

THE INTERNATIONAL JOURNAL OF HUMANITIES & SOCIAL STUDIES

India's Services Sector: Comprehensive Evaluation of Its Contribution to GDP, Employment and Trade

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Abstract:

This paper suggests that the services sector has played an important role in accelerating the growth rate of an Indian economy in the post-reform period. In India, services have been the fastest growing sector over the past few decades; there has been phenomenal increase in the services sector contribution to GDP, GDP growth rate, employment and trade. Within the services sector the growth has not been uniform, though Over the years, the contribution of financial and communication services to employment and GDP has increased, but their share in employment is very low as compared to share in India's GDP. The fastest growing services are those that are not generating sufficient growth in employment opportunities for the masses. Following economic liberalization, trade in services in India has expanded rapidly resulting in a favorable services trade balance. There has been a compositional shift in the structure of India's services exports away from traditional services such as travel and transport in 1980 towards other services such as computer and information, other business services and financial services post liberalization. India has a comparative advantage in export of computer and information services and other business services. Though there has been commendable growth in the trade in computer and business services but their employment generating capacity is not adequate to accommodate the workers displaced by the agriculture.

Keywords: Employment, General Agreement of Trade in Services, Occupational structure, Services sector, Trade
JEL Codes: L80, F13, O47, J21

1. Introduction

India followed an inward-looking development strategy for nearly four decades after its independence in 1947. This strategy was a major factor in India's poor growth performance in the pre-reform period. During the period from 1950-51 to 1979-80, growth in GDP stagnated around 3.5 per cent per annum while growth in GDP per capita was 1.4 per cent per annum (Nayyar, 2006). There was some acceleration in the growth rate of GDP in India in the late 1980s, which grew by 5.4 per cent per annum, while growth in GDP per capita was 3.2 per cent per annum. In the late 1970s and 1980s, India's followed a restrictive trade policy with greater emphasis on regulation of imports through a licensing system. The policies adopted by the government of India aimed directly at curbing imports, which, in turn, have resulted in a decrease in the importance of a trade sector over time.

In 1991, major economic crisis emerged, in the wake of severe balance of crisis, India embarked on a comprehensive reform of the economy to widen and deepen its integration with the world economy. The need for a policy shift from inward-looking to outward looking development strategy was much evident from the growth performance of East Asian countries. These countries have experienced a high growth and poverty reduction through export led policies and higher private sector participation in economic activities. The Indian government initiated the process of economic liberalization in 1991 with emphasis on export-oriented growth strategy. In order to make economy more competitive and expanding the role of private sector specific measures were undertaken such as opening up of core sectors for both private and foreign investment, simplification of restrictive import licensing regime, reduction in import tariff, deregulation of markets, reduction of taxes and deregulation of financial sector. After the economic reform of 1991, growth picked up registering a GDP growth of over 7 per cent for three consecutive years starting from 1994.

India's growth experience post liberalization has been characterized by a decline in the share of agriculture in GDP and an increase in the shares of industry and services. The service sector has played an important role in accelerating the growth rate of an Indian economy in post-reform period. In India, services have been the fastest growing sector over the past decade, there has been phenomenal increase in the services sector contribution to Gross Domestic Product (GDP) growth. The remarkable growth experience witnessed by Indian economy post-reform is attributable in significant part to the spectacular dynamism shown by the services sector. The World Bank (2004) attributes the significant part of Indian economy growth in the decade of the 1990s to the rapid growth of its services sector. According to the World Bank, the average growth rate of India's services sector was 9 per cent per annum during the 1990s, which, in turn, contributed to 60 per cent of overall GDP growth rate of the economy. Moreover exports of services sector grew at a much faster rate than the rest of the world-over 17 per cent per annum. While the phenomenal growth and export performance

witnessed in services like information technology and business process outsourcing, which exhibit India's competitive advantage in supply of knowledge based services. Other services such as telecommunication, financial services, community services and hotels and restaurants have also grown faster than GDP over time.

In India, over the last few decades services have emerged as a crucial economic activity. It not only provides the bulk of employment and income but it also serves as a vital input for producing other goods and services (Prabir De, 2011). Services sector is the fastest growing sector in the Indian economy; it had made significant contribution to GDP, GDP growth, employment, trade and investment (Chahal, 2015) and has thus helped accelerate the overall growth of the Indian economy, services have also facilitated India's integration with the world economy through trade and capital flows. Services have also helped improve productivity in other sectors of the economy, thus contributing to an improvement in overall competitiveness (Chanda, 2007). Despite such an impressive growth the employment generation capacity of services sector is doubtful. The employment growth in services sector has not been commensurate to the income growth in the sector (Bosworth and Maertens, 2010) or the increase in its share in India's GDP (Kochhar et. al., 2006). The change in the production structure in an Indian economy from agriculture to services has not been reflected in a proportionate change in occupational structure (Bhattacharya and Mitra, 1990).

Given above background, the present study makes an analysis of service sector in the Indian economy. The objective of this study is to evaluate the performance of services sector post liberalization in terms of its contribution to GDP growth rate, employment generation and trade in the Indian economy. In section I, we provide an overview of the Indian services sector, with emphasis on growth of services in India, its share in GDP and its contribution to GDP growth, it also analyze the comparative growth of different sub sector of the service sector. Section II assess the contribution of services in employment generation. Section III presents an overview of trade in services in India, including its composition and its comparative advantage in export. Section IV discusses India's negotiating position in services in the WTO and bilateral trade agreements. Section V concludes and discusses the policy implication for the study.

