



The Role of the Service Sector in the Indian Economy

Baliram Dadarao Undre

Department of Economics

New Arts, Commerce and Science College, A'Nagar (Autonomous)

Corresponding Author – Baliram Dadarao Undre

DOI - 10.5281/zenodo.18922887

Abstract:

The service sector has transitioned from being a supportive industry to the primary engine of India's economic growth, contributing approximately 55%–60% of the Gross Value Added (GVA). This paper examines the sector's evolution into a "high-growth, low-volatility anchor" for the nation. It explores the "servicification" of manufacturing, the impact of Artificial Intelligence (AI) on employment, and the sector's resilience amidst global geopolitical shifts. Through a multi-point analysis, the study evaluates growth drivers, structural challenges, and strategic recommendations to achieve the target of \$1 trillion in service exports by 2030.

Keywords: *Service Sector, Indian Economy 2026, GDP Contribution, Servicification, IT-BPM, AI Integration, Service Exports, GVA, Economic Survey 2025-26, Digital Transformation.*

Introduction:

Historically, economies moved from agriculture to manufacturing before reaching the service stage. India, however, bypassed the traditional industrial-led growth model, leaping directly into a services-led revolution. In 2026, the service sector remains the steadiest contributor to the Indian economy, propping up GDP growth even when global merchandise trade fluctuates. From IT-BPM and financial services to the emerging "Orange Economy" (creative industries) and space-tech services, the sector is the backbone of India's aspiration to become a "Viksit Bharat" (Developed India) by 2047.

Objectives:

1. To analyze the quantitative and qualitative contribution of the service sector to India's GDP and GVA in 2026.
2. To identify the key sub-sectors driving modern economic growth.

3. To evaluate the challenges posed by technological disruptions and global policy shifts sector's rapid digitalization
4. To evaluate the GDP and Employment Share in Service Sector
5. To provide actionable policy recommendations for sustainable services-led development.

Research Methodology:

This paper utilizes a descriptive and analytical research design. It relies on secondary data sourced from the Economic Survey 2025-26, Ministry of Statistics and Programme Implementation (MoSPI), NITI Aayog reports, and the Union Budget 2026. Data interpretation involves trend analysis of GVA growth, Foreign Direct Investment (FDI) inflows, and employment elasticity within the tertiary sector.

Role of Service Sector in Indian Economy:

1. **Dominant GDP Contributor:** The sector contributes over 55.3% to India's total **GVA**, maintaining an average growth rate of 9.1% in FY26.
2. **Employment Engine:** It now accounts for nearly 30% of total employment, having added approximately 40 million jobs between 2018 and 2024.
3. **Export Powerhouse:** India is the 7th largest services exporter globally. Services exports have grown at a CAGR of 14% post-pandemic, providing a critical buffer for the trade deficit.
4. **Magnet for FDI:** The service sector remains the largest recipient of FDI, accounting for over 80% of total inflows in recent years, particularly in IT, professional services, and finance.
5. **Servicification of Manufacturing:** Services like ICT, logistics, and data analytics now account for 17%–25% of the value-added in manufacturing exports, enhancing industrial competitiveness.
6. **Global Capability Centres (GCCs):** Over 1,600 GCCs in India employ 1.6 million+ professionals, transforming India into a global hub for high-end R&D and engineering.
7. **Financial Stability:** The banking and insurance sub-sectors have seen a surge in digital adoption, with India leading globally with an 87% fintech adoption rate.
8. **Resilience to Volatility:** Unlike the cyclical nature of agriculture and industry, the service sector acts as a "low-volatility anchor," providing stable growth even during global downturns.
9. **Social Infrastructure:** Growth in healthcare (telemedicine) and EdTech has democratized access to essential services across rural India.

10. **Digital Economy Multiplier:** The digital economy is projected to contribute nearly 20% of national income by 2029-30, fuelled by the service sector's rapid digitalization

GDP and Employment Share in Service Sector:

In 2023–24, the service sector continued to be the driving force of the Indian economy, contributing 54.4% to the country's Gross Domestic Product (GDP). This substantial share not only highlights the sector's dominance but also underscores its central role in shaping India's growth trajectory. Over the period from 2014–15 to 2023–24, the service sector recorded an impressive average annual growth rate of 6.3%, showcasing steady and sustained expansion. In the fiscal year 2023–24 alone, the sector witnessed a robust growth of 9.0%, reflecting strong performance in key sub-sectors such as information technology, telecommunications, finance, real estate, transport, and professional services. This remarkable surge also illustrates the sector's resilience and adaptability, particularly in the post-pandemic recovery phase and amid global economic uncertainties. The sector not only leads in output but is also a major source of employment, accounting for 29.7% of the workforce in 2023-24, according to the Periodic Labour Force Survey (PLFS).

