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INVESTMENT OPPORTUNITIES OF SERVICE SECTOR IN INDIA

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ABSTRACT

At the dawn of the 21st century, all the industrialized countries donned the avatar of 'service economy', at least when measured in terms of percentage of workforce employed, strictly following the three-sector hypothesis proposed by Allan Fisher (1935) and Colin Clark (1940). According to this hypothesis during the course of economic progress, the main focus of an economy's activity shifts from the primary, through the secondary and ultimately to the tertiary sector. Thus service sector is an important component of any country's economy. It has a direct and significant bearing on the GDP of a country, leads to job creation, and also provides crucial inputs for the rest of the economy; It thus has a significant influence on the overall investment climate of a country, which is an essential determinant of growth and development. In line with the global trend, service sector in India has also grown rapidly in the last decade. If we look at the growth statistics of India it is evident that for more than a decade, the growth of India so far is driven by its service sector. Service sector of India with its remarkable performance has emerged out as its fastest growing sector of the country leaving behind agriculture and manufacturing sector. In the absence of which the Indian economy would not have been able to achieve a strong and dominating place on the world platform. This research paper through seven parts including Introduction, Significance of the study, Objectives, Research Methodology, Literature Review, Importance of the service industry to the Indian economy and the conclusion emerging through the study makes an attempt to explore investment opportunities of service sector in India.

KEYWORDS

Service Sector, Investment opportunities, India.

1. INTRODUCTION

Services have come to dominate our economies. Whether you manage a traditional service firm or a manufacturing company, adding value through services has become an essential way to compete. Today customers are looking for service value, comprehensive solutions, and memorable experiences" (Gustafsson, Johnson, 2003).

This statement clearly indicates the importance of service industry to an economy. During the initial stages of economic development agriculture sector occupies the status of being the most important sector. But as the economic development gains momentum agriculture loses its primacy, giving way first to a rise in the industrial sector, then to a rise in the service sector. These two consecutive transitions are called industrialization and post-industrialization/ deindustrialization. All the developed countries including USA and UK have passed through these phases and the growing economies are either going through this transition or will be in future. So Service sector eventually is responsible for sustaining the economic development of the economies and India is not an exception to this.

Post-independence India struggled very hard to create an identity for itself from the scratch. The period of liberalization of Indian economy helped it to recover from slow paced economic growth. The current economic statistics of India are promising it to be the super power in the world. Now, the Indian economy boasts of a stable annual growth rate, booming capital markets, and rising foreign exchange reserves. The emergence of India as one of the fastest growing economies in the world in the 1990s can be attributed, to a large extent, on the rapid growth of its service sector. It has played a vital role in the transition of India from being the land of snake charmers to the Silicon Valley of Asia.

1.1 CLASSIFICATION OF SERVICES SUB SECTORS IN INDIA

As per the National Accounts classification of the services sector following are the service sub sectors in India.

TABLE 1: SERVICE SUB- SECTORS IN INDIA

Sector	Activities Included
Trade, hotels and restaurant	
Trade (distribution services)	Wholesale and retail trade in commodities both produced at home (including exports) and imported, purchase and selling agents, brokers and auctioneers.
Hotels & Restaurants	Services rendered by hotels and other lodging places, restaurants, cafes and other eating and drinking places.
Transport, storage and communication	
Railways	
Transport by other means	Road, water, air transport, services incidental to transport.
Storage	
Communication	Postal, money orders, telegrams, telephones, overseas communication services, miscellaneous.
Financing, insurance, real estate and business services	
Banking	Banks, banking department of RBI, post office saving bank, non-bank financial institution, cooperative credit societies, employees provident fund.
Insurance	Life, postal life, non-life.
Dwellings, real estate	
Business services	
Legal services	
Community, social and personal services	
Public administration, defense	
Personal services	Personal services Domestic, laundry, barber, beauty shops, tailoring, others.
Community services	Community services Education, research, scientific, medical, health, religious and other community.
Other services	Recreation, entertainment, radio, TV broadcast, sanitary services.