2. Overview of Services in India

We start by reviewing the structural transformation of an Indian economy from agriculture to services sector and the growth of services sector during the last few decades. Figure 1 display the shares of agriculture, industry and services in GDP. It shows that the share of agriculture in GDP has declined overtime while that of industry has stagnated around 25 per cent after an initial rise from 14.3 per cent in 1950 to 24.2 per cent in 1990. On the other hand, the share of services in GDP has increased from less than 30 per cent in 1950 to around 60 per cent in 2013. In 2013-14, agriculture, industry and services respectively accounted for 15.8 per cent, 24.2 per cent, and 59.9 per cent of India's GDP. In 1950, share of services in India's GDP was 30 per cent, its share in GDP increased to 37.6 per cent in 1980, then to 42.5 per cent in 1990 and then finally to 60 per cent in 2013-14. Despite such a remarkable performance of services sector in India, its share in GDP is lower than that of developed countries (US (78.6 per cent), France (78.5 per cent), UK (73.2 per cent), Italy (70.5 per cent)), but higher than that of China (46.1 per cent) (GOI 2014).

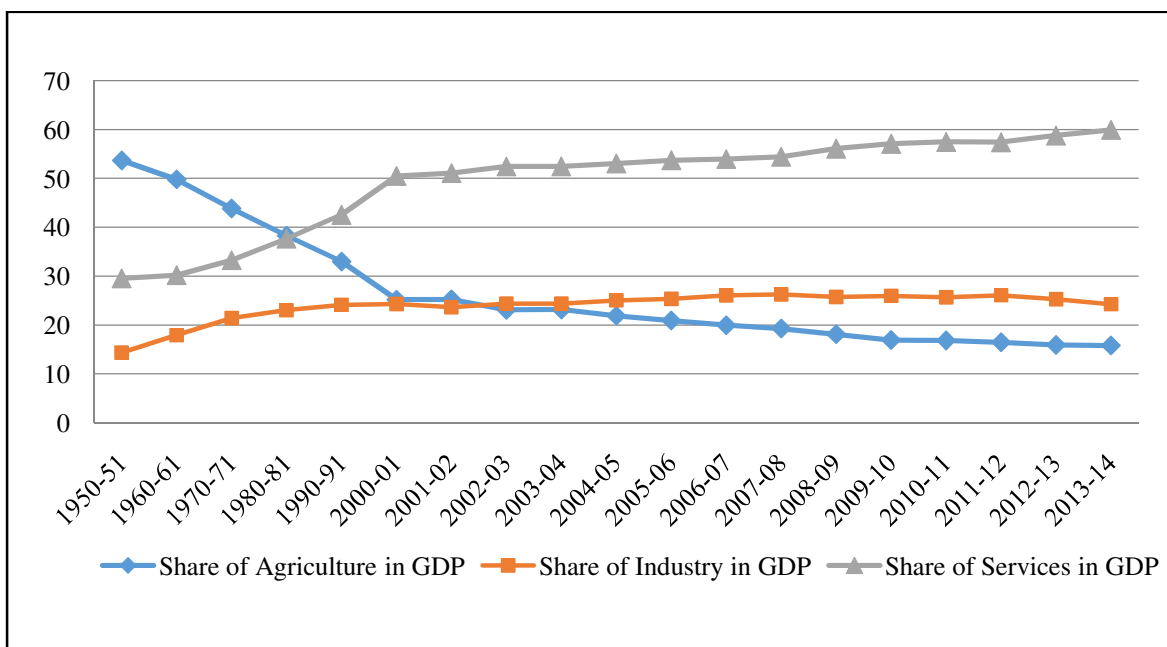


Figure 1: Share to GDP for each Sector

Source: Author's calculation based on data given in Economic Survey 2013-14

In order to analyze the growth and structure of services sector GDP in India, we need to know its constituent. Next I will analyze the constituents of service sector GDP in India. Based on the composition of services sector GDP, we will examine which services sub-sectors has grown faster and contributed the most to India's GDP since Independence.

2.1. Composition of Services Sector GDP in India

According to the National Income classification given by Central Statistical Organization, Services sector is classified in the following four sub-sectors:

1. Trade, Hotels and Restaurant
2. Transportation, Storage and Communication
3. Financing, Insurance, Real Estate and Business Services
4. Community, Social and Personal Services

The above four sub-sectors are further divided in sub-components.

Over the years, the share of services in GDP has increased but there are variations across services sub-sectors in terms of their share in GDP and its growth. Table 1 shows that services sector growth has always surpassed the growth rate of overall GDP in India. During the period 1950-1980, the compound annual growth rate (CAGR) of the GDP was below 3 per cent while for services it was around 4 per cent. Moreover, there is a wide variation in the growth rate of different sub-sectors within the services sector. Some services sub-sectors grew at a much higher rate than the aggregate services sector growth rate while others grew at the slower rate. From 1950 to 1980, transport, storage and communication services and trade, hotel and restaurant services have grown at the faster rate than the total services growth rate. Within the sub-sector transport, storage and communication services, transport by other means and communication services have grown at a much higher rate than the total services average growth rate. Although the sub-sector financing, insurance, real estate and business services have grown at a much slower rate than the total services growth rate, the banking and insurance services has grown at a much higher rate within this sub-sector. Similarly, within community, social and personal services, public administration and defense services have grown at a faster rate. Hence based on the analyzes, fast growers services i.e. sub-sectors which have grown faster than the total services include trade, hotels and restaurants; transport by other means; communication; banking and insurance; public administration and defence.

