CHAPTER 2

REVIEW OF LITERATURE

2.1 Introduction

This chapter deals with the review of existing literature related to topic of study. Chapter is divided into three sections dealing with theoretical foundations, global context and Indian context of study. Theoretical foundation deals with different theory of development through which any economy moves. Global and Indian context literature put light on different concepts and dimensions of development of service sector.

2.2Theoretical Foundations

2.2.1 Classical Theories of Economic Development

2.2.1.1The Linear stages of Growth Models

In these models capital is taken as injections for the growth of GDP. The concept of economic development and its model was formulated in the initial years after the world war 2nd. Rostow's stages growth and The Harrod-Domar Model are the two linear stages growth Model.

Rostow's Stages of Economic Growth

W.W Rostow provided a systematic process of economic development. He propounded five stages through which an underdeveloped country can move towards the development. These five stages are: The Traditional Society, The Preconditions for take-off, The take-off, The drive to Maturity and the last is the age of high mass consumption. Among these take-off stage is very important in which a country travel from an underdeveloped to a developed state. Investment is considered as necessary condition to boost up of per capita growth. *The Stages of Economic Growth* of Rostow has been discussing from the period of its commencement in literature.

The Harrod-Domar Model

On the other hand Harrod-Domar focuses on investment for development. This model is based on advanced economies. This model is a practice to attend steady state growth in the economy. The models of both economists are unlike in details, but they arrived at same result. They talk about double character of investment which is to create income on one hand and on other hand it increases capital stock. The creation of income referred as *demand effect* and the latter is known as *supply effect*. It is essential to increase the output and real income at the same rate at which the productive capacity of the capital stock is increasing to maintain full employment equilibrium level of income. R. F. Harrod talk about three growth rate for description of economy and its various phases, these growth rate are: The Actual Growth Rate, The warrented rate of growth, The Natural rate of growth.

2.2.1.2 Structural Change Models

These models came in existence during the period of 1960s and early 1970s. In these models development process is described as a shifting of labour from agriculture to industrial sector. Two sector model of Lewis (1959) and Chenery's (1960) the structural change and patterns of development are the structural change models.

The Lewis Theory

His concerned is about two sector economy. Lewis has propounded a theory with a title of *Economic Development with Unlimited Supplies of Labour*. He talks about shifting of labour from traditional sector to modern one. The reason behind this shifting is difference between the wages of these two sectors. Workers of agriculture sector earns only subsistence wage while wage of modern industrial sector is more. High wage and investment in modern sector attract labours and cause of expansion of economic growth.

Chenery's Patterns of Structural Change

Chenery identified some similar features in the pattern of development of less developed nations. He studied the several less developed countries during the post-war period. Chenery defines the development pattern *"as a systematic variation in any significant aspect of the economic or social structure associated with a rising* *level of income."* But he specially talk about sustained increase in per capita income. He has divided the development process in three principle development which also divided into ten basic development processes through which all dimensions of development can be described. These processes are: Accumulation Process, Resource allocation Process and Demographic and Distributional Process.

As per Structural change and patterns of development analysis concerns, it gives equal importance to the physical and human capital accumulation for economic growth with a consideration of saving and investment. Chanery (1960), Chenery & Taylor (1968), Kuznets (1971), and Chanery & Syrquin (1975) provided an essential explanation of this approach.

International Dependence Models

This model was developed in 1970s and early 1980s. Theory explained that the reason behind underdevelopment is dominance of developed of developed country over developing one. This theory is taken as the addition to Marxist theory. It concludes that developing countries should break up their relationship with developed countries to get rid of problem.

2.2.2 Contemporary Theories of Economic Development

New Growth Theory

New growth theory which is also known as endogenous growth theory emerged in 1990s to describe the poor concert of many underdeveloped countries, which have applied in neo-classical theories. Romer (1986), Lucas (1988), Aghion and Howitt (1920) are few new growth theorists who linked technological change to the productionof knowledge. It focuses on knowledge as compare to labour and capital for economic growth. Arrow's learning by doing, King Robson's learning by watching, Romer's learning by investment are few models of New Growth Theory all of which emphasis on human capital. Therefore new growth theory promotes the role of government and public policies to invest in knowledge intensive industries such as computer software and telecommunication (Meier, 2000).

