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India

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Introduction

India's IT and BPO sector has grown in the last decade or so, from about 1.1 per cent share in global services exports to about 2.6 per cent. So it has more than doubled its share in services exports, which is a phenomenal growth rate.

How come the Indian IT and BPO sector has done so well? One critical element was that there were several Indian entrepreneurs in global IT firms and multinational companies who were dealing with the IT and BPO work for those firms and they saw an opportunity in India. They saw the factors present in India that would enable the sector to take off. This happened in the mid-1980s.

The second thing that happened was a big move towards global cost cutting in the 1980s and 1990s. Global companies and multinational corporations wanted to reduce their operating costs, and that phenomenon continues. Given the competitiveness that has ensued, even a small margin of price and value can make a difference. The third factor was the technology. We had the digital revolution in the 1980s, which meant that the cost of communication and digitising information fell; it used to be much higher in the 1970s and 1960s. In the 1980s we saw a drastic drop in those costs, making it possible for the first time to do things offshore.

There were two other significant developments. One was the liberalisation experience in India, which people mistakenly think started in the 1990s. In fact, it started much earlier in 1984/1985 when Rajiv Ghandi was India's Prime Minister. Many reforms in the IT sector were put in place and liberalisation took off, enabling companies to come in with all kinds of new ideas. The other element is human resources. Part of the story goes back paradoxically to India's need for self-reliance, starting in the 1950s. India always believed in the importance of institutions in creating the skills for itself, so there was enormous investment in engineering schools and other kinds of science and technology centres, especially in the southern parts of the country, which produced the particular human resources needed for the IT sector. Many people often forget the major role of the state in setting up the engineering colleges that produced a very large pool of talent as an indirect result.

We should highlight the role played by the Indian entrepreneurs in coming back to India and seeing all these elements were in place recognised that India provided a great cost position for them to start up IT and BPO outsourcing. That is what provided the key to the Indian IT sector taking off. One good example is Raman Roy, Chairman and Managing Director of the global services company, Quattro,¹ who came back to Delhi in the mid-1980s with Amex when it started its Japan and Asia Pacific operations, BPO service and IT support service, in New Delhi.

India is still on its IT-BPO journey as it tries to capture the higher end of the value chain. For example, in financial services Hong Kong and Singapore have far greater shares of global trade because of the historical advantage they have in terms of brand liquidity and links with the rest of the world. There are several areas where India is lagging behind but catching up fast, so the Indian IT-BPO story is not yet over. There are many miles to travel and many places to go.

Industry statistics

Market share

The industry has shown resilience and in 2009/2010 grew by about 5.5 per cent. Exports contributed the majority share accounting for about US\$50 billion while the domestic market was about US\$23 billion. In total, we closed at about US\$73.1 billion. In spite of the difficulties we faced in 2009, the industry brought 90,000 jobs into the country, which will take total industry employment to about 2.3 million direct employees. Our research confirms that for every direct employee in the industry another four downstream indirect jobs are created, which puts the indirect employment that has been created by this industry at about eight million.

The US continues to be the single largest market, constituting about 61 per cent of all exports and the UK and Europe together constitute another 30 per cent, so about 91 per cent of all exports go to the US, the UK or Europe. This has been changing over the past few years: the US used to account for 80 per cent of the market. However, it is still not representative of the world and there is plenty of scope to move towards exploring other markets such as Japan, Northern Europe and the Middle East.

Industry sectors

Looking at the sectors that the IT-BPO industry in India serves, banking and financial services followed by telecoms and manufacturing constitute about 75 per cent of the share. Other emerging verticals that we see are health care, retail, and the public sector, but currently the success story, or the majority of the business, is derived from banking, financial services and insurance, manufacturing, and government.

2008/2009 was very difficult for the industry, which had been growing at more than 13 per cent year on year for more than 10 years. Suddenly global markets were going through a downturn, customers were not renewing their orders or taking a long time to renew, existing contracts were being renegotiated, there was huge pricing pressure and more work was being demanded from the industry for contracts that were already signed. Two things helped the industry to grow in spite of this downturn (indeed, it was one of the few industries in the world that grew in 2009). One was the domestic market. The structures and the vibrancy of the Indian economy supported the industry and the domestic market grew at a double-digit rate. The second stemmed from the rapid growth rate in the industry in the previous 10 years, when companies tended to activate a lot of plans. Since they had orders coming in there was no demand constraint, but there was a supply chain constraint and companies were planning to expand in terms of human and capital resources. Therefore, over a period of time companies built up a great deal of unnecessary infrastructure, which gave them an opportunity to look internally and to refocus their priorities on where they could get business from as well as how they could serve this business productively. In fact, some of the Indian companies had record profits in spite of not having significant growth in terms of revenue, because they looked internally, cut down the fat, became more productive and invested in the infrastructure required. These are the two factors that helped India weather the financial storm of 2008/2009.

