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Determinants of Competitiveness and Factors affecting Productivity in Services

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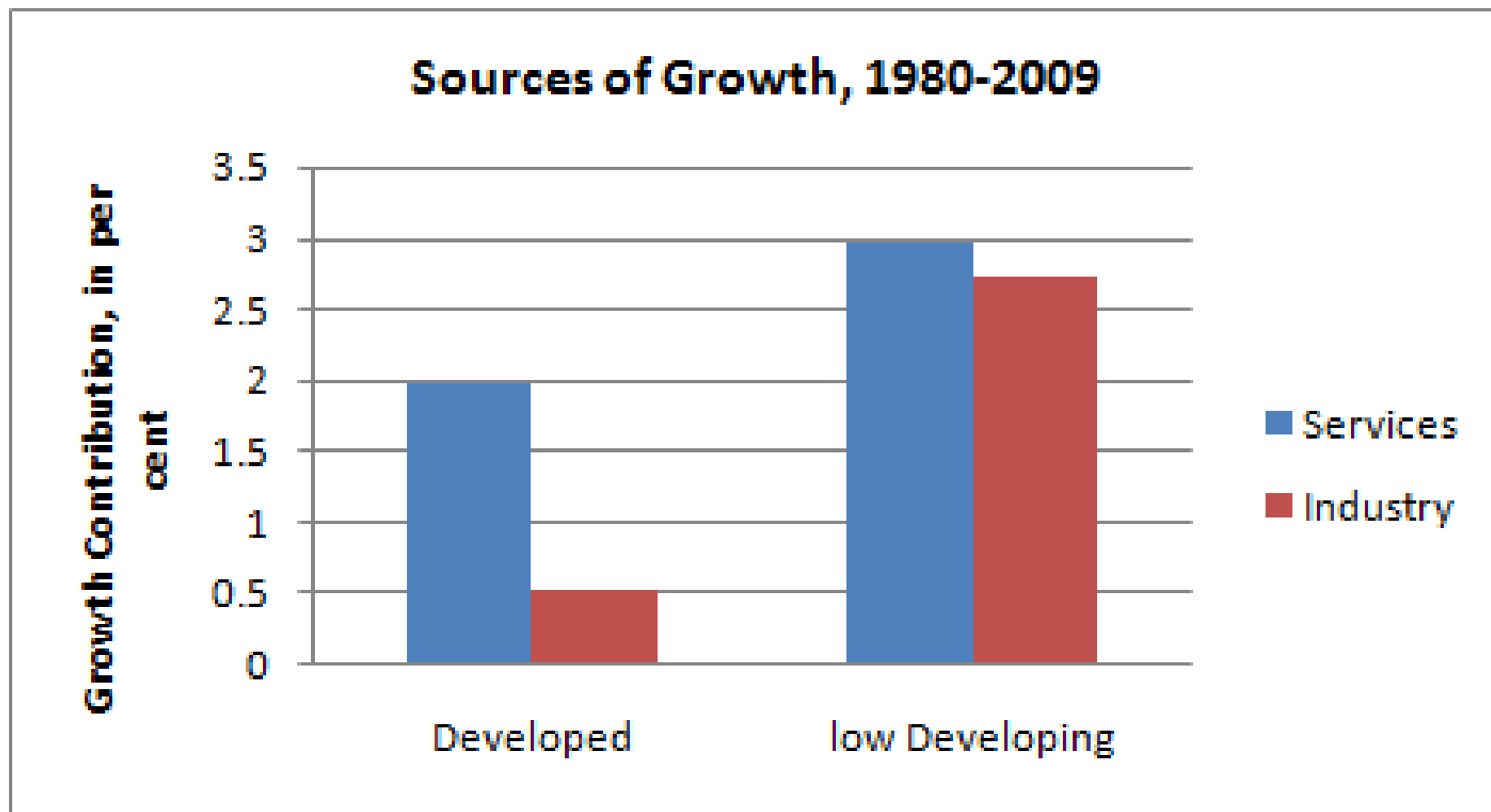