Theory of Coordination Failure

Theory of Coordination failure emerged in 1990s. Many times coordination does not exist among complementary activities and this is the reason of foundation of coordination failure. Rosenstein Rodan (1943) was the first economists who raise this concept first time. Nurkse (1953) and Hirschman (1957) followed his emphasized the role of government to solve the problem.

2.3 Global Context

Mark (1982) focused on the special challenges for productivity analysis in growth of Service economy. It discusses particularly labour productivity in service industries and explains how the Bureau of labour Statistics is working to overcome some of the problems. Problems related to output and input measurements are discussed in different service industries viz. Trade, Transport, Communication, Business and Personal Service, Finance.

Wachter (2001) focused on the employment and productivity growth in service and manufacturing sectors in France, Germany and the US. While Labour productivity increases faster in France and Germany than in the US. This paper starts out from the observation that the patterns of growth service sector can explain most of these differences. Manufacturing sectors grew in a same manner in all three countries. It focuses on the structural differences through a shift share analysis, in the sense that there is a lag in structural change in the European countries with respect to the US. But the aggregate growth differences derive from differences in sectoral rates of growth. The high growth rates in labour productivity of service sector in France and Germany seem to be partly driven by convergence to American levels of productivity. The paper represents how changes in capital-accumulation can only clarify around 50 per cent of the catch-up by using a growth accounting approach consistent with the incidence of biased technological change. Paper examines the Mechanism behind these patterns of growth by comparing the evolution of single, large service sector. If the growth of productivity in services decreases as convergence of labour productivity is attained, increase in employment of service sector in France and Germany may have to sustain output growth in future. To analyse the source of labour productivity growth, the paper assumes that the economies' and sector' production processes can be captured by a production function with constant returns to scale. The paper's aim is to assess the role of these sectoral differences in describing aggregate growth and its difference across countries. For this, it has examined and compared the impact of structural change on growth within countries. Through shift share analysis it has assessed the potential of differences in economic structure for explaining differences in growth across countries. Paper investigates the role of capital-accumulation in explaining diverging sectoral patterns of productivity growth. This is done in a constant way with the impact of non-neutral technological change, whose importance is suggested by growth patterns of capital shares. It uses various stylised facts regarding to the growth of manufacturing and service sectors which are 2fundamental to the analysis. Paper concludes that growth of labour productivity in France and Germany service sectors may be due to catch up process to the higher level of American service productivity. To speculate about the future development of service employment in Europe, the extension of the Baumol's model (1967) of 'unbalanced growth' is used.

Ghani (2011) compares the fastest growing economies China and India. Service sector's share in India's GDP is bigger than in China, China is dominated I manufacturing sector and it exports manufactured goods. Paper focuses on growth pattern of China and India. Services can be separated into two broad categories-Traditional and Modern Service. India is rich in Modern Service which is linked to ICT. By comparing India's share of IT and IT enabled service I total exports with the rest countries of the world it can be easily said India stands at significant outlier. China in other hand is better than Indian firms in traditional services, which is nearly related to manufacturing sector. Tradability, Technology, and Transportability are 3T's through which Modern services productivity is being derived. It focuses on role of service led growth in reduction of poverty and creation of job, also at this fact that the jobs created by services are good or not. It also examines the growth generated through service sector.

