

SERVICE SECTOR IN INDIA: TRENDS, ISSUES AND CHALLENGES

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Abstract

Service sector is the lifeline for the social economic growth of a country .It is today the largest and fastest and growing sector globally output and employing more people than any other sector. This paper provides an overview of the Indian services sector. It identifies the various reasons for the growth of service sector and the major barrier faced by the sector and provides policy recommendations which if implemented will lead to inclusive growth, increase productivity, and generate quality employment and increase trade and investment. It shows that services is the fastest growing sector in India, contributing significantly to GDP, GDP growth, employment, trade and investment. Labour productivity in services is the highest and it has increased overtime. India is a major proponent of liberalizing services both in the WTO and in its bilateral trade agreements. However, there are some concerns. Economic growth has slowed down. Growth in employment in services has not been commensurate with the share of the sector in GDP. A large part of the employment is in the non-corporate or unorganized sector, with limited job security.

Although India is portrayed as a major exporter of services, its rank among WTO member countries in services exports is lower than that of China's and its export competitiveness concentrate in few sectors and a few markets. The paper explain the over view of service sector in India, classification of service sector, growth and contribution of service sector identify the factors responsible for the new environment for the growth of service sector. Which is implemented, will lead to inclusive growth, increased productivity, generate quality employment, increase trade and investment, and enhances India's global competitiveness in services.

Keywords: Economic Survey, Services Sector, Services Exports, Trade, Investment, Productivity, Employment, Etc.

Introduction

**The able king gets, stores and guards
And spends them for people's safeguards.**

[A good government shell knows how to increase the resources of the country,
and how to enrich the treasury, and as to how to preserve and ultimately spend
the money.]

~ **Thirukkural**

India is among the fast growing economies in the world. The real reason for the growth of the service sector is due to the increase in urbanization, privatization and more demand for intermediate and final consumer services. Availability of quality services is vital for the wellbeing of the economy. In advanced economies the growth in the primary and secondary sectors are directly dependent on the growth of services like banking, insurance, trade, commerce, entertainment etc. Indian service sector has witnessed a major boom and this is the one of the major contributors to both employment and national income in recent times. The service sector includes trading, transportation and communication, financial, real estate and business services, community, social and personal services. The key factors for the service sector in India would be health and education. A strong healthcare system helps to create a strong and diligent human capital, who in turn can contribute productively to the nation's growth.

Post Liberalization

The Indian economy has moved from agriculture based economy to a knowledge based economy. Today the IT industry and ITE'S industry are the dominant industry in the service sector. Media and entertainment have also seen tremendous growth in the past few years. Information Technology Industry the Information Technology industry has achieved phenomenal growth after liberalization. The industry has performed exceedingly well amidst tough global competition. Being knowledge based industry India has been able to leverage the global

markets, because of the huge pool of engineering talent available and the proficiency in English language among the middle class.

The ITES sector emerges as one of the prominent sector and it also contributes positive change in the global economy. Some of the service covered by the ITES industry would be customer interaction service, back office, revenue accounting, data entry, data conversion, HR service, medical transcription, remote education, market research and GIS. Prior to liberalization, retail sector in India it is one of the under developed sector. After liberalization the scenario changed dramatically. Organized retailing with prominence on self-service and supermarket chains mushroomed, catering to the needs of vibrant middle class. This indirectly contributed to the growth of the packaged food industry and other consumer goods. Banking And Insurance, Prior to liberalization these two sectors were controlled and regulated by the government. Nationalized banks and insurance companies had a firm grip over the market. After liberalization the banking and insurance domain opened up for private participation, so three major changes have taken in the banking sector, they are 1) Step to increase the cash outflow through reduction in the statutory liquidity and cash reserve ratio. 2) Nationalized banks including SBI were allowed to sell stakes to private sector and private investors were allowed to enter the banking domain. Foreign banks were given greater access to the domestic market, both as subsidiaries and branches, provided the foreign banks maintained a minimum assigned capital and would be governed by the same rules and regulations governing domestic bank. 3) Banks were given greater freedom to leverage the capital markets and determine their asset portfolios. The banks were allowed to provide advances against equity provided as collateral and provide bank guarantees to the broking community. The Insurance Regulatory and Development Authority Act 1999 (IRDA Act) allowed the participation of private insurance companies in the insurance sector. The primary role of IRDA was to safeguard the interest of insurance policy holders, to regulate, promote and ensure orderly growth of the insurance industry. The insurance sector could invest in the capital markets and other than traditional insurance products, various market link insurance products were available to the end customer to choose from Some of the prominent insurance companies are: Bajaj Allianz Insurance Corporation, Birla Sun Insurance Co Ltd, HDFC Standard Insurance Co Ltd, ICICI Prudential Insurance Co Ltd, Max New York Insurance Co Ltd, Tata AIG Insurance Co Ltd,.

