

# Services in the UK economy

*This article<sup>(1)</sup> looks at some of the main factors which are likely to have influenced the share of services in total UK economic activity and employment and examines recent trends in the United Kingdom's exports and imports of services and their contribution to the balance of payments. Among the main points:*

- *Services have steadily increased their share of employment and GDP in current prices since the 1950s. The volume of services output, however, grew no faster than the rest of GDP up to the early 1970s, but its share in real output has risen since then.*
- *The surplus on UK trade in services increased from the early 1960s to the early 1980s. Financial and 'other' services made a significant contribution to this growth, as did the combined travel and civil aviation surplus, at least until 1977.*
- *Subsequently, the surplus declined, largely reflecting a deteriorating performance in travel and sea transport, and still remains below its 1981 peak. Net exports of financial and 'other' services, particularly banking, have, however, continued to grow strongly.*

## What are services?

A service can be defined as 'the change in the condition of a person, or of a good belonging to an economic unit, brought about by the activity of another economic unit with the former's consent'.<sup>(2)</sup> Services affecting persons may change either their physical or mental condition. Examples of the former would be passenger transport and medical services, and of the latter, education and entertainment. Services affecting goods would include repair, cleaning and freight transport. Certain activities, such as financial services, can affect the condition of either goods or persons.

In the case of many services provided by government (defence, public administration, law and order, fire services etc), direct measurement of the change in the condition of persons or of goods brought about by the provision of these services is difficult, because they are, in a sense, preventive by nature and cannot be identified by individual acts of consumption. In principle, the volume of output of such services is represented by the difference between the condition of persons or of goods as actually observed, and what this condition would have been in the absence of the provision of the services. In practice the output of these types of activity is measured from the quantities of, and payments to, the factor inputs used in their production.

It is a characteristic of services that they are purchased as they are produced: by definition the change in the condition of the person or good must happen at the time of production. In contrast, goods are usually stocked (even if only for a short period) in the sense that the transfer of goods between one economic unit and another takes place after production has been completed. This is not to say that the benefits derived from the purchase of goods and services—which must be distinguished from the goods and services themselves—are enjoyed at the time of purchase. Just as the benefits derived from food, clothing, or the purchase of a vacuum cleaner may extend well beyond the time of purchase, so will those from car repairs, house painting, dental treatment, or education.

For practical purposes, in what follows services are taken to be the activities which are so classified in the national accounts. In many respects, this is a rough and ready division. This should be particularly borne in mind in interpreting the statistical tables that appear in the text.

## The changing demand for services in the United Kingdom

Services can be categorised in a number of ways but for analysing the factors affecting the demand for services the following functional classification<sup>(3)</sup> may be the most appropriate:

(1) Primarily the work of T S T Key of the Bank's Economics Division.

(2) T P Hill 'On goods and services', *Review of Income and Wealth*, Series 23, No 4, December 1977. Some activities undertaken by economic units may well bring about unsolicited changes (welcome or unwelcome) in the condition of persons, or of goods owned by other economic units. Hill suggests that conceptually such 'externalities' ought to be included in the measured output of services, a portion of which would clearly contribute negatively to the total.

(3) Suggested by J Singlemann, in 'The sectoral transformation of the labour force in seven industrial countries 1920-1970', *American Journal of Sociology*, Vol 83, Number 5, 1978.

- Consumer services (which include the restaurant and hotel industries, household services and private transport): demand may be governed by price and personal income.
- Social services (which include health care and education): these services are often provided free or subsidised by the state and individual demand is therefore less constrained by price and personal income.
- Producer or intermediate services (which include consultancy, contracting and banking): used largely in the production of final goods and services; demand is governed by output or investment decisions of enterprises.
- Distributive services: these contribute to both intermediate and final demand and include freight transport and wholesale and retail trades.

### Consumer services

The distribution of consumers' expenditure in the United Kingdom between goods and services in 1983, and the growth in volume terms of the main components over the previous decade, are shown in Table A.

Excluding household expenditure on visits abroad (which has expanded faster than any domestic component of consumer spending), consumers' expenditure on services in volume terms has risen at a similar rate to spending on

**Table A**  
**UK consumers' expenditure<sup>(a)</sup>**

Percentages		
	1983 value share	Average annual real growth 1973-83
<b>Wants satisfied by goods</b>		
Food	14.8	—
Alcoholic drink	7.3	—
Tobacco	3.4	-2.3
Clothing and footwear	6.6	3.3
Fuel and power	5.1	—
<b>Wants satisfied by goods and services</b>		
Housing		<b>1.6</b>
Goods	1.2	3.6
Services	13.7	1.4
Household goods and services		<b>0.4</b>
Goods	5.8	0.9
Services	1.0	-2.4
Transport and communication		<b>2.3</b>
Goods	8.7	2.6
Services	8.5	2.0
Recreation and education		<b>2.5</b>
Goods	5.1	3.0
Services	3.9	1.8
Other expenditure in UK		<b>0.8</b>
Goods	2.9	—
Catering services	5.4	-0.4
Other services	4.4	3.1
<b>Total: domestic expenditure</b>		<b>1.3</b>
Goods	61.0	1.3
Services	36.9	1.4
Household expenditure overseas <sup>(b)</sup>	2.1	7.7

Source: United Kingdom National Accounts CSO 1984.

(a) Includes expenditure by foreign visitors but excludes expenditure by non-profit making bodies.

(b) Includes both goods and services.

goods. The most rapidly growing component—clothing and footwear—represents, of course, a demand for output of goods, and within the second fastest growing group—recreation and education (often thought to be supplied mainly by service industries)—growth is again dominated by goods (especially television sets, photographic equipment and other electronic goods), while expenditure on the services component has actually fallen in real terms since 1979. Demand for services has expanded most rapidly within the residual group 'other goods and services' including expenditure on insurance and other financial services. In contrast, the volume of spending on services within the household category (including laundry, dry cleaning and domestic services) has fallen, a trend shared by expenditure on hairdressing and beauty care.

**Table B**  
**The share of services in consumers' expenditure<sup>(a)</sup>**

Percentages		
	Volume (b)	Value
1953	27.2	21.5
1963	25.1	22.3
1973	24.6	23.7
1983	25.3	26.0

(a) Excluding housing services.