In the decade of 1980-90, the growth of services sector picked up, its CAGR increased from 3.96 per cent per annum in 1970 to 6.05 per cent per annum in 1980, the sub-sector that contributed the most to this growth rate was the financing, insurance, real estate and business services as it started growing at a faster rate. In fact in the 1980, financing, insurance, real estate and business services have grown at a much higher rate than the previous decades fast grower services sub-sectors such as trade, hotels and restaurants and transportation, storage and communication. During a period from 1980 to 1990, total services grew at a CAGR of 6.05 per cent per annum, while the financing, insurance, real estate and business services grew at a CAGR of 8.23 per cent per annum, within financing, insurance, real estate and business services, banking and insurance services (9.62 per cent per annum) have grown at a much faster rate followed by real estate, ownership of dwellings and business (7.49 per cent per annum). In the decade from 1990 to 2010, communication was the fastest growing services sub-sector, grew at a CAGR of 14.59 per cent per annum in 1990 and 21.54 per cent per annum in 2010, followed by banking and insurance services. These sub-sectors have grown at a much higher rate than the total services growth rate.

The CAGR of the services sectors are given in the table 1. for the period starting from 1950 to 2010. During the period from 1950 to 1970 the average annual growth rate of services sector was around 4 per cent per annum, in 1980s its growth rate increased to 6.05 per cent per annum later on to 6.83 per cent per annum in 1990s and then finally to 8.22 per cent per annum from 2000 to 2010. By examining the table given below, we can assert that in the 1950s, 1960s and 1970s, on an average transportation, trade, hotels and restaurants, public administration and defence, communication and financing and insurance services grew at a faster rate than the average of total services growth rate, these services contributed the most to services sector growth. In the decade 1980s, growth of financing, insurance, real estate and business services picked up strongly, in fact it was the fastest growing sub-sector within the services. In the decade 1990s to 2010, communication services grew at a faster rate followed by banking and insurance services, trade, hotels and restaurant services.

Components	CAGR 1950-60 (in per cent)	CAGR 1960-70 (in per cent)	CAGR 1970-80 (in per cent)	CAGR 1980-90 (in per cent)	CAGR 1990-00 (in per cent)	CAGR 2000-10 (in per cent)
Trade, hotels and restaurant	4.77	4.34	3.83	5.38	6.72	8.42
Trade	4.69	4.36	3.85	5.35	6.56	8.47
Hotels and restaurant	4.76	4.27	3.91	5.73	8.58	7.88
Transport, storage and communication	5.14	4.98	5.56	5.31	8.12	10.79
Railways	4.22	3.81	2.98	4.01	3.03	6.92
Transport by other means	5.51	5.39	6.42	5.89	6.72	7.76
Storage	2.39	2.48	8.33	3.08	1.97	5.99
Communication	5.79	6.57	5.85	5.27	14.59	21.54
Financing, insurance, real estate and business services	2.70	3.10	3.67	8.23	7.35	8.72
Banking and insurance	6.41	5.85	5.88	9.62	8.53	11.05
Real estate, ownership of dwellings and business services	2.11	2.46	2.89	7.49	6.55	7.00
Community, social and personal services	3.31	4.80	3.69	5.36	5.89	5.87
Public administration and defense	4.65	7.12	4.50	6.01	5.53	5.63
Other services	2.71	3.50	2.62	4.94	6.14	6.06
Total Services (excluding Construction)	3.75	4.27	3.96	6.05	6.83	8.22
GDP at factor cost	3.55	3.35	2.79	4.87	5.18	6.95

Table 1: Compound Annual Growth Rate of Services Sub-Sector

Note: 1. The calculations are made on the basis of GDP at constant prices (2004-05).

Source: Author's own calculations based on National Accounts, Central Statistical Organization, Ministry of Statistics and Programme Implementation, Govt. of India.

In the previous section, we attempt to analyze the services sub-sector GDP growth and structure for the period 1950 to 2010, of all the period considered for the analyzes, services GDP has grown at a much higher rate than the total services growth rate. The highest growth in services GDP was experienced in the decade 2000-2010, but not all services sub-sectors have grown at the same rate as the overall services sector. Some have grown at a faster rate while others have grown at a lower rate. Table 2 given below shows that the share of sub-sectors of services in the total services sector and GDP has changed overtime. The share of services in India's GDP has increased from 29.53 per cent in 1950-51 to 57.48 per cent in 2010-11 and to 59.92 per cent in 2013-14. But there is quite variation in contribution of different sub-sectors of services to India's GDP, some services have contributed the larger share to India's GDP while others have contributed a meager share. Since independence and post-liberalization share of many services in India's GDP and total services have altered.

From the period 1950 to 2000, trade, hotels and restaurant have the highest share in the overall services, followed by the financing, insurance, real estate and business services, which in turn is followed by other services. The highest share of trade, hotels and restaurants in total services is mainly because of the trade services and in case of financing, real estate and business services it's mainly due to community, social and personal services. In fact during the period 1950-2000, the sub-sector community, social and personal services within financing, real estate and business services have the highest share in total services and GDP among all the services sub-sector. However in 2010, financing, insurance, real estate and business services have the highest share in total services, followed by trade, hotels and restaurants and transport, storage and communication. Within trade, hotels and restaurants services, trade have the highest share in services in 2010, followed by community social and personal services, which falls under the sub-sector financing, insurance, real estate and business services. Banking and insurance services have achieved a highest increase in its share in services, from a meager 3.31 per cent in 1950 to 14.38 per cent in 2010, followed by communication services, its share in services increased from 0.48 per cent in 1950 to 6.66 per cent in 2010.

