Everest Group
RESEARCH

Market Vista™ : Select Findings Q1 2017

January – March 2017

Everest Group
MARKET VISTA™

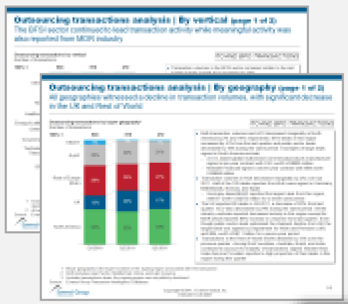
EGR-2017-8-E-2168

Market Vista | Overview

Covers global services market research, analysis, and insights to demystify the market and direct clear, impactful decisions

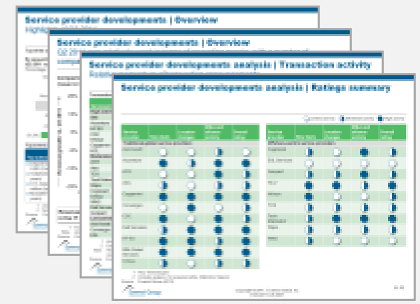
Overall sourcing market

- Detailed analysis of trends by industry vertical and geography
- Report of transaction volume, size, and momentum
- Perspective on events with significant industry impact (e.g., M&A)
- Implications of regulatory changes



Service provider landscape

- Updates on service provider market share, capabilities, and performance
- Service provider profiles, including data on:
  - Transactions
  - Location footprint
  - M&A activity



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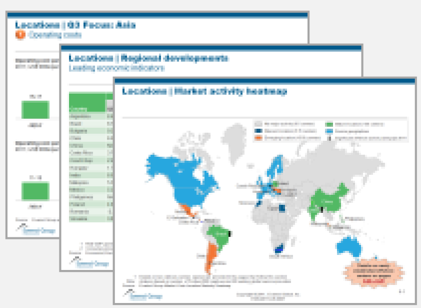
Location data and dynamics

- Data on market activity in key offshore geographies
  - Political
  - Macroeconomic
  - Promotion incentives
- Trends in wage inflation, attrition, and arbitrage



Processes and models

- Process-level trends
- Global In-house Center (GIC) set-ups, divestures, and overall trends
- Fact-based insights on adoption of emerging pricing models
- Data and perspectives on new opportunity areas

Quarterly report | Primer | Location database | Breaking viewpoint | Location insights e-newsletter | Industry trends

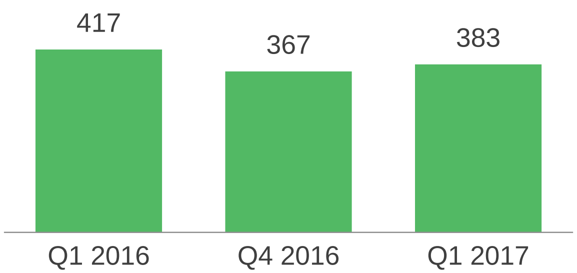
Global services | Key market trends in Q1 2017

1. While the overall outsourcing demand remained steady, there was a significant decrease in demand in United Kingdom given the uncertainty with Brexit
2. GIC setup activity continues to remain high, led by engineering/R&D services
3. Increase in delivery center setups in Asia Pacific relative to Nearshore Europe, reversing the previous year's trend
4. Service providers have acknowledged the uncertainty due to the U.S. visa reforms and have increased local hiring and overall onshore leverage to safeguard their businesses, especially in IT services
5. Rotating from arbitrage-first to digital-first leading to fundamental changes in talent and service delivery models of leading providers

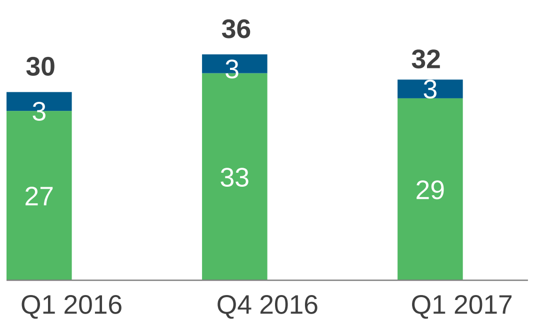
Key market indices – Q1 2017

Outsourcing/offshoring market overview

Increase in outsourcing demand compared to the previous quarter
Number of outsourcing transactions

