



Developing the Services Sector as Engine of Growth for Asia: An Overview

By

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**ICRIER-KAS Seminar on
Services Sector as an Engine for Inclusive Growth**
ICRIER, New Delhi, 19 December 2012

Introduction and Overview

- Developing Asia's growth fueled largely by export-oriented industrialization, but the manufacturing sector is maturing and global environment changing.
- Services sector performance has been less impressive.
 - Productivity lags manufacturing,
 - Concerns about weak backward and forward linkages.
 - Can it be an engine for inclusive growth and rebalancing?
- Presentation outline
 - Basic relationship: income, employment, education, and trade
 - Overview of the service sector in Asia
 - Productivity and poverty reduction
 - Conclusions
- Work in progress—incorporate other papers

Analytical issues

- Heterogeneity—high level of aggregation may obscure distinct characteristics of growth or tradability
- Measurement issues
 - Output of services is hard to measure (e.g., public education).
 - Many service sector activities are highly regulated and insulated from competition.
- Can have economy-wide impact

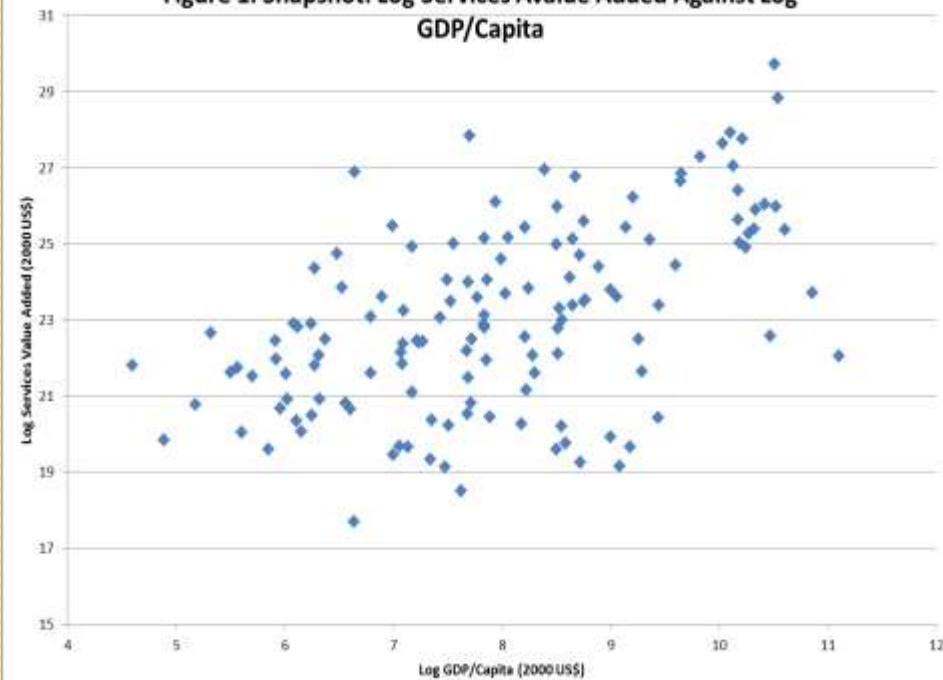
NAICS code	Sector
11	Agriculture, forestry, fishing, and hunting
21	Mining
22	Utilities
23	Construction
31-33	Manufacturing
42	Wholesale trade
44-45	Retail trade
48-49	Transportation and warehousing
51	Information
52	Finance and insurance
53	Real estate and rental and leasing
54	Professional, scientific, and technical services
55	Management of companies and enterprises
56	Administration and support and waste management and remediation services
61	Educational services
62	Health care and social assistance
71	Arts, entertainment, and recreation
72	Accommodation and food services
81	Other services (except public administration)
92	Public administration

NAICS = North American Industry Classification System

Source: US Census Bureau, www.census.gov

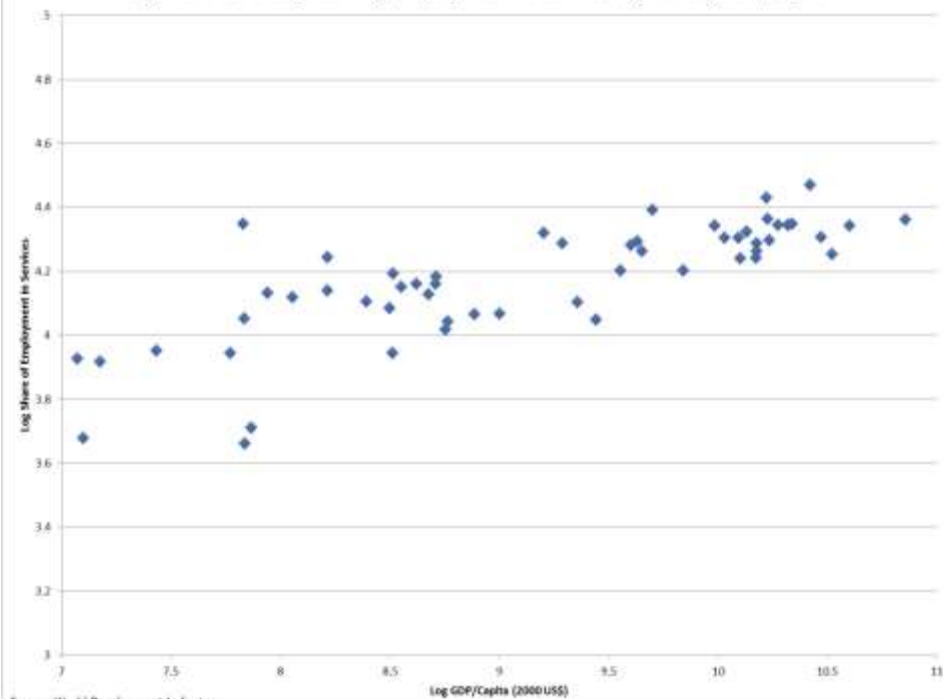
Robust empirical relationships: cross-sectionally...

Figure 1. Snapshot: Log Services Value Added Against Log GDP/Capita



Source: WDI Indicators, Data reflects available observations from all countries for 2009 and is reported in constant 2000 US\$.

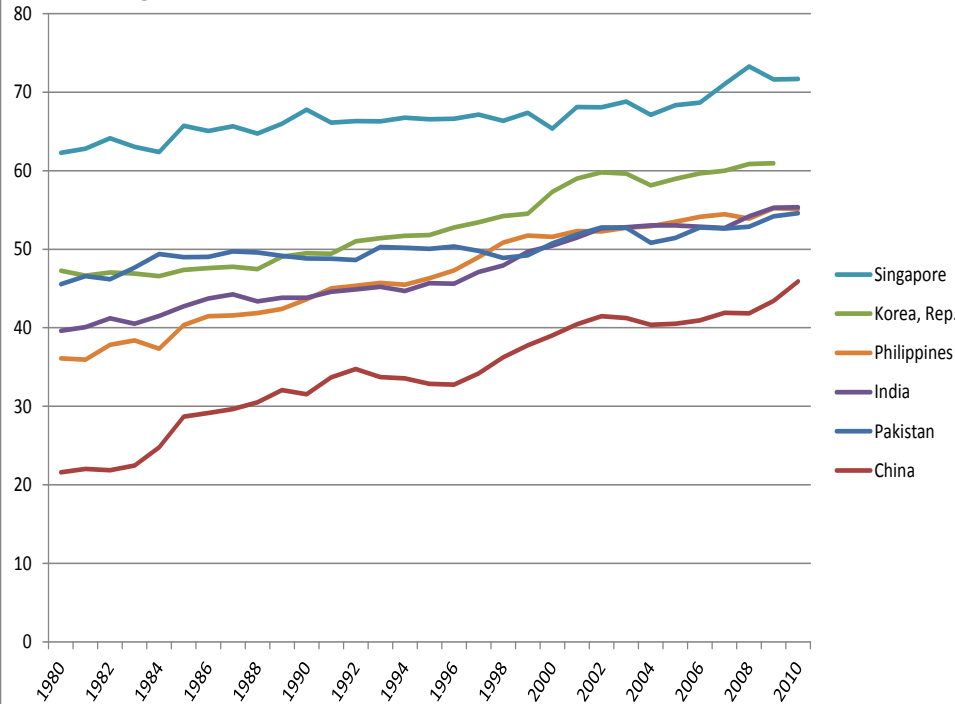
Figure 2. 2009 Snapshot: Log Employment in Services Against Log GDP/Capita