Source: Banga Rashmi (2005), Critical Issues In India's Service-Led Growth, ICRIER Working Paper No. 171.

1.2. IMPORTANCE OF SERVICE SECTOR FOR AN ECONOMY**1.2.1 AT GLOBAL LEVEL**

If we take a rear view we can see that Service sector is one of the most important sectors for an economy. At the global level the total world export of commercial services accounts for US \$ 3.7 trillion led by developed western countries in terms of share and by Asian countries in terms of growth rate. Since 2008 exports of commercial services by the Asian countries are expanding on an average by 13 per cent annually. Countries like China, India and Singapore are among the top traders of Services.

After the economic crisis of 2008:

- Asia led by India and China witnessed a rapid growth of commercial services, its exports rose by 22 per cent in 2010;
- Where as in European Union the export of services grew merely by 3 per cent, Central and South America, the Caribbean and the Commonwealth of Independent States recorded a growth of 12 per cent;
- While North America by 9 per cent and Africa by 10 per cent.

Thus the equations are changing and emerging economies like India and China are now playing a leading role in commercial services trade at global level.

If we combine the service trade of European Union (27) by ignoring intra EU trade then the EU (27), the USA, China, Japan and India with same ranks both in exports and imports of commercial services are the top five exporters and importers of commercial services. Only China and Japan are net importers of commercial services in the list of top five. India is an important player in the global commercial services trade. Five years back India's share in the total world trade of commercial services was merely 2.8 per cent and now it has increased to 4.3 per cent. In 2010 its exports grew by 33 per cent and imports by 45 per cent, making India the most dynamic exporter of commercial services.

1.2.2 AT NATIONAL LEVEL

Following the economic liberalization the service sector of India has gained prominence in the economy as it accounts for the largest share (68%) of the GDP, growing very rapidly at the rate 10 per cent annually. After Agriculture it occupies second place in generating about a quarter of total employment, attracting a very high share in foreign direct investment (FDI) inflows and sharing about one-third of total exports of the country, and recording very fast (27.4 per cent) export growth through the first half of 2010-11.

TABLE 2: SECTORAL PERCENTAGE SHARE OF GDP

Year	Agriculture & Allied Activities	Industry	Services
1950-51	55.28	10.65	34.07
1960-61	50.81	13.18	36.01
1970-71	44.31	15.46	40.23
1980-81	37.92	17.45	44.63
1990-91	31.37	19.80	48.83
2000-01	23.89	19.99	56.12
2005-06	19.54	19.36	61.10
2006-07	17.4	28.7	54.0
2007-08	16.8	28.7	54.4
2008-09	15.8	28.1	56.1
2009-10	14.7	28.1	57.2
2010-11	14.5	27.8	57.7
2011-12	19.2	25	55.1

Source: Tiwari Sanjay (2011), Service Sector in India: Performance and Reforms, *International Journal of Multidisciplinary Research*, Vol.1(7) and Exim Bank of India.

2. SIGNIFICANCE OF THE STUDY

As noted, Indian Service sector is emerging as a promising sector of the country by offering a lot of opportunities to all the stakeholders. It is therefore important to understand the dynamics of this sector. With this objective in consideration an attempt has been made through this paper to explore the investment opportunities of service industry in India by analyzing the current performance of its various sectors and sub sectors.

3. OBJECTIVES AND RESEARCH METHODOLOGY OF STUDY

This research paper is designed to evaluate the investment opportunities in India:

- To know the importance of Service Sector.
- To analyze the contribution of sectors and sub sectors of service industry in India
- To explore the investment opportunities of service sector in India

The study is based on secondary sources of data. The data and material to carry out this research was collected, marshaled and analysed to draw inferences and conclusions. Sources of data were largely from the various issues of Economic Survey, published by Government of India and Ministry of Commerce and Industry, Reserve Bank of India bulletin, Scholarly articles, Journals, and reports of WTO, World Bank etc. The present research is based on Explorative as well as descriptive research design.