India has the second fastest growing services sector with its compound annual growth rate at nine per cent, just below China's 10.9 per cent, during the last 11-year period from 2001 to 2012, the Economic Survey for 2013-14 said. Russia at 5.4 per cent is a distant third. Among the world's top 15 countries in terms of GDP, India ranked 10th in terms of overall GDP and 12th in terms of services GDP in 2012, it said, adding that services share in world GDP was 65.9 per cent but its share in employment was only 44 per cent in 2012. As per the survey, in India, the growth of services-sector GDP has been higher than that of overall GDP between the period 2001-2014. Services constitute a major portion of India's GDP with a 57 per cent share in GDP at factor cost (at current prices) in 2013-14, an increase of 6 percentage points over 2000-01. "An important factor in the increase in the Centre's fiscal deficit after 2008-09 has been the sharp increase in subsidies from 1.42 per cent of GDP in 2007-08 to 2.56 per cent of GDP in 2012-13. For 2013-14 the subsidy bill is 2.26 per cent of GDP,"

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. Contending this view, Gordan and Gupta 2003, Banga 2005 and Jain and Ninan 2010 have pointed out that India is not an outlier as the share of services sector in GDP has increased with rise in per capita income. Kochhar *ET. al.* 2006 argued that India was a negative outlier in 1981 compared to other emerging markets as the share of services in value added and employment was below that of other countries. After the economic reforms of the 1990s, services sector grew and in 2000 India became a positive outlier in terms of the share of services in value added but continued to be a negative outlier in terms of its share in employment.

In India, growth in services sector has been linked to the liberalization and reforms of the 1990s. In the first three decades (1950s to 1970s) after India's independence in 1947, GDP grew at an average decadal growth rate of less than four per cent. India was largely an agrarian economy. The share of services sector was small and a large number of services were government monopolies. Services sector started to grow in the mid-1980s but growth accelerated in the 1990s when India initiated a series of economic reforms after the country faced a severe balance of payment crisis. Reforms in the services sector were a part of the overall reform process, which led to privatization, removal of FDI restrictions and streamlining of the approval procedures, among others. Existing studies show that liberalization and reforms is one of the important factors contributing to the growth of services sector in India (Chanda 2002, Gordan and Gupta 2003, Banga and Goldar 2004 and Jain and Ninan 2010). With economic growth and rise in per capita income, there is a change in demand pattern from necessary to discretionary consumptions like education and personal and health care services (McKinsey & Company 2007). High income elasticity of demand for services has contributed to the high growth of this sector (Bhattacharya and Mitra 1990 and Gordan and Gupta 2003). Technological progress and availability of high skilled manpower has led to growth of services like information technology (IT) and IT enabled services (ITeS) (Chanda 2002). Developed countries outsource its services to developing countries like India leading to a rise in demand for services from the developing market (Bhagwati 1984, Gordan and Gupta 2003 and Hansda 2001). High government expenditure on certain services like community, social and personal services has also led to high growth of services (Ansari 1995).

The objective of this paper is to provide an overview of the Indian services sector. It identifies major barriers faced by the sector and provides policy recommendations which if implemented will lead to inclusive growth, increase productivity, and generate quality employment and increase trade and investment.

Classification of the Services Sector and Governance Structure

In India, the National Industrial Classification (NIC) provides classifications for services. Since the services sector has evolved over the years and the modes of services delivery have undergone changes, the UNCPD and the NIC have also undergone changes. At present,

Services Sectors included in the National Industrial Classification 2008 are as follows

- Wholesale and retail trade; repair of motor vehicles and motorcycles
- Transportation and storage.
- Accommodation and food service activities.
- Information and communication.
- Financial and insurance activities.
- Real estate activities.
- Professional, scientific and technical activities.
- Administrative and support service activities.
- Public administration and defense; compulsory social security.
- Education.
- Human health and social work activities.
- Arts, entertainment and recreation.
- Other service activities.
- Activities of households as employers; undifferentiated goods and services producing activities of households for own use
- Activities of extraterritorial organizations and bodies