Source: World Development Indicators

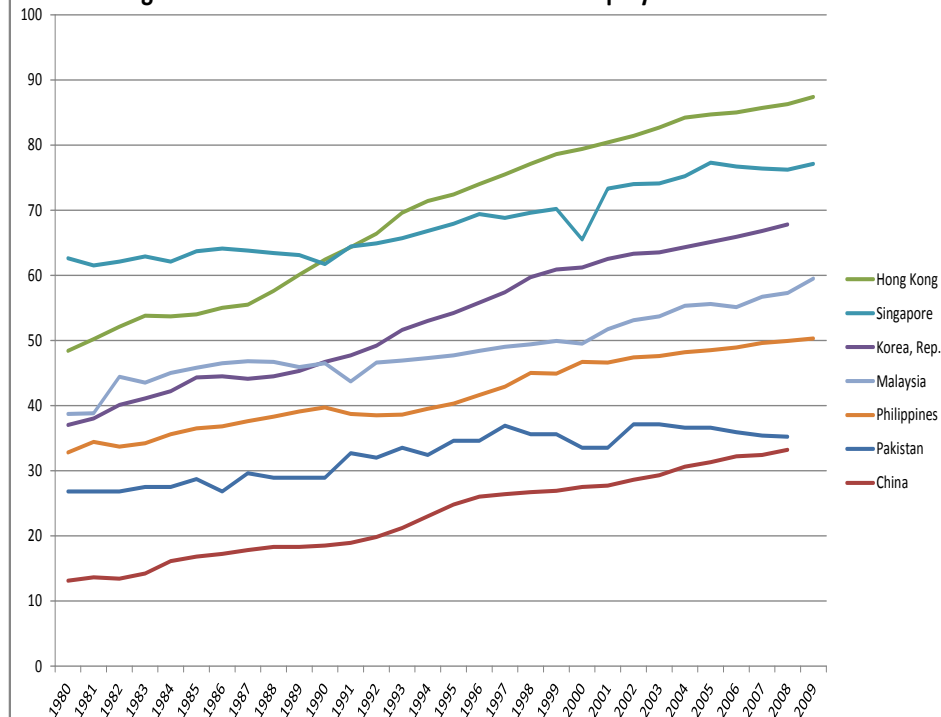
...and over time

Figure 5. Selected Asian Economies Services as % of GDP



Source: World Development Indicators

Figure 6. Selected Asian Economies Service Employment as % of Total



Source: World Development Indicators

Even within developing Asia

Figure 15. Developing Asia Log Services to Log GDP/Capita Relationship Across Time (1960-Present)

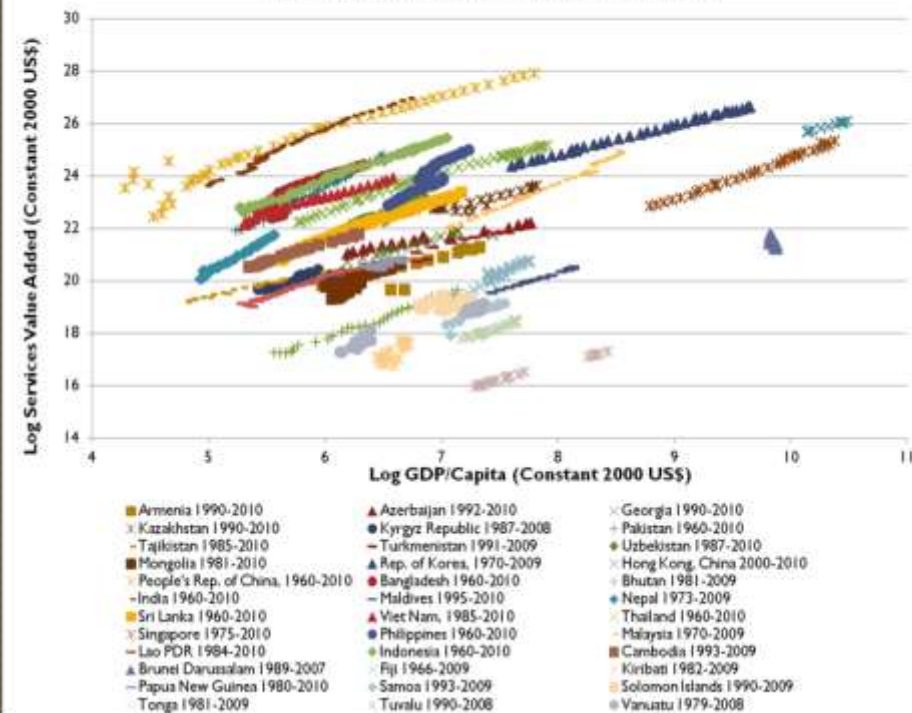


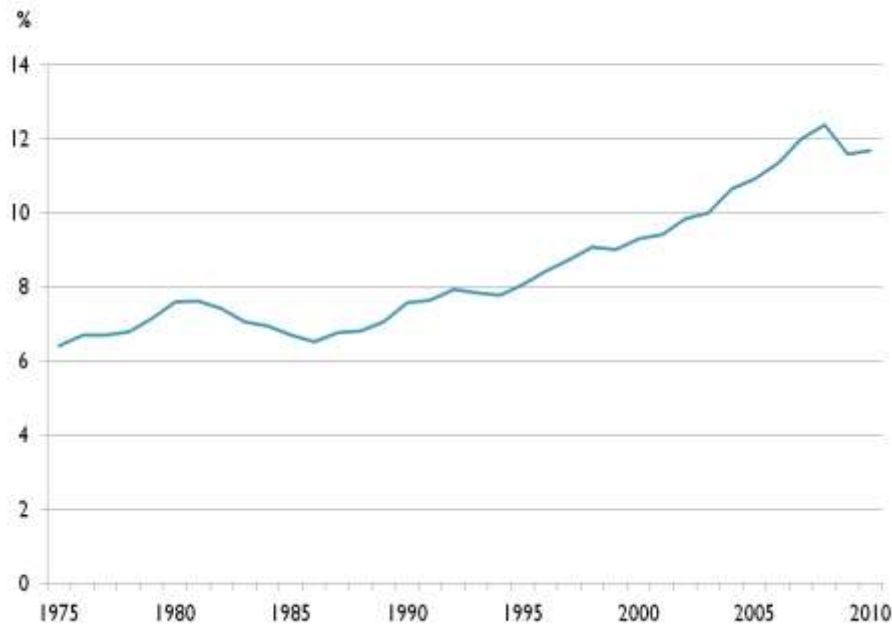
Figure 16. Developing Asia Log Services to School Life Expectancy Relationship Across Time (1998-Present)



Steady growth at the global level...