(b) Based on expenditure in 1980 prices. Strictly speaking it is not possible to derive a consistent measure of volume share for the whole period shown. The method of constructing constant price data in the national accounts has the result that, for years prior to 1978, the sum of the published components of consumers' expenditure differs slightly from the total. In the table, figures for 1953-73 are based on a total equal to the sum of the broad components of consumer spending that are published.

Table B shows both the volume and value shares of services in consumer spending over a somewhat longer period. The volume share has been fairly stable while the value share has risen steadily. One explanation for this divergence could be a tendency for the prices of consumer services to rise relative to those of consumer goods. While the demand for services—which are often considered as relative luxuries—might be expected to grow faster than incomes at a given set of relative prices, the effect of a higher income elasticity may be offset by a rise in the relative price of services, inducing consumers to switch their spending towards goods.

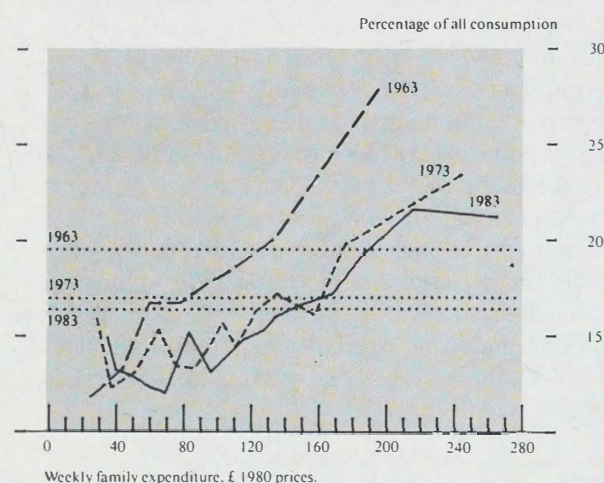
Cross sectional evidence from Family Expenditure Survey data lends some support to this argument. Chart 1 shows that at given relative prices the share of total household expenditure spent on services tends to rise as total spending increases, suggesting that the demand for services is relatively income elastic. However, the downward shift of the relationship through time—while also influenced by changes in income distribution, tastes and other factors—reflects a significant relative price effect. Between 1963 and 1973, the average volume share of expenditure on services fell sharply and there was a slight decline in the following decade. The relative price of consumer services rose by 20% between 1963 and 1973, but by only 9% in the 1973-83 period.

Another influence on the distribution of consumer spending between goods and services has been a tendency for wants previously satisfied by unmeasured services



**Chart 1**  
**Consumption of services<sup>(a)</sup>**

.... Average family expenditure in services in each year



(a) Suggested by J Gershuny and I Miles in *The New Service Economy*.

performed within households to be increasingly met by marketed goods and services as new consumer durables become available.

### Social services

The two main components of social services, public administration and defence, and education and health, accounted for 7% and 9% respectively of GDP in 1983.<sup>(1)</sup> In volume terms, measured output of the former grew fairly steadily from 1963 to 1973,<sup>(2)</sup> although not as fast as total output, and has remained fairly stable since then. Growth in the measured output of education and health services matched that of GDP overall between 1963 and 1973 but then quickened until 1980 before slowing subsequently. Most education and health services are provided by the state, with the private sector accounting for only a minor part of the total. The level of provision of social services will be determined to a large extent by demographic factors and, in the case of services provided entirely by the public sector, by political and budgetary considerations. Changes in household incomes and relative price effects, while important in determining the demand for consumer services, may, therefore, exert a lesser or indirect influence in this sector.

### Producer and distributive services

The output of this sector may satisfy either final demand or the demand for intermediate inputs. It is probable that purchases of services such as telecommunications, advertising, accountancy, consultancy etc by other sectors have risen relative to the output of those sectors in recent years.<sup>(3)</sup> Part of the increasing share of producer services in total output may, however, be attributable to the contracting out of services previously performed within firms, and is thus the result of a reclassification,

associated with a change in industrial organisation, rather than an increase in the activity itself. There has also been a rise in the number of service-type jobs in all sectors of industry as manual workers have been replaced by machinery operated by fewer, but more skilled, white collar workers. (Gershuny and Miles<sup>(4)</sup> have calculated that manual employment in all industries in the United Kingdom declined from 40% in 1968 to 31% in 1978.) Clerical jobs are being replaced in the same way.

### Contribution of services to employment

The share of services in total UK employment rose from around 43% in 1950 to nearly 60% in 1980 (Table C). In the United States the share has risen from about one half to two thirds over the same period. In both countries the fastest growing sectors, (as measured by employment trends), have been producer services. In other sectors different structural trends are apparent. The share of consumer services in employment remained fairly flat in the United Kingdom until 1970 but has since increased sharply. In contrast, in the United States the share has fallen steadily. Demographic factors may largely account for the different growth profile in the share of social services in the two countries. The share of the total labour force employed in distributive industries has remained fairly flat in the United Kingdom while falling somewhat in the United States.

### Overall contribution of services to the UK economy

Charts 2 and 3 compare the growth in the output of the services sector with that of the rest of GDP. The value

**Table C**  
**Distribution of the labour force by industrial sector in the United Kingdom and the United States**  
Percentage of total labour force

		1950	1960	1970	1980
<b>Non-service industries</b>					
Agriculture, fishing, mining and quarrying	UK	8.0	6.1	3.5	3.2
	US	14.4	8.1	4.5	4.1
Manufacturing, utilities and construction	UK	49.2	47.5	46.6	37.5
	US	33.9	35.7	33.8	29.6
<b>Service industries</b>					
Consumer	UK	8.3	8.9	8.1	11.3
	US	12.1	11.4	10.1	9.9
Social	UK	12.4	13.2	17.0	21.2
	US	12.4	16.4	21.7	24.7
Producer	UK	3.3	3.8	6.0	7.7
	US	4.8	8.1	9.1	11.3
Distributive	UK	18.8	20.0	18.8	19.1
	US	22.4	20.5	20.9	19.8
Total services	UK	42.8	45.9	49.9	59.3
	US	51.7	56.4	61.8	65.7

Sources: United Kingdom: *British Labour Statistics: Historical Abstract* (1950 and 1960) and *Statistical Year Book* (1970); for 1980 *Employment Gazette* October 1981 (figures relate to June 1980 and are for Great Britain only).