Services Trade – New Approaches for the 21st Century
PECC-ADB Conference; Chinese University of Hong Kong
Thurs 2 June 2011

Outline of Talk

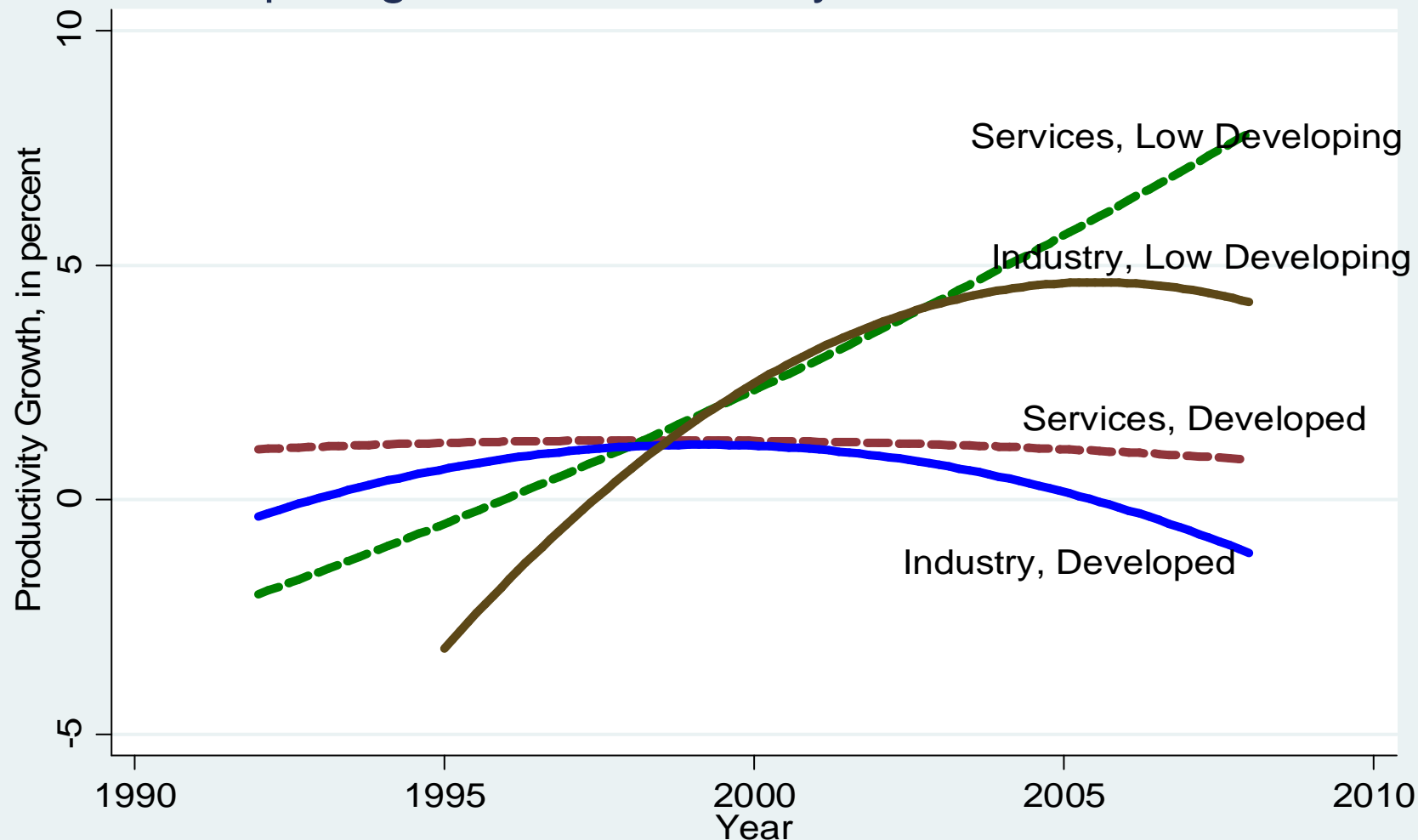
- Evidence of the importance of services
 - not just export of services that is important
- Factors underlying growth in services productivity
- Potential to “leapfrog”
- Policy toolkit
 - Institutions and regulation
 - International business engagement (trade and investment)
 - Innovation
 - education
- Sectors of importance
 - Financial and legal services
 - Information and communications technology