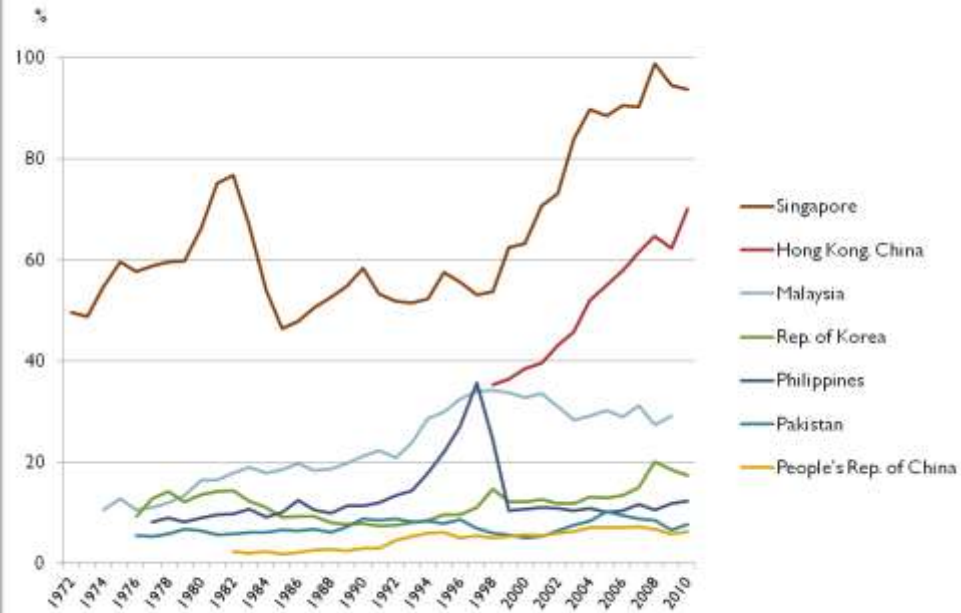
....less obvious within Asia

Figure 4. Global trade in services as share of world GDP



Source: World Development Indicators

Figure 7. Trade in Services as % of GDP

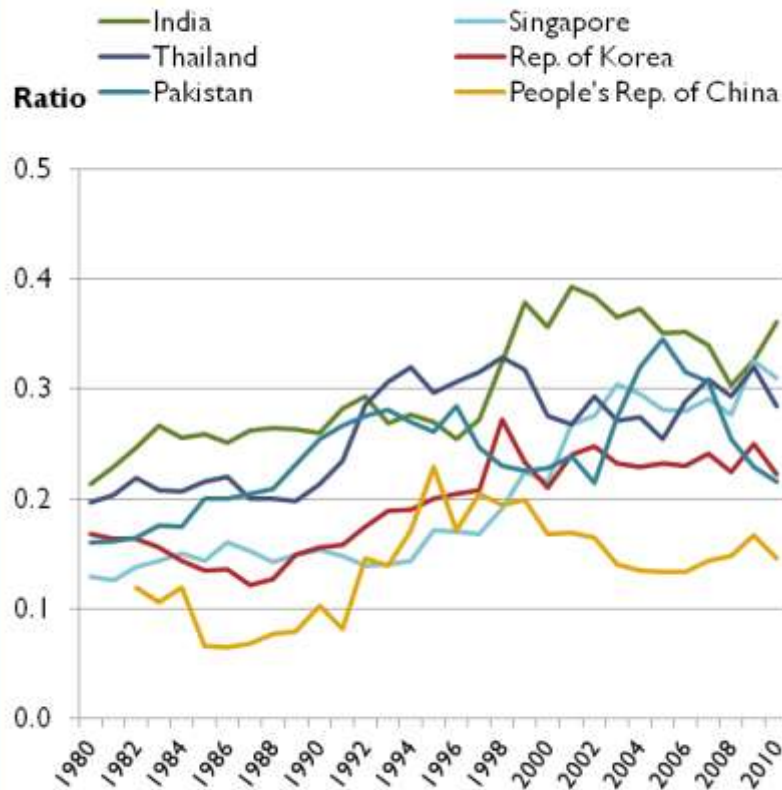


Source: World Development Indicators

Relationship to trade more complex

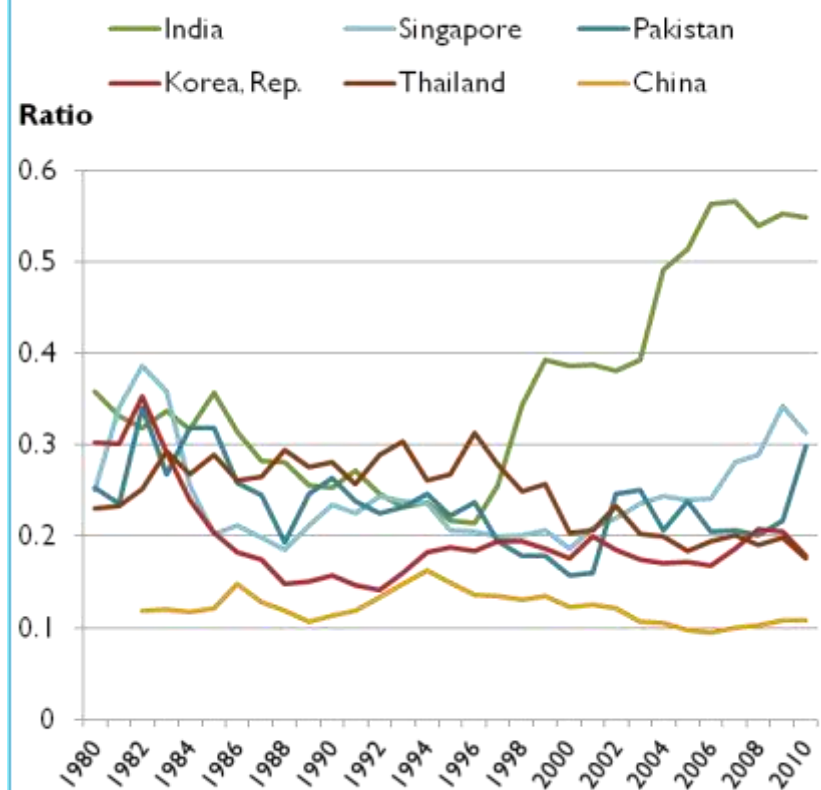
Some evidence of lagging regional competitiveness...

Figure 9. Ratio of Service Imports to Goods Imports



Source: World Development Indicators.