4. LITERATURE REVIEW

Rath, Deba Prasad and Raj, Rajesh (2006) in their research paper titled "Analytics and Implications of Services Sector Growth in Indian Economy" stated that the higher growth in services sector has added a dimension of stability to India's growth process. Growing complementarity between the industrial and services sectors augurs well for the medium-term growth performance of the Indian economy. Unlike other commodity-producing sectors, which have either seen a stagnant growth or decline in employment, they found that the services sector has generated some employment opportunities.

Tiwari Sanjay (2011) in his research paper titled "Service Sector in India: Performance and Reforms" concluded that India's potential for service economy is matchless as there is burgeoning middle class with enhanced aspirations. Their changing consumption pattern, growing retail, emerging domestic & international market for IT/ITES has opened new vistas of service subsectors (lifestyle based consumer services like personal care, health care etc.). With the revival of US economy and potential market of Indian IT-BPO sector in different parts of the world and the rise in domestic demand, the service led economy will definitely propel into higher trajectory in near future.

Banga Rashmi (2005) in her research work on "Critical Issues in India's Service-Led Growth" conducted a literature survey which argued that when an economy grows, both demand and supply 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:

A. 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.

B. Supply-Side Factors: Trade Liberalisation and Reforms

- Increased trade
- Higher foreign direct investments in services and

c) Improved technology

A) Demand-Side Factors

a) High-Income Elasticity of Demand for Final Product Services

Massimiliano Cali et. al. (2008) in their briefing notes on “The contribution of services to development and the role of Trade Liberalisation and Regulation” opined that the process of development generally coincides with the growing role of services in the economy. Many services offer key inputs to all or most other business e.g. infrastructure services such as energy, telecommunications and transportation; financial services which facilitate transactions and provide access to finance for investment; health and education services which contribute to a healthy, well-trained workforce; and legal and accountancy services which are part of the institutional framework required to underpin a healthy market economy. These service sectors are thus a key part of the investment climate, and can have a much wider impact on overall business performance and the level of investment, and hence growth and productivity in the economy. Trade in services can help create opportunities for countries to expand their outputs of services in sectors where they have a comparative advantage, thus creating jobs, contributing more to GDP and generating foreign exchange.

Gordon Jim and Gupta Poonam (2003) in their research paper “ A Tale of Two Giants: India’s and China’s Experience with Reform” discussed that the acceleration in growth of the service sector in India in the 1990s was due to fast growth in the communication, financial services, business services (IT)and community services (education and health). The other sectors grew at a constant or trend growth rate. According to them the factors such as high income elasticity of demand and increased input usage of services by other sectors are responsible for services growth in India. However, other factors such as economic reforms and the growth of services exports also played an important role in accelerating services growth in the 1990s. The findings of the paper suggest that there is considerable scope for further rapid growth in the Indian service economy and Indian service exports have strong future growth prospects.

Rath, Deba Prasad and Raj, Rajesh (2006) in their research work found that the higher growth in services sector has added a dimension of stability to India's growth process. Growing complementarity between the industrial and services sectors augurs well for the medium-term growth performance of the Indian economy. Unlike other commodity-producing sectors, which have either seen a stagnant growth or decline in employment, we found that the services sector has generated some employment opportunities. In the aftermath of nearly one and a half decades of sustained growth, services sector has led to widening of not only the tax base but also the buoyancy of taxes. With regard to inflationary impact of services sector expansion, the paper finds that growing service sector share in GDP has coexisted with low and stable inflation on account of inflation moderating forces operating, *inter alia* through the synergy between the two growth drivers.