Park and Shin (2012) analysed the 12 Asian countries which indicates that the service sector plays a great role for region's growth in the past. This paper provides substantial cause about the role of the service sector as an engine of growth in Asia. It also specifies few Asian countries such as Korea and Thailand where service sector is not so developed, i.e. in a stage of struggling and it will be very challenging for those countries to develop the sector. It explores the history of service sector in 12 major Asian economies. Separately and specially focuses on the share of service in total output and employment. The data are collected from the World Bank's World Development Indicators. The paper follows Einchengreen and Gupta (2009)'s quartic relationship of two waves of service sector growth between the service sector's share of GDP and per capita GDP. Data related to service sector value added, GDP and per capita GDP are taken it two phases first is from 1970-89 and second is from 1990-2010. Employment data is taken from 1980. To analyse the fact that is the service sector be a reason of growth of Asia. Paper investigates the GDP growth and productivity of Service sector compare to other sector.

Lee and Mckibbin (2014) used empirically based global intertemporal mutisector general equilibrium model to identify the impacts of rapid growth of labour productivity in the service sector in Asia. G-cubed model which is an intertemporal general equilibrium model is used to explore the impact of rise in labour productivity in the service sector in Individual Asian economies and then across all Asian economies at the same time. It emphasis on input output linkages and capital movements across industries and economies, and consumption and investment dynamics. The paper analyses the role of the service sector in structural adjustment and economic growth in Asia. Data are collected from the Groningen growth Developing centre (GGDC) which covers ears from 1970-2005. The data covers 10 Asian economies. Original data is divided into nine sectors. Shift Share analysis is used to examine empirically the impact of Tartarisation on aggregate productivity growth. Where on the one hand the paper finds that overall economic growth in Asia is hampered by lower labour productivity in the service sector relative to the manufacturing sector similarly on the other hand it finds that all sectors are benefited by the faster productivity growth in Service sector.

2.4 Indian Context

Mukhopadhya (2002) emphasised on Globalisation and Indian service sector describes the method for development of service sector and its subsectors. Through data of World development indicators (1998, 2001) and CSO this paper highlight the increasing contribution of service sector in Indian economy. Paper suggests that for increasing service sector's contribution in economy it is important to liberalise trade and investment in service sector.

Joshi (2004) analysed the sectoral composition of GDP and employment for the period 1950-2000. It exposes various facts related to employment, growth in various sector, through data of governmental agencies. In addition, it emphasis not only on employment as whole but divides it into formal and informal sector. Service sector is as a very important sector for employment generation and poverty alleviation, but in long run the development of all three sectors is important.

Banga (2005) Growth of Service sector in India Has increased tremendously in the last ten years but the growth of employment in Service sector has not been accompanied by growth of service sector. The paper finds that the growth of service sector has been jobless. It examines that some sectors have witnessed a high growth rate in the in the last decade, example business service and communication while some sectors have witnessed a decrease in their growth rates e. g, real estate and railways. The sectors with low and negative growth rate have a large potential for generating employment e g, Transport, construction and professional services. Reason of reduction of the scope for increasing employment in these sectors is raising labour productivity in the faster growing sectors. Growth in services has increased to higher use of services in manufacturing sector which implies that the service sector will be able to create its own demand in future. Study shows that due to growing external markets for services, India's service sector is growing. The domestic reforms and liberalisation through lowering of barriers to trade and allowing FDI, have improved growth of Indian Economy in the corresponding services. Paper suggests that to overcome the problems of lack of employment growth in services, it is necessary to achieve uniformity in the growth of different services.

Guha (2007) focuses on the demand pattern as a factor which is responsible for growth pattern. By following Baumol and Kaldorian views paper tries to examine the Indian growth structure through the validity of the production structure based explanation. It finds that the production structure based explanations is inadequate fir GDP growth structure. Service sector's productivity is higher than manufacturing and agriculture sector but the terms of trade have moved against the services. These are the features Kaldor had predicted for the manufacturing sector. The paper finds that decrease in price of service and increase in income inequality should lead a greater demand for services. For Kaldor's growth structure it focuses on the service and IT sector and for this paper examines the linkages of sector with the rest of economy. Leontief inverse matrix is used for this. Input-Output published by CSO is used to track the backward and forward linkages. It concludes that the structures of Indian growth do not follow the theories of Kaldor and Baumol, and the cause is that these theories provide explanations based on production structure of GDP growth. In India the case is different; here the growth structure can be better explain through demand component, increasing exports and consumption demand. The reason of service dominated growth structure is decrease in relative price of service.