Figure 10. Ratio of Service Exports to Goods Exports

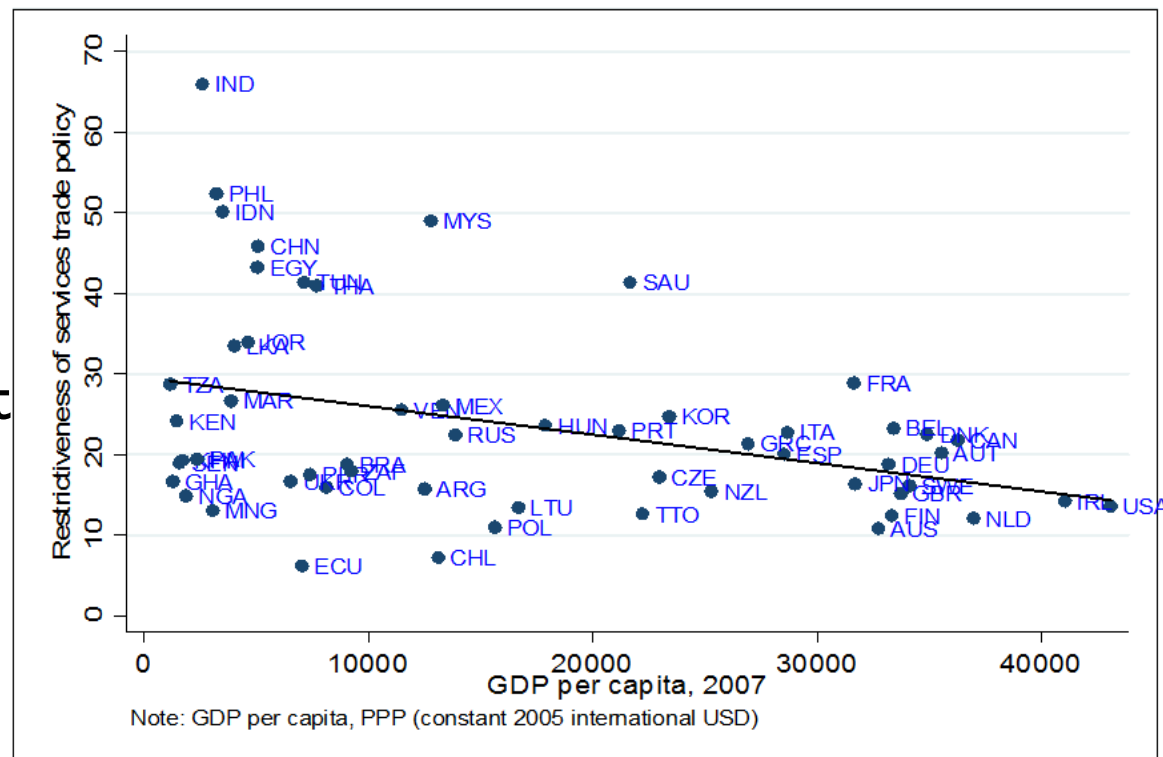


Source: World Development Indicators.

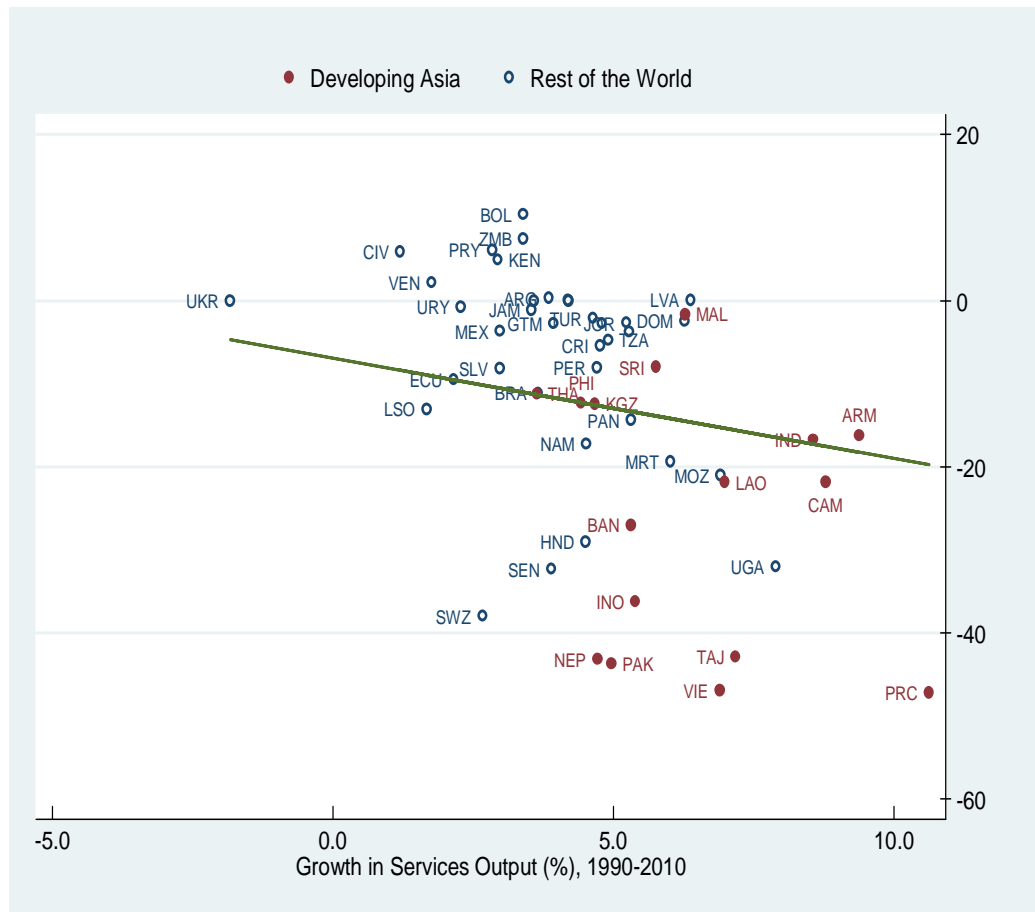
And an explicit role for policy

- Trade restrictiveness declines with income, though causality is debatable
- Trade engagement at multilateral, plurilateral, regional, sub-regional, and bilateral levels

Figure 8. Restrictiveness of Services Trade Policies by GDP per capita, 2007



Services, inclusive growth and poverty reduction



Note: The line is the predicted poverty change after controlling for initial level of poverty, growth in services outputs, former CPE, female educational attainment and time period. Poverty is based on \$1.25 a day poverty line.

- Connected to trade liberalization is concern of some policymakers that creation of modern, high-productivity services could worsen poverty or unemployment.
- Cross-sectional analysis of 56 economies shows some evidence that services growth can lower poverty.

Cross-country Regressions on Change in Poverty Headcount (at \$1.25 a day), 1990-2010

Table 3. Cross-country Regressions on Change in Poverty Headcount (at \$1.25 a day), 1990-2010

	(3.1)	(3.2)	(3.3)	(3.4)	(3.5)	(3.6)
Initial Poverty Level	-0.424*** (0.064)	-0.421*** (0.072)	-0.465*** (0.067)	-0.465*** (0.072)	-0.437*** (0.068)	-0.428*** (0.071)
Former CPE	-7.818*** (2.459)	-7.681*** (2.465)	-6.031* (3.230)	-6.007* (3.231)		-3.781 (3.536)
Developing Asia					-6.816** (3.088)	-6.819* (3.533)
Services output growth	-1.242*** (0.454)	-1.179*** (0.438)	-1.205** (0.481)	-1.138** (0.480)	-0.908* (0.515)	-0.711 (0.509)
Agricultural output growth		-0.358 (0.819)		0.105 (0.778)		
Manufacturing output growth		0.051 (0.326)		-0.104 (0.425)		
Share of females attending secondary school or higher in 1990			-0.118* (0.068)	-0.123* (0.070)	-0.129** (0.056)	-0.097 (0.071)
Constant	21.418*** (5.831)	21.706*** (5.905)	24.622*** (6.388)	24.941*** (7.251)	18.572*** (6.078)	18.917*** (6.554)
Observations	56	56	52	52	54	52
R-squared	0.684	0.685	0.692	0.692	0.706	0.716

Notes: Robust standard errors are reported in parentheses. “***” means significant at 1%, “**” at 5%, and “*” at 10%.

All regressions control for time period.