Unemployment

One constant concern in key markets is whether the IT-BPO industry causes unemployment due in particular to the fact that it works on the offshore delivery model. The large slowdown in most major markets, especially the US, UK and Europe, gave rise to questions about whether unemployment was being caused by the IT-BPO industry and how that could be addressed. We were concerned about whether this would make governments overseas become protectionist and start coming out with legislation or regulation that would hamper the industry. We worked extensively on this and have a team that continues to work with key policy-makers around the world. We are happy to look back and see that sanity prevailed and there was no major restrictive legislative or regulatory action anywhere in the world. However, in this period before employment picks up in the US, the local populations are putting pressure on the elected representatives to do something about unemployment and they do not have an answer, so they have to look at what other responses they can give to their local population.

Changing demographics

Having said that, if one takes a slightly longer-term view, 10 years from now there is going to be tremendous movement in terms of demographics and economics across the world. Large geographies such as Japan, Germany and Spain are undergoing

demographic shifts in that their populations are ageing. In the coming decade there will be an absolute decline of 7 per cent in Japan's population. Spain and Germany are not at that level, but they are going down the same path. Even the US, which will have a net addition to its population, will still have a larger population retiring than is in the workforce. Across the developed world the productive workforce aged between 21 and 59 is diminishing and this is an opportunity for countries such as Mauritius and India – young countries – to see how they can fit into the global world order and provide the amount of services required.

Economic shift

The global downturn has shown that the centre of economic growth is shifting east and more and larger business opportunities are coming from markets that are not traditional ones. India's telecoms success story is a prime example. India adds about eight million mobile connections every month. This is by far the largest absolute market in terms of growth across the world, but this market is very different from the market in Europe or the US because the average revenue per user is 1 per cent or 2 per cent of what it is in the US. However, companies are still profitable and able to serve this market because they have a business model that is very different from the traditional telecoms business model. Therefore, if we are to serve the new and growing geographies, such as China, Korea, India and Malaysia, there is a need for new business models to be developed that can tap this opportunity.

Growth to continue

All in all, the industry is very optimistic that India's growth story will continue. In fact, a NASSCOM study projects that exports will increase from US\$50 billion in 2010 to US\$175 billion by 2020. India continues to be a destination that will be part of this IT-BPO growth story for the following reasons:

- The talent pool and the education infrastructure are in place;
- The costs of working out of India continue to be very competitive in the rest of the world because there is scale available;
- Companies are moving up the value chain, so they are able to provide more services at a competitive rate and cost;
- Over the past 10 years companies have developed robust processes to enable employees to carry out a significant part of work that used to require consulting experience;
- As the Indian market continues to grow it provides more and more stimulus for the industry;

- The acceptance of the Indian consulting story across the world has helped the industry to grow.

Lessons

What messages are there for those Commonwealth countries that have yet to jump into the business? We can start with the basics, the availability of finance for this particular business and the encouragement of entrepreneurship through various policies. These are the government policies that need to be looked into. This was done very well in India and is one of the reasons that enabled the Indian IT industry to grow. In addition, there needs to be skilled people and language proficiency. In India we have technical education, and language has played a very positive role. As the population in urban cities is largely English speaking, the education in public schools tends to be more English-oriented. We now have emerging markets that we want to cater to and, accordingly, we need to work on language proficiency.

Certification played a very important role. India was one of those countries that had the maximum number of ISO-certified companies, because being a developing nation we knew that the developed countries were concerned that we might not do a good job quality-wise. There are very good laws on quality certification and security certification and companies have been forthcoming in these areas.

The basic requirements for success are as follows:

- A business environment that is conducive to industry needs, with the onus on infrastructure (e.g. telecoms infrastructure) and licensing. This requires government regulatory bodies to work very closely with the industry, understanding the challenges, needs and requirements as they come along.
- Workplace policies, such as requirements to work night shifts or in a general security environment, are very important.
- Social awareness creation to combat certain stigmas related to particular jobs. For example, the debate on call centres typically focuses on whether it is knowledge work or marketing work, or whether the younger generation is being encouraged into slavery rather than to study and do PhDs. The industry and government should take responsibility for this kind of awareness creation, arranging training from bodies such as NASSCOM and CII, which have been working very closely with the industry. Indeed, within universities the programmes for ITES education have also progressed, so students with potential can be picked up and trained accordingly.