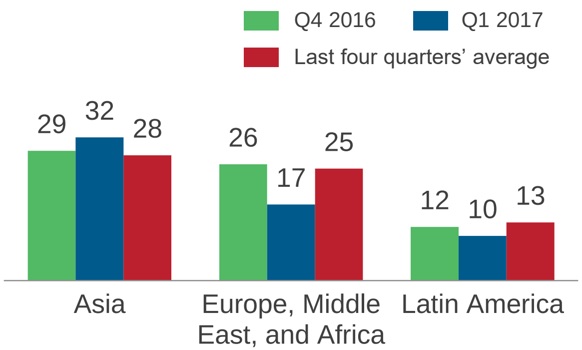


The overall GIC activity continued to remain high

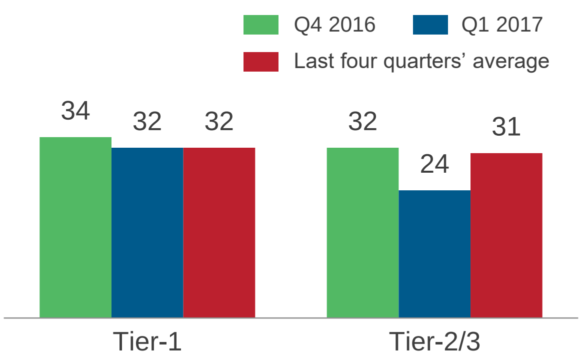


Location dynamics

Increased activity in Asia, while Europe witnessed significant decline
Number of offshore delivery center setups

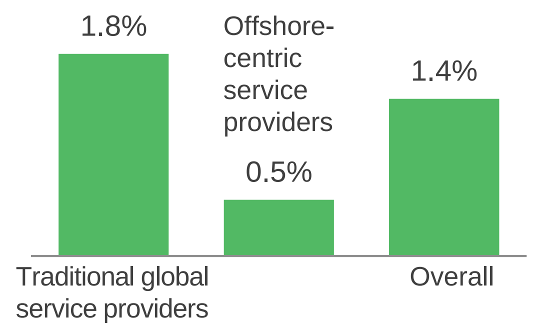


Share of tier-1 locations was higher than tier-2 locations
Number of offshore delivery center setups

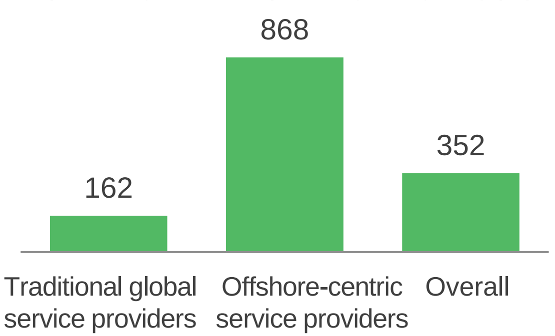


Service provider developments and trends

Both traditional global service providers and offshore-centric providers reported sequential increase in revenue
Sequential growth in revenue (percentage)



Operating margins for both traditional global providers as well as offshore-centric providers increased during the quarter
Sequential growth in operating margins (bps)



Summary of key developments in Q1 2017 (page 1 of 2)

Transaction activity increased in Q1 2017 with 383 deals, compared to 367 in Q4 2016

- Activity in the outsourcing market witnessed a notable increase owing to significant rise in ITO deals, while BPO transactions declined over the last quarter
- The healthcare and technology & communication vertical saw an increase in volume of transactions, while the energy & utilities sector reported a decline in number of contracts vis-à-vis Q4 2016
- Outsourcing activity across North America increased significantly; however, there was a decline in the number of deals across Europe
- The volume as well as share of renewals / restructured deals increased over the last quarter
- Volume of very short-term deals (zero to three years) increased considerably, while contracts with short-term (three to five years), medium-term (five to seven years), and long-term (more than seven years) duration declined over the last quarter
- Demand for application outsourcing services remained high throughout the quarter; however, datacenter, network, and desktop services witnessed a decline in adoption vis-à-vis Q4 2016

GIC market activity declined in Q1 2017, with 29 new setups, three expansions, and no divestiture