United States: Singlemann *op cit* and J Singlemann and M Tienda 'The process of occupational change in a service society: the case of the United States, 1960 to 1980' in B R Roberts, R Finnegan and O Gallie (eds) *New approaches to economic life: economic restructuring, unemployment and the social division of labour*. Manchester University Press, 1985. The figures derive from census data and refer to 'about' the dates specified.

(1) The share in GDP of the services produced by the public sector should not be confused with the share of general government (central government and local authorities) expenditure on goods and services in GDP, which amounted to about 24% in 1983. Total general government spending (including subsidies, social security and other transfer payments, lending, debt interest, non-trading capital consumption etc) was equal to (but not the equivalent of) about 46% of GDP in 1983.

(2) Output in this sector is usually proxied by employment and therefore may underestimate real growth.

(3) The input/output tables show that the value of intermediate purchases of services by the manufacturing sector rose from 13.5% of its gross output in 1954 to 18.3% in 1979. This may, however, reflect increases in the relative price of services.

(4) J Gershuny and I Miles (1983). *The New Service Economy*.



share of the services sector in GDP shows a marked upward trend similar to the employment trends noted above. However, the pattern of relative volume growth (Chart 3) suggests that real output in the services sector grew at much the same rate as total GDP until the early seventies but that since then GDP growth has slowed down, whereas the rate of growth of services output has been maintained.

What factors account for these different trends?

Measurement problems may be important. It is widely recognised that the output of some parts of the services sector is difficult to measure. Employment data are used as a proxy for output of some private sector services and of the entire public sector, including health and education. Services treated in this way necessarily show little or no productivity increase. The effect is to impart a systematic downward bias to measured services productivity and output and an upward bias to price. Calculations by Smith<sup>(1)</sup> on data covering the period

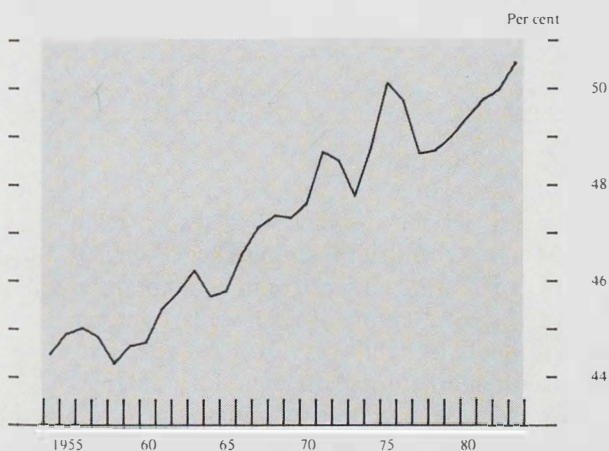
1951–66 suggest that, as a result, the annual growth rate of output in the services sector in the United Kingdom was underestimated by 7% to 11%. For purposes of illustration, the addition of, say, 10% to the annual growth rate of services output from 1950 to 1983<sup>(2)</sup> would have the effect of increasing the volume share of services in GDP in 1983 from 50.3% to 51.9%.

The rising share of employment in services, coupled with the real output trends shown in Chart 3, suggest that productivity growth has been lower in services than in other sectors, even where output is not measured by employment.

As average earnings in different sectors tend to increase at roughly similar rates (at least over the long term), relative unit labour costs and relative output prices in services have tended to rise (Chart 4) boosting the value share of services in GDP relative to volume share but tending to depress the volume of traditionally supplied services demanded in relation to other goods.

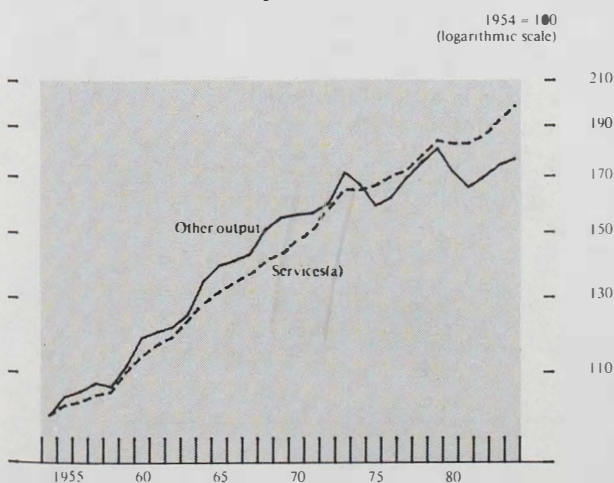
It is often suggested that productivity growth in services is relatively slow because service activity is less amenable than the production of goods to technical innovation, mechanisation and economies of scale. Mechanisation is, by definition, the application of manufactured goods to the productive process. In some cases, mechanisation simply increases the productivity of the producer of services, while in others it may result in the substitution of goods for services. Service activities which are most easily mechanised may therefore also be those which are most easily replaced by manufactures, leaving mainly those activities which are more difficult to mechanise, and therefore less amenable to improvements in productivity. Transport, domestic services and entertainment provide examples of this process: the private car has tended to replace bus and railway travel, washing machines have replaced laundries, and television has replaced the cinema.

**Chart 2**  
Share of services in GDP by value<sup>(a)</sup>



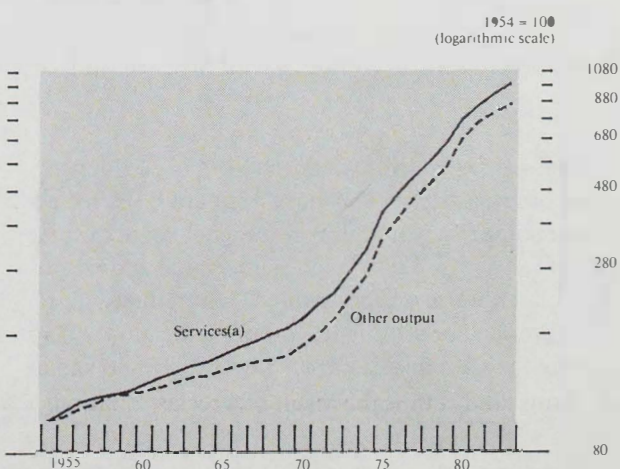
(a) Excluding ownership of dwellings.

**Chart 3**  
Growth in UK real output



(a) Excluding ownership of dwellings.

**Chart 4**  
Implied price indices



(a) Excluding ownership of dwellings.