Challenges

When a country sets out to establish an IT industry, it is likely to face the following challenges:

- Very strong employee attrition;
- Scalability;
- Rising operational costs and decreasing margins while the industry is growing;
- Data security;
- Storage infrastructure management;
- Disaster management: identify distant geographical locations that are available for use in emergency situations (tsunamis or earthquakes or terrorism or other such periodic environmental/political crises);
- International bandwidth and telecoms connectivity, which is very important feature.

Niches

Ultimately, every country needs to assess the positives in its own market since the IT-BPO global sourcing market is very big. In India there has been phenomenal growth in the telecoms area, some manufacturing and high tech, banking and finance, knowledge development and BPO. But while it may enjoy the largest share of the global sourcing market, the ratio of the total market size compared to its exports is less than 10 per cent. So there is plenty of room for growth and each country can participate in this. In fact, the more countries that can participate in it and make it more secular the larger the rate at which the global sourcing market will grow.

However, each country needs to find its own niche, its own speciality. For example, the speciality for Mauritius is its bilingual population. The French market is one that the Indian industry has not penetrated or been able to succeed in at the rate at which it has succeeded in the English-speaking market. Mauritius has that strength and should play to it. Similarly, each country can identify its strength and play to it rather than becoming a 'me too' to the bigger service providers across the world, like an IBM or an Infosys. This country perspective also applies within the industry. In the Indian IT industry, the larger companies are growing at a faster rate than the smaller companies, because the smaller companies are not able to compete with the larger companies when it comes to economies of scale and operations across the world. The only smaller companies that are growing fast are the ones that decided to specialise.

One could decide to specialise in a particular geographical region, like the French market, for example, or a particular service line, like having a centre with excellent telecoms connectivity and infrastructure that data centres could look at. It could even

be with respect to a specific vertical. For example, Sri Lanka has a disproportionately high number of chartered accountants compared to the rest of the world, so maybe something in the insurance or accounting industry could be the specialisation for Sri Lanka.

The idea is for countries to look internally at what their strengths are, specialise in that strength and be a part of the global dynamic. The Philippines has recently done exceedingly well in English-speaking call centres, with call centres growing faster than they have been in India. The growth is coming from global clients, but also from a lot of Indian companies that are relocating their centres from India to the Philippines. This is excellent, because that will help the entire ecosystem to grow. If the strengths are in the Philippines compared to India then companies can invest and go there as well. Therefore, it is advisable for individual countries to look at what their strengths are and then target not just the end customers but also the large service providers to set up operations. That will make the country grow much faster.

Entrepreneurship

We must emphasise the role of private entrepreneurship in overcoming the initial hurdles posed by the poor quality of infrastructure. Infrastructure continues to be a big challenge, whether in terms of the traffic jams or the power demand. In India, the government has given a free hand to the entrepreneurs and the industry has not been heavily regulated. The entrepreneurs sensed the opportunity and looked at what could be done. So most of the BPO firms that are present in India generate their own power whenever power fails. For instance, in the IT-BPO hub outside New Delhi in a suburb called Gurgaon, there is no power for more than 12 hours a day, so it is captive power units run by the IT and BPO firms that provide power. The same is true for transportation. Most of the companies have very intense Six Sigma-level taxi management services to get their employees to the office and back home again. At Six Sigma level there are 500 taxicabs waiting outside a BPO, each working to ensure on-time performance, maximum fuel efficiency, and that the load of each taxi is not below a certain limit. There is no public transport, so it has to be done this way. In education, the firms did a lot of in-house training to prepare talent for the global market. What the Indian universities provided were language skills and the basic analytical framework, but the firms developed internally the specific skills sets needed for servicing this market. Hence the entrepreneurs have played a very important role and that has led to the companies and the industry growing and succeeding.

Another very important point relates to the linkages that Indian entrepreneurs had with global markets from the outset. Many of the firms that were started in India, whether they were third party or multinational companies coming back to invest in the economy, were led by Indians who were based abroad and had already acquired experience in this field. India gained a unique advantage from having a Diaspora

that was so well networked in the global IT and BPO sector. This is not going to be true for many of the African nations perhaps, in which case they should look to the services providers in mature countries like India or perhaps within Europe and get them to relocate to their countries to offer those services. That is going to be critical; foreign direct investment will play a very important role in ensuring the success of an ITO-BPO sector for these countries.