5. IMPACT OF SERVICE SECTOR ON THE INDIAN ECONOMY

Indian economy today stands as one of the most influential and attractive economy of the world. Given the magnitude of services growth in India and its inter-linkages with other sectors of the economy, it is important to discuss the performance of different sub sectors of the service industry in India. The following table brings out clearly the rank and share of different sub sectors of service in international trade:

TABLE 3: INDIA’S SECTOR-WISE RANK AND SHARE IN WORLD EXPORTS/ IMPORTS OF SERVICES

Services		Rank		Share		Percent change in 2010
		2009	2010	2005	2010	
Transportation Services	Export	13	10	1.0	1.7	21
	Import	13	5	3.0	4.8	31
Travel Services	Export	14	12	1.1	1.5	27
	Import	-	-	-	-	-
Other Commercial Services	Export	4	3	3.1	4.9	36
	Import	8	5	1.9	3.5	66
Communication Services*	Export	4	5	-	2.1	-5
	Import	11	7	-	2.0	-7
Construction Services*	Export	12	-	-	-	-
	Import	13	10	-	1.6	-8
Insurance Services*	Export	7	8	-	2.0	17
	Import	7	7	-	3.1	24
Financial Services*	Export	7	7	-	1.5	64
	Import	5	3	-	3.9	81
Computer and Information Services*	Export	2	2	-	19.2	-
	Import	4	7	-	2.6	12
Other Business Services*	Export	6	7	-	3.8	-
	Import	6	6	-	3.3	-89
Personal, Cultural & Recreational Services*	Export	5	8	-	1.3	-28
	Import	12	-	-	-	-

Source: Economic Survey 2011-12.

In the year 2009 and 2010 India was ranked among the top ten exporters of services in the world for most of the services leaving transportation, construction, communication where it ranked 13th and 11th respectively. In import of services also India is among the top importers of services. In terms of share India's share is on the rise and is still growing.

TABLE 4: INDIA’S EXPORT OF SERVICES

S. No.	Commodity Group	Value (US\$ Billion) 2010-11	Percentage Share				CAGR 2000-01 to 2008-09	Growth Rate*			
			2000-01	2010-11	April-September			2009-10	2010-11	April-September	
					2010-11	2011-12				2010-11	2011-12
1	Travel	15.3	21.5	11.5	10.9	12.9	15.3	8.9	28.8	26.2	38.7
2	Transportation	14.3	12.6	10.7	11.0	12.8	23.8	-1.2	27.7	26.5	36.1
3	Insurance	1.9	1.7	1.5	1.5	1.7	23.1	11.9	22.5	10.2	38.8
4	GNIE	0.5	4.0	0.4	0.4	0.4	-6.2	13.4	21.3	9.5	30.6
5	Miscellaneous	100.9	60.3	75.9	76.2	72.1	30.4	-12.4	42.1	35.3	10.7
	a) Software Services	55.5	39.0	41.7	42.7	45.2	28.2	7.4	11.6	11.688	24.1
	b) Non-software services of which:	45.4	21.3	34.2	33.5	26.9	33.8	-40.3	113.4	5.6	-6.3
	i) Business Services	24.1	2.1	18.1	18.5	15.9	65.3	-39.4	112.4	111.4	0.3
	ii) Financial Services	6.5	2.1	4.9	5.2	4.2	37.5	-16.6	76.3	64.9	-6.7
	iii) Communication Services	1.6	7.0	1.2	1.3	1.1	9.2	-46.6	27.2	2.3	1.1
Total Services Exports		132.9	100.0	100.0	100.0	100.0	26.4	-9.4	38.4	32.7	17.1

Source: Economic Survey 2011-12.

