

Indian IT Services – SMAC – New Wave of Opportunity

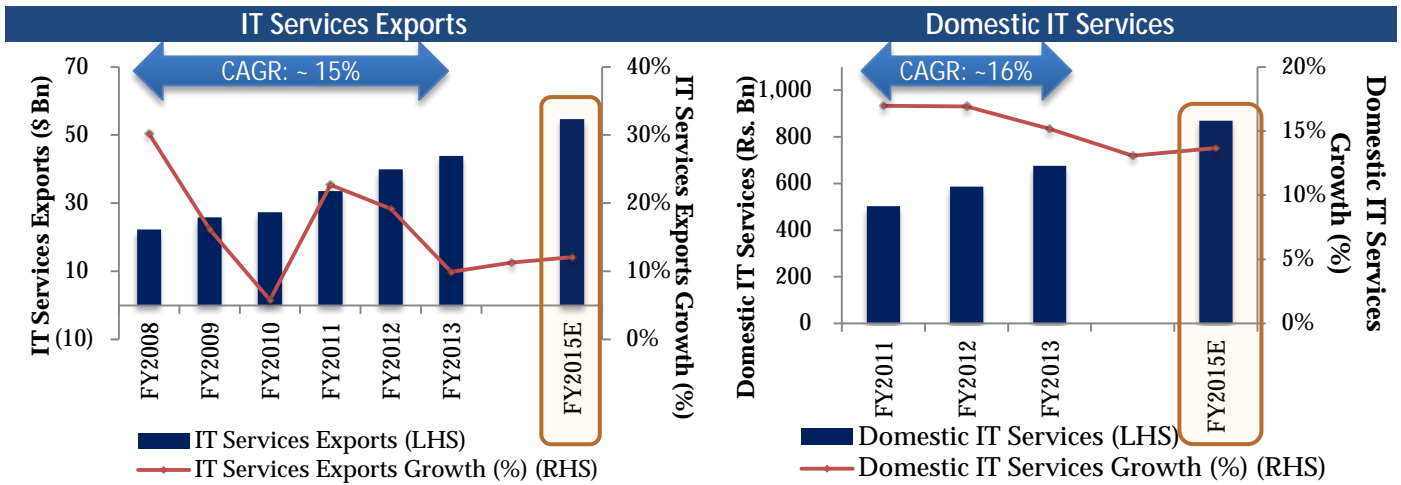
Indian IT services conquered the global technology landscape capitalizing on India's low-cost, English-speaking talent pool. Over the years, Indian IT players have transformed their business models from labour arbitrage to that of a value-added, end-to-end service provider, reaching out to more than 60 countries thriving on the success of the robust Global Delivery Model (GDM). Indian IT sector is predominantly exports driven, with exports comprising 80% of the total revenue, and employs more than 3 million people directly. Globally, corporates are using outsourcing as a strategic tool to reduce costs evident from the fact that global sourcing is growing twice as fast as global technology spend, Indian outsourcers being primary beneficiaries of the same. Indian IT services exports are dominated by Indian companies, contributing around 3/4th of the total, whereas rest of the share is distributed almost equally among global IT multinational players and captive centres of global corporates. IT-BPM players have established an empire of close to 600 global delivery centres around the globe in 75 countries.

Of late, unemployment fuelled by financial meltdown has given rise to anti-outsourcing protests in the developed markets forcing governments to enact curbs on outsourcing such as the new Immigration Bill in the U.S. Nevertheless, with more than two decades of experience, Indian IT players would weather the storm.

IT services Exports to continue winning streak; domestic market to complement the growth

IT services exports have grown at a CAGR of around 15% from FY08-FY13 on the back of rise in global offshoring. FY2013 witnessed a dent in IT services exports with the ongoing weakness in the U.S. and contraction in the European economy. This also resulted in declining propensity to spend on discretionary projects. This was evident from the fact that the project related revenue (revenue from IT Consulting, System Integration, Application Development, Network Integration etc) lost some share to outsourcing related revenue (revenue from application management, Infrastructure Services Outsourcing etc) as the latter grew at a faster pace in FY 2013.