Services sector in Asia: the basic facts

- Services sector has clearly been on the rise, whether viewed in terms of output or employment.
 - From 44% average share in 1980, services now account for slightly over one-half of GDP in developing Asia.
 - But with some variation across subregions.
- Services sector is a key provider of jobs.
 - Most of the employed are in services in Kazakhstan, Malaysia, Maldives, Philippines, and the NIEs.
- Despite the rapid rise in India's services output share, its services employment share remains relatively low (27%).
 - same with other South Asian economies.
- Services sector has been a huge contributor to overall growth.

Figure 11. Sectoral shares in GDP

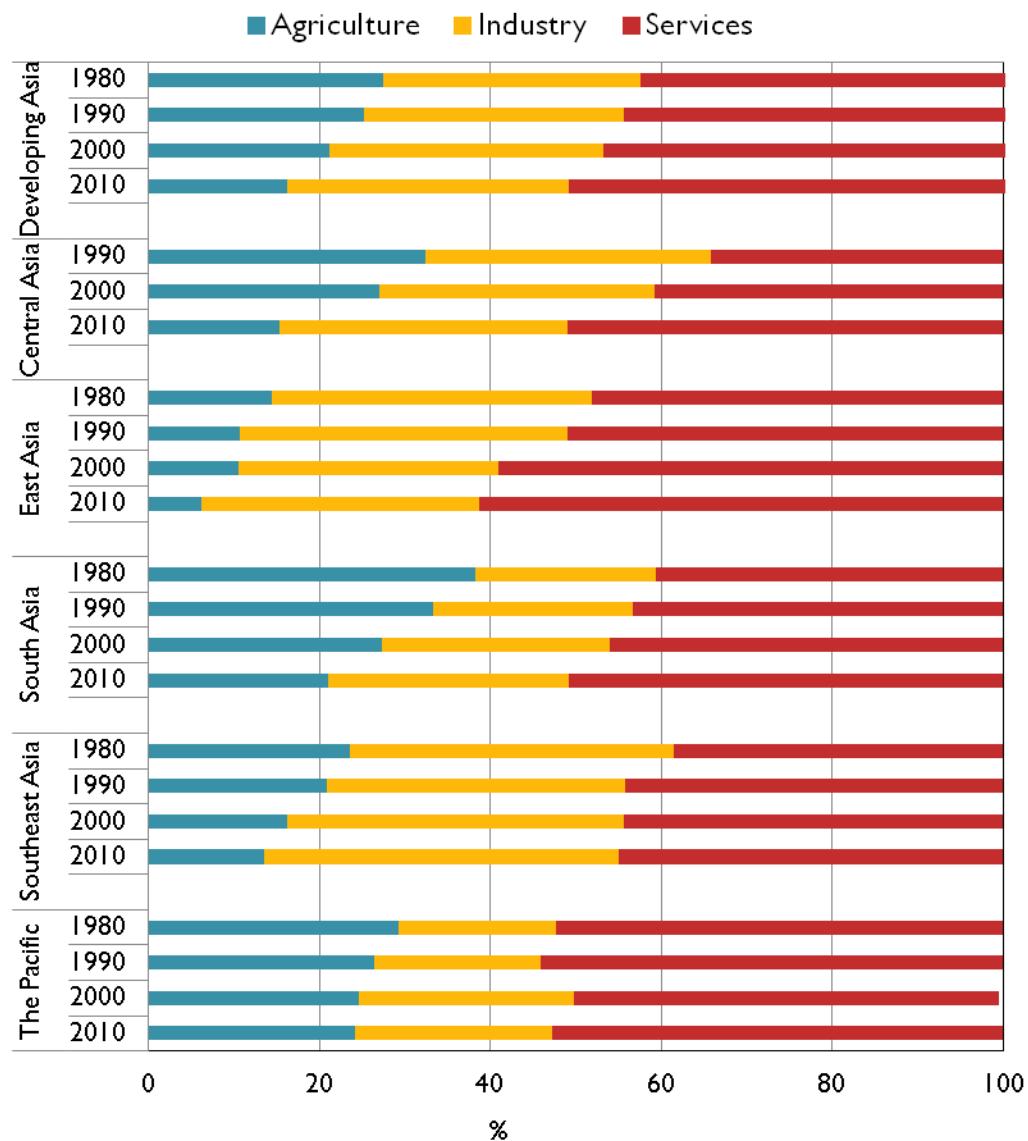


Figure 12. Share of Services in GDP

■ 1980 ■ 1990 ■ 2010

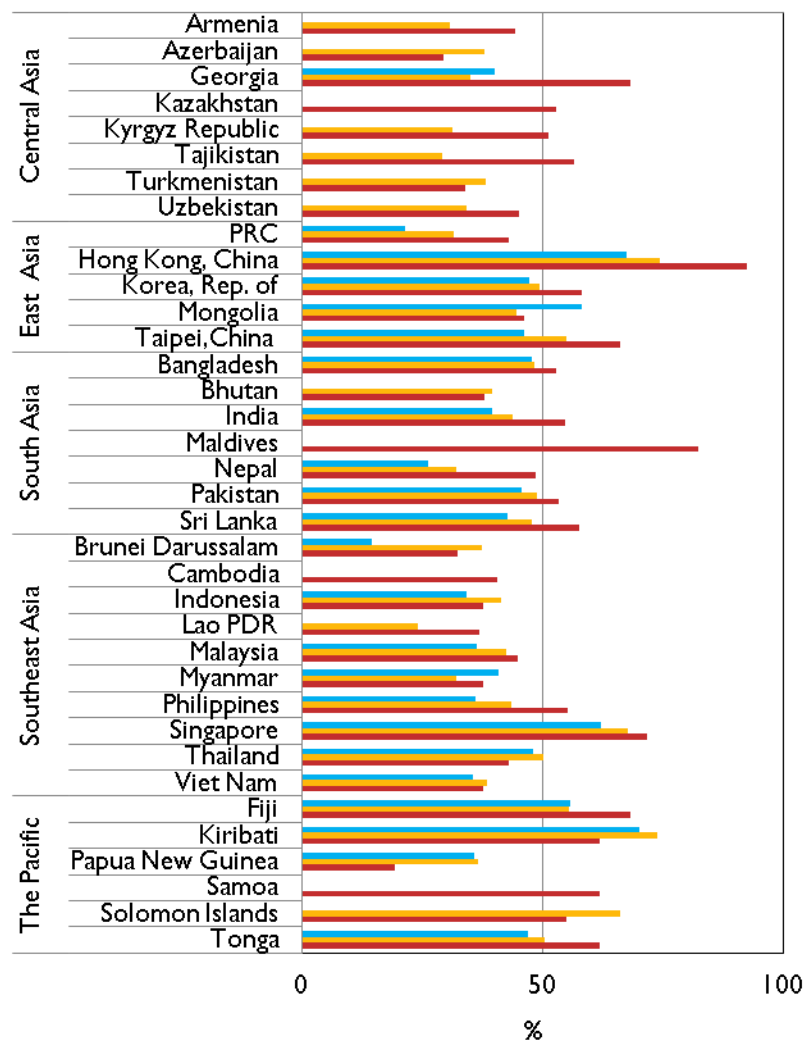


Figure 13. Share of Services in Employment

■ Around 2009 ■ 2000 ■ 1990

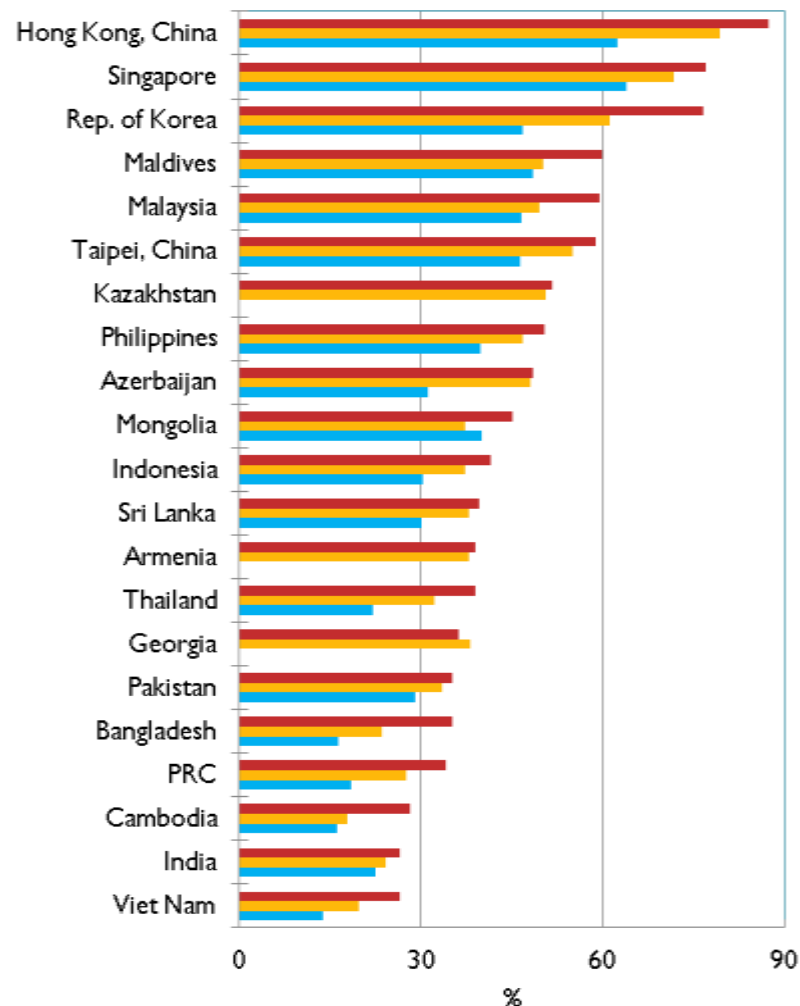
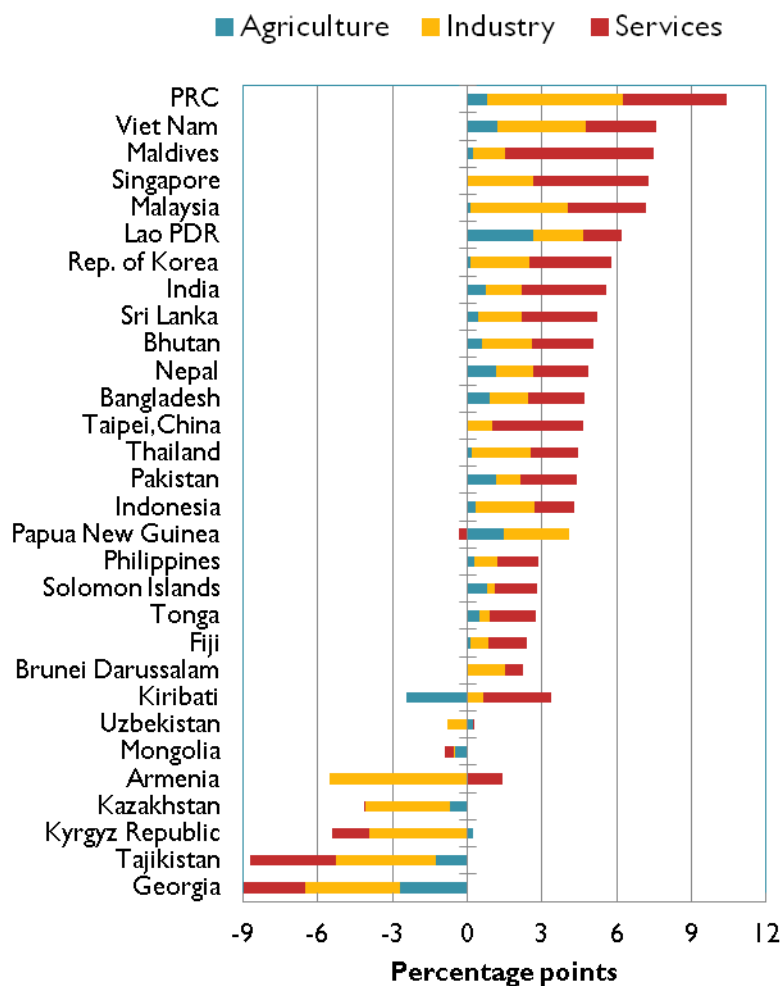
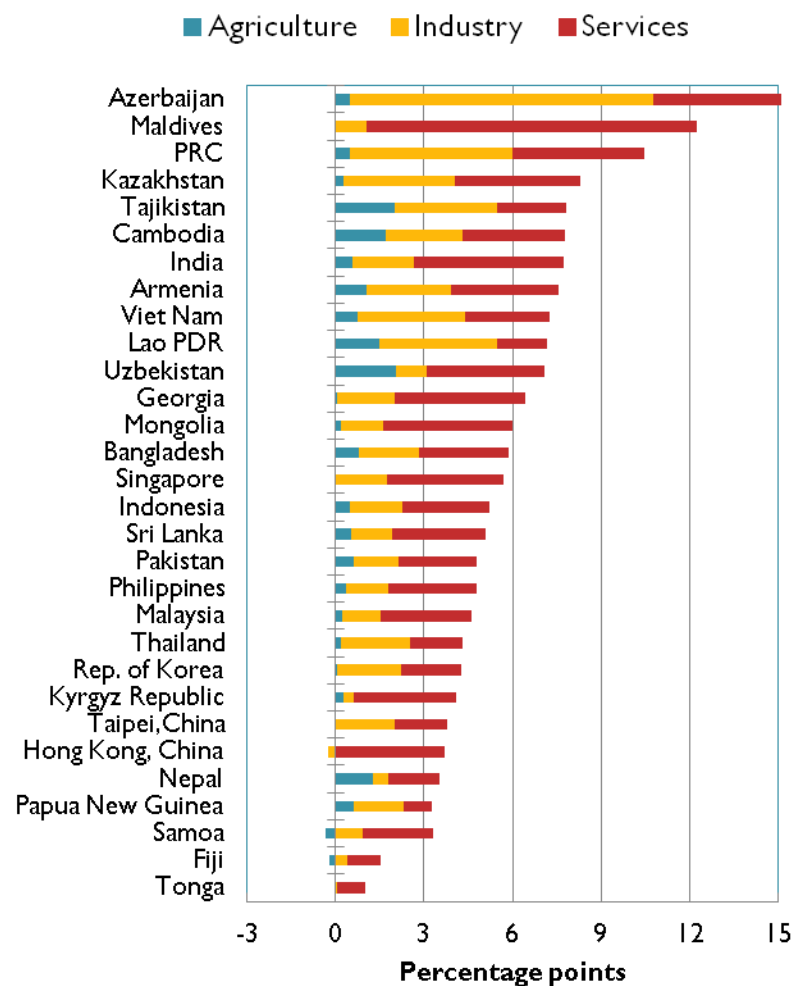