TABLE 5: INDIA'S IMPORTS OF SERVICES

S. No.	Commodity Group	Value (US\$ Billion) 2010-11	Percentage Share				CAGR 2000-01 to 2008-09	Growth Rate*			
			2000-01	2010-11	April-September			2009-10	2010-11	April-September	
					2010-11	2011-12				2010-11	2011-12
1	Travel	11.1	19.2	13.2	13.8	19.1	16.4	-0.9	18.9	15.1	39.7
2	Transportation	13.9	24.4	16.5	18.2	20.7	17.4	-6.9	16.3	33.2	14.5
3	Insurance	1.4	1.5	1.7	1.9	2.0	22.5	13.7	8.9	6.3	3.6
4	GNIE	0.8	2.2	1.0	1.0	1.0	12.1	-33.8	56.2	49.4	9.2
5	Miscellaneous	56.9	52.6	67.6	65.1	57.2	17.5	32.5	53.9	65.5	-11.2
	a) Software Services	2.2	4.1	2.6	3.2	1.6	20.1	-42.7	49.5	39.9	-47.5
	b) Non-software services of which:	54.7	48.6	65.0	61.9	55.6	17.3	40.1	54.1	67.1	-9.4
	i) Business Services	27.8	7.0	33.0	35.2	34.3	40.3	17.8	53.8	62.6	-1.7
	ii) Financial Services	7.5	13.5	8.9	9.1	10.9	5.2	56.9	61.2	68.0	21.1
	iii) Communication Services	1.2	0.9	1.4	1.4	2.0	30.8	24.7	-15.0	-14.2	42.8
Total Services Imports		84.1	100.0	100.0	100.0	100.0	17.2	15.3	40.0	48.3	1.0

Source: Economic Survey 2011-12.

5.1 TRADE

- Retail is considered as the 'SUNRISE' sector of the economy.
- The value of trade (including wholesale and retail in the organised and unorganised sectors) in India's GDP has grown from Rs. 4,33,963 crore in the year 2004-05 to Rs. 7,42,621 crore in 2010-11.
- In January 2012, the govt. of India has allowed 100% FDI in the single brand retail sector and on September 14, 2012 the Government allowed 51% FDI in multi-brand retail but foreign retailers must get approval from state governments where stores will be located.

5.2 TOURISM, INCLUDING HOTELS & RESTAURANTS

- Not only a growth engine but also an export growth engine and employment generator
- The number of foreign tourist arrivals in India increased from 5.78 million in 2010 to 6.29 million in 2011, registering a growth of 8.9 per cent (Financial Express, May10, 2012).
- During the same period Foreign Exchange Earnings (FEE) were Rs. 77,591 crore with a growth of 19.6 per cent (Incredible India, 2012).
- A Hospitality development and Promotion Board has been set up at central level to monitor and facilitate clearance/ approval for hotel project both at central and state level.

5.3 TELECOM AND RELATED SERVICES

- India's telecom network is ranked as second largest in the world next only to China
- India's telecom sector received foreign direct investment (FDI) of Rs.48,220 crore in the last 11 years - 8 percent of the total FDI the country received (Northern Voices Online).
- According to consultancy firm Boston Consulting Group (BCG), The sector is expected to witness up to US\$ 56.3 billion investments and the market will cross the US\$ 101 billion mark in five years (OIFC).

5.4 IT AND IT ENABLED SERVICES (ITeS)

- As per the estimates of software industry body National Association of Software and Service Companies NASSCOM, in 2011-12 India's IT & BPO sector revenues were US\$ 87.6 Billion and
- The Indian IT-BPO sector is expected to grow up to US\$ 100 billion during FY 2012
- As a proportion of national GDP, IT & ITeS revenues have grown from 1.2% in 1997-98 to 7.5% in 2011-12.
- This sector is also a generator of skilled employment with direct employment expected to reach 2.8 million in 2011-12 as compared to 2.5 million in 2010-11.