Exports: U.S. economy, accounting for more than half of the Indian IT services exports, is the growth engine for Indian IT and is showing signs of revival as indicated by labour market data. IT budgets are expected to show improvement. Going by other indicators like Industrial Production and continuing stimulus, U.S. economic growth still remains cautiously optimistic. CARE Research believes that Indian IT services will continue to grow at the historical average rate garnering early double digit growth over the next couple of years.



Source: NASSCOM and CARE Research Estimates

Domestic: As Indian IT market is considerably under-developed as compared to the matured markets such as the U.S., Europe and Japan, Indian IT firms have rarely had India specific strategies as their primary focus was cost arbitrage in the developed markets. Most of the IT solutions used in India were stripped down versions of global products. Nonetheless, Indian market is considered as one of the disruptive forces because of its pace of growth since the domestic IT-BPM market has grown at a CAGR of 25% over a period of FY2000-2013, four times faster than the global IT-BPM spend during the same period. CARE Research believes that Domestic IT services will continue to grow at a double digit rate, growing marginally better than the exports over the next couple of years. Domestic IT sService demand will be driven by infrastructure services, cloud and mobility. Though Indian economic growth has halved from its peak, with ailing industrial production, CARE Research believes that incremental IT demand from under-penetrated pockets and government projects related to e-Governance and financial inclusion, especially from state governments' would provide the steam to fire the growth engine of the domestic IT services.

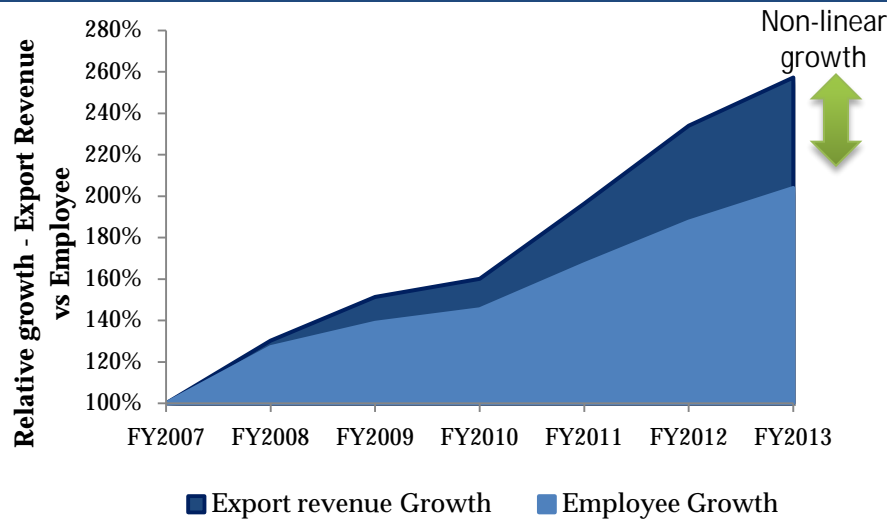
Where would the next \$100 billion come from for Indian IT-BPM Industry?

Ø **Marching towards non-linear Growth**

For years, IT services industry growth could be easily traced by simply gauging the expected number of employees to be hired. However, the headcount in the IT services exports has grown at a CAGR of 12.6% through FY07-12 as compared to revenue growth of 17% during the same period. Since the billing rates haven't improved substantially, it shows that the IT Services industry is moving up the value chain embracing newer practices of non-linear growth. Indian IT Service providers are transcending to value-added offerings like consulting, system integration etc, which demand a differential pricing as the client's focus shifts from cost-saving to quality. This has

led to emergence of non-linear pricing models, which links the clients' expenses to their business outcome or usage and revenues are linked with productivity, ensuring vendors share productivity gains with clients.

