Services

The services sector, long regarded as the main prop of robust economic growth in the country, has not been immune from the overall slowdown. Lead indicators from the second quarter suggest the momentum is unlikely to pick up in the remaining part of the year. Services exports may prove an exception to the generally subdued trend given that these are a function of global growth.

S.1 Growth rate turns lower in second quarter of 2013-14

The services sector, excluding construction accounts for nearly 62 per cent of India's GDP as on date. Unfortunately, the growth rate of this sector has fallen steadily from 7.9% in 2011-12 to 6.8% in 2013-14 and dipped further to 5.8% in 2013-14:Q2. Construction forms 7.8% of the Indian GDP and here too, growth has fluctuated throughout 2012-13. In the second quarter of 2013-14, the growth rate of the construction sector improved to 4.3% from the first quarter of 2013-14 (2.8%). Therefore, if construction is included in the services sector, the growth rate of the services sector remains nearly the same at 5.8% in 2013-14:Q2. Services sector including construction accounts for about 70% of India's GDP.

The growth rate of the components of the services sector is mixed (Table S.1). The subsector 'Trade, Hotels, Transport and Communication' that accounts for 28% of India's GDP, witnessed nearly the same growth rate of 4% in 2013-14:Q2 as compared to 3.9% in 2013-14:Q1. The subsector 'Finance, Insurance and Real Estate', which accounts for little over 20% of GDP, showed an improvement in growth to 10% in 2013-14:Q2 over 8.9% growth in the earlier quarter, suggesting an upturn in growth since 2012-13:Q4 in this sector.

The growth in subsector 'Community, Social and Personal Services' dipped to 4.2% in 2013-14:Q2 compared to a more robust growth of 9.4 % in 2013-14:Q1. The improvement in growth during 2013-14:Q1, which earlier anticipated due to improved government spending remained subdued in 2013-14:Q2.

S.2 Lead Indicators from the Second Quarter of 2013-14

Lead indicators suggest mixed picture for services sector growth in Q3. On the one hand the services sector recorded the lowest growth in 12 years at 5.8 per cent during Q2 of 2013-14. This was largely due to the moderation in the growth of 'Trade, hotels, restaurant, transport & communication' and 'Community, social & personal services' sectors. However, various lead indicators of the services sector portrayed a mixed picture during Q3 of 2013-14 (Table S.2).

The Reserve Bank's services sector composite indicator, which is based on growth in indicators of construction, trade & transport and finance witnessed an upward trend in Q2 of 2013-14, but showed a downturn in October-November 2013. However, partially available data for December suggest some pick up.

Cargo handled at major ports grew by just 1.1% during the third quarter, 2013-14. Though this was improvement over the decline of 2.6% in the comparable quarter of the previous fiscal, it reflects the subdued level of activity in the economy. The silver lining is that domestic cargo traffic is up 21.9% in the Oct-Nov 2013 period as against a decline of 3.8 % in the comparable period of the last fiscal. (Table S.2)

Both, international and domestic passenger traffic show improved growth rates during April-October 2013.

International passenger traffic shows the improvement to nearly 12% this year compared to 1.8% increase last year. Domestic passenger traffic registered an increase of nearly seven percent compared to a decline of 5.2% last year

S.3 External Sector

Services exports as a percentage of GDP showed an improvement in the second quarter of the current fiscal (9.1%) as compared to the first quarter (8.4%). IT is the largest component in total invisibles exports, accounting for a share of 64% in total exports. De-composing services exports one finds that software (46%) and non-software miscellaneous services (31%) are the largest components of service exports.

The growth rate of software exports improved to 5.7% in the second quarter, an improvement over the first quarter of the current fiscal (5.5%).

Compared to the 2011-12 numbers of double digit growth, the improvement in the first two quarters seems paltry. Non-software miscellaneous services show an upturn in growth in the second quarter of the current fiscal compared to negative growth since the second quarter of 2011-12. (Table S.3). Exports of travel services which showed a remarkable turnaround in the first quarter (9.1%) were subdued during the second quarter (0.9%). The remaining components of services, namely, 'transportation', 'insurance', and 'G.n.i.e' show negative growth rates.

FDI inflows were subdued during April-October period of current fiscal. The services sector (Financial and Non-Financial) received nearly 11 % of total FDI inflows between April – October, 2013. This is lower than the historical cumulative share of nearly 19% between April' 2000 to October 2013. All the major components of the services sector (except computer software and hardware), viz 'construction development, 'Telecommunication' received lower FDI during this period. Computer software and hardware bagged 3.9% of total FDI. Lower FDI inflows to the sector reflect the generally less optimistic outlook in the services sector.