Sources of growth in rich and poor countries



Ejaz Ghani Arti Grover Homi Kharas 2011, *Service with a smile: A new growth engine for poor countries*, 4 May 2011 VoxEU.org

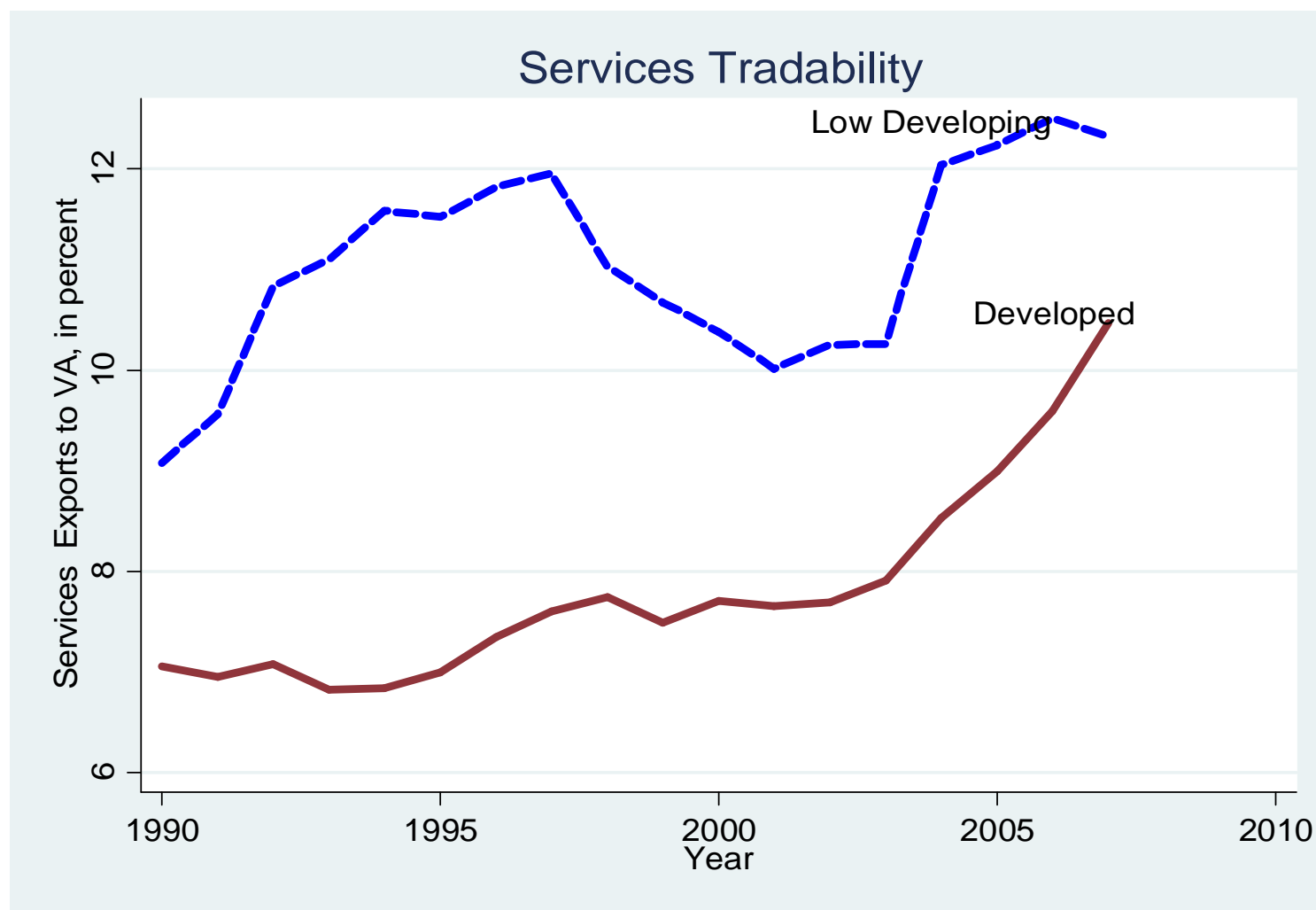
Comparing Labor Productivity Growth across sectors



Ejaz Ghani Arti Grover Homi Kharas 2011, *Service with a smile: A new growth engine for poor countries*, 4 May 2011 VoxEU.org Source Authors' calculation based on World Development Indicators.