Non-Linear Growth in IT Services



Source: NASSCOM and CARE Research

IT players are moving away from Full Time Equivalent (FTE) and per hour basis billing practices to transaction based, outcome based models in new deals. This change in pricing models also helps in camouflaging outsourced business at client's end with no need to disclose the number of jobs being outsourced. Also, with these models, the client does not take the risk of non performance of FTE's and the vendor reaps the efficiency gains.

Ø **Global recovery at the doorsteps**

Technology spends globally, especially on discretionary projects, are closely linked with the overall economic growth. Being an export driven industry with a major exposure to developed economies, Indian IT is closely dependant on world economic revival as close to half of the IT exports revenue comes from project based services which are discretionary in nature.

§ **Global Economic Growth to revive over next couple of years**

IMF has forecasted a robust 3.1% and 3.8% global GDP growth in 2013 and 2014 respectively in its July 2013 World Economic Forecast, marginally down from its previous forecasts. The impulse to global growth is expected to come mainly from the U.S. where activity will move into high gear as fiscal consolidation eases and monetary conditions stay supportive. Though the GDP growth in U.S. is expected to come down to 1.7% in 2013 from 2.2% in 2012, it will rise to 2.7% in 2014. In the Euro area, policy actions have reduced major risks and stabilized financial conditions, although growth in the periphery is still constrained by credit

bottlenecks. The region is expected to gradually pull out of recession, with growth reaching 0.9% in 2014, after contracting by about 0.6% in 2013.

§ **Global IT Outsourcing industry will continue to outpace global technology spending**

Global IT spend has grown close to 5% in CY2012 and is expected to grow at a lesser pace in CY2013 on account of lesser than expected recovery in the global economy, with a gradual recovery in CY2014. Global IT Outsourcing has been beating the overall technology spend, growing at almost double the rate. Indian IT has a major share of more than 60% in global IT outsourcing with a successful Global Delivery Model. Indian IT outsourcing has not been threatened by other destinations unlike BPM industry, as the skill-set required for IT is higher than other outsourcing services such as voice-BPM.

Ø **Social Media, Mobility, Analytics and Cloud Computing (SMAC) – Four engines to fire the growth**

Eruption of social media and mobility had been the two game-changing technology-enabled innovations that changed human life in recent times. The pace of their growth has been astonishing and is compelling enough to initiate its use in all the aspects of business. Cloud computing has gradually penetrated technology landscape and is revolutionizing the way products and services are delivered to clients. As the world gets flooded with zeta bytes of data every day, analytics is enabling efficient use of the same for corporates in strategic and tactical decision support. These market forces do not necessarily work in isolation and their convergence is going to drive the market, creating opportunities for IT players.

1. Social Media

Social media is touching every aspect of human life – right from connecting with people to influencing purchasing decisions. Collectively the social networking sites reach out to nearly one fourth of the global population. The social network user-base is expected to cross the 1.7 billion mark in 2013, an 18% increase from 2012, driven by rising adoption in emerging countries.

As more than 1 billion people are glued to social media at any point in time globally, corporates are enthused and also compelled to use social media for activities ranging from promoting their offerings and connecting with their current and prospective employees to effective brand building. Enterprises are also trying to use social media analytics to better understand consumer behaviour.

1 out of 5 minutes online by an average user is spent on social media related sites.