- Overall, the GIC set-up activity decreased as compared to the previous quarter, with a significant decline in activity in Europe
- Leading companies, such as Boeing, Deloitte, Ericsson, Etihad Airways, Microsoft, Royal Dutch Shell, and Salesforce, announced new centers

Summary of key developments in Q1 2017 (page 2 of 2)

Location activity in Q1 2017 was significantly lower as compared to the previous quarter, Nearshore Europe witnessed decline in center setups; activity in tier-1 locations was higher than tier-2 cities

- Location activity in Q1 2017 was significantly lower as compared to the previous quarter. There were 59 setups in Q1 2017, driven by Asia, with growth in India and Singapore. Europe witnessed a significant decline. Activity was equally driven by both GICs and service providers with similar number of setups
- Key location risk/opportunity trends for Q1 2017 include – IT-BP firms likely to face challenges, as multiple onshore geographies make immigration and work visa rules stringent; uncertainty around Brexit leading to delayed decision on center setups in UK; service providers increasingly investing in onshore locations for building/delivering new capabilities; and recent changes in the United States trade policies may affect Mexico's attractiveness as an IT-BP delivery location

Most service providers reported sequential growth in revenue

- Operating margin increased sequentially, while it declined on annual basis for both traditional as well as offshore-centric providers. Revenue increased for both offshore-centric service providers as well as traditional service providers
- Both, the overall transaction activity as well as share of Market Vista Index service providers increased in Q1 2017 as compared to the previous quarter
- Overall M&A activity increased, attributed to growth in acquisitions from traditional service providers. On the other hand, offshore-centric providers contributed to increased alliance activity, compared to the previous quarter
- Overall location activity for leading service providers increased as compared to the previous quarter, attributed to an increase in activity for offshore-centric service providers

Key trend to watch (page 1 of 2)

Service providers are increasingly making digital investments to improve efficiency and adapt to changing market dynamics…

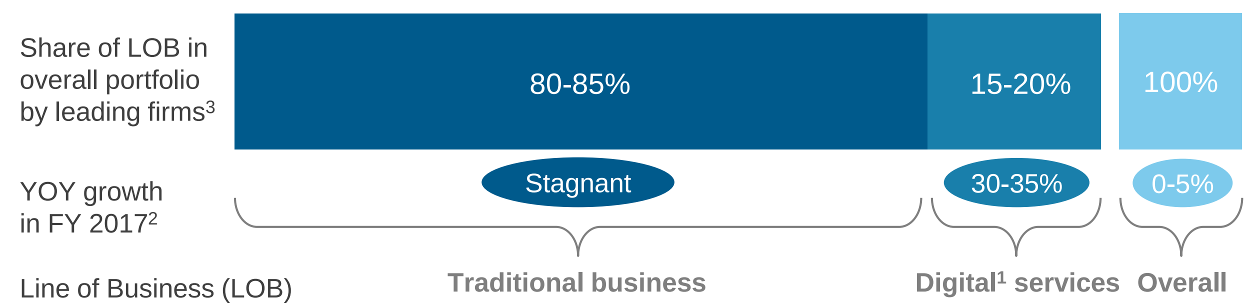
Significant digital[1] investments in FY 2017[2] by leading providers[3]

~40 Acquisitions	Firms followed the inorganic route and made tuck-in acquisitions to develop capabilities and bridge gaps, especially in newer areas such as service design and user experience design
~140 Alliances	Service providers collaborated with technology providers and startups to deliver a broad spectrum of digital capabilities, leveraging platforms offered by startups to build digital solutions
~35 New centers	Firms set up design studios and digital pods to help clients rethink digital strategies; the United States and India emerged as leading locations

Digital focus cannibalized traditional business

Many service providers witnessed sluggish revenue growth in their legacy business, while their digital business grew remarkably

- Increased focus on next-generation technologies pulled away investments from traditional business, thereby limiting growth
- Increased investment in cloud services cannibalized the traditional infrastructure business
- Demand from enterprises for next-generation services increased
- Digital-focused deals increased nearly three-folds in FY 2017, with cloud application and analytics forming a major portion of digital deals



Transition from traditional services to the digital model led to deceleration in the overall revenue growth of the service providers in FY 2017

1 Digital includes social, media, analytics, cloud, cybersecurity, blockchain, Internet of Things, and automation
2 April 2016 to March 2017
3 Index includes digital revenue for Accenture, Atos, Capgemini, Cognizant, DXC Technologies (merged entity of CSC and HP ES), HCL Technologies, Infosys, TCS, Tech Mahindra, and Wipro

Key trend to watch (page 2 of 2)

…however, 'digital dip' in some enterprises may result in uncertain digital business for service providers

Enterprises are running digital initiatives at varying levels of scale and maturity. However, not all of them succeed due to the hindrances in realizing benefits from digital initiatives. **More than one-third[1] of enterprises are facing challenges** in scaling and earning payback from digital investments.

