Analysis: Indian IT mart booming says NASSCOM IDC

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Information technology isn't simply a big export for the Indian economy. The surge in the domestic economy has meant that demand for IT services within India's own borders is becoming a money-spinner too, including multinationals such as IBM and HP.

Until now, call centers and other technology "has been associated only with export, but there is huge opportunity waiting to be tapped as globalization demands higher efficiencies and competitiveness from Indian businesses," said Kapil Dev Singh, country manager, IDC India, adding, "Domestic demand for IT in India is witnessing a gradual transformation from being predominantly hardware driven towards a solutions oriented approach resulting in a growing emphasis on services."

According to a joint study by NASSCOM, the local IT lobby, and IDC India entitled "Study on the Domestic Services (IT-ITES) Market Opportunity," revenue growth in the services sector has been faster than that for the overall domestic IT market (including hardware, software and services) over the past few years."

Indeed, over the last decade, even as India's IT services sector has grown to be a role model globally for its outsourcing services, the sector has thrived primarily on exports. And unlike China, which has a burgeoning domestic IT market but little exports of IT services, the domestic IT services market was hardly a story worth talking home.

But that seems to be starting to change. "If you look at the trend in the last two years, a distinct awareness of outsourcing seems to be emerging in India," said Rajdeep Sahrawat, the newly appointed vice president of NASSCOM tasked to develop the domestic IT market.

In March 2004, Bharti Televentures, the country's largest mobile-phone operator, created quite a stir when it outsourced the transformation and management of its IT infrastructure to IBM in a $250 million deal entered for five years.

The next outsourcing deal in the local domain came when SBI, the country's largest bank that roped in TCS Ltd., India's No. 1 IT services company, to be its system integrator. Although in money terms -- exact figure unknown -- the deal was not significant, it was the first ever instance of an Indian bank outsourcing a part of its core-banking IT function.

The Bank of Baroda-Hewlett Packard and Dabur-Accenture outsourcing deals followed thereafter.

"It is against this backdrop of the increased interest in the domestic IT services market by major IT vendors that has been fuelled by high value deals, NASSCOM commissioned IDC India to conduct a base line research study," said NASSCOM.

"The liberalization of Indian economic policy, de-regulation of key sectors and progressive moves towards further integrating India with the global economy has been a key driver of increased IT adoption in the country," the study said.

This is best reflected in the fact that most indigenous players in telecom and banking, two key sectors with significant multinational corporation (MNC) participation, have significantly upgraded their levels of IT adoption to offer best-in-class services comparable to those offered by the global competition.

These two sectors together account for approximately 35 percent to 40 percent of the domestic spend on IT services.

The study has projected that over the next five years, domestic spending on outsourced IT services will more than double, from about $2 billion in 2005 to over $5 billion in 2009.

That's hardly a tempting number considering that fact by 2009 exports of services by the Indian IT sector will touch $60 billion.

"Yet it is not an opportunity to scoff at," says Kapil Dev of IDC. "The most important highlight of the study is that for the first time we have been able to estimate as to what is the actual potential of the domestic IT market, which is huge."

The study has estimated that in-house spending on IT services (including training costs, salaries of in-house IT staff and associated overheads) still accounts for more than half of the corporate IT spend in India, while the outsourced/vendor addressed spends account for just 45 percent of the total.

"Therefore," says Kapil Dev, "assuming that $2 billion worth of IT services is outsourced today, the actual potential is at least double than that."

"Moreover, our future revenue projections are based on the growth expectations of just the current verticals" said Sahrawat of NASSCOM. "But as the economy opens up further, new sectors like retail, healthcare, travel will get more exposed to competition and lead to a greater surge in demand for outsourcing services, the quantum which is anybody's guess."

The study said that competitive pressures in more recently deregulated service sectors such as airlines and insurance; the uptake in the manufacturing and industrial sectors; and the several large e-governance initiatives launched by the government under the National E-Governance Plan could provide sustained growth in domestic demand for IT services over the next few years.

Yet another important element of the domestic IT market is that unlike the IT services exports market where price arbitrage plays an important role, the domestic market will be driven more by access to specialist skills and helping businesses to free up their scarce resources for focusing on core business areas.

Nevertheless, there are challenges ahead. "And the biggest challenge is in terms of convincing the Indian CIOs to outsource," says Dev of IDC, "because in India, it still takes a lot of time and effort."

After "undertaking in-depth interviews with CIOs" the study said that it has found willingness to move from an in-house captive sourcing model to outsourcing is very low. "Satisfaction with existing systems, lack of trust in outsourced service providers, high cost of services, unavailability of suitable vendors and lack of skilled personnel (with vendors) are the most commonly cited reasons that pose hurdles for CIOs for looking at outsourcing" it said.

The other problem is a lack of favorable policy environment to achieve its potential. "For instance the imposition of the 8 percent excise duty on software and services in the recent fiscal budget (announced on February 28) could puncture growth," said Kiran Karnik, president, NASSCOM.