(1) A D Smith, *The measurement and interpretation of services output changes*, National Economic Development Office, 1972.

(2) This raises the average growth rate of services between 1973 and 1983 from 2.5% to 2.75%.



Prior to about 1973, UK output of services rose at a similar rate to the average of other sectors of the economy but since then has grown faster and has been less subject to cyclical fluctuations (Chart 3). The experience in the earlier period might be taken to be indicative of a low income elasticity for services.<sup>(1)</sup> However, as in the case of consumer services, the impact of both income and price substitution effects must be taken into account. Prior to the early seventies the relative price of services was rising faster than that of other output (Chart 4) and this is likely to have been a factor dampening demand. Subsequently, the relative price of services output has changed little.<sup>(2)</sup> The diminished importance of the relative price effect from the early seventies may explain some, but by no means all, of the relatively strong performance of services. A second factor is probably the deterioration of UK performance in world trade in manufactures. This will have tended to reduce the share in total output of internationally traded activities (mainly manufactures) relative to non-traded activities (mainly services). The more recent stability of the relative price of services may be a reflection of a convergence of productivity growth in the services and manufacturing sectors: productivity growth in manufacturing fell from an average of 4.4% per annum between 1961 and 1972 to 2% per annum between 1973 and 1983.

### Comparison of overall UK experience with that of other countries

Table D shows the share of service industries in the volume and value of output<sup>(3)</sup> and in employment in six major industrial countries. Although differences in definition and base periods for the volume measure render meaningful comparisons between levels impracticable, the figures should give an acceptable impression of rates of change. In all countries the share of services in employment and GDP value has risen over time while the share in GDP volume has been flatter, implying a rising relative price of services. Most countries also show a fall in the volume share of services in GDP until the early 1970s. However, subsequently there has been some increase in all countries with the exception of Japan.

Cross-sectional expenditure data also provide evidence on the income elasticity of services. It might be expected that richer countries would devote a higher share of total spending to services. Table E shows the value and volume shares of expenditure on services in GDP in thirty-four countries grouped according to output per head in 1975. In deriving the volume shares, account has been taken of

**Table D**  
**Output shares of services in GDP and employment**

Percentages	GDP Value	GDP Volume	Employment
<b>United Kingdom</b>			
1954	44.5	47.9	42.5
1963	46.2	47.6	48.7
1973	47.8	46.9	54.3
1983	50.5	50.3	63.8
<b>United States</b>			
1953	44.5	50.4	49.5
1963	47.5	51.4	54.5
1973	51.5	51.9	61.8
1983	54.1	54.6	66.7
<b>Japan</b>			
1964	43	51.7	
1972	50	50.3	44.2
1982	53.9	48.8	52.7
<b>Germany</b>			
1964	39.6	45.2	37.4
1972	44.4	45.9	42.4
1981	50.3	49.7	48.1
<b>France</b>			
1964	47.2	51.6	
1972	49.9	49.7	52.5
1981	46.7	53.7	58.0
<b>Italy</b>			
1964	45.5	48.2	36.1
1972	49.7	48.6	42.6
1982	51.4	49.6	50.0

Sources: United Kingdom: Blue Book 1973 and 1984 and Department of Employment Gazette. Base year for GDP volume 1980, chain weights.  
United States: Survey of Current Business and Economic Report of the President 1984. Base year for GDP volume 1972.  
Rest: OECD National accounts, Volume II 1983 and 1984. Base year for GDP volume: Japan 1975, Germany 1976, France and Italy 1970.

differences in the relative price of goods and services across countries. Services are generally cheaper (relative to goods) in poorer countries than in richer countries, so the value of expenditure on services in poor countries will tend to give a biased measure of volume. To overcome this problem, goods and services can be revalued at a common set of 'international' prices and the volume of expenditure on services relative to GDP in individual countries recalculated in these terms.

On this basis, there does not seem to be a systematic relationship between value or volume share and income per head. The value share rises sharply between the poorest and second groups but then declines somewhat before rising with increasing per capita income. The

**Table E**  
**Share of services in expenditure: analysis by per capita income of countries, in 1975**

Real GDP per capita: index, US = 100	0-14.9	15-29.9	30-44.9	45-59.9	60-89.9	100
Number of countries	8	6	6	4	9	1
	Per cent					
Value share of services in GDP(E)	22.2	28.4	27.4	25.6	36.8	43.9
Volume share of services in GDP(E)	33.8	31.7	31.8	30.3	31.2	32.3

Source: I B Kravis, A Heston and R Summers, 1983, 'The share of services in economic growth' in *Global econometrics, essays in honour of L R Klein*, ed F G Adams and B G Hickman.

(1) Strictly speaking, statements about income elasticities apply to shares in expenditure. Kravis et al (In I B Kravis, A Heston and R Summers, 'The share of services in economic growth' in *Global econometrics, essays in honour of L R Klein*, ed F G Adams and B G Hickman) attempted to regress UK output of services on total GDP and relative prices but with little success.

(2) The deflator for non-services output excluding oil and gas production has risen rather more slowly than that for total non-services output because of the sharp rise in the relative price of oil and gas. Thus the price of services relative to other, non-oil output has risen somewhat faster. Non-services real output excluding oil and gas fell more sharply than total non-services activity after 1979 and subsequently recovered more slowly.

(3) The methodology of measuring services output differs little between countries, so adjustments could reasonably be made to the volume share in these countries similar to those made for the United Kingdom. The results shown are not significantly affected by the choice of years.



volume share initially tends to fall as income rises but subsequently increases. The results probably reflect the net impact of offsetting income and price substitution effects but other factors, for example differences in the relative importance of recorded and unrecorded work by households, are also likely to be important. For the three richest country groups shown, the evidence seems consistent with an income elasticity greater than unity and rising relative prices of services: while labour in richer countries tends to be more productive in all sectors, it is relatively less so in the services sector and this leads to higher relative prices of services as incomes increase.

### Internationally traded services

By their nature, many services are provided directly by the producer in close proximity to the consumer, so that the scope for international trade in services is generally more limited than for trade in goods.<sup>(1)</sup> Often the consumer must travel to the country of the producer (eg tourism) or the producer to that of the consumer (eg most retail banking). As a result, normally only a small proportion of the output of service industries is traded internationally. Moreover, internationally traded services are typically limited to the producer, distribution and consumer groups (the last being largely confined to tourism and related transportation); there is little trade in social services, except for a small element within health care and education and government spending abroad.