This may lead to a phenomenon called **"digital dip"** where digital initiatives begin to stall after the initial success, which is attributed to initial enthusiasm and high level of investment. It requires a fundamental need for digital initiatives to be more closely aligned with the business requirements. It is, therefore, imperative to take into account subsequent process alignment and management changes, post the technology initiative.

Inability to deal with this phenomenon can lead to failed implementation as well as a longer term investment crisis and stillborn digital transformation.

Some considerations for service providers:

- Service providers may help enterprises avoid digital dip by helping them undertake subsequent processes and management changes, along with direction on strategic objectives and effective stakeholder engagement
- Following a balanced approach and evaluating the cost-effectiveness of digital investments may help providers reduce the risk of sunk investments, in case the overall IT demand falls

1 Based on research with more than 200 global enterprises

List of Market Vista Index service providers

Traditional global service providers

accenture High performance. Delivered.

Atos

Aon Hewitt[3]

Capgemini CONSULTING.TECHNOLOGY.OUTSOURCING

CONDUENT[5]

CONVERGYS Outthinking Outdoing

CSC

Hewlett Packard Enterprise[2]

IBM[4]

NTT DATA[1]

UNISYS

Offshore-centric service providers

Cognizant

EXL

GENPACT

HCL

Infosys

Tech Mahindra

TATA CONSULTANCY SERVICES

WIPRO Applying Thought

WNS Extending Your Enterprise

1 NTT Data acquired Dell Services and the acquired entity is now called NTT Data Services
2 HP Enterprise Services (HP ES) is the global business and technology services subsidiary of Hewlett Packard Enterprise (HPE)
3 Aon acquired Hewitt in October 2010. The combined entity is now called Aon Hewitt
4 The services division of IBM is referred to as IBM Global Services (IBM GS)
5 Xerox spun off its business services division to create Conduent

Additional research recommendations

The following documents are recommended for additional insight into the topic covered in this report. The recommended documents either provide additional details on the topic or complementary content that may be of interest:

1. **Market Vista™ Q4 2016** (EGR-2017-8-R-2091); 2016. This report summarizes the key trends and developments for Q4 2016 in the global offshoring and outsourcing market

2. **Market Vista™: 2016 Year in Review: Global Services Industry Facing "Winds of Change"** (EGR-2017-8-R-2138); 2016. This report gives an overview of the developments that took place in the global services industry in 2016

3. **Impact of Changes to H-1B Visa Program on Service Provider Margins** (EGR-2017-8-V-2149); 2017. The proposed visa reforms and greater scrutiny of H-1B visa applications is impacting IT services firms (especially offshore-heritage providers) that have been the largest beneficiaries of this visa program. Almost 60% of the approximately 85,000 H-1B visas in 2016 were granted to these providers. These visa reforms, if passed, will impact the delivery structure of outsourcing service providers extensively, and consequently, their margins. In this viewpoint, we have explored the impact of proposed H-1B visa reforms on the overall margins of IT service providers, especially offshore-heritage providers

4. **Buyer Geography and Industry Trends reports:** Trends for Q4 2016. These reports provide data, developments, and insights on outsourcing and offshoring trends for a particular buyer geography / industry. These reports provide the research and analysis that enable users to navigate through complexity and make clear, effective decisions suited to their focus region or specific industry. These reports provide detailed information on transaction activities, Global In-house Center (GIC) developments, service providers' market shares, and key outsourcing transactions. Regions covered include: the United States and Canada; Europe; and Rest of the World. Industries covered include: Banking, Financial Services, and Insurance (BFSI); Manufacturing, Distribution, and Retail (MDR); Energy & Utilities (E&U); Healthcare; Technology; Telecom; Public Sector; and Travel & Hospitality

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