Top IT Vendors Lower Guard to Bag Big Contracts, Stay in Game

Cos are increasingly spending upfront on deals, accepting delayed payments by customers

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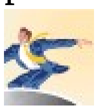
Varun.Sood @timesgroup.com Bengaluru: India's top IT outsourcers, including the traditionally conservative Infosys and Wipro, are becoming increasingly risktaking as they chase commoditised contracts. While cut-throat competition is giving more bang for the buck for customers, technology vendors are risking future cash flow and locking up resources, say experts.



Delayed ' risk on fees' or milestone-related payments have become a norm in the IT industry, while bank guarantees that the vendors need to provide upon winning projects have increased to as much as a fifth of the deal value from 5% in the past. The aggressive pricing strategy being adopted by the IT companies and their promise of value-added offerings to win contracts have made customers cautious and they want to see results before paying up, say industry trackers.

"In the last year-and-a-half, we have seen customers holding back the risk-on-fees which we normally get upon completion of certain milestones," said a bid manager working with a large IT company and is based out of Noida. "Across industries, we have seen customers holding back this money which they normally give more in a staggered manner than at the time when payments are due."

Indian firms play the pricing card often these days as they battle with global majors like IBM and Accenture to win bread-and-butter outsourcing deals, experts say.

"In earlier years, the top Indian IT services firms generally avoided heated price competition with each other. But the IT services industry has definitely become more competitive, and today I see certain Indian firms actively pursuing price-to-win strategies," said Rod Bourgeois, head of research at USbased DeepDive Equity Research.

Some of these strategies include vendors coughing up money upfront as they sweeten the deal to win large contracts. Wipro, for instance, spent $195 million to buy the IT unit of ATCI as part of a $1.2 billion recent outsourcing deal with the Canadian utilities company. To be sure, operating margins of the homegrown IT outsourcers have significantly improved over the past two years. One of the biggest cost components for IT companies is manpower, and technolo- gies like artificial intelligence and automation for completing repetitive low-end work have helped them cut down on this cost. Still, delayed payment by customers and upfront spending could prove to be an issue in the event of turbulence in the markets these companies op- erate in, or if the customers face financial troubles. Promising tough-to-achieve milestones is another problem that could affect expected cash flow.

“A pricing trend I've seen is Indian firms taking on more risk by tying more fees to contractual milestones — milestones that in a number of cases are tough to predict and achieve, especially as work assignments get more complex,” said Bourgeois. “This trend tends to occur on deals in which the client is large and experienced with outsourcing contracts and on deals in which an outsourcing adviser is helping the client with vendor selection and pricing.”

A senior executive at Wipro, the nation’s third largest software exporter, confirmed the trend but said it was more a function of maturity of the deal and depends on how effectively a customer was able to negotiate with an IT vendor. “Agreed, more customers nowadays are holding back fees in some industries but then this is more a function of what kind of contract it is. As more customers mature in their use of outsourcing and are able to manage their IT vendors, they will explore different models,” the executive said.