In table 2. the share of services sub-sector in GDP of India are given, since independence the share of most of the services in GDP have increased. The share of trade, hotels and restaurants, transport, communication, banking and insurance, real estate, ownership of dwellings and business services, community, social and personal services, public administration and defence sector in total GDP of India have increased while that of railways and storage has declined. In 1950, community, social and personal services (10.18 per cent) have the highest share in India's GDP followed by trade (7.81 per cent), other services (7.77 per cent) and real estate, ownership of dwellings and business services (7.52 per cent). In 2010, trade (15.53 per cent) have the highest share in GDP of India followed community, social and personal services (12.89 per cent), real estate, ownership of dwellings and business services (9 per cent), banking and insurance (8.27 per cent) and other services (7.20 per cent). During the period 1950 to 2010, highest increase have been experienced by communication services, its share in GDP has increased from 0.14 per cent in 1950 to 3.83 per cent in 2010, followed by banking and insurance, the share has increased from 0.98 per cent in 1950 to 8.27 per cent in 2010, and transport services, its share in GDP has increased from 1.73 per cent in 1950 to 5.46 per cent in 2010.

Components	1950	1960	1970	1980	1990	2000	2010
Trade, hotels and restaurant	28.40 (8.39)	31.60 (9.54)	31.84 (10.59)	31.42 (11.83)	29.30 (12.47)	28.99 (14.64)	29.58 (17.00)
Trade	26.43 (7.81)	29.19 (8.81)	29.46 (9.80)	29.12 (10.96)	27.08 (11.52)	26.34 (13.30)	27.02 (15.53)
Hotels and restaurant	2.07 (0.61)	2.30 (0.69)	2.30 (0.77)	2.29 (0.86)	2.21 (0.94)	2.65 (1.34)	2.56 (1.47)
Transport, storage and communication	8.89 (2.62)	10.29 (3.11)	11.08 (3.69)	13.12 (4.94)	12.15 (5.17)	13.88 (7.01)	17.96 (10.32)
Railways	3.91 (1.16)	4.11 (1.24)	3.92 (1.30)	3.53 (1.33)	2.85 (1.21)	1.91 (0.97)	1.68 (0.96)
Transport by other means	5.85 (1.73)	7.03 (2.12)	7.91 (2.63)	10.24 (3.85)	10.07 (4.28)	9.96 (5.03)	9.50 (5.46)
Storage	0.30 (0.09)	0.26 (0.08)	0.22 (0.07)	0.34 (0.13)	0.25 (0.11)	0.15 (0.08)	0.12 (0.07)
Communication	0.48 (0.14)	0.60 (0.18)	0.76 (0.25)	0.93 (0.35)	0.86 (0.36)	1.86 (0.94)	6.66 (3.83)
Financing, insurance, real estate and business services	28.24 (8.34)	25.23 (7.62)	22.30 (7.42)	21.64 (8.15)	27.06 (11.51)	28.56 (14.42)	30.03 (17.27)
Banking and insurance	3.31 (0.98)	4.37 (1.32)	5.17 (1.72)	6.32 (2.38)	9.10 (3.87)	10.83 (5.47)	14.38 (8.27)
Real estate, ownership of dwellings and business services	25.45 (7.52)	21.35 (6.44)	17.61 (5.86)	15.72 (5.92)	18.24 (7.76)	17.73 (8.95)	15.65 (9.00)
Community, social and personal services	34.48 (10.18)	32.89 (9.93)	34.78 (11.57)	33.82 (12.73)	31.49 (13.40)	28.57 (14.42)	22.43 (12.89)
Public administration and defence	9.48 (2.80)	10.42 (3.15)	14.02 (4.66)	14.85 (5.59)	14.79 (6.29)	12.94 (6.53)	9.91 (5.70)
Other services	26.32 (7.77)	23.54 (7.11)	21.69 (7.21)	18.82 (7.09)	16.78 (7.14)	15.63 (7.89)	12.52 (7.20)
Total of Services	100.00	100.00	100.00	100.00	100.00	100.00	100.00

Table 2: Share of Services Sub-sectors in Total Services Sector and GDP (in per cent)

Note 1. Share of services sub-sector in GDP are given in bracket and values given above the value given in bracket are the share of services sub-sector in total services.

Source: Authors own calculations based on National Income Accounts, Central Statistical organization, Ministry of Statistics and Programme Implementation, GOI.

3. Employment in the Services Sector

Economic growth in the India is accompanied by a change in the production structure with a shift away from agriculture sector towards services and the industry sector. During the 1950s, agriculture accounted for the largest share in GDP but over the years its share declined while that of services and industry increased. Today services sector is the dominant sector in India accounting for about 60 per cent of GDP. However despite its growing importance, the share of the working population employed in services sector remains low. Thus there is a serious doubt about the employment generation capacity of the services sector. It has been argued that over the years, while output growth rate in service sector has increased, employment growth rate has decelerated significantly leading to a considerable fall in the employment elasticity (Nayak and Pattanaik, 2011). There has been disproportionate growth in services sector, as its share in employment is far much lesser than its share in GDP (Joshi, 2008). As a result, services driven growth in the Indian economy has been ‘‘jobless growth’’ intensifying the problems of informal labor and unemployment (Banga, 2005 and Bhattacharya and Sakthival, 2004)

	Absolute number (million) (Share in percent given in parentheses)					CAGR (per cent)
	1993-94	1999-00	2004-05	2009-10	2011-12	1993-12
Agriculture	204.3 (61.1)	214.7 (58.5)	226.8 (54.5)	220.5 (51.6)	204.4 (47.1)	0.002
Industry	53.5 (16.0)	61.7 (16.8)	81.0 (19.5)	93.1 (21.8)	106.1 (24.4)	3.87
Services	76.6 (22.9)	90.6 (24.7)	108.0 (26.0)	113.7 (26.6)	123.9 (28.5)	2.70
Trade, hotels, and restaurants	26.8 (8.0)	34.1 (9.3)	46.5 (11.2)	48.4 (11.3)	50.5 (11.6)	3.58
Transport, storage, and communication	11.0 (3.3)	15.0 (4.1)	18.7 (4.5)	19.9 (4.6)	22.8 (5.2)	4.13
Financial, insurance, real estate and business services	3.7 (1.1)	4.8 (1.3)	7.5 (1.8)	9.4 (2.2)	10.7 (2.5)	6.07
Community, social, and personal services	35.1 (10.5)	36.7 (10.0)	35.3 (8.5)	36.1 (8.4)	39.9 (9.2)	0.71
Total	334.4 (100.0)	367.0 (100.0)	415.7 (100.0)	427.4 (100.0)	434.4 (100.0)	1.46

Table 3: Employment in Different Sectors and Some Services Sub-sectors in Absolute Number and as a Percentage of Total Employment in India

Source: Based on data from National Sample Survey Office (NSSO) different round reports and Central Statistical Organization (CSO).