In comparison, the agriculture sector, while still vital to rural livelihoods and food security, contributed a relatively smaller 17.8% to India's GDP in 2023–24. The sector maintained a moderate average annual growth rate of 4.4% between 2014–15 and 2023–24. However, its performance has been more volatile, influenced by monsoons, input costs, and policy changes. For instance, it expanded by a healthy 6.3% in 2022–23, but this momentum slowed significantly to just 2.7% in 2023–24.

This sector is affected due to erratic rainfall patterns, rising input costs, and structural constraints such as limited irrigation and fragmented land holdings. Despite challenges, agriculture continues to play a critical socio-economic role, especially as it provides employment to 46.1% of the workforce in 2023-24 according to PLFS.

The industrial sector contributed 27.8% to GDP in 2023–24, making it the second-largest contributor after services. Between 2014–15 and 2023–24, the sector achieved an average annual growth rate of 5.7%, reflecting a moderate but steady expansion in manufacturing, mining, electricity, utilities, and construction. The sector has shown signs of recovery following the disruptions caused by the COVID-19 pandemic, with growing emphasis on Make in India, production-linked incentive (PLI) schemes, and investment in infrastructure. However, challenges such as global supply chain disruptions, high energy costs, and labour market inefficiencies continue to impact its pace of growth. The sector employs 24.2% of the workforce in 2023-24 according to PLFS data.

Employment Share in Service Sector:

Over the past four decades, employment in India's service sector has grown steadily, reflecting the country's broader economic transformation. According to RBI's KLEMS data, the share of total employment in service sector rose from around 15% in 1981–82 to over 30% by 2022–23. Business services saw a dramatic rise from just over 1.0% to more than 9.0%, reflecting increased demand for professional and technical roles. Trade consistently dominates, maintaining a share above 33%. Financial Services also grew steadily, rising from 1.8% to over 3.3%. Conversely, public administration dropped significantly, from 16.2% to just 4.6%, indicating shrinking government employment. Education

and health sectors show modest but stable growth. Overall, the data highlights a gradual transformation toward private and skill-based service sectors over four decades. The trend highlights a clear shift in India's employment landscape toward a more service-oriented economy, emphasizing the need for continued investment in skills development and service infrastructure.

Opportunities Ahead:

While India's service sector has seen remarkable growth and diversification over the past few decades, it is not without its challenges especially in the face of a rapidly changing global landscape. One significant area that remains underutilized is tourism. Despite India's rich cultural heritage, diverse geography, and historical sites, the sector has yet to reach its full potential due to issues like inadequate infrastructure, limited international marketing, and bureaucratic hurdles. In 2023, India recorded 18.9 million international tourist arrivals, which is just 1.4% of the global tourist arrival of approximately 1,300 million. By enhancing connectivity, simplifying visa processes, improving cleanliness and safety, and investing in quality tourist facilities, India can transform tourism into a robust driver of both employment and foreign exchange earnings.

Another pressing challenge is the impact of emerging technologies, particularly artificial intelligence (AI), on the structure of service jobs. As AI continues to automate routine and repetitive tasks, sectors like call centres and business process outsourcing (BPO), once major employment engines, are at risk of shrinking.

This evolution demands a proactive shift in strategy. India must prioritize reskilling and upskilling its workforce to prepare for a future where success will hinge on advanced digital capabilities. Areas such as cybersecurity, data

science, cloud computing, blockchain, and AI development offer high-growth opportunities that require more specialized and innovative skill sets. If India is to maintain its global leadership in IT and digital services exports, it must invest heavily in education, continuous learning, and research to stay ahead in a technology-driven world. Government initiatives like the IndiaAI Mission, with an allocation of ₹10,300 crore over the next five years, aim to strengthen nation's AI capabilities and enhance India's competitiveness on the global stage.

Furthermore, the service sector is uniquely positioned to address one of India's most urgent challenges that is creating jobs for its large and growing population. With more than 65% of its population is under the age of 35, the demand for quality employment is immense. Services such as healthcare, education, logistics, fintech, and e-commerce are labour-intensive and can absorb a significant portion of the workforce if properly nurtured. The rise of digital platforms and gig-based employment models also presents new ways to generate income, particularly in semi-urban and rural areas.

