

## One comes with the other

*Tech companies are mulling linking pay with performance, to boost productivity and cut attrition. But not everyone thinks this will work..*

Adith Charlie

Try your hand at cracking the Indian IT conundrum!

On the one hand, there is a strong pick-up in demand for software services, predominantly from the US.

In order to benefit, the HR teams of IT companies are back to their hyperactive best after a lull of two years. While existing employees are being retained through offers of wage hikes, new ones too are being drawn in large numbers, thereby increasing overall cost overheads.

In the midst of all this, the yo-yoing rupee is reducing the overall profitability of many a deal. While billing rates seem to have stabilised, there are some contracts where pricing cuts have been very drastic.

Another party pooper for the industry has been the Euro, which has dipped by 15 per cent against the US dollar and by 20 per cent against the Indian rupee. As a result, the profitability of many outsourcing engagements has come down.

"If all of these factors continue unchecked, we are not far away from the days when the IT sector will be forced to operate at margins of 2-3 per cent," avers Vishnu Dusad, Managing Director of technology products company, Nucleus Software.

For an industry built on the premises of labour arbitrage and skillset availability, this position is alarming as it gives competition the opportunity to sneak in. Given that manpower-related costs account for over 50 per cent of any IT companies' expenditure, are there any supply side tweakings possible to maintain India's competitive advantage as the preferred destination for outsourcing?

### **eWorld tries to find out.**

Ratan Tata, Chairman of Tata Consultancy Services, recently admitted that his company, and the industry in general, is facing competitive pressures from China, the Philippines and others who are replicating India's cost arbitrage model.

"Five to seven years down the line, when China becomes a stronger player in the IT products and services arena, they will do work at half the Indian rates. If we are not able to control our cost overheads, we will not be able to compete with them," says Dusad of Nucleus Software.

And the pressure on billing rates is already evident, thanks to cut-throat competition, maturity of large procuring companies and the general need to reduce costs. Billing rates on bread and butter IT projects (such as application development, application support, etc) did come down during the economic meltdown.

Smarter outsourcing companies managed the situation well by quickly cutting costs and implementing operational efficiency improvements, during the slowdown, and hence the profitability of new contracts is “probably unchanged”, according to Peter Schumacher, Chief Executive Officer of strategic management consulting firm Value Leadership Group. “In contrast, European IT services firms have been hit much harder by pricing pressure and continue to experience more pricing pressure than the offshore firms,” he says.

Indian companies achieved operational efficiencies on the back of wage cuts, hiring freezes and other cost reductions. However, most of these cost-cutting calculations, going forward, will be upset because of wage hikes and increase in employee costs. Moreover, it is too early to talk about a democratic rise in billing rates

Given the current situation, it is inevitable for the productivity of workforce to go up from current levels, feels Ajoy Mukherjee, Vice-President and Global Head of Human Resources at TCS.

“Either, you get into different offerings and enhance your capabilities to offer high- value services for which you can demand a higher price. If it is some kind of commoditised service that you offer, then you have to improve productivity. So, if it was taking 10 people to keep a ‘lights on’ system functional, you have to figure out how you do it with eight. This will help balance out the pressure on billing.”

(High-end work such as consulting, infrastructure services, and platform-based BPO offer lucrative margins but currently account for a very small proportion of revenues for Indian companies. Billing pressure is more evident when it comes to the bread and butter business of application development and support)

One of the options is to have more freshers on low margin projects, so that overall profits do not come down. In line with this strategy, several IT companies hire more of freshers and less of laterals — another indication of the kind of work they are getting.

Some sector watchers feel that the Indian industry may have to tinker with the compensation structures of their employees.

### **Taking the cue from consulting**

T.V. Mohandas Pai, HRD head and board member of Infosys Technologies, feels that the software firms could take cues from the pure-play consulting industry on how to link an employee's compensation directly to his/her billability. “...the challenge in this industry is correlating high performance to billing rates and that has not happened. We have to come out in the next one to two years to correlating higher payment and higher performance to higher billing rates and that correlation is something that needs to be addressed for the industry to become more competitive, to become more of a consulting industry where compensation will depend upon your billing. We are working on a strategy for that,” Pai said in a conference call with analysts in April.

In a separate conversation with eWorld in May, Pai said: “If an employee is going to be compensated at ‘x’, he/she should be capable of billing at ‘y’ rates. ...if you are billing a higher rate then we should be willing to pay you more”.

(The consulting industry follows a productivity-linked wage system that ensures wage increases are commensurate with higher productivity increases. A management consultant is expected to earn anywhere 6-10 times of his annual salary for the company through his client-facing assignments. Each consulting organisation has a billing target for individual consultants)

PR Chandrasekar, CEO and Vice-Chairman of Hexaware Technologies, likes the idea mooted by Pai of Infosys. However, he is not in favour of trying it out immediately, as “the demand-supply situation is still manageable”.

“Due to the lack of hiring last year, salary expectations are still somewhat manageable. Since we need good people you do not want to create too many disincentives in the minds of these people by being too revolutionary in your model,” Chandrasekar had said after the March quarter results of Hexaware.

Moreover, productivity-linked compensation systems are a tricky affair. On the one hand, tracking every project worker's billing on an ongoing basis is a very cumbersome affair, especially in large projects.

“Within a project, it is very difficult to drill down and find whether a person did something more contributory than the others. In any case your utilisation is 100 per cent once you are engaged in a project,” says Mukherjee. Moreover, people need to have stronger measurement systems in place so that there are no disputes over productivity.

“As is well known, cultures driven by bonuses and incentives can create a lot more harm than good. Objective performance measurement remains wishful thinking,” says Schumacher.

### **Non-monetary incentives**

Another option, according to Sunil Goel, Director of executive search firm GlobalHunt India, is to increase variable pay of mid-level staff.

He is of the view it will raise accountability and motivate the staff to increase their relevance to the company, especially since 10-30 per cent of overall compensation is variable in nature.

However, another school of thought suggests that the failure of Indian offshore firms to think beyond cost and efficiency-oriented employee performance metrics is one of the main reasons for high attrition. Schumacher believes that Indian companies ought to increase focus on non-monetary employee incentives such as mentoring, helping employees create better work-life balances (work-at-home initiatives, flexible hours, onsite child care, etc), among others.

“Without a shift in mindset amongst Indian HR executives, the risks are real that employees will become disenfranchised and see themselves just as cogs in a wheel,” says Schumacher.

Needless to say, a disenchanted employee base always adds to a company's costs.

adith@thehindu.co.in