Figure 14. Contributions to annual GDP growth

1990-2000



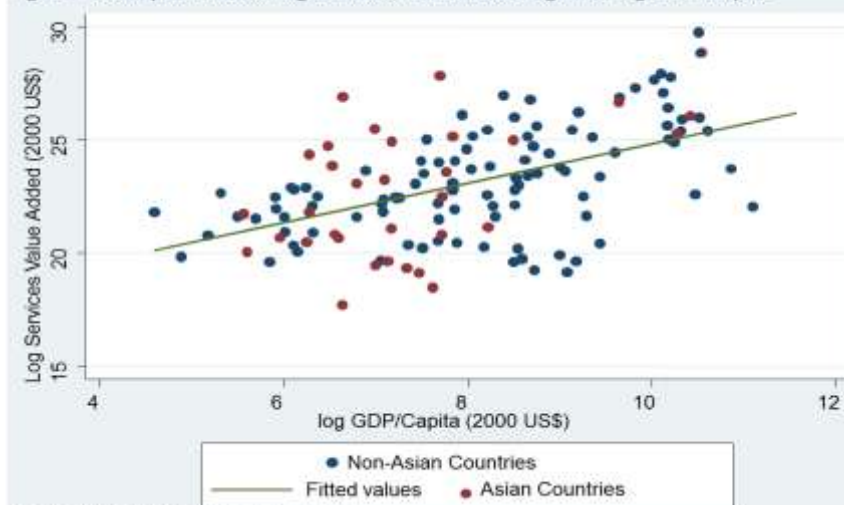
2000-2010



Services sector in Asia: the basic facts

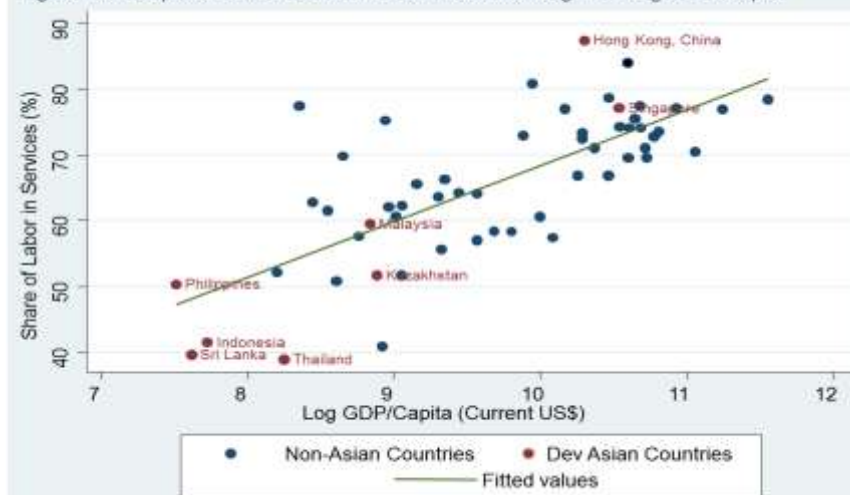
- Asian countries not consistently above or below international norms
- However, those below norm tend to be poor
- Moreover, aggregates mask critical issues:
 - degree of backward and forward linkages.
 - extent of diffusion of services productivity advances to the rest of the economy.

Figure 17. Snapshot 2009: Log Services Value Added against Log GDP/Capita



Source: World Development Indicators

Figure 18. Snapshot 2009: Share of Labor in Services against Log GDP/Capita



Source: World Development Indicators

Services sector in Asia: the basic facts

- Growth of services is correlated with rise in income and educational attainment.
- But countries in developing Asia are not consistently above or below an international norm.
 - As seen by regressing log services value added against per capita GDP.
 - A similar observation holds true for employment.
- The aggregate figures mask critical issues such as:
 - degree of backward and forward linkages of the services sector.
 - extent of diffusion of services productivity advances to the rest of the economy.

Services' low productivity in Asia

- Asia's services sector is still dominated by traditional activities:
 - wholesale and retail trade, hotels and restaurants, real estate, transport, personal services, and public administration.
- Modern services (i.e., information and communication, finance, and professional business services) are only 8-12% of GDP in PRC, India, Indonesia, Thailand, and Taipei, China.
 - Compared to 17-25% in OECD such as France, Japan, and the US.
 - Only Hong Kong, China; Korea; and Singapore have comparable sizes of modern services with OECD.

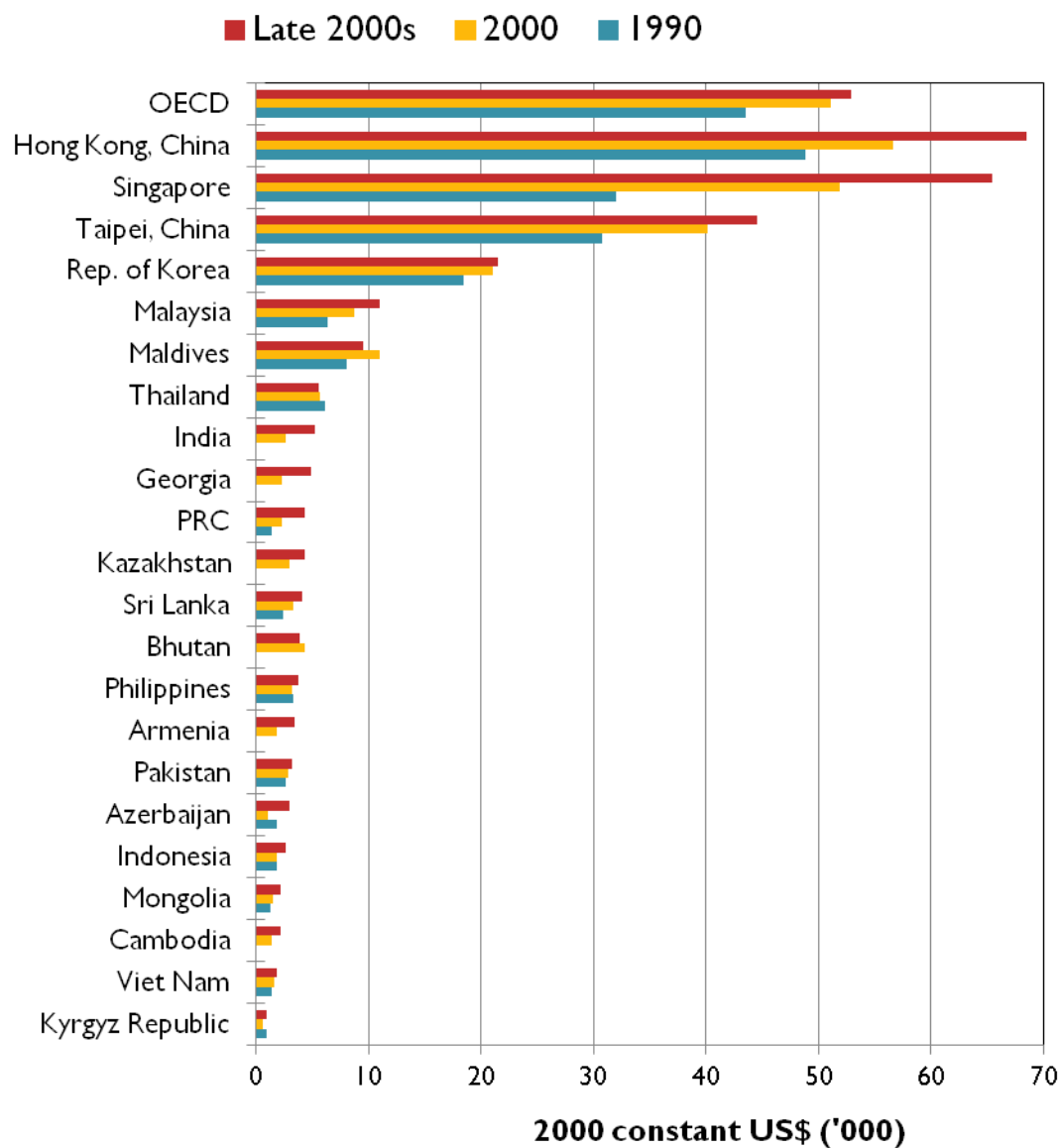
Table 2. Share of Services in Value-added, 1990 and 2010 (%)