Challenges of Service Sector:

1. **The AI Skill Gap:** Rapid AI integration threatens routine BPO jobs; there is a critical shortage of workers skilled in advanced data science and machine learning.
2. **Infrastructure Bottlenecks:** High-growth services like data centers face challenges in power reliability and high land costs.
3. **Global Protectionism:** Tightening immigration norms (H-1B visas) and data localization rules in the West hamper the ease of doing business for Indian firms.
4. **Missing Middle in Manufacturing Linkages:** While "servicification" is rising, the lack of a robust domestic manufacturing

base limits the full potential of industrial-service synergy.

5. **Underperforming Sub-sectors:** While IT thrives, sub-sectors like postal, courier, and insurance services require urgent modernization.
6. **Regulatory Hurdles:** Complex compliance for startups and MSMEs in the service space remains a deterrent to scaling.
7. **Urban-Rural Divide:** Most high-value services are concentrated in Tier-1 cities (Bengaluru attracts 55% of tech investment), leading to regional imbalances.
8. **Data Privacy Concerns:** With the Digital Personal Data Protection (DPDP) Act in play, firms face high compliance costs to ensure data security.
9. **Informalization of Gig Work:** A large portion of service employment is in the gig economy, lacking social security and stable pay.
10. **High Logistics Costs:** Despite the National Logistics Policy, logistics costs in India remain higher than the global average of 8%, affecting trade services.

Conclusion:

1. **Primary Anchor:** The service sector has solidified its status as the primary driver of the Indian economy in 2026.
2. **Shift to High-Value:** India is successfully moving from low-cost outsourcing to high-value "Knowledge Process Outsourcing" (KPO) and R&D.
3. **Macroeconomic Buffer:** Robust services exports (surplus of ~\$118B in FY26) are vital for managing the Current Account Deficit.
4. **Technological Vanguard:** The sector is the lead adopter of AI, blockchain, and 5G, setting the pace for the rest of the economy.

5. **Employment Elasticity:** Job creation is increasingly responding to output growth, with an improved elasticity of **0.63** post-pandemic.
 6. **Policy Centricity:** The 2026 Budget explicitly places services at the heart of the "Viksit Bharat" strategy.
 7. **Global Competitiveness:** With a **4.3% global share**, India is closing the gap with major exporters like China and France.
 8. **Urbanization Driver:** Service sector growth is the main catalyst for the "New India" urbanization and real estate boom.
 9. **Digital Inclusivity:** The "India Stack" (UPI, ONDC) has enabled even small service providers to enter the formal economy.
 10. **Future Outlook:** The sector is on track to contribute to a **\$5 trillion economy**, provided skill gaps and regulatory hurdles are addressed.
5. **Simplified Compliance:** Implement the "Single Category" IT services classification (as per Budget 2026) to reduce tax litigation.
 6. **Strengthening Gig Worker Laws:** Introduce a comprehensive social security framework for the millions of delivery and platform workers.
 7. **FDI in Underperforming Areas:** Actively court FDI in logistics, warehousing, and green energy services.
 8. **Promotion of the "Orange Economy":** Support the creative arts and live entertainment through specialized visas and event-based tax breaks.
 9. **Data Center Incentives:** Offer a "Data Centre Tax Holiday" until 2047 to attract global hyperscalers to India.
 10. **Export Diversification:** Move beyond the US and UK markets to tap into Southeast Asian and African markets for service exports.

Recommendations:

1. **Aggressive Re-skilling:** Launch a "National AI Mission for Services" to train 5 million professionals in generative AI and cloud computing.
2. **Tier-2/3 City Focus:** Provide tax incentives for IT and financial firms to set up operations in smaller cities to decentralize growth.
3. **Service-Manufacturing Linkage:** Incentivize the "Service-as-a-Product" model where manufacturers bundle high-end software with hardware.
4. **Regulatory Sandbox Expansion:** Expand the RBI's regulatory sandbox to include health-tech and legal-tech to foster innovation.

References:

1. Ministry of Finance. (2026). *Economic Survey 2025-26*. Government of India.
2. NITI Aayog. (2025). *India's Services Sector: Insights from Employment Trends*.
3. Reserve Bank of India (RBI). (2025). *Handbook of Statistics on Indian Economy*.
4. IBEF. (2026). *Service Sector Contribution to India's GDP - Research Report*.
5. World Trade Organization (WTO). (2024). *World Trade Report: The Future of Services Trade*.
6. Press Information Bureau (PIB). (2026). *Union Budget 2026-27: Key Highlights*