Approximately **46%** of online users count on social media when making a purchase

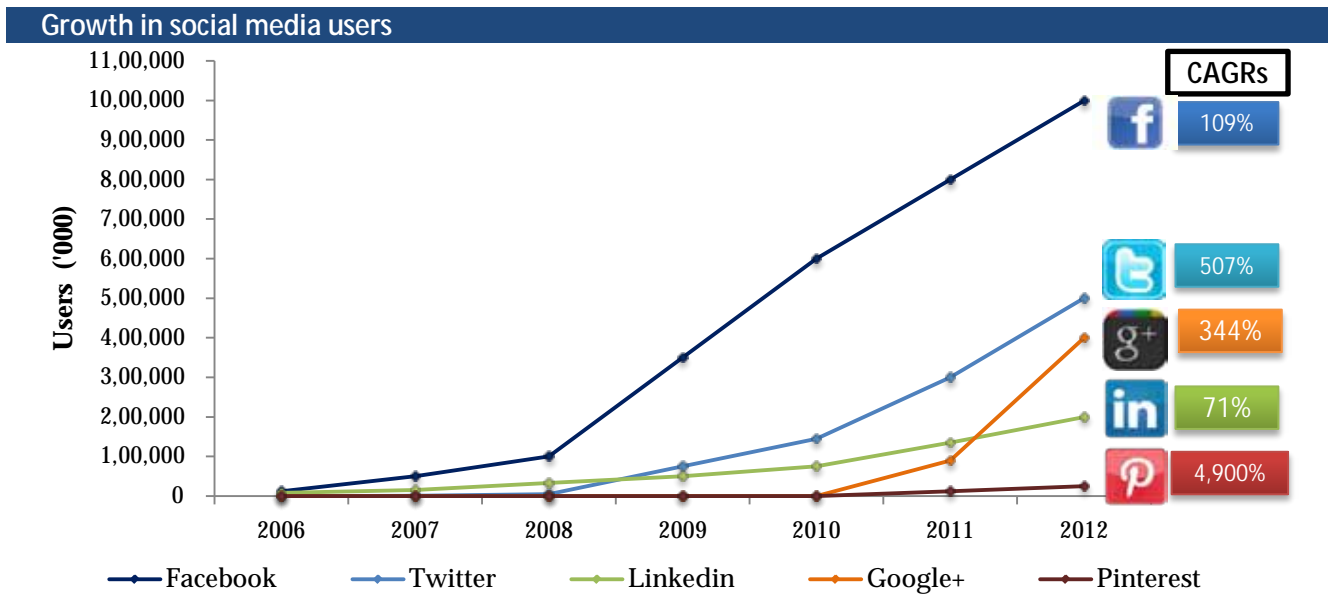
30% of the world's population is online at any point in time

Nearly **90%** of top global banks use social networking to acquire customer

Close to **70%** of Fortune 500 companies have presence on Twitter, Facebook and YouTube; retailers and telecom players being the top users

Source: Industry and CARE Research

Almost all the social media services have grown exponentially over last 6-7 years, encompassing more than a fifth of global population.



Source: Company Data, Industry and CARE Research

Note: CAGR for Google+ and Pinterest has been calculated over last 2 and 3 years respectively

Indian IT-BPM players can find opportunities in providing consulting services to create social media roadmap, architecture and social media strategy for their clients.

2. Mobility

Mobile data traffic grew **70%** in 2012.

More than **6.4 billion** mobile subscription, with more than **1.7 billion** mobile broadband subscriptions in Q1 2013

