1.60	1.80	1.70	11.50
Electricity, water, etc.	-4.80	1.90	-0.60	0.30
Construction	6.40	9.70	8.40	9.70
Trade (Retail + Wholesale), Hotel and Restaurant	6.30	2.40	3.80	11.40
Transport, Storage and Communications	5.30	3.40	4.10	4.50
Other Services like Financial, Business, Public Administration, Education etc.	-0.70	2.40	1.20	9.80
Above Three Services	2.90	2.60	2.70	25.70
All Sectors	1.00	1.40	1.30	100.00

Note: Employment is measured by number of workers by usual status (ps+ss).
Source: NSS Employment and Unemployment Surveys adjusted for population censuses.

Table 1: Employment Growth Rates by Industry in India: 1993-94 to 2009-2010

The three services taken together accounted for more than 59.2 per cent in the year 1999-2000 and 58.10 per cent in the year 2009-2010.

Industry	1999-2000	2009-2010
Agriculture	8.70	7.50
Mining	0.80	0.60
Electricity	0.70	0.60
Construction	7.90	10.20
Manufacturing	22.70	23.00
Trade, Hotels and Restaurant	26.90	24.20
Transport, Storage, Communication	8.70	8.70
Other Services like Financial, Business etc.	23.50	25.20
Above Three Services	59.20	58.10
All Workers	100.00	100.00

Table 2: Structure of Urban Employment by Industry

Some of the plausible explanations for the slow growth of employment in the service sector can be:

- Sectors that have large potential for generating employment are growing slowly?
- The fast growing services sectors also witness high labour productivity growth as a result the employment potential is lower in these sectors?
- Trade is positively affecting the growth in those services that do not have large potential for generating employment?

4. Reasons for Growth of Indian Service Sector

When an economy grows, both demand side and supply side factors operate that lead to higher growth in the service sector as compared to the other sectors and also lead to a larger share of service sector in total employment. These factors are:

- Demand-Side Factors
- High-income elasticity of demand for final product services,
- Slower productivity growth in services that leads to higher employment potential and
- Structural changes within the manufacturing sector, which make contracting out services more efficient than producing them in the firm or household.
- Supply-Side Factors:
- Increased trade
- Higher foreign direct investments in services and
- Improved technology

5. Challenges for Growth of Service Sector

- The immediate challenge for the services sector is not only to maintain its present growth tempo but also to accelerate it.
- To retain and expand India's competitiveness in those services where it has already made a mark such as IT & ITeS and Telecommunications.
- Another challenge is to remove or ease domestic regulations in the different services. Removing or easing them can lead to dynamic gains for the Indian economy.
- The challenge lies in making inroads into some traditional areas such as tourism and shipping where other countries have already established their selves, but where the potential for India is nevertheless very high.
- Making forays into globally traded services in still niche areas for India, such as financial services, health care, education, accountancy, and other business services where India has a large domestic market and but only a very small part of the full potential has been tapped.
- There are also challenges related to collecting better data and developing a better coordinated strategy to pull together all the dispersed information.

6. Conclusion

6.1. Recommendations and Suggestion

- Indian Government needs to focus on policy making for service sector.
- There is need of complementary investments in physical infrastructure as well as in human capital
- FDI should be encouraged in service sector for its growth
- For service sub sectors like tourism sector , shipping sector, entertainment sector , aviation sector there should be rationalizing of taxes to encourage there growth. India has a high corporate tax - 30-40% compared to around 17% in Singapore and up to 25% in China

- Services sector has not been able to generate employment in terms of both numbers and quality. There is skill shortage in sectors like IT and organised retail.

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