During the past two decades, the pattern of the sectoral share of employment has changed with the share of agriculture falling and of industry and services rising. Despite this agriculture sector employs the highest number and percentage of people among all the different sectors in India. Table 3 reports the sectoral distribution of workforce during the period 1993-94 to 2011-12. It reveals that the structural changes in terms of employment have been slow in India as the agriculture sector continue to absorb 47.1 per cent of the total workforce even in 2011-12, followed by services and industrial sectors (28.5 per cent and 24.4 per cent) respectively. During the period 1993-94 to 2011-12, employment in the services sector grew at a CAGR of a 2.70 per cent per annum (Table 3). However, within the services sector there were several sub-sectors where employment grew at a much faster rate. Employment in financial, insurance, real estate and business services grew at the highest rate at the CAGR of 6.07 per cent per annum, followed by transport, storage, and communication; trade, hotels, and restaurants; and community, social, and personal services. There was continuous increase in employment share in trade, hotels, and restaurants; transport, storage, and communication; and financial, insurance, real estate and business services. Employment share of community, social, and personal services has fallen continuously except for 2011-12.

Over the years, financial services and communication services registered a faster growth both in terms of employment and GDP share, but their share in employment is very low as compared to share in GDP (Table 3). Community, social and personal services, which used to have a largest share in employment and GDP till 2000, has experienced a decline in its importance in services sector and is now the smallest in regard to GDP contribution. Though services sector is gaining the primary position in terms of its contribution to India's GDP, in terms of employment its contribution is very low as compared to agriculture. Moreover the large numbers of jobs in services sector are created in the sectors driven by unskilled sectors like trade, hotels and restaurants and community, social and personal services (Table 3) pushed out by agriculture and not absorbed by the industry. There is a little job creation in skilled labor intensive sectors like financing, insurance, real estate and business services. This has led to the accentuation of income inequality problem in the Indian economy.

4. India's Services Trade

In the past few decades, India has witnessed a structural shift towards the services sector, with services accounting for more than half of India's GDP. Despite the impressive rise in the contribution of services sector to India's GDP, there has not been parallel rise in the services trade share in GDP. Table 4 shows that the services trade share in India's GDP was meager 0.91 per cent in 1980, it increased to 3.38 per cent in 1990 and finally to 13.29 per cent in 2013, whereas it accounted for more than half of the India's GDP in 2013 (59.9 per cent). Nevertheless, in the last few decades, trade in services in India has been expanding rapidly following domestic liberalization. India share in world services trade has increased post liberalization from slightly above 1 per cent in 1990 to 3 per cent in 2013. Moreover overall trade in services in India has grown at a much faster rate than the world trade in services over the past few decades. In 2013, India's total trade in services stood at over US\$ 277 billion, of which the value of exports and imports were US\$ 151 billion and US\$ 125 billion, respectively, resulting in a positive trade balance of the amount US\$ 26 billion.

In India during the period 1990-2013, services trade has grown twice as faster than the world services trade, exports has grown at a much faster rate than the imports thus resulting in a growing surplus in trade balance except for the year 1995-96 (Figure 2). The compound annual growth rates (CAGR) of services total trade, exports and imports in India was 14.5 per cent, 15.6 per cent and 13.4 per cent respectively during the period 1990-2013, in case of World these figures are much lower as compared to India (Table 4).

Year	Share of Services Trade in GDP (per cent)	World			India			Share in world (per cent)
		Export (in US\$ billion)	Import (in US\$ billion)	Total (in US\$ billion)	Export (in US\$ billion)	Import (in US\$ billion)	Total (in US\$ billion)	
1980	0.91	395.66	447.77	843.43	2.97	2.98	5.95	0.70
1990	3.38	831.35	875.19	1706.54	4.62	6.09	10.71	0.11
2000	7.84	1521.98	1519.39	3041.37	16.68	19.18	35.86	1.17
2010	12.35	3896.26	3739.25	7635.51	116.94	114.45	231.39	3.03
2011	12.48	4372.89	4180.64	8553.53	138.75	124.73	263.48	3.08
2012	13.11	4473.81	4292.68	8766.49	146.14	128.83	274.97	3.13
2013	13.29	4720.18	4499.19	9219.37	151.38	125.68	277.06	3.00
CAGR (in per cent)								
1980-1990	2.40	6.98	6.28	6.62	4.10	6.71	5.49	-0.01
1990-2000	6.01	5.65	5.14	5.39	12.38	10.99	11.61	0.23
2000-2010	9.24	8.92	8.53	8.73	19.37	17.63	18.47	1.98
1990-2013	11.72	7.50	7.06	7.28	15.65	13.44	14.52	6.74

Table 4: India's Services Trade Growth

Source: Authors calculation based on UNCTAD handbook of statistics 2014 database and RBI 2014.