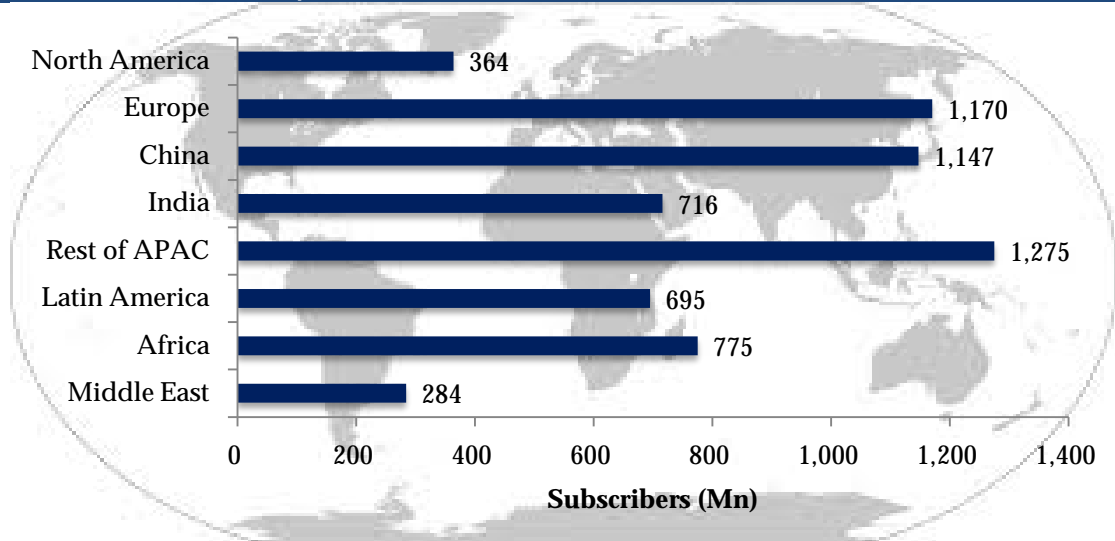
46% of social media users use their smart phones to access social networks

More than **60 billion** mobile apps have been downloaded in 2012 and this number is expected to rise to more than **100 billion** in 2013.

Source: Industry and CARE Research

Though the mobile subscribers globally are growing at single digit rate, mobile data usage is growing at a very rapid pace. Mobile broadband subscriptions stood at more than 1.7 billion compared to global mobile subscriptions of 6.4 billion during Q1 2013, with 4.5 billion individual subscribers, a considerable chunk of which comes from Asia-Pacific.

Number of Mobile subscriptions – Q1 2013

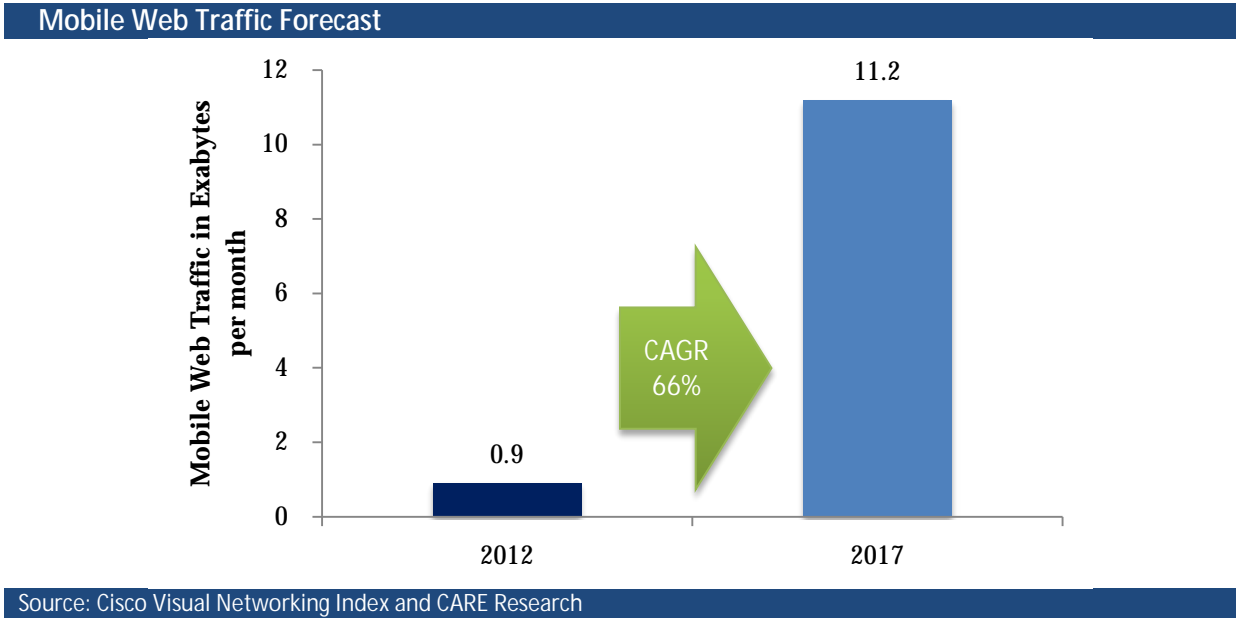


Source: Ericsson Mobility Report, 2013

Mobile banking and m-commerce are supposedly the most influential data applications of mobility which are reshaping businesses and transactions globally.