Where a producer moves operations to an overseas market the firm's net output becomes part of the host country's GDP. Benefits to the home country accrue as income in the form of interest, profits and dividends and service receipts such as royalties and technical fees. This article is not in general concerned with overseas investment income. However, in the area of financial services it is important to consider exports of services and investment income jointly. Part of what is recorded as the overseas investment income of the financial services sector constitutes, in principle, an export of services. For instance, although UK banks have net external liabilities in foreign currency, their overseas earnings on this business are (usually) positive. The margin between their borrowing and lending rates, which is generally sufficient to produce positive net earnings, can be regarded as an element of total receipts for banking services in addition to that explicitly recorded as fees and commissions. As a corollary, 'pure' investment income receipts of the banking sector will be lower than recorded.

At a world level, the available data on internationally traded services are rather aggregated and of doubtful accuracy. Estimates can, however, be compiled for the three main subsections of trade in services—transport, tourism and other services (Table F).

It appears that exports of services as a whole have not grown significantly faster in value terms than exports of

manufactures or other goods, although they may well have grown faster than total output of services. It is difficult to determine trends in real terms as there are no global volume figures available for exports of services. Estimates based on price indices for domestic services or

**Table F**  
**World exports of services**  
Percentages

	Percentage of total world trade in goods and services in 1983	Average annual growth rates 1968–83 in current dollar prices
<b>Goods</b>		
Manufactures	49	11
Other	33	11½
<b>Total goods</b>	<b>82</b>	<b>11½</b>
<b>Services(a)</b>		
Transport	6	10½
Travel(b)	44	11½
Other(c)	7½	14½
<b>Total services</b>	<b>18</b>	<b>11½</b>

Source: International Monetary Fund, Balance of Payments Year Book.

(a) Excluding government transactions.

(b) Including business travel and tourism.

(c) Including financial services, consultancy etc.

for exports of manufactures might be misleading. Although prices of domestic services may tend to rise faster than those of manufactures, it is not possible to be sure that the same relationship applies in international trade: internationally traded and non-traded services tend to be very different activities.

Within internationally traded services, just as in domestic economies, producer (or other) services have grown faster than consumer or distribution services. It is perhaps surprising, given UK experience, that tourism has grown no faster than other trade. However, UK experience may be atypical; the share of foreign travel in US consumer spending did not rise between 1970 and 1982.

### The United Kingdom's overall performance in traded services

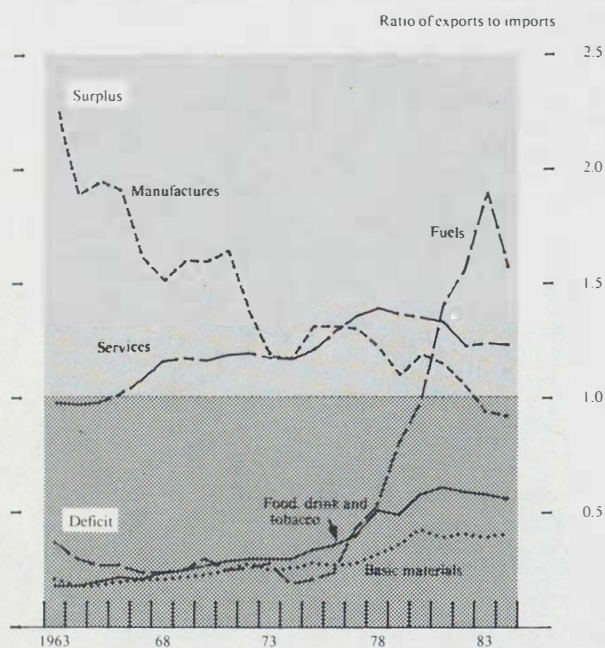
The relative values of the United Kingdom's exports and imports in the main categories of trade since 1963 are shown in Chart 5. (A value above unity indicates a trade surplus.) The surplus on services rose fairly steadily until 1981, but since then there has been some decline. The surplus in manufacturing fell more or less continuously from 1963, and in 1983 trade in manufacturing went into deficit. The performance of other sectors (particularly North Sea oil and gas) has improved.

The growth in the value of exports of services generally exceeded that of imports of services until the late seventies, although more recently imports have tended to grow faster. The aggregate figures for services, however, tend to mask different trends within the total. The contribution of financial and 'other' services to the account has built up steadily but the trends in other sectors are less clear (Chart 6). Sea transport and civil aviation have been broadly flat, although recently the balance of trade in sea

(1) In 1979, around 11% of the United Kingdom's gross output of services was exported, compared to 33% of the gross output of manufacturing.

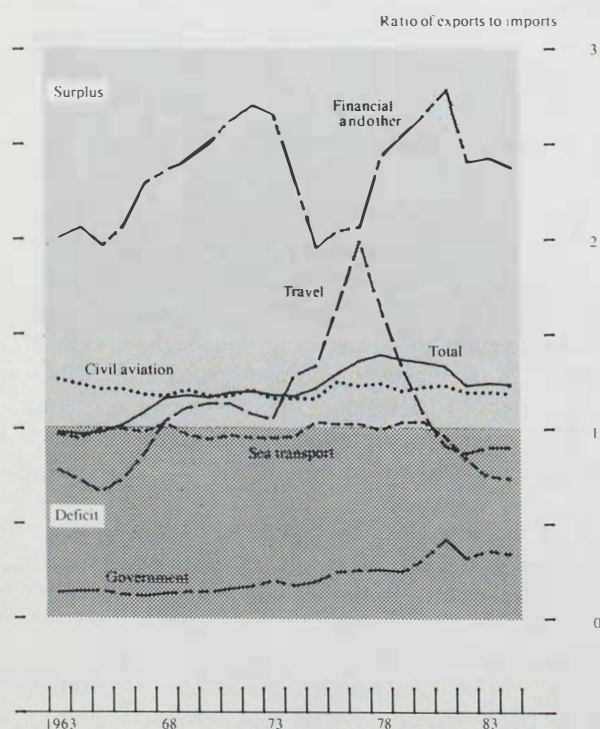


**Chart 5**  
Relative value of exports and imports in main categories of trade



transport has declined sharply. Travel's contribution reached a peak in 1977 but then fell, mainly as a result of the real appreciation of sterling. However, the depreciation of sterling since 1980 has led to some improvement.