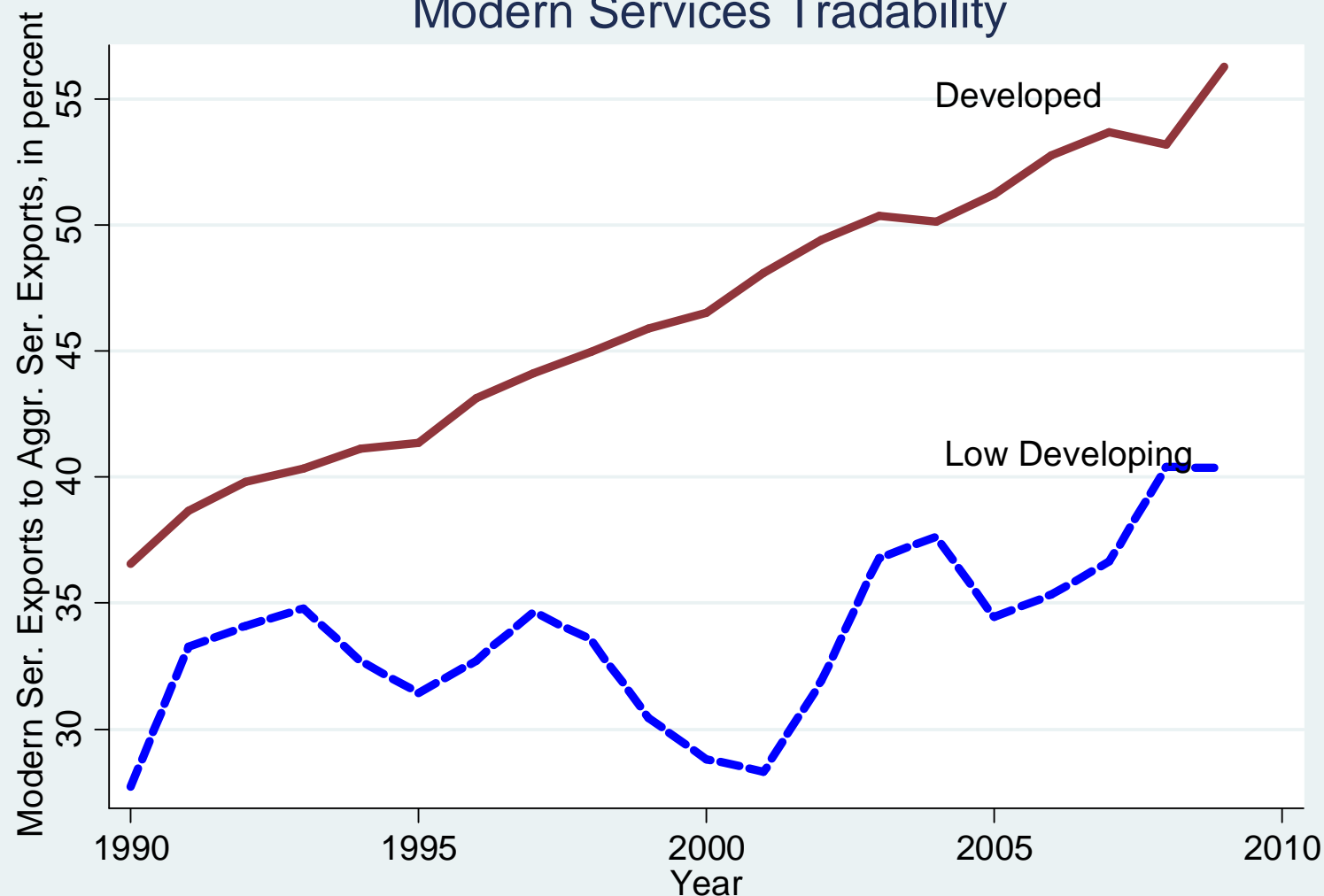
Note: Labour productivity is calculated as the sector value added per employee. Line shown is the best-fit quadratic function.

