

## How the Indian IT Industry can cope with the US recession

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*The US downturn is slowly but surely redefining the Indian IT paradigm and if Indian IT companies are not watchful, they may lose the outsourcing advantage soon.*

The signs are for all to see. US employment fell for the first time since 2003, manufacturing declined 5.3%, first time house buying - a good proxy for economic health - plunged 8.1 percent in December. Technically, it might not qualify as a recession, but according to Warren Buffet, "by common sense definition", the U.S. economy already is.

A December report on the Indian tech sector by Morgan Stanley says the uncertainty in the United States may delay tech spending in the first half of 2008. Margins are already under tight pressure due to the weakening dollar. With offshore salaries rising 10-15% a year, the overall operating margins have been squeezed by 6%. The major crisis in the US financial markets has had a ripple effect on all sectors and it might be a while before things remotely start looking up. As Laksmi Narayanan, Nasscom chairman and V-C at Cognizant said, "The current situation is not temporary. It is the new baseline. The industry will have to learn to operate under the new parameters." Anecdotal evidence suggests that fewer development projects from existing clients are coming through. The sales cycles have increased and winning new customers has become increasingly difficult.

If there was a major watershed in the Indian IT Industry post Y2K, this is it. After the dizzying growth of the last 10 years, it is time to pause, reflect and realign strategies. If the software industry has to survive, then it needs to adapt to the changing market scenarios quickly. Talk of a software upgrade.

### **Diversify Globally**

For far too long, Indian IT industry has focused on the US. Yes, US does account for about 60% of the total IT spending. However, IT spending of American companies is bound to slip with the slump. It's also been a long time since US firms embraced the outsourcing model, so further growth seems very limited. With that in mind, the Indian IT firms need to focus their attention on the other markets, especially Europe. Using UK as the base, software firms can branch out onto mainland Europe. There will be a certain amount of language and cultural resistance in countries like France, Germany, and Netherlands, that Indian firms will need to grapple with. Language training and cultural orientation should form a big part of the foray into Europe.

The potential of nearshoring in the context of IT, also needs to be tapped fully. Customers are looking for IT service providers who are geographically closer and culturally similar. With respect to Europe, the East European countries satisfy both these criteria. Moreover, East Europe has a large number of skilled software programmers. According to Arkadiy Dobkin, CEO of outsourcing powerhouse EPAM, the so-called "Soviet heritage" of traditionally strong engineering education is responsible for the region's large pool of trained professionals. The cost advantage of India over such locations is also significantly diminished as salaries in Eastern Europe are not significantly higher than those in India.

The need for nearshoring is especially highlighted by the fact that many UK IT service providers have recently invested in 3 global delivery centers in Eastern Europe and Morocco each and 4 in China. Such nearshore locations will be able to service EMEA and South East Asia region and their capabilities cannot be replicated by similar centers in India. Many global firms want to continue offshoring, however they are looking at non-India based partners as a way of addressing the issues of talent shortage, salary hikes and high turnover which are commonplace in India. Such firms are even willing to back development centers run by Indian giants elsewhere, purely from the standpoint of flexibility, business continuity and seamlessness in global operations. Hence, Indian IT companies should establish a strong presence globally through delivery centers in emerging regions, so as to acquire a bigger portion of the IT revenues pie.

## **Local Foray**

With the rupee gradually strengthening against the dollar, it makes imminent sense to enter the local markets with a purpose. Indian IT market is growing a compounded annual rate of 21%. Indian companies have been traditionally slow in embracing IT but are now implementing IT internally with a vengeance. Some large multi-million dollar contracts like the Bharti-IBM, Dabur-Accenture and SBI-TCS deals should make the rest of industry sit up and recognize the potential of the Indian market. Some of these deals have been jaw-dropping huge – TCS' \$140 million deal with BSNL, Wipro's \$80 million and \$60 million deal respectively with HDFC and Dena Bank equal, if not exceed, deals of similar nature with international clients. The opportunity is not worth ignoring.

South East Asia is another region where IT big-wigs can focus their energies. China, Korea, Japan, Australia are big markets and Indian firms should attack them, all guns blazing. The region can not only be tapped for local markets, but also be used as satellite facilities to support their Indian counterparts.

## **Tighten Recruitment and Retention Processes.**

Since the last few years, the composition of IT resource pool has undergone a substantial shift. Earlier, many reputed companies only recruited engineers through campus placements. These placements were also carried out in Tier 1 colleges. The selection process was tough - base criteria was first class academic qualification, followed by test of GMAT style logical questions, and a rigorous interview process. Only the top few got through.