**Chart 6**  
Relative value of exports and imports in categories of services



The volume of exports of services as a whole in fact grew less rapidly than that of manufactures between 1974 and 1984 (Table G). However, this can be attributed entirely to a rapid decline in sea transport earnings. Exports of other services grew faster than those of manufactures. Moreover, the volume of services imports also grew more slowly than that of imports of manufactures. This trend was, however, also attributable to a fall in the volume of imports of sea transport and government services; the volume of imports of other services rose faster than that of manufactured goods.

**Table G**  
UK exports and imports of goods and services

Percentages

	Exports			Imports		
	Share of value		Average annual real growth(a)	Share of value		Average annual real growth(a)
	1974	1984		1974	1984	
Fuel	3	17	15.8	15	11	-9.8
Manufactures	56	51	0.9	42	55	6.1
Other goods	10	9	3.3	22	16	0.6
Services	29	23	—	21	19	1.5
of which:						
Sea transport	12	4	-8.7	10	5	-5.6
Air transport	3	3	6.3	2	3	8.1
Tourism	4	5	0.2	3	5	10.0
Financial and other	10	11	2.4	4	5	1.5
Government	—	—	1.9	2	2	1.4

Source: 1985 Pink Book and Department of Trade and Industry *Monthly review of external trade statistics*.

(a) In practice it is difficult to obtain entirely satisfactory measures of volume in services. Little significance should therefore be attached to small differences in real growth rates.

## UK performance in individual service sectors

The United Kingdom has lost share in the value of world exports of services at a rate similar to that at which it has lost share in the value of world exports of manufactures (Table H). This is perhaps not surprising given the declining share of the United Kingdom in world output. Within services, only travel has raised its share. The following sections examine UK performance in the main categories of trade.

### Sea transport

The decline in British sea transport earnings is well recorded; the UK share of the world fleet fell from 11.3% in 1968 to 3.8% in mid-1984.<sup>(1)</sup> Table J shows the share accounted for by UK-registered vessels of shipments of UK exports and imports.<sup>(2)</sup>

Tonne-miles of UK exports have risen, mainly as a result of increasing exports of oil, but the share carried by UK ships has declined since 1975. Tonne-miles of imports have fallen considerably, mainly as the result of lower oil imports; however, the UK share has remained more or less constant. There is no obvious explanation for the difference. It is not primarily an oil effect, as the share of UK non-oil imports carried by UK registered ships has fallen only a little. Despite the decline of the UK fleet, the

(1) Lloyds Register of Shipping, *Statistical Tables* 1984.

(2) Freight payments made to foreign shipping operators for the carriage of UK exports of goods are not included in UK payments for shipping services. Conversely freight payments on UK imports of goods made to UK carriers are not treated as shipping services receipts. However, a shift by UK firms to the use of foreign carriers will clearly reduce UK exports or increase UK imports of shipping services. Ships' bunkers are also treated as part of trade in shipping services rather than trade in goods.



**Table H**  
**UK share of world exports by category of trade**  
Percentages of world exports, by value

	Transport	Travel	Other services (a)	Total services	Manufactures	Total visible trade
1968	16.0	4.8	13.9	11.9	9.6	7.2
1973	14.7	5.4	10.9	10.7	7.5	5.9
1978	10.4	6.8	8.7	8.7	7.3	5.6
1983	7.1	6.1	8.2	7.3	6.2	5.5

Source: IMF Balance of Payments Year Books, IFS and UN Year Books.

(a) Including financial services, consultancy, etc.

sea transport account has only recently moved into deficit. A fall in earnings from the carriage of exports and from cross trading (the carriage by UK ships of third country trade) has been offset somewhat by falling payments abroad (eg bunkering, port charges and charter payments). As a consequence of North Sea oil, the total weight of imports has declined steeply and, as a result, the rise in overall freight payments abroad has moderated despite a rapid increase in the volume and value of non-oil imports. The decline in world oil trade has also reduced the need for UK oil companies to charter ships from overseas residents (payments for which are recorded as services debits). However, these offsets have been diminishing recently and the shipping account has swung into large and increasing deficit.

**Table J**  
**Sea transport<sup>(a)</sup>**  
Billion tonne-miles; percentages in *italics*

	Exports carried	UK vessels' share	Imports carried	UK vessels' share
1972	102.2	48	1,182	32
1973	111.8	48	1,310	32
1974	107.7	48	1,292	30
1975	103.7	45	1,030	31
1976	108.5	40	901	32
1977	135.6	35	720	32
1978	146.6	29	722	29
1979	138.3	27	712	24
1980	138.0	27	615	28
1981	191.4	21	489	25
1982	195.6	18	416	30

Source: *Business Monitor* MA8 1983.

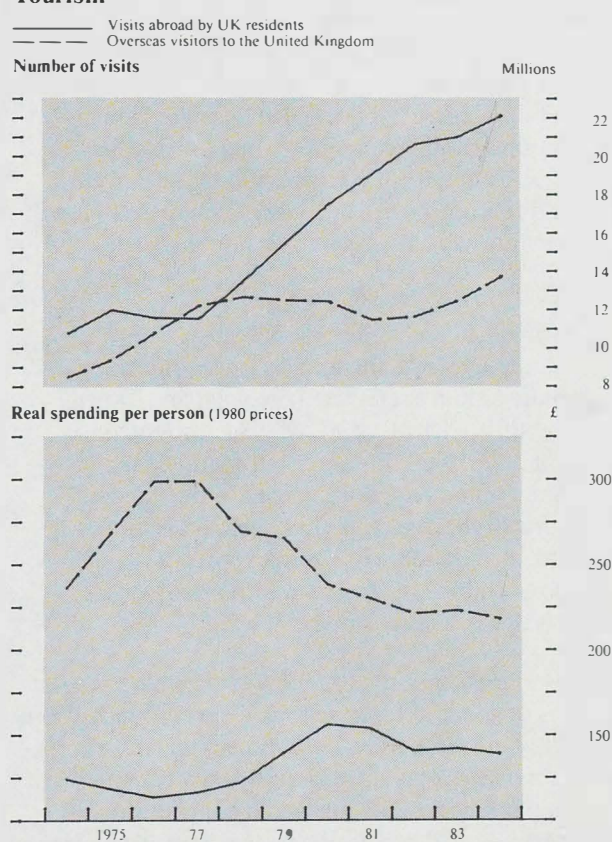
(a) This table is compiled on the basis of flag of carrier while the balance of payments accounts are compiled on the basis of nationality of operator.

