VII

Services Sector

1. Overall Growth

The emergence of India as one of the fastest growing economies in the world during the 1990s is attributable to the rapid growth of its services sector to a great extent. The sector has been experiencing double-digit growth during the past two years (2004-05 and 2005-06), importantly, a strong growth of 10 per cent in 2005-06 has been instrumental in providing an impetus to overall real sector activity in the economy and propelling it to record a sturdy growth of 8.4 per cent (at 1999-00 prices).

Table 7.1: Quarterly Estimates of Production for Major Components of Services Sector
(Rs crore)

Sub-Sectors	2006-07 (Q1)	2005-06 (Q1)	2004-05 (Q1)	2006-07	2005-06
At 1999-00 prices				Percent change over previous year Q1	
1. Trade, hotels, transport and communication	175025	154642	138390	*13.2*	*11.7*
	(26.7)	(25.7)	(24.9)		
2. Financing, insurance, real estate and business services	91527	84021	77245	*8.9*	*8.8*
	(14.0)	(13.9)	(13.9)		
3. Community, social and personal services	88,771	82637	77009	*7.4*	*7.3*
	(13.5)	(13.7)	(13.9)		
All Services (1+2+3)	**355323**	**321300**	**292644**	***10.6***	***9.8***
	(54.2)	(53.3)	(52.7)		
GDP at factor cost	656,064	602476	555,075	*8.9*	*8.5*
At current prices					
1. Trade, hotels, transport and communication	211022	181769	156187	*16.1*	*16.4*
	(25.3)	(24.7)	(24.1)		
2. Financing, insurance., real estate and business services	124695	109469	95654	*13.9*	*14.4*
	(14.9)	(14.9)	(14.8)		
3. Community, social and personal services	112716	99761	88797	*13.0*	*12.3*
	(13.5)	(13.6)	(13.7)		
All Services (1+2+3)	**448433**	**390999**	**340638**	***14.7***	***14.8***
	(53.7)	(53.2)	(52.7)		
GDP at factor cost	835109	734510	646806	*13.7*	*13.6*

Notes: Figures in brackets denote percent share of total services in GDP.
Source: CSO, Ministry of Statistics and Programme Implementation

Subsequent to this, the sector has continued to exhibit vibrant growth (10.6 per cent) during the first quarter of 2006-07 over the corresponding period of the previous year, mainly propelled by growth in 'trade, hotels, transport and communication' (13.2 per cent) followed by 'finance, insurance, real estate and business services' (8.9 per cent) (Table 7.1).

Due to the structural transformation of the Indian economy in the new millennium in favour of a service-dominated economy from an agrarian one, the share of the services sector in the total GDP has increased notably from 49.8 per cent in 2000-01 to 54 per cent in 2005-06. During the first quarter (April-June) 2006-07, the services sector has accounted for a share of 54.2 per cent as compared to 53.3 per cent in the comparable period during last year (Table 7.1).

The remarkable sectoral performance of the services sector as a whole has been reflected in the select lead indicators of the services sector, which have continued to grow at robust rates in the initial months of 2006-07 (Table 7.2). The tourism sector has performed well in terms of foreign tourist arrivals, although there has been a slow down in foreign exchange earned thereby. There has been a strong growth in production (33.5 per cent) as well as domestic sales (37 per cent) of commercial vehicles during April-September 2006 over the corresponding period of 2005. Similarly, the passenger vehicles production and domestic sales have also recorded double digit numbers during the same period. The overall upsurge in the production of automobiles has been on account of overwhelming demand for small cars and sports utility vehicles (SUVs). Similarly, substantial activity has been witnessed in cargo and passengers handled at international airports and passengers handled at domestic airports during April-May 2006. During April-August 2006, Indian Railways has also exhibited reasonably good performance except freight traffic handled.

In the communication sector, there has been a growth of 139 per cent in new cellular connections during April-September 2006 over 37 per cent in the same period last year. Apart from these physical indicators, there has been a considerable growth in the monetary indicators, like aggregate deposits, non-food credit and central government expenditure during April-September 2006. The increasing non-food credit during this period reflects growing demand for retail and personal loans, especially on account of the upcoming festival season.

The sector that has grown moderately as compared to the last year has been shipping in terms of cargo handled at major ports which has also shown a moderate growth of 6 per cent

during April-August 2006 as against 15 per cent during the comparable period of the previous year. A major expansion is required in the port infrastructure sector in order to handle sea borne traffic arising from increased foreign and coastal trade. This could be achieved through private sector participation by reducing the gestation period for setting up new facilities, bringing in latest technology and improving management techniques in order to upgrade cargo handling, both in terms of quality and quantity.