India has a quasi-federal governance structure and according to the Constitution of India Telecommunications, postal, broadcasting, financial services (including insurance and banking), national highways, mining services are under the jurisdiction of the central government (Union List), Health and related services, real estate services, retail, services incidental to agriculture, hunting and forestry are under the state governments (State List) and the remaining Professional services (legal, accounting, auditing and book-keeping, taxation, architectural,

engineering, integrated engineering, urban planning and landscape architectural, medical and dental services and service provided by midwives, nurses, etc.), education, printing and publishing, electricity are under the joint administration of central and state governments (Concurrent List) At the central level, multiple ministries and government department regulate services such as energy and transport while others like construction and retail do not have a nodal ministry. Some services such as telecommunications has one independent regulator while others like electricity have state level regulators. Professional bodies regulate professions such as doctors, architects and accountants.

Contribution of the Services Sector to India's GDP

After India's independence, for more than a decade share of services in the GDP was less than 30%. Table shows that overtime the share of services in GDP has increased while that of agriculture has declined. In the last decade, the share of services has surpassed the combined share of agriculture and industry, making it the most important contributor to the country's output. In 2009-10, services, industries and agriculture respectively accounted for 57.3%, 25.7% and 16.9% of India's GDP.⁶ Nevertheless, the share of services is lower than that of developed countries (the United Kingdom (UK, 78.4%) and the United States (US, 78.2%)), but higher than that of China (41.8%).⁷

Decadal Average of the Year on Year Share of the Different Sectors in India's GDP for the Period 1950-2010 (in %)

Sector	1950/51-1959/60	1960/61-1969/70	1970/71-1979/80	1980/81-1989/90	1990/91-2000/01	2000/01-2009/10
Primary/Agriculture	55.3	47.6	42.8	37.3	30.9	21.8
Secondary/Industries	14.8	19.6	21.3	22.3	23.3	24.5
Tertiary/Services	29.8	32.8	35.9	40.3	45.7	53.7

Source: *Economic Survey of India 2011-12.*

The growth of services sector accelerated in the late eighties. In the late nineties; the sector surpassed the growth of industries to become the fastest growing sector of the Indian economy. Even during the global slowdown the services sector remained resilient to external shocks. In 2009-10, the services sector grew at 9.96% compared to 8.81% growth in industries and 1.57% in agriculture.⁸ The compound annual growth rates (CAGR) of services in China and India during 2001-2010 was respectively 11.3% and 9.4%.⁹ This implies that even though the present share of services in GDP for China is lower than India, since it is growing at a faster rate, in future the share of services will be higher and can even surpass that of India.

The Reason for the Growth of Service Sectors in India

The growth of service industries can be traced to the economic development of society and the socio-cultural changes that have accompanied it. Changing environmental forces brought out of the services in forefront of the economy. Those environmental forces separately or in combination create new type of service.

The Following Environmental Factors are Responsible to Make a New Service

1. Economic affluence: One, of the key factors for the growth of demand for services is the economic affluence. The size of the middle income consumer is raising fast and the percentage of the very poor household's declining. The rural households in the upper income category are growing at a much faster pace than the urban households in the corresponding categories. The Economic liberalization Process has had a positive impact on the Indian households. Their income as well as their expenditure has been pushed, creating a demand for many goods and services.
2. Changing Role of Women: Traditionally the Indian woman was confined to household activities. But with the changing time there has been a change in the traditional way of thinking in the society. Women are

now allowed to work. They are employed in defense services, police services, postal services, software services, health services, hospital services, entertainment industries, Business Process Outsourcing and so on. The percentage of working women has been growing rapidly. The changing role of women has created a market for a number of product and services. Earning women prefer to hire services in order to minimize the innumerable roles that they are required to perform. The demand by woman is forcing service organizations to be more innovative in their approach.