Indian IT majors have established capabilities in enterprise mobility to cash in on this sunrise sector. At the same time, smaller firms such as MobileOne, Rapidvalue are creating a niche for themselves. The larger firms would widen their offerings by acquiring smaller firms or tying up with them. Specific opportunities lie in the areas of mobile application development and maintenance, integration of enterprise level applications with mobile applications, mobile data security etc.

While mobiles are rapidly grabbing the share of internet from PCs, telecom operators worldwide are focusing more on Value Added Services as the primary revenue stream as compared to voice telephony. Mobile web traffic constitutes more than 10% of the total web traffic and is expected to grow eleven-fold over the next five years. This is creating opportunities to develop, integrate, manage, secure mobile content for consumer centric applications.



Smartphones and tablets are becoming an integral part of human life, making inroads into the corporate world, giving rise to need for integration of enterprise applications with mobile devices, security and storage related applications. Organizations are slowly moving towards the 'Bring-Your-Own-Device (BYOD)' concept creating opportunities in the enterprise mobility segment related to integration, security etc.

On the consumer side, mobile applications (apps) are becoming a central strategy for a range of stakeholders to access the consumer's share of time spent on mobile, of their wallets, of advertisements and so on. There had

been more than 60 billion mobile app downloads in 2012 and this number is expected to cross the 100 billion mark in 2013. Though free apps constitute more than 90% of the total app download, mobile apps generated a revenue of \$17-18 billion in 2012.

3. Analytics

With rise in technology, digitization made significant strides in the recent years, creating zettabytes of data. Advent of internet, ascent of Social Media and a rise in mobility services are the main contributors to the rise of data. Organizations are trying to capture this opportunity in using this data in strategic as well as operational decisions. One of the biggest challenges for organizations is how to handle such a huge amount of unstructured data and develop or adopt new technologies for the same as data has become more dynamic in nature. There lies the opportunity for the specialized IT-BPM firms to exploit the value chain – data generation to analysis.

Worldwide Big Data technology and services opportunity in 2012 is estimated to be \$5 billion and the same is expected to grow at a CAGR of more than 40% over next 4-5 years. The Big Data market is emerging at a rapid pace and incorporating technology and services from a wide range of existing and new market segments. The fastest growing sub-segment within Big Data will be Storage.

India is expected to showcase its core competence in capturing the Big Data market as it grows five-fold from around \$0.2 billion in 2012. India's integrated IT-BPM players will have more than 80% of the share of the Big Data India pie in 2015 as compared to the pure play BPM companies.

Big data outsourcing has opened floodgates of opportunities for Indian IT-BPM players. More than 80% of the big data opportunities are in the area of IT services encompassing technology solutions for gathering of data, processing and designing big data architecture whereas analytics comprises the remaining opportunities. As the Indian IT-BPM players already have a leading position in industry-specific software development and implementation, they have a huge growth opportunity to build big data end-user applications and develop big data management and storage service portfolio.

2.5 exabytes of data is created everyday

Global Big Data technology and service opportunity is estimated to be **USD 5 billion** in 2012

90% of the data in the world today was created in the last 2 years alone.

Digital information created annually will grow by a factor of **50** from 2010 to 2020, reaching **40,000 exabytes**

Source: Industry and CARE Research

It's all in the Data

telecommunications
 big data Provide faster, better analysis transformed hundreds of terabytes of customer data into actionable insights to develop highly targeted, personalized offerings.