Table 7.2: Select Indicators of Services Sector Activities
(*Growth Rates in per cent*)

Sub-sector	2006-07	2005-06
1. Tourism (April-September)		
Tourist arrivals (in numbers)	13.8	13.0
Foreign exchange earnings (in US $)	9.5	24.4
2. Transport		
Automobiles (April-September)		
Commercial vehicles production	33.5	13.4
Passenger vehicles production	18.5	7.2
Commercial vehicles domestic sales	37.0	7.1
Passenger vehicles domestic sales	20.7	7.0
Railways (April-August)		
Revenue earning freight traffic (in tones)	-3.4	10.9
Revenue earning passenger traffic (no. of passengers)	8.5	-
Passenger earnings (Rs crore)	11.7	-
Goods earnings (Rs crore)	16.5	18.3
Civil Aviation (April-May)		
Freight handled at international terminals	17.1	16.7
Freight handled at domestic terminals	4.2	13.0
Passengers handled at international terminals	17.6	14.2
Passengers handled at domestic terminals	52.1	17.2
Shipping (April-August)		
Cargo handled at major ports (in tones)	6.0	15.1
3. Communication (April-September)		
New cell phone connections	139.1$	36.7
New landline connections	-0.4	57.4
Total new telecom connections	104.2	39.2
Broadband connections	9.3	-
4. Banking and Finance (April-September)		
Aggregate deposits *#	9.2	7.7
Non-food credit *	10.6	11.2
5. Public Administration (April-August)		
Central government expenditure	22	10.4

Notes:'-' means not available; $ Data for 2006-07 includes WLL-F subs and hence the figures are not strictly comparable.
*Refers to scheduled commercial banks and figures are as on Sep 29, 2006.
Data reflect redemption of India Millennium Deposits (IMDs) on December 29, 2005.
Sources: Data are taken from respective ministries or other government authorities.

2. Performance of Key-Drivers of the Services Sector

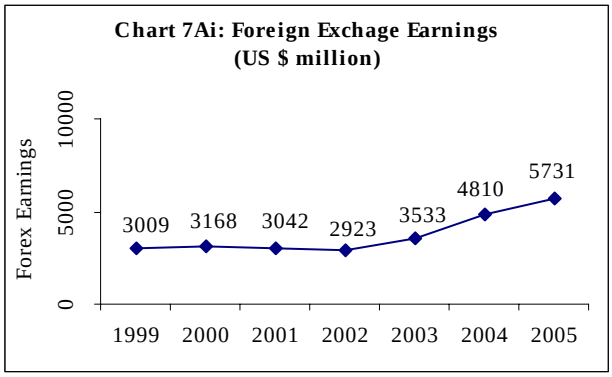
a) Travel and Tourism

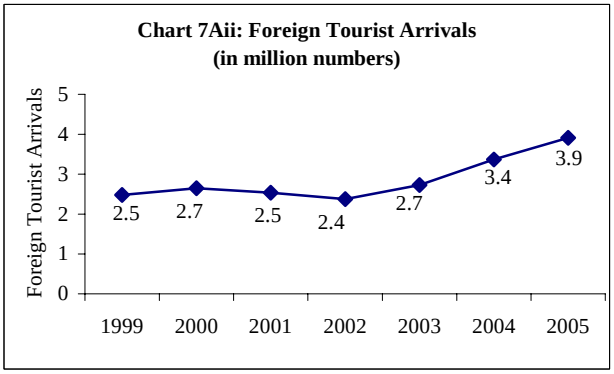
With an impressive growth of tourism in 2005, India's share in world tourism, hovering around 0.38 per cent for nearly a decade (1995 to 2003), has reached 0.46 per cent in 2004 and is estimated to be around 0.49 per cent in 2005. The key performance indicators of tourism sector are inbound and outbound tourist traffic and foreign exchange earnings from the same. After experiencing positive growth in 2005, the number of foreign tourist arrivals and the corresponding foreign exchange earnings have increased by about 13 per cent and 12 per cent, respectively, in January-September 2006 over the corresponding period in 2005 (Table 7.3).

