SET
SUPPORTING ECONOMIC TRANSFORMATION
SERVICES AND ECONOMIC TRANSFORMATION

- Services share in employment and output growing in all countries.
  - In SE Asia/Latin America is the reversion of a previous more or less successful industrialisation process.
    - Modern services tend to dominate the transformational process
  - In Africa, there is a movement of resources from agriculture into services.
    - Traditional services predominantly absorb labour, but modern services are also present.
- Pessimistic view of the role of services: Movement of resources from agriculture to services keep resources in low productivity activities.
- However, recent evidence indicates 3 pathways of services into productivity.
  - Services have been a major driver of productivity growth in the last decades
  - Exported services are particularly relevant in driving productivity and trade
  - Services value added is increasingly embedded in other product exports
- Nevertheless, services are very protected (more than agriculture) around the world, especially in LDCs.
  - Financial regulations are blocking the expansion of mobile financial services in the EAC.
  - Services provided under mode 4 remain mostly restricted (only 0.5% of US imports of services are mode 4)
1. Services have been a major driver of productivity growth in the last decades

2. Exported services are particularly relevant in driving productivity and trade

3. Services value added is increasingly embedded in other products exports
AS INCOME INCREASES, SERVICES BECOME A MAJOR FACTOR IN PRODUCTIVITY GROWTH

Contribution of different sectors to labour productivity change, 1991–2013
SERVICES EXPLAIN MUCH OF THE PRODUCTIVITY GROWTH IN DEVELOPING COUNTRIES

Annualised labour productivity growth 1991-2013

Source: Own calculations based on World Bank-WDI
1. Services have been a major driver of productivity growth in the last decades

2. Exported services are particularly relevant in driving productivity and trade

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IN MANY LDCS, EXPORTS OF SERVICES HAVE GROWN FASTER THAN TRADE IN GOODS

Source: Own calculations based on UNCTAD
LARGER PRODUCTIVITY GAP BETWEEN EXPORTING AND NON-EXPORTING SERVICE FIRMS IN LICs THAN IN THE REST OF THE WORLD

Source: Own estimations based on World Bank Enterprise Survey
AMONG THE EXPORTING FIRMS, SERVICES FIRMS ARE MORE PRODUCTIVE IN LICs

Source: World Bank Enterprise Survey
1. Services have been a major driver of productivity growth in the last decades

2. Exported services are particularly relevant in driving productivity and trade

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SERVICES EXPORTED FROM DEVELOPING COUNTRIES INCREASINGLY PART OF VALUE CHAINS IN OTHER COUNTRIES

Share of exports of intermediate services 1992 vs 2012

Source: Own calculations based on EORA-MRIO
VALUE ADDED FROM SERVICES GREATER THAN EXPORTS OF SERVICES IN SOME DEVELOPING COUNTRIES

Source: Own calculations based on EORA-MRIO
## Services Sector Development and Jobs Effects

<table>
<thead>
<tr>
<th>Sector</th>
<th>Direct effects</th>
<th>Indirect effects (static and dynamic)</th>
<th>Induced/ productivity effects</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Jobs (skilled, medium or low-skilled workers)</td>
<td>Exports</td>
<td>GDP</td>
</tr>
<tr>
<td>Accommodation and restaurants</td>
<td>Low and Medium skilled</td>
<td>+</td>
<td>++</td>
</tr>
<tr>
<td>Education</td>
<td>Medium skilled</td>
<td>+</td>
<td>++</td>
</tr>
<tr>
<td>Finance and insurance</td>
<td>Skilled</td>
<td>+++</td>
<td>++</td>
</tr>
<tr>
<td>Health</td>
<td>Medium skilled (nurses)</td>
<td>+</td>
<td>+</td>
</tr>
<tr>
<td>Information and communication</td>
<td>Skilled</td>
<td>+++</td>
<td>++</td>
</tr>
<tr>
<td>Professional and support services</td>
<td>Skilled</td>
<td>+++</td>
<td>+</td>
</tr>
<tr>
<td>Public administration</td>
<td>Low and medium skilled</td>
<td>-</td>
<td>++</td>
</tr>
<tr>
<td>Real estate</td>
<td>Medium skilled</td>
<td>-</td>
<td>+++</td>
</tr>
<tr>
<td>Transport and storage</td>
<td>Medium skilled</td>
<td>++</td>
<td>+++</td>
</tr>
<tr>
<td>Wholesale and retail</td>
<td>Low and medium skilled</td>
<td>+</td>
<td>+++</td>
</tr>
</tbody>
</table>
Use five case studies to identify ways in which different services sectors contribute to ET

- Financial services (Kenya and Nigeria), hydropower transmission services (Lesotho and Nepal), ICT (India, Mauritius and Senegal), tourism (Mauritius and Tanzania), air transport services (Ethiopia and Kenya)

Some are more useful as employment creators and there is heterogeneity in labour and skill intensities

- Financial, ICT and hydropower transmission services employ mostly skilled workers; tourism is less skill- and more labour-intensive

Some are important revenue and foreign exchange earners (e.g. hydropower, tourism, ICT), others have more prominent linkages with the rest of the economy (e.g. tourism), and some are key for supporting productivity/trade in other sectors (e.g. ICT, financial services)

Developing these services sectors can have positive effects on ET in developing countries
EXPLAINING SUCCESS IN TRADE IN SERVICES SECTORS

- Presence of certain **basic structural factors** is key to success in some services sectors (e.g. natural resources for hydropower or tourism; geographical location for air transport services)

- Quality of infrastructure and skills influence **domestic productive capabilities** and can generate significant differences in the performance of services exports (e.g. hydropower infrastructure in Lesotho vs. Nepal; ICT infrastructure in India or Mauritius vs. Senegal)

- **An appropriate domestic regulatory framework** is important to promote competition and improve efficiency, especially in utility services (e.g. financial, energy or transport services with oligopolistic producers). Liberalisation can help to improve competitiveness (e.g. telecommunications in Mauritius and Senegal)

- **Trade policy** has been a key driver of success in all five sectors
  - e.g. regional integration boosting Kenya’s financial services exports; bilateral agreements with neighbouring countries for hydropower exports; mode 1 and mode 4 access for ICT exports

- **Iterative, adaptive and flexible approaches** have been successful in setting up mechanisms to coordinate investment in certain services sectors (e.g. hydropower in Nepal)
• Services have been a major driver of productivity growth in the last 20 years
• The combination of trade and services is particularly powerful in boosting firm productivity in LICs
  – Services exporters firms present higher productivity
  – Among exporters, services firms present higher productivity in LICs
• The potential for ET and trade in services is particularly strong when seen under the light of trade in value added.
  – Services contribute to the productivity growth of the whole economy.
• Services provide jobs opportunities across all skilled levels, through both direct and indirect channels
• Case studies suggest that the success of trade in services is explained by
  – The presence of basic structural factors
  – The existence of domestic productive capabilities
  – An appropriate domestic regulatory framework
  – Trade policy, particularly through regional trade agreements
The Supporting Economic Transformation (SET) is an ODI programme funded by UK DFID to support countries in their quest for economic transformation through data and policy analysis and convening. The views expressed are those of the researchers and do not necessarily represent the views of ODI or DFID.

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