Tradability of services is higher for poor countries



Ejaz Ghani Arti Grover Homi Kharas 2011, *Service with a smile: A new growth engine for poor countries*, 4 May 2011 VoxEU.org

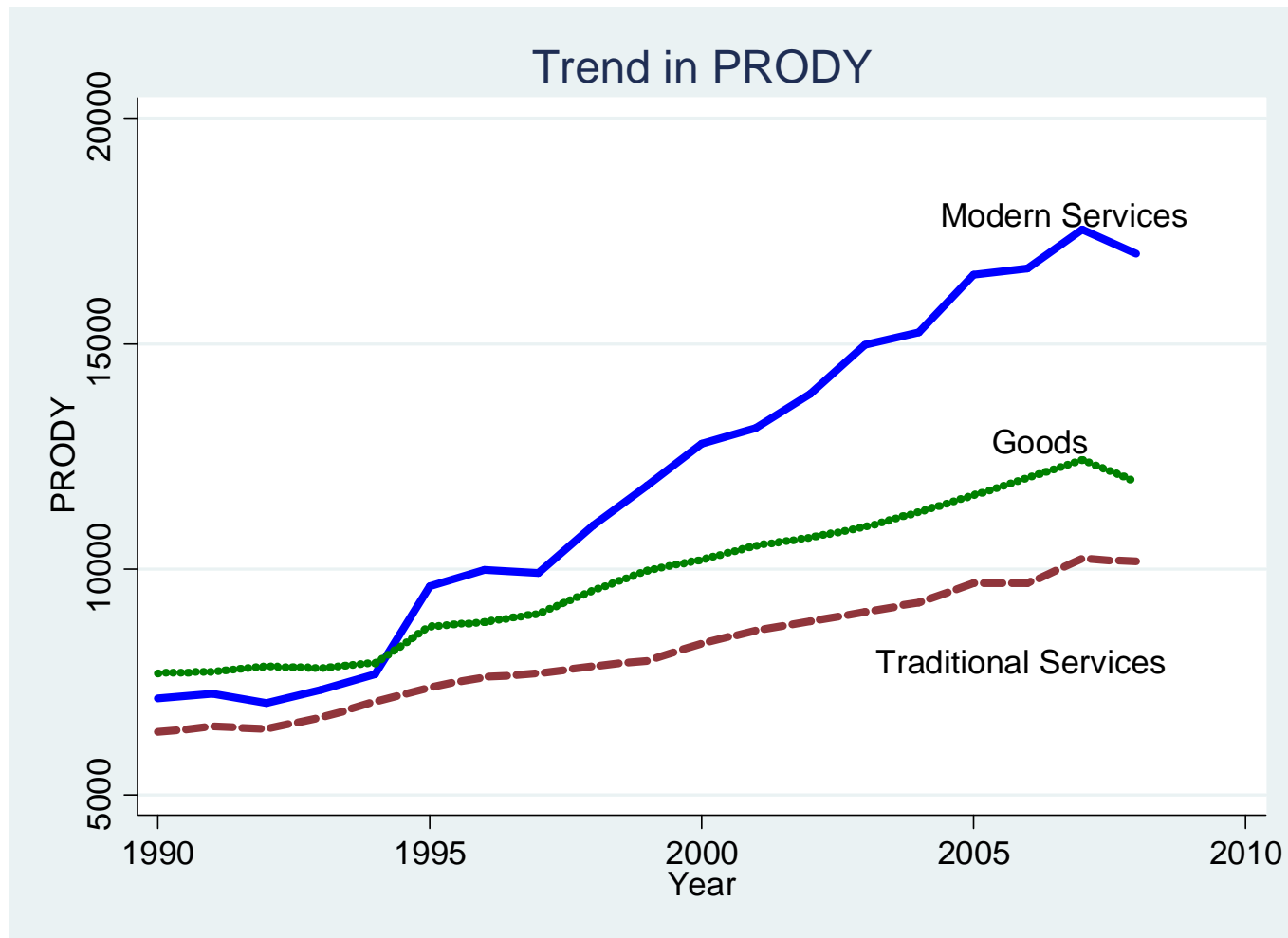
Modern Services Tradability



Modern services
defined as ICT
intensive services

Ejaz Ghani Arti Grover Homi Kharas 2011, *Service with a smile: A new growth engine for poor countries*, 4 May 2011 VoxEU.org

Modern services increasingly more sophisticated than goods and traditional services



Ejaz Ghani Arti Grover Homi Kharas 2011, *Service with a smile: A new growth engine for poor countries*, 4 May 2011 VoxEU.org

Factors underlying growth in services productivity

- ICT
- Specialisation, outsourcing, privatisation, disintermediation, supply chain, interoperability, performance based standards, deregulation
 - Post-Chandlerian firm
 - Move of services into the market economy
 - Growth of financial services
- Innovation
 - Increased application of economy of scale and customisation processes
 - Self service/ better understanding the client interface
 - Application of research, including social science, humanities and arts as well as science and technology
- Knowledge-intensity
 - Increased value of knowledge
 - Increased share of workforce in professional and managerial occupations

How do services firms engage internationally?

- Cross-border supply of services; eg digital services capable of being delivered via the internet
- Cross-border movement of services provider or services client
- Commercial presence/Investment in the target market
- Most services firms, in all services sectors, increasingly use a flexible combination of all these ways of engaging