Table 7.3: Performance of Tourism Sector in India

Year	Foreign Tourist Arrivals *(in million)*		Domestic Tourist Visits *(in million)*		Outbound Tourist Traffic *(in million)*		Foreign Exchange Earnings *(US $ million)*	
2001	2.54	*(-4.2)*	236.5	*(7.5)*	4.6	*(4.5)*	3042	*(-4.0)*
2002	2.38	*(-6.3)*	269.6	*(14.0)*	4.9	*(6.5)*	2923	*(-3.9)*
2003	2.73	*(14.7)*	309.0	*(14.6)*	5.4	*(10.2)*	3533	*(20.9)*
2004	3.45	*(26.4)*	367.6	*(19.0)*	6.2	*(14.8)*	4769	*(35.0)*
2005	3.91	*(13.3)*	-	-	7.2	*(16.1)*	5731	*(20.2)*
Jan-06	0.44	*(15.1)*	-	-	-	-	632.4	*(18.8)*
Feb-06	0.42	*(10.1)*	-	-	-	-	594.6	*(10.9)*
Mar-06	0.40	*(11.0)*	-	-	-	-	547.2	*(8.2)*
Apr-06	0.32	*(24.7)*	-	-	-	-	473.4	*(25.1)*
May-06	0.26	*(14.7)*	-	-	-	-	368.6	*(10.6)*
June-06	0.28	*(10.6)*	-	-	-	-	401.2	*(6.9)*
July-06	0.33	*(13.3)*	-	-	-	-	497.3	*(5.7)*
Aug-06	0.30	*(10.5)*	-		-	-	456.8	*(4.9)*
Sep -06	0.25	*(9.2)*					424.7	*(5.7)*
Jan-Sep 05	2.7	*(15.3)*					3968.4	*(22.5)*
Jan-Sep 06	3.1	*(13.0)*					4441.2	*(11.9)*

Note: Figures in bracket represent percent variations over the previous year or the corresponding period in the previous year.
Source: *Ministry of Tourism* (*www.tourism.nic.in)*



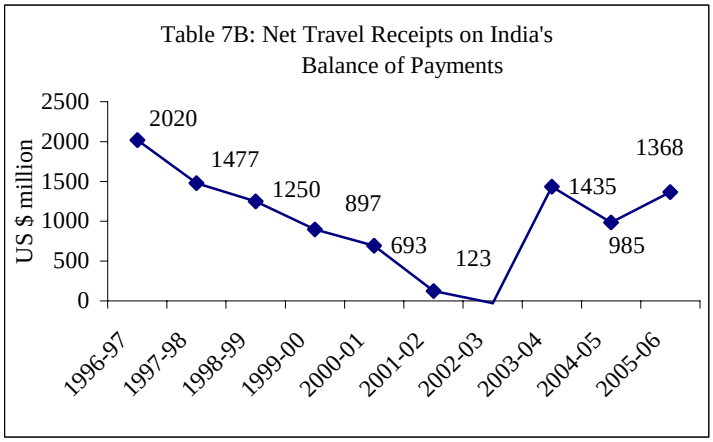


On the back of this optimistic growth, the government expects tourist arrivals to touch 4.4 million in 2006 from 3.9 million in 2005, 9.9 million by 2011 and 15.9 million by 2014. The number of foreign tourist arrivals during January-September 2006, which has already touched 3.1 million and as per the trend of larger tourist inflows during the winter season, the target for 2006 appears attainable. Moreover, following the trend, it is expected that the foreign exchange earned during this period would exceed those in the previous quarters due to the higher average room rates during the winter period.

Table 7.4: India's Net Receipts from Travel on Balance of Payments

Year	Receipts	Payments	Net Receipts	Foreign Tourist Arrivals
	(in million US$)			(million no.)
2000-01	3497	2804	693	2.7
2001-02	3137	3014	123	2.4
2002-03	3312	3341	-29	2.5
2003-04	5037	3602	1435	2.9
2004-05*	6495	5510	985	3.5
2005-06**	7789	6421	1368	4.1

Notes: * partially revised ** preliminary
Source: *RBI Bulletin, various issue and Ministry of Tourism (www.tourisim.nic.in)*



However, although gross receipts from travel have shown a steady rise except for the year 2001-02 (when the tourism industry was hit by terrorist attack in the US in 2001), there had been a deceleration in net receipts, due to increasing number of Indians taking up foreign travel resulting in higher travel payments than travel receipts under the balance of payments account (Table 7.4).