3. Cultural Changes: Change is the underlying philosophy of culture place of change in Indian culture is not uniform. However, during the last century the factors of change are prominent. The emergence of the nuclear family system in place of the traditional joint family system creates a demand for a host of services like education, health care, entertainment, telecommunication, transport, tourism and so on. There has' been a marked change in the thought Processes relating to investment, leisure time perception and so on which has created a huge demand for services.
4. I.T. Revolution: For the last 15 years in India IT became one of the key service businesses of the country. India has the largest software skilled population in the world. The domestic market as well as the international market has grown substantially. Realizing the potential for this area many state governments have made IT as their most, prioritized segment states such as Karnataka, Andhra Pradesh, Madhya Pradesh Maharashtra and Delhi have already achieved substantial progress in Information Technology the In Ile years to come 'Lille IT enabled se Aces will have a bright future. The growths of population, industrialization and indiscriminate consumptions have affected the, natural resources, environment and the ecological balance. Due to this there is an imbalance of the ecology various service organizations have been promoted in order to take up social marketing. Thousands of Crores of rupees are being spent on safeguarding the rare animals and birds, water pollution, conservation of oil & energy and research to develop new technologies that can promote effective use of natural resources and safeguard the environment.
5. Development of Markets: During the last few decades the wholesaler and the retailer population has grown in the country. Urban India has become a cluster of wholesaling and retailing business. In the Semi – urban areas, retailing has spread to the nooks and corners of the streets and in the rural areas retail business is significantly present. A new breed of organizations, offering marketing services has come up. The government also offers marketing services to the small-scale agricultural farmers, artisans and other traditional business sectors such 'as promotion of regulated markets, export promotion councils, development boards etc.
6. Market orientation: The changing competitive situation and demand supply positions has forced the manufacturing organization to shift their philosophy from production orientation to market orientation. Market is a service function that has been added in the organization. The pressures in the market has further forced the manufacturing organizations to have marketing research, accounting, auditing, financial management, human resource management and marketing research divisions – all of which are services functions.
7. Health-Care Consciousness in India: the healthcare market has grown substantially. The increased life expectancy is the result of the consciousness of the people regarding the health issues. The growth of fitness clubs, diagnostic centers, medical counseling, and health related information sites are the reflections of the growing demands for health care services. The government as well as the social organizations has taken up the mass campaigns in order to create awareness among the illiterate persons and the rural population on health service. Hence, the growth of health related services.
8. Economic liberalization: The economic liberalization of the 1991 has brought many changes in the Indian scenario. With the Disinvestment and the Privatization policies the state owned monopolies in many service areas came to an end Multinationals were permitted to enter the Indian market. Liberal lending policies and lower interest rates motivated many people to become self-employed. Different sectors like Banking, Insurance, Power projects, Telecommunication, Hospitality sector, Health Services, Entertainment, Air transport, and Courier services witnessed intense competition, due to the entry of multinationals. The flow of time-tested service technology from various parts of the world changed the attitude of the Indian consumer towards sources.

9. Rampant migration: One of the important reasons for the growth of services in India is the rampant migration of rural to semi-urban and urban areas. Migration to urban areas for the want of jobs and livelihood has resulted in the expansion of cities and townships due to which businesses like real estates, rentals, transportation and infrastructure services are rapidly expanding.
10. Export potential: India is considered to be a Potential source for services. There are a number of services that India offers to various parts of the world like banking, insurance, transportation co data services, accounting services, construction labor, designing, entertainment, education, health services, software services and tourism. Tourism and software services are among the major foreign exchange earners of the country and that the growth rate is also very high as compared to the other sectors.

Conclusion

Services sector is the fastest growing sector in India, contributing significantly to GDP, GDP growth, trade and FDI inflows. The share of services sector in India's total trade is higher than the global average and India is among the top 10 WTO member countries in services exports and imports. India is distinctive for the rapid growth of its service sector – high-tech information technology, communications and business services in particular. Whether the service sector provides a route out of poverty for the masses is disputed, however. Some say that the skill education requirements of modern service sector jobs make them an impractical destination for the rural masses. Others counter that as more skilled and educated workers “graduate” from manufacturing and traditional services into modern services, they open up economic space for less educated workers capable of upgrading their skills. They argue that the skilled-unskilled mix of the manufacturing and service sectors, each taken as a whole, is not as different as commonly supposed. However, the increase in employment in services has not been commensurate to share of the sector in the GDP. Moreover, majority of the people employed in the services sector are concentrated in the unorganized sector, which offers lower salary and limited job security. Hence, the quality of employment in this sector is a cause for concern.

The paper 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. 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. It can only attract FDI and private investment with a stable, transparent, non-discriminatory and competitive policy environment. If the new environment factors which are responsible for the growth of service sectors are implemented it will not only enhance the productivity and efficiency of the service sectors but will also lead to overall growth of the economy through backward and forward linkages. It will enhance India's global competitiveness and trade in services.

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