- Growth of cross-border digital intra- and inter- firm trade has enabled development of services supply chains, and national centers of expertise

Can poor countries catch up or even “leapfrog” in services

- Once it was believed that you could not leapfrog in manufacturing
 - Only when the factors underlying manufacturing competitiveness became well understood did it become possible
- It is more complex in services
 - Although services exports are growing, most services are domestic and therefore the biggest economic gains lie in raising the productivity of the domestic services sector
 - Services sector is ‘too big’ to subsidise
 - A modern legal, financial and ICT systems are needed as the foundation of a modern services economy
 - Is dependent on professional and other high level skills, although these by themselves are not sufficient.

References

Services - the new Manufacturing, ASR blog, Andrew McCredie, 28 April 2011

Can poor countries leapfrog manufacturing and grow rich on services? May 19th 2011, The Economist

Policy toolkit

- Institutions and regulation
- International business engagement (trade and investment)
- Innovation
- Education

Institutions and regulation

- Specialisation, outsourcing, privatisation, disintermediation, supply chain, interoperability, performance based standards, deregulation
 - Post-Chandlerian firm
 - Move of services into the market economy
 - Growth of financial services
- A major source of services productivity has been through increased engagement by business in the delivery of services, including 'essential services' formerly delivered by government
- Information asymmetries are feature of many services markets, but we are understanding better how to regulate these markets so they work efficiently
- Competition policy and interoperability