Nayyar (2009) analysed the employment nature created in the different subsectors of services, relative to industrial sector. It includes educational requirements and quality of employment to define the nature of employment in which it takes three measures for quality of life: wages, job security and social protection. Cross sectional analysis has been done for sample over 600000 individuals in India in 1993-1994 and 2004-05. The choice of surveys is identified by the two facts. First, The period from 1990-91 to 2004-05 saw the most dramatic enhance in the output share of the services sector. Second, 2004-05 survey is recent while surveys of before 1993-94 are not as comprehensive in the variables. The surveys do not cover the same individuals over time. Data is collected at individual level through Pan- India Surveys on employment, conducted regularly by India's National Sample Survey Organisation (NSSO), which collects micro level data. It finds that in certain subsectors of services, the level of education of an individual has an important effect on the probability of being employed, while in others it does not. In comparison to the industrial sector, Services sub- sectors with quality of employment have low educational requirements.

Einchengreen and Gupta (2011) Working paper on the service sector as India's road to economic growth focuses on modern services as a reason for the growth in service sector's output and employment. Business services, communication and banking considered as modern services. This study observes that for sustaining economic growth and raising living standard will require shifting labour into both manufacturing and services.

Mukherjee (2012) quotes the contribution of service sector and subsector in GDP and employment of India through the data available on official government website and agencies like MOSPI, CSO and NSSO. In the 1950s and 1960s, transport, storage and communication services and trade, hotels and restaurant services grew faster than the overall services sector growth in India. In the 1970s and 1980s, financing and business services started growing at a faster rate. In fact, in the 1980s, financing and business services surpassed the growth of services such as transport, storage and communication and trade, hotels and restaurant. In the decade of 2000-2010, transport, storage and communication services are the fastest growing services sub-sector, followed by financing and business services. Both the sub-sectors have grown faster than the overall services sector growth. This paper identifies a number of barriers faced by the service sector and recommends the policy measures which if implemented will lead to inclusive growth, increased productivity, employment, trade and investment.

Das (2013) focuses the INDIA KLEMS Panel data to examine the labour productivity in Indian Service Sector during the period 1980-2009. The empirical results suggest that labour productivity in Indian Service Sector has been growing substantially over decades, and much of this productivity gain is accruing through acceleration in market services labour productivity. The observed growth pattern in the service sector has not been uniform across all services in India. The performance of market based ICT intensive sector is impressive especially telecommunications and financial services.

Mukherjee A. (2013) presented the service sector as the vast and fastest growing sector of India. Service sector has the highest labour productivity, and it will be increase continually. Quality of employment generated through service sector is not as good as needed. The service's share in total trade of India is higher than the global average. India places among top 10 WTO members in service exports and imports. There are so many reasons among which are: India does not have a policy that can lead to inclusive growth, no. of governing bodies and in coordination among them adversely affect the growth of sector, FDI restrictions and regulatory barriers. India's service sector growth and exports of service are less than that of competing countries and exports are concentrated in few services and markets only. There are wide inequality in the growth of different types of services and great inconsistency in access to services, a major proportion of the poor in India do not basic services such as healthcare and education. Infrastructure is poor, so the cost of service delivery is high. Although India wants to develop as a knowledge hub, there is no equality in the quality and standard of education. The service sector will be able to contribute to inclusive growth sby increasing investment, generating employment and human capital and developing infrastructure. It is essential for a developing country like India, to generate quality employment. India requires private investment in key and telecommunications. It can attract FDI and private investment only with a secure, clear, unbiased competitive policy environment. The paper suggests various reforms, if these are implemented, it will increase the productivity and efficiency of the service sector and lead to inclusive growth.

Singh and Kumar (2014) analysed the contribution and growth of service sector and its components to GDP for the period years (1950-51 to 2010-11). The paper describes that the service sector marked growth took place especially in the post liberalisation period. This paper using National account statistics, Economic survey and MOSPI as a data base and compound growth rate in methodology to show that the contribution of service sector in total GDP has been increased as compare to primary and secondary sector during the study period.