However, the demand for Indian IT services kept getting bigger. Post dot com bust and 9/11, business conditions in the US became tougher and companies wanted to focus on key operational and strategic functions and outsource technical application development and support to the experts. India as an IT destination offered notable cost advantage, better flexibility, 24/7 support and improved accountability.

To cater to the rising demand, there has been a mad rush to recruit more people. Earlier, a 4 year engineering degree, the premier choice of top ranking students, was a de-facto selection criterion. Now, companies have started recruiting from non-engineering colleges. Recruitment cells are covering lower ranked colleges during campus placements. Consequently, the quality of new recruits has gone down noticeably. Figures suggest that only 25% of the total graduates in India have employable 'production-worthy' skills. Not only are the much celebrated analytical skills poor amongst such fresh hires, but even basic communication skills are a cause for great worry.

Fewer contracts in a sluggish economic scenario would automatically drive down the break-neck speed of recruitment. However instead of a complete stop to all recruitment, the IT industry should use this period for people overhaul. The employees who have demonstrated continuous below par performance need to be put on notice. They must be mandated to undergo training programs to hone and upgrade their skills – technical as well as inter-personal. In the absence of any significant improvements, they should be let go. At the same time, campus and lateral hiring of high performing individuals needs to continue. It will help restore the quality of talent that has deteriorated over the years.

## **Address the Skills Shortage**

At the same time, this quiet period needs to be used to get the existing resource pool ready for the next big wave. Most programmers are caught up in the daily nitty-gritty to catch up on the latest technical advances and recognize the breakthroughs that will sweep the IT world. To address this gap, workshops and technical trainings to educate the workforce should be held at regular intervals. Similar sessions on soft-skills and cultural orientation programs should be conducted to make the people more customer-centric.

Service Oriented Architecture, Software as a Service, [Cloud Paradigm](#) (or desktop virtualization) are emerging as some of the biggest IT trends. Additionally, platform consolidation is the biggest IT change

that many CIOs have on their radar. Much of the work coming along will be governed by these trends. The software designers should be brought up to speed on these new trends and the programmers trained on technologies that underline these trends.

### **Improve Productivity**

Addressing the skills shortage amongst the existing employees will partly lead to better productivity. But a concerted effort is needed for flexible and savvy use of the existing talent pool. The recent growth of IT has left many organizations with massive shortage of middle level managers. Hence, techies have progressed to managerial roles far too quickly. At the same time, the inter-operability found in foreign tech heavyweights— where senior staff continues to be technically hands-on even after 5-10 years – is not to be seen. In India organizations such resources tend to be entirely locked up doing administrative tasks and managerial reporting.

Resolving this can be fairly straight forward. Technical tasks should form a sizable portion of a project lead's tasks. Technical advancement through training and project work should be an integral part of a manager's appraisal criteria. For smaller projects, senior resources need to be encouraged to code themselves, thereby reducing the overheads.

Simple tools like word and excel, if used effectively provide fantastic productivity gains. Trainings on such desktop tools need serious thought.

Some Indian IT organizations have world-class in-house systems. But there is still tremendous scope in making these functions quicker and simpler. What better time to get those things sorted than this slack period? Programming is one of the most intense and focused activities, and any hindrance to it – availability of software, training material, access issues – should be resolved speedily through a system that exists to support the programmer more than anyone else. There is a sense that the rapid and reflexive adoption of security management controls like BS7799 has done more harm than good by cramping creativity and adventurous spirit of the computer programmer. An elaborate review might be in order.

### **Upside down in a Flat World**

Cut-throat competition from global players and the falling dollar have squeezed the margins for typical run-of-the-mill work. Yes, consulting is a niche that eventually all Indian IT companies would want to get into. But basic factors like maturity (dearth of experienced consultants), perception (image of application developers and implementors) and location (Failing of global delivery model in primarily client based work) will hinder any real attempt into consulting space.

The trick is to innovate – do things differently, and not necessarily do different things. In that regard, the focus on innovation of some of the top Indian companies is a step in the right direction. Wipro's Applied Innovation framework lays down a roadmap for systemic change to deliver sustainable business benefits. An illustrious case in point is Wipro's **transformational engagement**, with Credit Suisse. In this trailblazing flex-sourcing model, three primary ownership models (captive, outsourced, co-managed) have been employed together in effect to cater to different business requirements. It was a risky manoeuvre which has paid off handsomely.

### **Summing IT up**

This is indeed a tricky time for the Indian IT industry, but there's no real reason to panic. The IT guns showed great character and resilience during the years following the dot com bust. They are wise enough to read the signs and realize that change is in order. With a slight course correction and an unswerving view on the long-term, the India IT industry can emerge stronger and bigger.