There has been a revival of the tourism sector since 2003-04 resulting in improved net receipts thereafter. What has been encouraging is the sharp increase in net receipts by US $ 1368 during 2005-06 as against lower earnings of US $ 985 in 2004-05. This can be attributed to a higher influx of foreign tourist (4.1 million in 2005-06 as compared to 3.5 million in 2004-05), especially during the winter months of 2005. (Please note that the travel account on Balance of Payments not only includes tourist travel, but also business related travel for personal purposes.)

b) Retail Sector

The organised retailing is at a very nascent stage in India contributing a mere 3 per cent of the total retail industry of US $ 230 billion (www.*apparelreview.com*). However in comparison to the growth of unorganised retail which is growing at a mere 5 per cent per annum, the organised retail is growing at a noteworthy pace of about 25-30 per cent and is expected to touch US $ 33 billion by 2010 enabling the contribution of organised retail sales to be almost 9 per cent of the total retail sales. However, there still exists a tremendous untapped potential for India as compared to the developed retail markets like US, Taiwan and Malaysia where penetration of organised retail sales is more than 50 per cent. Retailing is the second largest employer (22 million people) in India, second only after agriculture. The booming retail market has attracted large players like Kishore Biyani's Pantaloon Retail, K Raheja Groups Shoppers Stop, Tata Group's Trent, RPG's Spencer and Micky Jagtiani owned Landmark Group's Lifestyle stores and now Reliance Retail to expand their foray nationally. Also, regional giants like Subiksha, Vivek's, Nilgiris and Trinethra are expanding rapidly.

Moreover, due to its correlation with other industrial and service sectors, organised retailing is generating a great deal of indirect employment in other sectors; security, and electrical and mechanical maintenance, property management services, parking, sorting, packaging, etc. If both direct and indirect employment is taken together, organised retailing is bound to create a larger number of better-paid, better-quality jobs. This is a large growth opportunity in an organised business that the country would witness in a long time. Apart from the direct jobs, every retail job created adds further jobs in the support businesses.

At present, the most crucial issue regarding the retail sector is that of FDI. The Foreign Investment Promotion Board (FIPB) has permitted 51 per cent equity cap on a single brand product since February 2006. Simultaneously, the equity cap on FDI in 'trading for exports', which is permitted under the automatic route has been raised from 51 per cent to 100 per cent. However, whether the government should introduce 100 per cent FDI in other cases is a matter of dispute with the proponents advocating competition to result in better quality while the opponents being concerned about survival of small shops. A detailed study undertaken by the Ministry of Consumer Affairs and the Indian Council for Research on International Economic

Relations (ICRIER) has concluded that FDI should be allowed in retailing in a gradual and phased manner through permitting joint ventures.

FMCG

According to a recent HSBC report, the FMCG sector is projected to grow by over 60 per cent till 2010. It is estimated that the total size of the FMCG sector will rise from around US$ 12.51 billion in 2005 to US$ 20.40 billion in 2010. Apart from packaged food, which has recorded the fastest growth (25 per cent) in 2005, other fast growing segments in the sector are hair care, household care, male grooming, female hygiene, chocolates and confectionery. The buoyant performance of the FMCG sector has also been reflected in the aggregate results for April-June 2006-07 of 12 FMCG companies with sales of Rs 9,231 crore, a rise of 16 per cent. The profits of these companies have increased by 16.6 per cent to Rs 1,415 crore.

Consumer Durables

On the back of robust semi-urban and rural demand, the consumer durables industry has recorded upbeat growth trends in 2006 (*India Brand Equity Foundation*). The consumer durable companies expect sales to grow by 40 per cent in the forthcoming festive season. According to the industry estimation, the prices of most of consumer durables have declined by 5 - 8 per cent as compared to the last year, mainly due to a rationalised duty structure and manufacturers' initiatives to support new products. With the ownership of high value durable goods like LCD plasma TVs and front loading washing machines now being seen as a symbol of social status, manufacturers are bullish on sales targets. Based on recent trends, the Indian colour television market would increase to 10.5 million units during the current fiscal year while the refrigerator market would touch 4.2 million.

Real Estate and Prices

Driven by positive growth in the economy, real estate in India is booming. The year 2006 started on a promising note when the Government of India opened the construction and development sector in February 2006 and allowed 100 per cent foreign direct investment (FDI) under the 'automatic route' in order to spur investment in the vital infrastructure sector. Groups showing interest in India include insurance company American International Group Inc (AIG),

High Point Rendel of the UK, Edaw-US, Japan's Kikken Sekkel, Lee Kim Tah Holdings and Cesma International from Singapore.