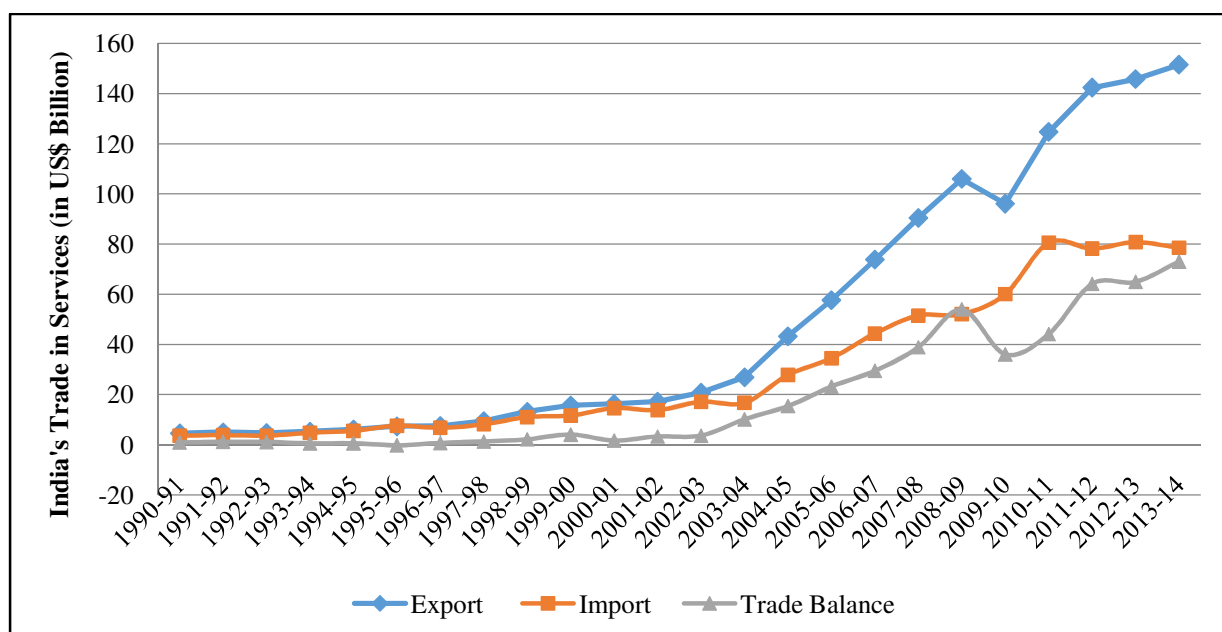


Figure 2: India's trade in Services during the period 1990-2013

Source: RBI Handbook of Statistics, 2014

Given that trade in services in India has expanded rapidly in the past decades resulting in a favorable trade balance, it is worth exploring which services sub sectors exports has grown rapidly over the years. According to the World Trade Organization in 2013, the world trade in services is dominated by the top 10 traders accounting for a half of the world trade in commercial services. India is the most dynamic exporter of the commercial services in the world. It ranks 4th among the top 10 exporters of commercial services in the world in 2013 (European Union (ranks 1st), United States (ranks 2nd) and China (ranks 3rd)), with a value of US\$ 151 billion and a share of 4.3 per cent and a growth rate of 4 per cent.

According to the WTO, 2014 the growth rate of world exports of services was around 5.5 per cent in 2013, and about 7 per cent in the first quarter of 2014, compared with the same period of the previous year. In 2013, it reached \$4.7 trillion, representing 20 per cent of total exports of goods and services-a share that has been quite stable since the 1990s. During 2001-13 the CAGR of global services export was 10 per cent, with India at the top among the top fifteen largest economies at 20.1 per cent followed by China at 16.5 per cent. In 2013, services exports of the United States, the largest exporter of services, grew by 5 per cent while they decelerated for China to 7.5 per cent and India to 3.6 per cent due to decline in exports of transport services by 3 per cent in both the countries.

Table 5 presents the major components of India's services exports during the period from 1980 to 2013. In India other services have always constituted the major component of India's services export. The share of both transport and travel services in total services exports has declined drastically. Transport services share declined from 15 per cent in 1980 to 11.2 per cent in 2013; travel services share declined from 52.2 per cent in 1980 to 12.2 per cent in 2013. In case of other services, the share in total services export jumps from a 32.8 per cent in 1980 to 75.3 per cent in 2013. Within other services, in 2013, other business services (33.6 per cent) constituted the highest share in the total services export in India, followed by computer and information services (32.7 per cent), financial services (3.9 per cent), communication services (1.5 per cent) and insurance services (1.4 per cent). There has been a compositional shift in the structure of India's services exports away from traditional services such as travel and transport towards other services such as computer and information, other business services and financial services.

The shift in composition of services exports in India is consistent with the changes in the world composition of services exports. The world exports decreased, from 23.2 per cent in 2000 to 19.5 per cent in 2013 in transportation services, from 32.0 per cent in 2000 to 25.5 per cent in 2013 in travel services, whereas it increased from 44.8 per cent in 2000 to 54.9 per cent in 2013 in other commercial services (WTO, 2014). In 2013, India was a 4th largest exporter of other commercial services with a share of 4.5 per cent, 9th largest exporter of transportation services with a share of 1.9 per cent, 11th largest exporter of travel services with a share of 1.6 per cent. Within other commercial services, India was a 2nd largest exporter of computer and information services with a share of 19.7 per cent after European Union (23.4 per cent) in 2013; 4th largest exporter of other business services with a share of 4.9 per cent and a 6th largest exporter of financial services with a share of 1.8 per cent in a top 10 exporters of the world.