Public-private partnerships

There were some initial public-private partnership investments made in the 1970s and early 1980s when the hardware segment of the industry was taking off. They were not very successful. There were some success stories, such as HCL, which benefited from some public partnership, but that was purely in the hardware sector. However, it did create some critical skills that were later adapted by the IT-BPO industry. For the most part though, the industry was led by the private sector and, at least in the initial stages, there was not much public investment. In fact, it is often said in India, 'The best thing that the government did with the IT-BPO sector was not to do anything with it at all.' There was no government industry promotion policy or anything of that sort; it grew naturally under its own entrepreneurial steam.

However, there were some government projects and schemes that came later, in the mid-to-late 1990s and continue today; the Software Technology Parks of India (STPI) is one such development scheme and there have been some others. The government has also now taken on board the industry's concerns about the skills shortage and there have been some initiatives there. But private sector leadership has been one of the main reasons why the industry has succeeded so well, because more than any other it needs flexibility to adapt very quickly to changing global situations and it would not be amenable to a five-year plan.

It would be true to say that this has been a private sector success story, but the government has played a very significant enabler role. There have not been any formal partnerships in the industry, but the government has provided an enabling environment in terms of tax policies, encryption, data security and information security policies, and the education support that is required. This approach has proved to be successful in India's case.

Venture capital

On the question of attracting venture capital there is a very simple answer: money flows where there is opportunity. There was no significant government policy to promote venture capital. In fact, the government used to run a number of venture firms that were not utilised for many years. It is the domestic growth along with the success of the industry that has opened the floodgates for venture capitalists to come

in; they see an opportunity and they come in. There is more capital in the world today than ever before and that capital chases the opportunities, which are growing because the traditional markets such as Europe, Japan and the US are not growing. There is de-growth over there, so the venture capitalists have to look at emerging markets for opportunities and that is why they are moving here.

Although the government did nothing in terms of policy on venture capital, it does have an interest. For instance, it created a task force on IT that involved some of the venture capitalists from the US who would make regular visits to India and interact with both the government and the industry. There is a company called Citigroup in India, which played a positive role in providing much of the initial seed funding to many of the IT companies. Citigroup had a scheme whereby it would identify those entrepreneurs who were creating waves and establish a promotional stake with them. A company called I-Flex is one that has grown because of this scheme. There is also some focused venture capital available through government funding agencies. When these companies want to develop they put venture capitalists on their boards to evaluate such entrepreneurship and, as mentioned above, that is how money came in.

To sum up therefore, government can encourage venture capital but this cannot be done on a formal basis. It is also smart to allow multinational companies to come in and do some handholding.

India and Africa

Many of the national member companies have invested in Africa, though largely the involvement has been with northern Africa. Investments have gone into Egypt, Morocco, Tunisia and Algeria. In some of these locations our customers as well as our own member companies have set up development centres and we have some level of interaction and agreements. With Egypt, for example, we are working to see how we can co-operate and work together. It is difficult to generalise for one large continent as such, but we work on a number of mutually beneficial models with various countries, largely at the level of IT assembly. Large companies have the resources and the teams to go ahead and do the evaluation and development in a particular country, but the small and medium-sized companies prefer to work under a platform such as NASSCOM and to interact with their counterparts. Thus we have a fair number of delegations interacting and spending time in other companies.

Tier II and III cities

Developing tier II and tier III cities has been a challenge. It must be acknowledged that India has not been successful in getting tier II and III development to the desired level. About 91 per cent of all business in the IT-BPO industry in India takes place in just six cities. India is a very large country and the rest of the country accounts for only 9 per

cent of the business. Typically, since many of the large cities in the tier I category have educational hubs, the supply of talent is concentrated there as the graduates pass out of the university system. That is one challenge.

The second challenge is infrastructure connectivity, availability of international airports, telecoms and power connectivity. There is also a social challenge we struggle with: the tier I cities have all the amenities required by industry employees – schools, hospitals, shopping complexes, movie theatres – but these are not available in the tier II and tier III locations. This social infrastructure needs to be developed in tier II and tier III locations to attract people to run the offices and developments when they are set up. We are working with the government on this important challenge to ensure that these social aspects are put in place.

Note

1. Raman Roy founded Quattro in 1992 and it now has more than 220 enterprise clients, 9,000 small and medium enterprises and 300,000 individual customers around the world.