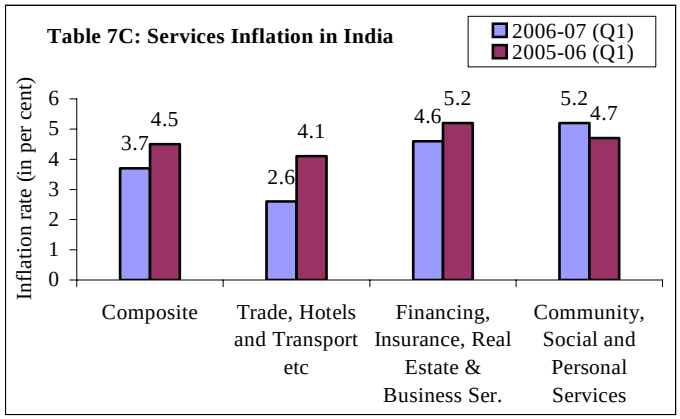
Along with strong supply-side factors, the dynamics of demand have also been quite strong, which has led to an escalation of real estate prices in almost all tier I and tier II cities in India during the last couple of years. The simple demand-supply dynamics indicate that until one of these factors undergoes a change, the high property prices will probably persist due to demand far outstripping supply. The property market has remained firm since the beginning of 2006. For example, in the first quarter of 2006, the real estate markets in Mumbai, Thane and Navi Mumbai have shown price increases varying between 3-15 per cent. Further, any rise in interest rates (interest rates have risen by around 2.5 per cent during last 24 months) is expected to impact only speculators and not genuine home buyers. One of the reasons behind this continued demand is unaffected equated monthly instalments (EMI) as the banks have extended repayment periods of loans leaving the monthly instalment amount unaltered.

Recent Developments: Real Estate Index

The government is planning to float the first housing price index to track price variations in different locations within cities which would help simply the decision making process for the consumers easier. The index is expected to track the extent of inflation taking place in housing prices across the country. Since a single measure would not be able to fully represent price variations in housing sector, the government is planning to make it flexible enough to track local variations. India will be the third country in the world to launch such an index after the US and UK.

3. Services Inflation

Given the fact that the services sector contributes more than 50 per cent to GDP, it is useful to throw light on services inflation in the first quarter of 2006-07 (Table 7.5 and Chart 7C). The general practice to measure services



inflation till date has been the use of a deflator. As per the CSO's recently released new annual GDP series (1999-00=100) at current and constant prices, the overall services sector inflation during April-June 2006 has been estimated at 3.7 per cent, lower than the inflation rate of 4.5 per cent during the corresponding period in the last year and the average WPI inflation at 4.5 per cent during the first quarter of the current financial year.

Table 7.5: GDP Deflator of the Services Sector Quarterly (April-June) Series

	2006-07 (Q1)	2005-06 (Q1)	2004-05 (Q1)
Services Sector GDP at current prices	**448433**	**390999**	**340638**
1 Trade, Hotels and Transport etc	211022	181769	156187
2 Financing, Insurance, Real Estate & Business Services	124695	109469	95654
3 Community, Social and Personal Services	112716	99761	88797
Services Sector GDP at 1999-2000 prices	**355323**	**321300**	**292644**
1 Trade, Hotels and Transport etc	175025	154642	138390
2 Financing, Insurance, Real Estate & Business Services	91527	84021	77245
3 Community, Social and Personal Services	88771	82637	77009
Services Sector Deflators (1999-2000 =100)			
Composite	**126.2**	**121.7**	**116.4**
	(3.7)	**(4.5)**	
1 Trade, Hotels and Transport etc	120.6	117.5	112.9
	(2.6)	(4.1)	
2 Financing, Insurance, Real Estate & Business Ser.	136.2	130.3	123.8
	(4.6)	(5.2)	
3 Community, Social and Personal Services	127.0	120.7	115.3
	(5.2)	(4.7)	
WPI Inflation Rate (average)	4.5	5.3	

Note: Figures in brackets are percent variations over previous year.
Source: Central Statistical Organisation (www.mospi.gov.in)

Given the importance of the services sector, there is a need to develop 'service price indices' for selected service sectors, particularly in the national accounts framework. The need for such indices has been recommended by the Working Group set up to revise the WPI and has been emphasised by the National Statistical Commission. The Office of the Economic Adviser, Ministry of Commerce and Industry has been implementing a plan aimed at developing service sector price indices as per international best practices. Under the plan schemes, studies are being commissioned for ten selected services like, road transport, railways, air transport, port, banking, insurance, posts, telecommunication, business services and trade services to develop service price indices.