Major Components	1980 (in %)	1990 (in %)	2000 (in %)	2005 (in %)	2006 (in %)	2007 (in %)	2008 (in %)	2009 (in %)	2010 (in %)	2011 (in %)	2012 (in %)	2013 (in %)
Transport	15.0	20.7	11.9	11.0	10.8	10.4	10.8	11.9	11.3	12.7	12.0	11.2
Travel	52.2	33.7	20.7	14.3	12.4	12.3	11.0	12.0	12.4	12.8	12.3	12.2
Other services	32.8	45.6	67.4	74.8	76.8	77.3	78.2	74.1	71.9	69.9	73.1	75.3
Communications	-	-	3.6	3.0	3.1	2.7	2.3	2.1	1.3	1.2	1.1	1.5
Construction	-	-	3.0	0.7	0.9	0.9	0.8	0.9	0.4	0.6	0.6	0.8
Insurance	1.2	2.7	1.5	1.8	1.6	1.7	1.5	1.6	1.5	1.9	1.5	1.4
Financial services	-	-	1.7	2.2	3.4	3.9	4.0	3.9	5.0	4.5	3.5	3.9
Computer and information	-	-	24.3	30.6	30.6	31.6	33.5	34.9	33.3	32.8	32.3	32.7
Royalties and licence fees	-	-	0.5	0.4	0.1	0.2	0.1	0.2	0.1	0.2	0.2	0.3
Other business services	27.8	42.5	-	35.3	36.2	35.3	35.0	29.5	29.5	28.0	32.9	33.6
Personal, cultural and recreational services	-	-	-	0.2	0.4	0.6	0.7	0.5	0.3	0.2	0.5	0.8
Government services n.i.e.	3.7	0.3	3.9	0.6	0.4	0.4	0.4	0.4	0.4	0.4	0.3	0.3

Table 5: Composition of India's Services Exports

Note1. Blank given in place of figure indicate a non-availability of data in that particular year.

Source: Authors own calculation based on International Monetary Fund, 2014 Database.

4.1. India's Competitiveness in Services Export

To understand the pattern of India's services trade specialization, and to find out whether or not the services sector in India is globally competitive, the relative competitiveness of services trade can be examined with the help of the Revealed Comparative Advantage (RCA) (formula for calculating RCA is given in Appendix A) of different services trade sector. This index shows the country's specialization in individual services subsectors and therefore their comparative advantage vis-à-vis rest of the world. If the RCA is greater than one the country is said to have comparative advantage in that particular services vis-à-vis rest of the world.

The RCA scores of India's services exports are given in Table 6. India has a comparative advantage in travel services in 1980 and 1990, which has been replaced by other services from 1990 onwards. During the period from 1990 to 2013, India has a comparative

advantage in an export of other services. Within other services, India has a strong comparative advantage in computer and information services. India also has a comparative advantage in other business services. Since transport and travel are associated with infrastructure while computer and information and, other business services are technology and knowledge intensive services trade, it reflects India's comparative advantage in skill and knowledge-intensive labor-based services. India's comparative advantage in these services is attributed to its growing pool of highly skilled, low cost workers.

Major Components	1980	1990	2000	2005	2006	2007	2008	2009	2010	2011	2012	2013
Transport	0.4	0.8	0.5	0.5	0.5	0.5	0.5	0.6	0.5	0.6	0.6	0.6
Travel	2.0	1.1	0.7	0.5	0.5	0.5	0.4	0.5	0.5	0.5	0.5	0.5
Other services	0.8	1.1	1.5	1.5	1.5	1.5	1.5	1.3	1.3	1.3	1.3	1.4
Communications	-	-	1.6	1.3	1.3	1.1	0.9	0.8	0.5	0.5	0.5	0.6
Construction	-	-	1.5	0.3	0.4	0.3	0.3	0.3	0.2	0.2	0.3	0.4
Insurance	-	-	0.8	0.9	0.7	0.8	0.7	0.6	0.6	0.8	0.7	0.7
Financial services	-	-	0.3	0.3	0.4	0.5	0.5	0.5	0.7	0.6	0.5	0.6
Computer and information	-	-	8.1	7.6	7.1	7.1	6.7	6.5	6.1	5.7	5.5	5.4
Royalties and licence fees	-	-	0.1	0.1	-	-	-	-	-	-	-	-
Other business services	-	-	-	1.5	1.5	1.5	1.4	1.2	1.2	1.1	1.3	1.3
Personal, cultural and recreational services	-	-	-	0.2	0.5	0.8	0.9	0.6	0.3	0.3	0.6	0.9
Government services n.i.e.	0.5	0.1	1.9	0.3	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2

Table 6: India's RCA in Services Exports

Note1. Blank given in place of figure indicate a non-availability of data in that particular year.

Source: Authors own calculation based on International Monetary Fund, 2014 Database.

5. India's Position on Trade Negotiations in Services

India is always actively involved in the WTO negotiations on services. During the Uruguay Round services were brought under the preview of trade negotiations and the outcome was the GATS Agreement that came into force along with the WTO in 1995. During the initial years of Uruguay Round, India was strongly opposed to the inclusion of services in the WTO agreement. It was believed by the policymakers that opening up of services sector for trade would badly affect the Indian services sector by exposing it to global competition. In fact in 1980, the contribution of services sector to GDP was quite low (37.6 per cent). With the initiation of the process of liberalization in Indian economy and the General Agreement on Trade in Services (GATS) under the WTO, a wide range of services was brought under the purview of trade negotiations, which were earlier considered to be non-tradable. The growth of services sector picked up in 1990, the share of services sector in India's GDP increased from 37.6 per cent in 1980 to 42.5 per cent in 1990, then to 50.48 per cent in 2000 and finally to 60 per cent in 2013-14. The India's share of services in world trade increased from 0.1 per cent in 1990 to 1.2 per cent in 2000 and to 3 per cent in 2013. In fact, the share of services trade in India's GDP increased from 0.91 per cent in 1980 to 3.4 per cent in 1990, to 7.8 per cent in 2000 and then finally to 13.3 per cent in 2013.