S.4 Outlook

Services sector will continue to grow, though at a slower pace during the latter half of the current fiscal. However, a recovery in the external sector or an improvement in domestic industry could help boost services sector growth.

Box S.1: IT-BPM Sector in India – A run up to the Next Fiscal

The enhanced global spending on IT technology and newer opportunities enabled through adoption of disruptive technologies is projected to be a major growth driver. As per NASSCOM estimates a year ago, the sector's export revenue is estimate to touch ÜS$ 84-87 billion, with a growth of 12-14 % this fiscal. Domestic revenues are expected to reach INR 1180-1200 billion and are likely to grow at 13-15 per cent. Huge investments by IT services companies are already in place. These have helped build up appropriate skill-sets and could be viewed as part of the endeavour on the part of the IT-BPM sector to ride the next wave of IT growth.

SMAC (social, Media, Analytics, and Clouds) technologies are expected to fuel the growth in IT-BPM sector. An earlier estimate by NAASCOM- IDC suggests that Indian IT vendors could be expected to generate US $225 billion SMAC-related revenue by 2020. The future of the industry lies in a blend of services, products, solutions and platforms.

Some of near-term challenges in the sector are increasing competition on billing rates and increasing commoditisation of lower-end ADM services. There is a pressing need for IT firms to re-invent their business models.

Another major challenge is the hardening of the regulatory environment in major world economies like the US, Canada and Australia. IT-BPM firms might see tough times as these firms have to meet mounting operational expenses which could further pinch their profit margins. On the domestic front too, the coming Lok-Sabha election this year could delay government's IT spending which is expected to touch $6.4 billion this fiscal.

***Sources*:** NASSCOM

Table S.1: Slow growth persists with slack in industrial output and under-performance of services sector
Sector-wise GDP growth rates (2004-05 prices)

										(Per cent)	
	2011-12*	2012-13#		2012-13				2013-14		2012-13	2013-14
		Growth	Share	Q1	Q2	Q3	Q4	Q1	Q2	H1	H1
Services	**7.9**	**6.8**	**67.4**	**7.6**	**7.1**	**6.2**	**6.3**	**6.2**	**5.8**	**7.3**	**6.0**
Trade, hotels, transport & communication	7.0	6.4	27.8	6.1	6.8	6.4	6.2	3.9	4.0	6.4	4.0
Financing, insurance, real estate and business services	11.7	8.6	18.7	9.3	8.3	7.8	9.1	8.9	10.0	8.8	9.5
Community, social & personal services	6.0	6.6	13.0	8.9	8.4	5.6	4.0	9.4	4.2	8.6	6.6
Construction	5.6	4.3	7.8	7.0	3.1	2.9	4.4	2.8	4.3	5.1	3.5
GDP at factor cost	**6.2**	**5.0**	**100.0**	**5.4**	**5.2**	**4.7**	**4.8**	**4.4**	**4.8**	**5.3**	**4.6**

* First Revised Estimates. # Provisional Estimates.
Source: Central Statistics Office

Table S.2: Services sector witnessed a mixed picture in Q3
Lead indicators of services sector activity

				(Growth in per cent)		
Services Sector Indicators	**2011-12**	**2012-13**	**H1**		**Q3**	
			2012-13	**2013-14**	**2012-13**	**2013-14**
Tourist arrivals	9.7	2.0	1.7	4.3	2.1	4.9
Cement	6.7	7.7	9.1	4.5	3.3#	2.6#
Steel	10.3	2.5	2.6	4.5	1.6#	3.7#
Automobile Sales	11.1	2.6	3.5	1.2	6.3	4.1
Railway revenue earning freight traffic	5.2	4.1	4.8	6.2	5.9	1.9
Cargo handled at major ports	-1.6	-2.5	-3.3	2.3	-2.6	1.1
Civil aviation						
Domestic cargo traffic	-4.8	-3.4	-0.8	0.6	-3.8*	21.9*
International cargo traffic	-1.9	-4.2	-4.9	-0.9	-2.5*	7.1*
International Passenger traffic	7.6	5.5	2.7	12.0	-2.4*	12.1*
Domestic Passenger traffic	15.1	-4.3	-3.7	6.6	-15.6*	11.3*

* Data refer to Oct.; # Data refers to Oct.-Nov.
Source: Ministry of Statistics and Programme Implementation, Ministry of Tourism, IPA, SIAM and CMIE