Latha et al. (2014) focused on health and education of India which are subsectors of service sector. The development of both health and education sectors have made the advancement of service sector. The study has done with the focused on service sector growth, health and education services of India. Secondary data is used which is obtained from economic survey of Government of India. Analysis covers the period from 1950-51 to 2010-11. Over the period between 1950-2011 the contribution of service sector has doubled and the contribution of other service sector is increasing much faster as compare to growth rate of GDP in the last decades during 2000-2001 and 2010-11. As civilization progresses human desires enhance leading to the evolution of education activities.

Verma et al. (2014) explained that service sector in India has emerged as a prominent sector in terms of its contribution to income, FDI inflows, employment and trade inflows in the context of national and state. It focuses on two objectives. First, is to identify those factors through which the India’s export growth increases during recent years and the second is to identify the growth and performance of subsectors of service sector in India. The study says that the service sector is the only sector which can take India to achieve the golden target of becoming one of the developed nations of the world by 2020. Trade hotels and restaurants as a group are presented as a largest contributor subsector. On the basis of GSDP of 2011-12 of different states and Union territories, the service sector is the dominant sector in most of the states in India. The share of cumulative FDI inflows to the service sector would be 43.33 per cent during 2012-13. In exports the software services are the major constituent which includes both IT enabled services and business processing and outsourcing. The paper gives importance to venture capital and private equity investment because service sector influences it.

Pais (2014) A working paper on Growth and structure of the service sector in India by analyses the subsectors within services that have contributed mainly to GDP growth and employment growth. This paper observes the dimensions of employment in service sector by which the quality of employment is examined in service sector through the analysis of the productivity levels in different services.

Basha et al. (2014) a study on impact of service sector in Indian Economy identifies that most of the economies are depending on service sector. Through using data available on official websites of National Accounts Statistics, CSO and MOSPI, this paper explains that which sub sector is growing rapidly, growth of service sector in different states of India and people’s dependency on service, agriculture and industrial sector. It also concludes that growth rate of the economy should not be only limited to service sector but it should also develop in agricultural and industrial sector. This paper explains about how our economy has developed since 1951-2013.

Chahal (2015) presented Service sector as an engine of growth for Indian economy. The ccdata of Planning Commission, MOSPI and CSO has been taken. The study confirms that service sector have grown at the significant rate in comparison to other sectors. Rising share of this sector in GDP over covers the poor performance of agriculture sector. Paper finds that as a service sub sector, trade is dominant all in terms of its contribution in Indian GDP and the employment percentage in service sector as well as in industry sector is rising while in agriculture, it is falling continuously.

Joshi (2015) provided remark of the shift in India's development strategy from import substitution growth strategy (ISS) to an Export-led –growth Strategy (ELGS). It argues that if Hindu rate of growth is due to ISS in the first three decades of planning, then. India unstoppable growth is due to service led growth. It emphasis the openness of services and foreign direct investment in services as an essential determinants of GDP growth during the period 1995-2005. Trade is an engine of growth in the context of ELGS due to globalization. It focuses on deregulation of various subsectors of service sector which has done by government of India in the post 1991 period. It presents service sector as a source of foreign exchange reserves, FDI, GDP growth. The paper also identifies that the for sustainable growth, along with openness in services, industrial and agricultural reforms are important. India has need to diversify the services, explore new destinations for its exports and also to move higher up in value chain as Philippines, China and Ireland which are providing tough competition to India. It also focuses on social sector allocations in which especially the fact about education has taken.

2.5 Research Gap

Various national and international literatures have been found which deals with structural change and labour productivity of various sectors of economy and economy as whole. This study provides the structural change and labour productivity of services sector by using theoretical analysis of 'Shift Share Analysis' as whole and within sector rather than regional analysis which has been done in maximum of studies. It is an attempt to measure the labour productivity of service sector in India at aggregate and disaggregate level.