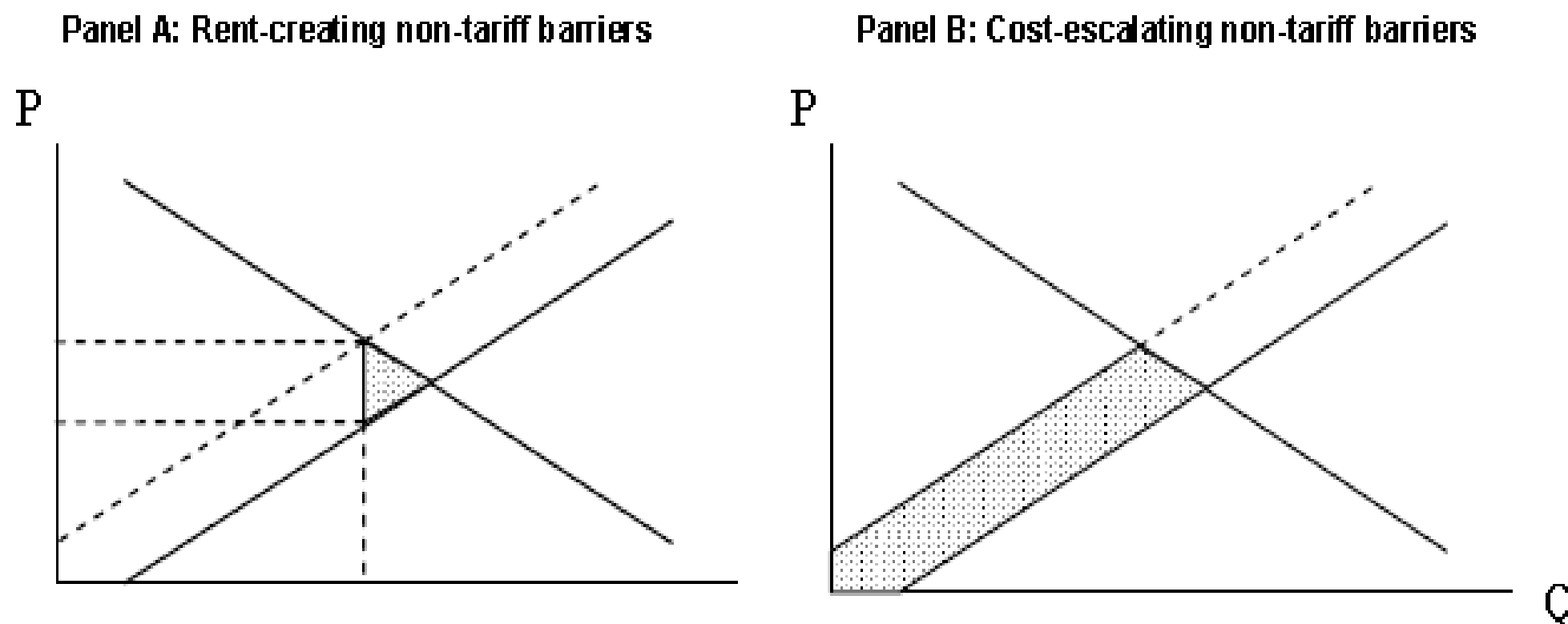
International business engagement

- There are strong spillovers from foreign investment into the domestic service economy
 - Economic literature on investment is focused on manufacturing and export related investment
- There are concerns in developed and developing countries that services trade liberalisation leads to job losses
 - The evidence is that the dominant effect is a rise in productivity
 - This economic impact is much like technological change
- Most services jobs are domestic – and cannot be ‘taken by foreigners’
 - Domestic productivity however can be substantially raised through international engagement, through adoption of new business models, technologies and absorbing new skills.
- Australian legal services, liberalised in 1986 and Malaysian retail liberalised in 1990s.

Services Trade Barriers are mainly cost-escalating

From *New Economic Challenge: responding to the rise of services in the Australian economy* ASR 2010

