

IT SERVICES

19 May 2020

Takeaways from Gartner IT spending quarterly outlook

As the coronavirus continues to spread, Gartner now expects worldwide IT spends to decline 8% in CY20 vs. growth of 5% forecast earlier. Per its quarterly outlook, consulting and implementation services will be the worst affected as clients defer discretionary spends. Covid-19 has also triggered a shift in tech budget focus from digital transformation to cost reduction. Gartner forecasts prolonged weakness for BPO services due to automation and insourcing. Vendor consolidation and M&A would gain pace, putting larger players with diversified verticals on a better footing.

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Tech spend estimates slashed: Amid the continued spread of the pandemic, Gartner has revised its CY20 tech spending outlook and now expects a 7.7% YoY decline in global IT services spend vs. 5% YoY growth earlier (in dollar terms).

Consulting to be worst hit: Out of the four service lines, Gartner expects consulting and implementation services to see the highest decline of 10.5% each in CY20. As many as 25% of firms surveyed by the research agency (sample of 317 leaders) have already frozen their consulting & contractor spending while 20% have delayed implementation. Managed services are forecast to contract by 2% and BPO by 4.9% YoY in CY20.

Cost reduction a dominant trend: The pandemic has triggered a shift in technology spend focus from digital transformation to cost reduction, with 46% of the CFOs surveyed by Gartner across industries expecting 10-30% revenue contraction. About 65% of surveyed CFOs plan to suspend at least some or all long-term IT investments. The survey revealed that (1) 49% delayed capex spends, (2) 25% put consulting on hold, (3) 23% delayed payments to suppliers, and (4) 20% delayed implementation.

BPO to suffer prolonged weakness: Based on initial client surveys and feedback, Gartner expect IT spends to stabilise in Q3CY20 and recover in Q4CY20. The agency expects the BPO service line to face hurdles when the industry bounces back due to increased preference for automation and insourcing. Moreover, in instances where transition to remote BPO operations proved challenging during lockdowns, clients will actively evaluate the possibility of alternatives.

KEY RECOMMENDATIONS

Ticker	Price	Target	Rating
INFO	670	730	ADD
WPRO	184	160	SELL
HCLT	519	650	BUY
LTI	1,668	2,230	BUY
MPHL	820	740	SELL
PSYS	520	530	REDUCE

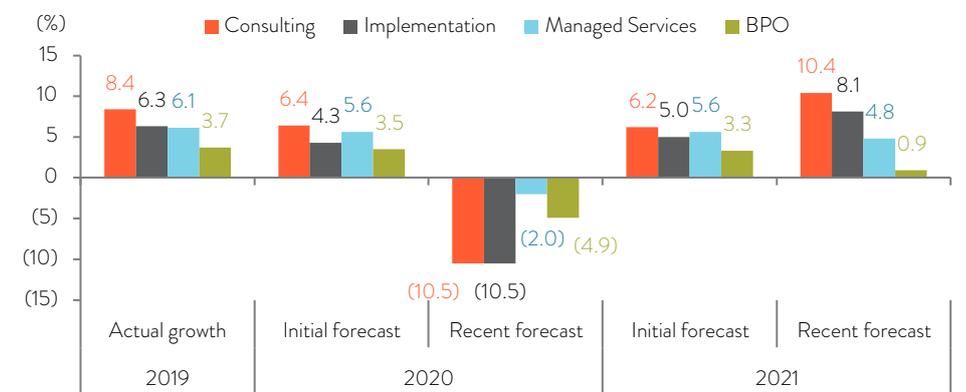
Price & Target in Rupees



Key emerging trends

- Cost-cutting measures:** Gartner’s survey of CFOs and senior financial leaders across industries shows that 20% of the respondents have already deferred on-premise technology upgrades and 25% have frozen consulting and contractor spends. About 23% of clients are delaying payment to suppliers. These trends will have a direct impact on IT service revenue.
- Recalibration of demand:** As per the research firm, the new normal has led to increased demand for services such as (1) cloud capacity to support remote working system needs, (2) mobile managed workplace services, (3) infrastructure utility services, (4) cost optimisation consulting, (5) supply chain management, (6) predictive analytics solutions, and (7) hyper-automation.
- Outlook:** Over the near-term, the outlook is negative for all verticals barring education, public sector, healthcare and insurance. Gartner expects technology spends to stabilise in Q3CY21 as service providers reopen in phases, though clients will continue to focus on cost saving. Industry will see consolidation with increased M&A activity, especially in the mid-tier segment. The demand for captive centres is expected to pick up.

FIG 1 – BPO TO SEE LAGGARDLY RECOVERY



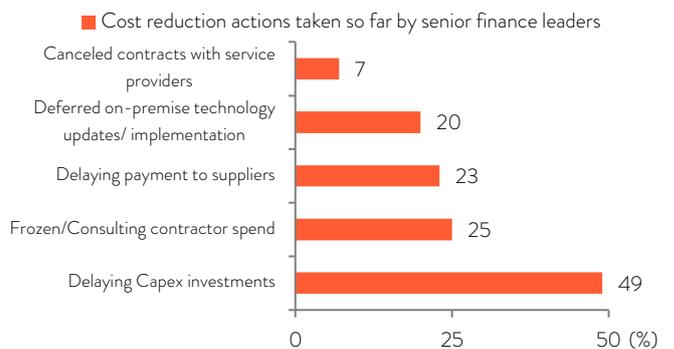
Source: Gartner, BOBCAPS Research

FIG 2 – ~65% OF SURVEYED CFOs PLAN TO SUSPEND AT LEAST SOME OR ALL LONG-TERM IT INVESTMENTS



Source: Gartner, BOBCAPS Research. Note: Survey for investments with a 3 year or longer payback period

FIG 3 – CLIENTS RESORTING TO DELAYED OR DEFERRED ENGAGEMENTS



Source: Gartner, BOBCAPS Research

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Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

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