### Civil aviation

The United Kingdom's civil aviation account has shown a small surplus over the past twenty years (although in real terms this has fallen recently). The overall balance hides a stronger growth of foreign airlines' earnings from British passengers than of UK airlines' earnings from foreign passengers, a trend which can be attributed to a faster increase in the number of UK visits overseas than in the number of overseas visitors to the United Kingdom (Chart 7). The effect of this trend has been offset by a more rapid rise of foreign airlines' spending in the United Kingdom (on landing fees and fuel etc) than of UK airlines' spending abroad. Chart 8 shows UK airlines' share of passenger movements to and from the United Kingdom. (Third country trade is comparatively small).

UK airlines' capacity on international scheduled operations is regulated, with the number of flights

**Chart 7**  
**Tourism**

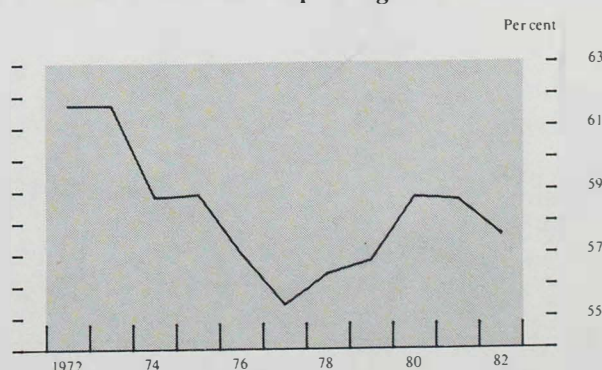


allocated to UK and foreign carriers subject to international agreement. Charter operations, which are subject to fewer restrictions, have expanded faster. Changes in UK airlines' share of international traffic at UK airports mainly reflect this differential market growth rather than the relative competitive performance of UK airlines. In assessing future prospects, the trend towards deregulation and the privatisation of British Airways must be taken into account. It is unclear what the overall impact will be on the international performance of UK lines, although UK consumers are likely to benefit from greater competition between UK and foreign airlines.

### Travel

The United Kingdom has on balance tended to increase its share of world exports of travel services over the

**Chart 8**  
**UK airlines' share of UK passenger traffic**





past fifteen years (Table H). In the longer term, this has not led to an improvement in the UK travel balance as the number of UK visits abroad has risen rapidly and real expenditure abroad per UK tourist, in contrast to visitors' per capita spending in the United Kingdom, has also tended to increase (Chart 7). Nevertheless, there have been times (notably in 1977) when tourism has provided a substantial net contribution to the current account and this appears to be a sector where exchange rate movements have a strong impact on the trade balance.

### Producer (financial and 'other') services

Since 1974, the United Kingdom's surplus on trade in non-transport producer services (financial and 'other') has risen rapidly (Chart 6), and by 1984 amounted to £6 billion or 2.9% of GDP. Somewhat surprisingly, however, the United Kingdom's share of the value of world exports of these services has declined at about the same rate as the UK share of world exports of manufactures (Table H). However, imports of these services have grown fairly slowly.

Financial services amounted to 3.1% of the value of total UK exports of goods and services (3.7% excluding oil) in 1984, roughly the same as in 1974. In real terms, exports of financial services may have risen by only 0.1% per year over the same period.<sup>(1)</sup> The measured contribution of financial services to the overall balance, however, is larger than the export figures suggest, because of the small volume of imports recorded. However, the latter may be under-recorded; for instance, commissions paid to overseas brokers by UK pension funds on sales and purchases of overseas securities cannot be separately identified and are not entered on the services account but are netted off, along with commissions paid to UK firms, from the recorded value of the investment flow. Imports are, however, still thought to be fairly small in this sector.

Table L gives the 'real' growth rates of exports of various financial services. Those for banking and insurance are also shown inclusive of net investment income (other than direct investment earnings) as, for reasons given earlier, part of these earnings can be considered as part of receipts for supplying financial services.

**Table K**  
**Composition of UK trade in financial and 'other' services**  
Percentages, by value

	Exports		Imports	
	1974	1984	1974	1984
Banking	6	9	—	—
Insurance	11	6	—	—
Other financial	17	12	—	—
Consultancy	12	12	—	—
Royalties and services to related companies	15	19	29	33
Oil services	1	2	21	17
Telecommunication and postal	4	4	9	13
Film and television	1	3	3	4
Students, diplomats etc	15	15	—	—
Other services	18	18	38	33

(1) Volume measures in this area may be unreliable.

**Table L**  
**UK exports of financial services 1974-84<sup>(a)</sup>**  
'Real' average growth rate, percentage per annum

<b>Excluding net investment income</b>	
Insurance	- 3.9
Banking(b)	6.8
Commodity trading	- 5.0
Export houses	1.9
Other brokerage	0.9
Total financial services	0.1
<b>Including net investment income(c)</b>	
Insurance	1.2
Banking	12.2

Source: Pink Book 1985: value estimates deflated by the retail price index.

- (a) Earnings are calculated net of overseas expenses of the institutions concerned.  
(b) Excluding earnings on services provided to related firms overseas.  
(c) Other than net direct investment income and net service earnings from related firms abroad.

### Banking

The export earnings of UK banks have grown strongly both including and excluding net investment income. Table M shows the share of London in world financial markets and the share of British banks within the London market. Under both measures, the United Kingdom appears to have maintained its share in recent years, although there was some fall in 1984.

A number of factors will influence the future development of UK exports of banking services. Growth in international banking markets has been affected by international debt problems, making banks reluctant to take on international business for any but the best names, although as banks of different nationalities have differing degrees of exposure and are reacting to the debt situation in differing ways, the effect will vary between countries. In addition, tighter supervisory capital requirements have encouraged banks to build up their off balance sheet business, making the market share measure used in Table M a less satisfactory guide to performance. The traditional boundaries of banking, which have become less distinct in recent years as the banks have widened the range of services offered, will continue to blur as the banks move into new areas, such as stockbroking (through the acquisition of stock exchange firms). This process is also likely to be influenced by the application of new information and communication technologies.

