Evaluate the role of the service sector in the late Victorian and Edwardian periods.

Services can be organised, by the International Standard Industrial Classification, into four types: wholesale and retail trade, hotels and restaurants; transport, storage and communication; finance, real estate, insurance and business services and community, social and personal services. Adam Smith noted that, contrary to commodities, services rendered "generally perish in the very instant of their performance, and seldom leave any trace or value behind them for which an equal quality of service could afterwards be procured". This characteristic makes the service industries difficult to measure in the way that commodities like steel or wheat are valued, especially as services tend to merge imperceptibly with other activities. However, their defining characteristic is that given by Smith, that they disappear when performed and cannot be stored, although, of course, they can be repeated. There has been conflicting views over the role of the service sector during the late 19th century and the early 20th century, some believing Adam Smith's distinction between manufacturing as productive labour and employment in services as unproductive labour, others purporting the idea that services made a positive contribution to the British economy. We shall evaluate both views to discover the nature of the tertiary sector in the late Victoria and Edwardian periods.

The service industry has been accorded little credit by some economists in their accounts and explanations of economic growth. The thesis developed by classical economists in the 19th century relied heavily on the notion of capital accumulation in terms of tangible goods. Kaldor (1965) developed an explanation of economic growth driven by manufacturing productivity: the rate of growth of national product is determined by the growth of output in manufacturing. Labour productivity in manufacturing is simply a function of the growth of output, attained through economies of scale. As manufacturing alone stimulates growth and productivity, its expansion will entice labour away from less productive sectors, like services. This change in structure will increase labour productivity in services by drawing off under-utilised labour and enhance the productivity of the workers transferred to manufacturing. The main catalyst for economic growth is therefore industrial growth and its own expansion being determined mainly by export demand with services playing a completely passive role. Concentrating resources in services will therefore inhibit growth by starving manufacturing of productive resources. However, in the second half of the 19th century, services accounted for half the growth in national income and for approximately one third in the inter-war decades. Services contributed around three quarters of the total increase of employment in the century after 1850. While Kaldor's theory is that growth is industry-led and that only manufacturing is able to achieve substantial productivity increases, the links between service sector growth and GDP are no less impressive and services have also demonstrated a capability to generate impressive productivity gains. Kaldor's notion that manufacturing will attract labour away from services is most obviously false as service sector employment growth prior to WW1 came primarily from expansion of the workforce through population increase.

A condition described by William Baumol and referred to as the "cost disease" imagines again a pessimistic scenario: the economy is divided into two sectors, the technologically progressive sector and the non-progressive sector. The former is capital intensive and exhibits economies of scale, all of which make for a cumulative rise in output per man hour. Since labour is paid according to marginal productivity, wages will be high because of the large amount of capital each worker is working with. For example, automobile production has shifted much of the work previously done by people to machines. With the number of workers decreasing and capital input increasing, the marginal productivity of each worker has been going up over time. The non-progressive sector is labour-intensive and has little room for substituting capital for labour. This sector includes activities in which quality is judged directly in terms of the amount of labour. Cost disease arises because wage rates in the economy are set by the progressive sector. Workers are fairly mobile between industries and wages significantly influence occupational choice. Firms in the non-progressive sector must compete for workers by raising their offered wages to match wages in the progressive sector. As a result, the price of any given service produced in the non-progressive sector will rise as the price of labour rises in the technically progressive sector. As a consequence, in order to produce the same amount of total goods and services, an increasing proportion of labour resources will have to go into non-progressive industries and a decreasing proportion into progressive industries. This diminishes overall productivity and reduces the growth rate of the economy. On productivity levels the evidence generally supported the view that the services for which more reliable data are available, transport and communications, and distribution, were more productive than manufacturing. Also, service sector employment in Britain increased over the late Victorian and Edwardian period: in 1856 services accounted for almost 40% of GDP and 30% of employment, while industry produced around 30% of GDP but employed 40% of the workforce. By 1913, the shares of both GDP and employment were higher in services, with the services GDP share at 48% (compared to 36% in industry) and that for employment at 45% (compared to 44% in industry). Gemmel and Wardley (1990) and Lee (1990) have calculated that the level of labour productivity in services in the late 19th century was higher than in manufacturing or agriculture. This evidence opposes Baumol's thesis.

During 1856-1913 GDP per head grew at an average rate of 1.1% annually; this increase in affluence, which was particularly concentrated in the middle class, resulted in aggregate consumption expenditure doubling between 1870 and 1914 at an annual growth rate of 1.7%. Any substantive economic growth must create the need for an improved transport network and there was an emergence and replacement of transport systems from canals to railways, motor vehicles and aeroplanes. In particular, coal and other mineral traffic was of great importance to Victorian railway proprietors and accounted for one fifth of all revenue at the time. The increase number of people and growing complexity of economic life also stimulated distributive services, which were partly orientated towards consumers, as the range and quality of consumption increased and partly a necessary adjunct to productive industries. The growth in these producer services essentially led to development and amelioration of the infrastructure.

Important parts of the service sector made significant contributions: it seems that both Kaldor and Baumol's theories face contradictory evidence, the service sector proving itself to have been a positive influence on the economic development and productivity in Britain rather than parasitic, feeding and starving off more productive sectors such as manufacturing. It is reasonable to conclude that the service sector in the late Victorian and Edwardian periods played a beneficial role.