Figure 21 **Differential economic impact of reducing trade barriers**

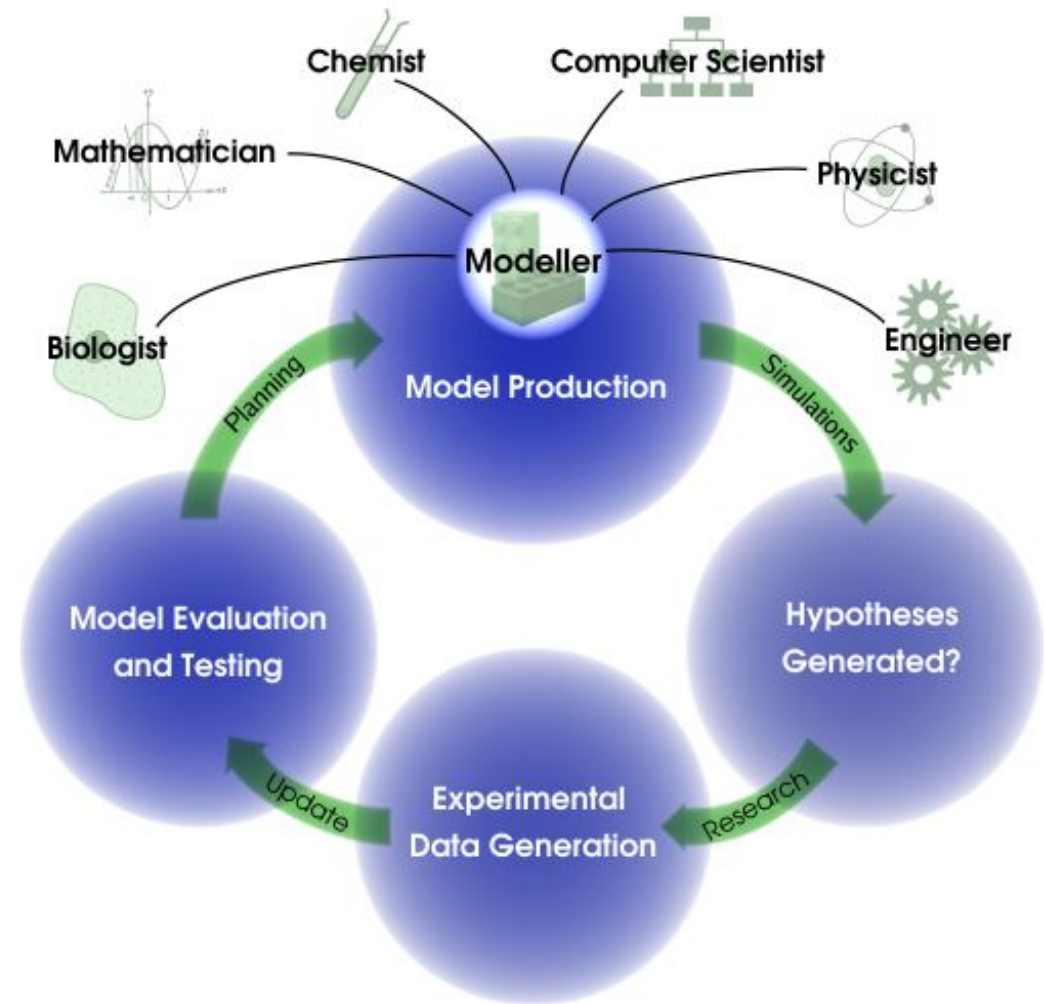


Service Innovation

- Has been under-estimated and under-valued, in many instances can respond to similar approach as applied in traditional sectors
 - Increased application of economy of scale and customisation processes
 - Self service/ better understanding the client interface
 - Application of research, including social science, humanities and arts as well as science and technology
- Application of markets and marketing techniques to traditional services
 - Immunisation of children in rural Rajasthan, abysmal immunisation rates reversed by a small bag of lentils given as a sort of “reward”. This was opposed by public health officials, who thought “bribing” people was a bad way to go. *Poor Economics*, Abhijit Banerjee and Esther Duflo 2011
- Development of Service Science

Services Innovation underpinned by Science

- Service Science - an emerging discipline that integrates:
 - Computer science
 - Engineering and design
 - New business strategies
 - Operational research
 - Social science and law
- Significant potential to enhance services innovation by adopting a multi-disciplinary approach



SRII Focus on Services

Service Verticals

- Health care
- Financial
- Energy
- Education
- Government
- Telecom
- Transportation
- Retail
- Etc....

See www.thesrii.org

Service Horizontals

- Technology
(Architecture/Platform,
Hardware, Software,
Infrastructure)
- Service Business--
Process/Tools/Models..
- Service Operation
management
- Service
Management/Leadership
- Service Marketing
- Human Factor Engineering/
Skill sets

Conclusions

- The services sector has long been neglected as a source of productivity and economic growth
- In both developed and developing countries the services sector is now the dominant source of economic growth
- At a conceptual level services productivity growth and the factors underlying it have been slow to develop, but are now reasonably well understood.
- A toolkit of policies to rapidly improve developing countries' services productivity has been described.