**Table M**  
**UK banks' share of international lending<sup>(a)</sup>**  
Percentages

	London in world market	British banks in London market
1975	30.3	22.6
1976	27.7	21.5
1977	25.0	22.8
1978	24.3	22.9
1979	25.3	23.1
1980	25.9	23.9
1981	25.6	23.2
1982	25.4	22.0
1983	25.0	21.7
1984	23.7	20.4

(a) Foreign currency lending to residents and non-residents, and sterling lending to non-residents. End-December.



### Other financial services

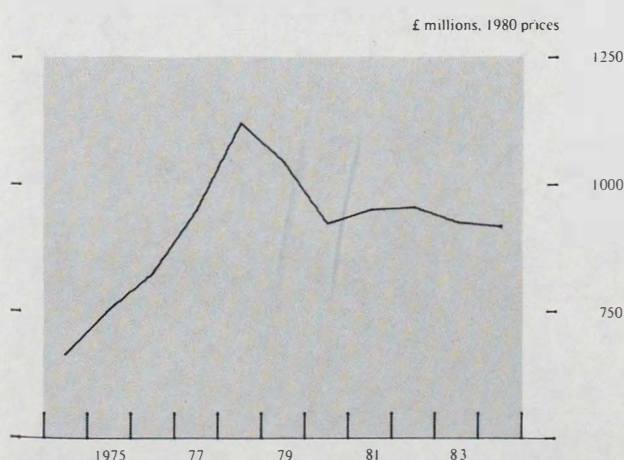
Growth in the volume of overseas services earnings in insurance and other brokerage has been lower than in banking in the last ten years (Table L). Anecdotal evidence suggests that insurance has been affected by protectionism abroad and the growth of competing 'Lloyds type' insurance markets overseas.

Other brokerage includes earnings from The Stock Exchange (17% of the total), the Baltic Exchange (46%), Lloyds Register of Shipping (5%) and others (31%). The United Kingdom appears to have lost share in the market in securities trading. Part of the market for the shares of several large UK companies has shifted to the United States where shares are traded in the form of American Depositary Receipts (ADR). Transactions costs for ADR are lower, mainly because of the absence of stamp duty (ADRs are legally American securities). Forthcoming changes in the structure and regulation of The Stock Exchange are likely to have a major impact. It is not clear by how much any resulting increase in UK exports of financial services will be offset elsewhere within the current account by a rise in direct investment profits due abroad to the parents of foreign companies participating in UK markets for the first time.

### Consultancy

The volume of consultancy earnings from overseas peaked in 1978, since when there has been a decline (Chart 9). However, as with financial services, recorded imports of consultancy services are negligible (except for North Sea oil related consultancy) and the net contribution to the current account was £1.4 billion at current prices in 1983. It should be noted that these figures exclude UK exports of plant and raw materials associated with consultancy contracts, which are recorded in the visible trade figures. If these are included, total exports in the construction related field were thought to be about £3.8 billion in 1982/83.<sup>(1)</sup>

**Chart 9**  
Real UK service earnings from consultancy



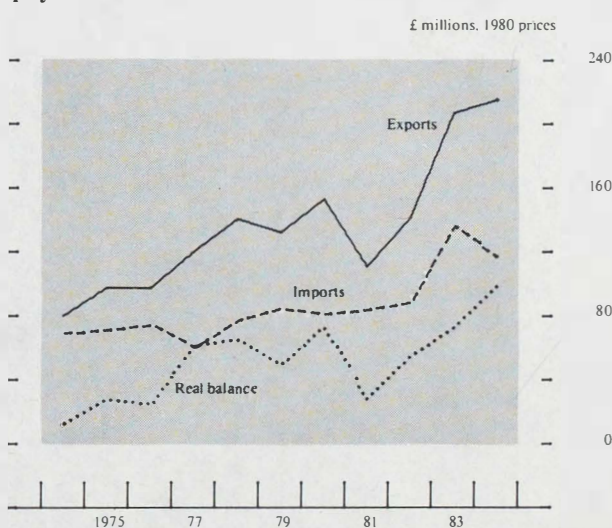
(1) Department of Trade and Industry, *British Business*, 26 October 1984.

With the export market for construction and consultancy services being concentrated in the Middle East and in other developing countries, the recent fall in OPEC's oil revenues and balance of payments problems in the third world may limit the scope for significant growth in this sector.

### Films and television

Earnings from films and television amounted to 2.8% of exports and 3.5% of imports of financial and 'other' services in 1984, and showed a surplus of £131 million. Real growth in this sector has been strong, but somewhat erratic, in recent years (Chart 10).

**Chart 10**  
Films and television: UK service earnings and payments



### Conclusion

In value terms the share of services in GDP in the United Kingdom has risen steadily since the war. However, prior to the early seventies the output of services in volume terms grew at much the same rate as the rest of the economy, probably because a rise in the relative price of services, attributable to lower productivity growth, dampened demand.

More recently the output of service industries has increased faster than that of other sectors (other than oil and gas) and has been less susceptible to cyclical fluctuations. The share of the total labour force employed in the services sector has risen significantly, particularly in the areas of social and producer services.

Demographic trends may well have been the most important factor behind the rise in the share of social services in employment, but the growing importance of producer services probably reflects a number of factors, including specialisation and innovation and a more general tendency for other sectors to make proportionately greater use of the output of service industries in their



production. These recent trends have probably been encouraged by the greater stability of the price of services in relation to that of other output in the past ten years or so. Another factor is that only a fairly small proportion of the services sector is internationally traded; services output as a whole has, therefore, been more insulated from the affects of changes in the real exchange rate. The relative buoyancy of the services sector in the past decade is in part also a reflection of a slowdown in the growth of other non-oil UK output: since the first oil price shock of the early seventies, underlying productivity growth in the manufacturing sector has fallen, reinforcing an

already deteriorating trend in manufacturing trade performance.

Until the late seventies the United Kingdom's surplus on international trade in services increased steadily. However, this should not be taken to be an intrinsic feature of the UK economy. Trade in services is subject to the same influences as trade in goods. Thus the rise in sterling's real exchange rate probably accounts for much of the deterioration in the balance of trade in services in volume terms between 1978 and 1982, a period when the surplus in value terms continued to rise.