RETAIL
 macy's
 Walmart collects 2.5 petabytes of data every hour from customer transactions.

HEALTHCARE
 Pharmaceutical companies like Bristol Myers Squibb are using Big Data to support drug development.

BANKING
 Scoring Credit Risks
 Managing Rising Security Costs

Macy's uses Analytics to predict sales

Source: Industry and Press Articles

4. Cloud Computing

Cloud computing has been one of the most disruptive phenomena in the history of information technology. It has the ability to serve the 'bottom of the pyramid' businesses by revolutionizing the whole model of IT from 'ownership' to 'pay-as-you-use'. It also enables quick scalability for technology providers as technology is getting more vibrant with diminishing shelf-life.

Indian players would find opportunities around cloud computing in areas such as cloud consulting, migration to cloud, integration, cloud specific application development and maintenance, software testing. As small businesses adopt cloud especially in the infrastructure as a service and cloud platform, it will throw enormous opportunities for integration with other applications and creation of virtualized networks.



Source: Industry and CARE Research

*IaaS – Infrastructure-as-a-Service

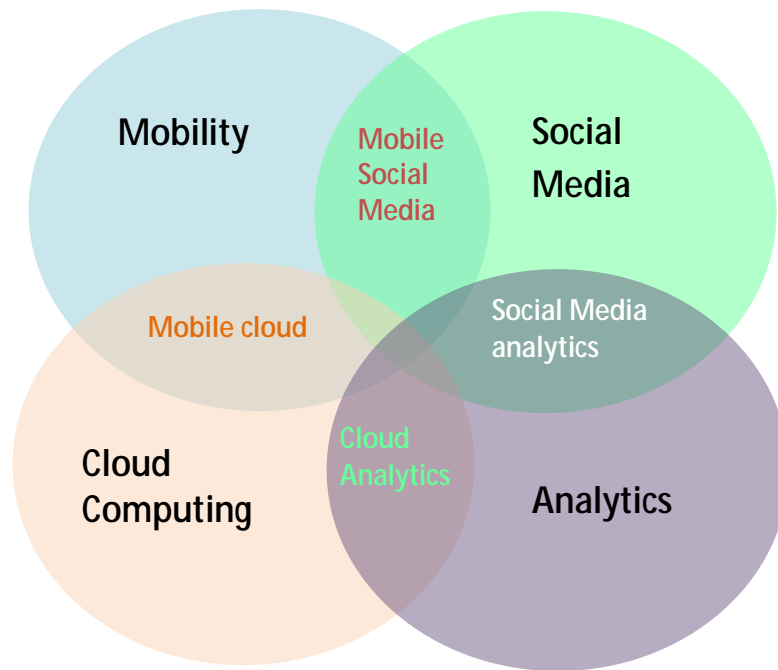
Convergence of the Four

While these four technologies continue their exponential rise, organizations would be able to make most of it by combining two or more of these. SMAC will help organizations in 'consumerization' of technology as it brings consumers, technology and vendors closer to each other. An overlap between these technologies, if captured early and efficiently, would offer enterprises an edge over their competitors as it makes organizations more agile to changing consumer preferences.

The convergence of SMAC opens up various avenues for the IT services industry. These technologies when combined provide additional functionality. Social Media Analytics involves gathering data from blogs and social

media websites to analyze and pick out consumer sentiments and trends for marketing and customer related services. Mobile Social Media involves using mobility to access social media on the go while a Mobile cloud enables accessing cloud services through mobile devices. Cloud analytics allows data analytics to be performed through a cloud providing easier sifting through vast amounts of data.

CARE Research believes that Indian IT Industry has always been dynamic and agile to capture the newer avenues of growth, especially when the traditional business lines are on the verge of maturity and the industry is hunting for greener pastures.



Source: CARE Research



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