Economy	Total Services		Wholesale and Retail Trade		Hotels and Restaurants		Transport and Storage		Real estate and dwellings		Communication, finance, and business services		Public administration, community, personal, and other services	
	1990	2010	1990	2010	1990	2010	1990	2010	1990	2010	1990	2010	1990	2010
Developing Asia														
PRC	31.5	43.4	6.8	8.5	1.6	2.1	3.8	4.9	2.1	7.3	9.4	9.4	7.9	11.2
Hong Kong, China	87.2	92.9	21.8	24.0	3.0	3.3	7.7	8.1	5.1	5.2	19.4	24.4	30.3	27.9
India	46.1	54.7	11.8	15.1	1.0	1.4	6.4	6.3	5.0	6.1	8.7	11.0	13.3	14.5
Indonesia	42.4	37.7	13.5	10.9	3.2	2.8	6.1	3.4	2.9	2.6	6.5	7.8	10.1	10.2
Korea, Rep. of	51.5	58.5	11.8	8.3	2.4	2.4	4.7	4.5	6.5	8.1	11.2	16.4	14.8	19.2
Malaysia	44.9	46.0	10.9	11.9	2.2	2.3	3.8	3.3	5.4	4.1	14.4	14.6	8.3	9.7
Philippines	50.8	55.1	14.7	17.4	-	-	3.2	3.9	5.8	6.5	11.5	13.9	15.7	13.4
Singapore	67.8	71.7	13.1	16.5	3.5	2.2	11.4	8.6	3.6	4.1	26.6	29.6	9.6	10.7
Taipei, China	55.0	66.2	13.4	18.8	1.7	2.0	4.6	3.3	6.4	8.9	11.4	12.4	17.5	20.8
Thailand	50.9	43.0	17.8	13.1	5.4	4.7	4.5	4.1	2.2	1.4	11.3	7.7	9.7	12.0
OECD														
United States	73.4	80.2	12.9	11.6	3.4	3.8	3.0	2.8	12.1	12.2	18.9	25.1	23.0	24.8
Japan	59.8	72.6	12.8	12.3	-	-	4.9	4.5	9.4	13.0	13.6	17.2	19.1	25.7
France	69.2	79.7	11.8	10.6	2.3	2.6	4.6	5.0	9.8	13.4	18.9	22.0	21.7	26.1

Services' low productivity in Asia

- There is a huge gap between Asia's productivity in services and that of OECD.
- For most Asian economies, services productivity is only less than 10% that of OECD.
- But there are economies, which have already caught up with OECD—Hong Kong, China in 1990 and Singapore in 2000.
- For most, it might take about 15-30 years to reach even about one-fifth of OECD's current productivity.
- This suggests that much remains to be done to transform Asia's services sector.

Figure 19. Labor productivity in services



Quality of data: a major problem in the analysis of Asian services

- One key challenge is the need to improve basic data collection.
- Dearth of data prevents the study of more narrowly defined range of services, e.g. “business services”.
- There is tendency for employment/wage data to have finer levels of disaggregation than sectoral output data.
- Greater coordination and consistency across reporting sources could improve usefulness of data.

Table 4. Available services data in selected developing Asia economies

Selected Asian Economies	<u>Economic Data on Services</u>			<u>Employment Data on Services</u>		
	Types of Data	Level of Disaggregation in Services	Years Available	Types of Data	Level of Disaggregation in Services	Years Available
China, People's Rep. of	Services Value Added	13	2005-present	Average Wages by Sector	14	2003-present
	GDP by Sector	6	1978-present	Employment by Sector	14	2003-present
Hong Kong, China	Exports & Imports of Services by Sector	7	2006-present	Average Wages by Sector	6	2005-present
	GDP by Sector	8	2005-present	Employment by Sector	6	2005-present
Korea, Rep. of	Service Industry Survey (Sales, # of establishments, Employment)	6	1996-2007	Average Wages by Sector	12	2011
	GDP by Sector	12	1985-present	Employment by Sector	17	2004-present
India	Net Domestic Product by Sector	10	2005-present	Employment by Sector	Full 4-digit Indian NIC Coding System	2010
	Classification of Output/Value Added by Sector	10	2000-present	Employee Compensation by Sector	10	2000-present
Malaysia	Revenue/Expenses by Sector/Occupation	37	1971-2007	Employment By Sector/Occupation	37	1971-2007
	Value of Fixed Assets by Sector/Occupation	37	1971-2007	Total Wages by Sector/Occupation	37	1971-2007
Philippines	GDP by Sector	6	2009-present	Employment by Occupation	17	1990-present
				Employment by Sector	11	2001-2009
Singapore	Value Added by Sector	7	2004-present	Employment by Occupation	25	2010
	Number of Establishments by Sector	7	2004-present	Employment by Sector	12	2011
Taipei, China	GDP by Sector	5	1986-present	Employment by Sector	55	2011
				Wages by Sector	55	2011

Concluding observations

- Need to remove structural and policy impediments to enhance potential of services sector as engine of growth and jobs.
- These include strengthening of labor and capital markets, reform of tax regimes, and elimination of burdensome regulations.
- Reducing barriers to services trade not only promotes efficiency and productivity but also contributes to exports and growth.
- Overall guiding principle is to create a more competitive environment for services.

Concluding observations

- The manufacturing sector is now maturing, reducing its scope for further growth and capacity to generate employment.
- We find that Asia's services sector already accounts for a large share of the region's output and employment.
- Services sector also makes a substantial contribution to Asia's growth.
- We also find some limited evidence that services sector development can lower poverty in the region.
- Since services tend to be labor-intensive, invigorating services has become even more critical.

Concluding observations

- Services sector diversity means that each country faces different priorities in services sector development.
- But strengthening modern services remains a common region-wide challenge.
- Traditional services continue to account for a substantial share in the region's services sector.
- Partly as a result, Asia's services sector productivity lags far behind that of OECD.

Some conceptual issues

- The either-manufacturing-or-services fallacy
 - Some point to experiences of India and Philippines in ICT-BPO as evidence of services-led growth.
 - Technological progress allows countries to leapfrog industrialization.
 - But leapfrogging hypothesis can be misused as an excuse for failures of manufacturing.
 - Real challenge is to address structural and policy impediments to efficient manufacturing *and* services.
 - A good balance between services and manufacturing remains the most viable growth strategy.

Some conceptual issues

- Services sector development, inclusive growth, and role of government.
 - Services sector development can promote inclusive growth by creating jobs in both modern and traditional services.
 - Avoid generalizing about job-creating capacity of manufacturing versus services since both are heterogeneous.
 - In general manufacturing is more skewed toward capital than services: but most capital held by a wealthy few.
 - A shift in economic structure toward services can thus help to reduce poverty and inequality.
 - What other policies can Asian governments pursue to stimulate growth of services?
 - ICT infrastructure, given large spillover effects on services, and its role in transforming nontradable into tradable services.
 - Telecom liberalization.