Under GATS, the provision of services was classified into four modes: Mode 1- cross border supply; Mode 2 –consumption abroad; Mode 3 -commercial presence; and Mode 4 – movement of natural persons. In view of the various trade barriers that affect India's key modes of export interest and as an emerging global power in IT and business services, India has taken a proactive position in the services negotiations on temporary cross-border movement of service providers (Mode 4) and cross-border supply of services (Mode 1) under the GATS. With respect to Mode 2, which requires consumption of services abroad India has taken an offensive interest. India has taken offensive position in Mode 3, which requires the establishment of a commercial presence in a country. India also wants liberal commitments in Mode 1 or cross border trade and in sectors like computer and related services. India also seeks greater access to the EU and the US in terms of the movement of natural persons (Mode 4). Movement in Mode 4 is opposed by the EU and the US, as there interests lie more in Mode 3 supply of services. Accordingly there is demand for more liberal policies on foreign direct investment in sectors like insurance services. While the demanders have high expectations in terms of the market access they want, they are not willing to open up their own economies to the same degree, particularly in Mode 4. Although as far as delivery of services through commercial presence (Mode 3) is concerned, an increasing trend of Indian companies acquiring assets and opening up of businesses in foreign markets is observed, India is not a proponent of supply of services through Mode 3. This conflict of interest among EU, US and India are acting as a barrier to India's exports.

In order to enhance India's services export, Indian government is taking several measures. Recently government has raised the FDI cap in insurance sector to 49 per cent from 26 per cent. The policy was also relaxed in other sectors such as defence, railways and medical devices. The government has announced a series of steps such as fixing timelines for approvals to improve ease of doing business in the country and to attract domestic and foreign investments. In order to prevent any kind of market failure, such attempts to liberalization of services sector must be accompanied by effective regulatory reforms. A further study is needed to examine the gains that can accrue to India through such autonomous liberalization. Even in the absence of additional liberalization, India's services exports would continue to grow. Any market access commitments that India might make during the ongoing negotiations must be based on the possibility of finalising mutual recognition agreements with the main importers of services, so that differences in national regulatory systems do not act as barriers to its exports.

In India, during the Ninth plan period the emphasis was given to regional trade agreements in trade policy but the move intensifies during the Tenth Plan. India has signed four bilateral agreements covering services. These include India-Singapore Comprehensive

Economic Cooperation Agreement (August 2005), India-Korea Comprehensive Economic Partnership Agreement (January 2010), Comprehensive Economic Cooperation Agreement between India and Malaysia (July 2011) and Comprehensive Economic Partnership Agreement between India and Japan (August 2011). India's engagement in a large number of FTA is inevitable as it needs foreign investment and technology, particularly in infrastructure sector. This raises some issues, before implementing any agreement; our social and physical infrastructure must be brought on par with the trading partner with whom we are entering into an agreement. It is particularly necessary to raise the level of education and skills and to improve infrastructure in the country, as otherwise these agreements will result in flight of capital from the country.

6. Conclusion

The study highlights that with the initiation of the process of economic liberalization in India, the services sector has gain prominence in the Indian economy as it accounts for the largest share of GDP and also the share of this sector in employment and trade has been rapidly growing. It has not just outperformed the other sectors of the Indian economy, but has played an important role in integrating Indian economy with the world economy. The contribution of services sub-sectors to India's GDP has also increased during the past few decades. The share of different sub-sectors of services in the total services sector and GDP has changed overtime. Even though India has experienced profound changes in output shares, the same is not true for employment shares. A striking feature of India's development is that in contrast to the substantial decline in the share of agriculture in GDP, there has been rather little change in the share of employment in agriculture. Thus while production structure of the economy has changed in favour of services sector, employment creation in services has lagged far behind. The fastest growing services are those that are not generating sufficient growth in employment opportunities for the masses. More broad based growth within the services is required in services sub sectors such as trade, hotels and restaurants; and community, social and personal services which has high employment intensities.

Over the years, the share of financial and communication services has experienced a fastest growth both in terms of employment and GDP share, but their share in employment is very low as compared to share in India's GDP. Following economic liberalization, trade in services in India has expanded rapidly resulting in a favorable trade balance. According to the World Trade Organization in 2013, the world trade in services is dominated by the top 10 traders accounting for a half of the world trade in commercial services. India is the most dynamic exporter of the commercial services in the world. It ranks 4th among the top 10 exporters of commercial services in the world in 2013. There has been a compositional shift in the structure of India's services exports away from traditional services such as travel and transport in towards other services such as computer and information, other business services and financial services. India has a comparative advantage in export of computer and information services and other business services. Though there has been commendable growth in the trade in computer and business services but their employment generating capacity is not adequate to accommodate the workers displaced by the agriculture. If India wants to continue with its services sector drive growth momentum, it must take significant measures to bring services sector parallel to the primary and secondary sector in terms of employment generation. As far as India's position in services trade negotiation is concerned, any market access commitments that India might make during the ongoing negotiations must be based on the possibility of finalising mutual recognition agreements with the main importers of services, so that differences in national regulatory systems do not act as barriers to its exports.

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Appendix A

The Revealed Comparative Advantage for services exports given in Table 6. are calculated as per the Balassa's index (1965). The formula is

$$RCA_{ij} = (x_{ij}/X_{it}) / (x_{wj}/X_{wt})$$

where,

RCA_{ij} = Revealed comparative advantage of the i^{th} country (India) in j^{th} services,

x_{ij} = Exports of the i^{th} country (India) in j^{th} services,

X_{it} = Total service exports of the i^{th} country (India) in period t ,

x_{wj} = Total world exports of j^{th} services,

X_{wt} = Total world exports of services in period t .

If the RCA is greater than one the country is said to have a comparative advantages in the particular services sub-sector *vis-à-vis* rest of the world.