5.5 CONSTRUCTION SERVICES

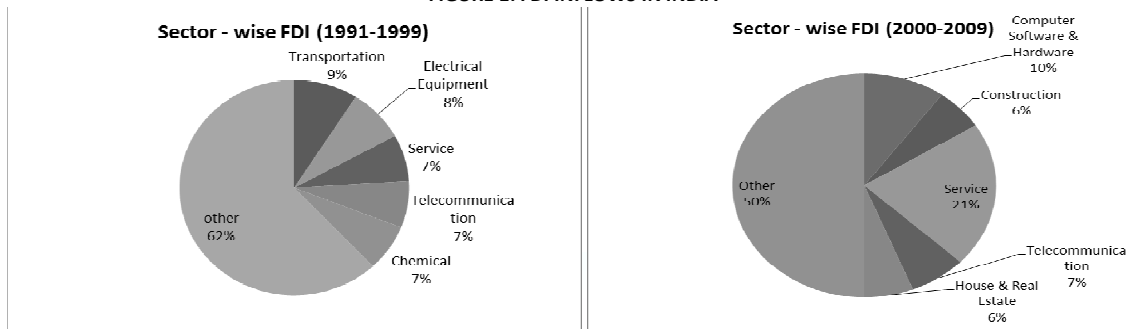
- FDI upto 100% under automatic route is allowed in townships, housing, built-up infrastructure and construction of development projects
- Service sector's importance is clearly seen in its contributions to different aspects of the economy which is greater than the combined contribution of industrial and agriculture sectors. This sector had accounted for 68 per cent share in the country's GDP and it was the topmost country in terms of increase in its services share in GDP (7 percentage points) followed by Spain and Canada (5.3 percentage points each), UK (4.5 percentage points) and Italy (3.2 percentage points). After Agriculture, Service sector occupies second place in generating employment opportunities in the country. According to a report of the National Sample Survey Organization's (NSSO) in the year 2009-10 for every 1000 people employed in India service sector employed 241 from rural and 683 from urban India. 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.

6. FDI IN INDIA'S SERVICE SECTOR

FDI to developing countries in the 1990s was the leading source of external financing and has become a key component of national development strategies for almost all the countries in the world as a vehicle for technology flows and an important source of non-debt inflows for attaining competitive efficiency by creating a meaningful network of global interconnections. It provides opportunities to host countries to enhance their economic development and opens new vistas to home countries to optimize their earnings by employing their ideal resources. India ranks fifteenth in the services output and it provides employment to around 23% of the total workforce in the country.

Following an international trend, FDI inflows into India have shifted away from manufacturing, and towards services sector.

FIGURE 1: FDI INFLOWS IN INDIA



Source: Narendra Singh Bohra, et.al.(2011)

The figures reveal that during the first decade of economic reforms in India (August 1991 to December 1999), Indian service sector was unable to attract FDI, but in the second decade (January 2000 to March 2009), due to the growth of sub sectors like IT, Financial Services, Insurance sector etc., the composition of foreign direct investment in India changed in favour of service sector (Narendra Singh Bohra, et.al.(2011).

Thus the flow of FDI in Indian service sector is boosting the growth of Indian economy. The top five sectors attracting highest FDI in the country are financial and non-financial Services sector, tele- communications, computer software and hardware, housing and real estate and construction activities.

6.1 SERVICES ATTRACTING HIGHEST FDI EQUITY INFLOWS

TABLE 6: SERVICES ATTRACTING HIGHEST FDI INFLOWS IN INDIA (Rs. Crore)

Sector	2009-10	2010-11	2011-12	Cumulative Inflows	Percentage of total
Service Sector (Financial and non-Financial)	19,945	15,053	21,431	1,42,539	20.1
Telecom	12,270	7,542	8,969	57,035	7.9
Computer software and hardware	4,127	3,551	2,626	48,940	6.9
Housing and real estate	14,027	5,600	2,544	48,819	6.9
Construction	13,469	4,979	7,635	46,216	6.5

Source: Business Line

Though, due to global economic and economic crisis FDI in all main service industries including business services, finance, transport, communications and utilities declined from US\$ 392 billion in 2009 to US\$ 338 billion in 2010, resulting in sectoral FDI decline from 33 per cent to 30 percent in this period. FDI is a tool for economic growth through its strengthening of domestic capital, productivity and employment. FDI also plays a vital role in the up gradation of technology, skills and managerial capabilities in various sectors of the economy.

7. CONCLUSION

The foregoing analysis reveals that services hold immense potential to accelerate the growth of an economy and promote general well-being of the people. It offers innumerable business opportunities to the investors. This sector has the capacity to generate substantial employment opportunities in the economy as well as increase its per capita income. Without it, Indian economy would not have acquired a strong and dominating place on the world platform. Thus, service sector is considered to be an integral part of the economy that includes various sub-sectors spreading all across the country. It in fact is sine qua non for the future growth of India.

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