

IT exports resilient but face new threats

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India's merchandise exports declined 22% in January and February, and the slump looks like continuing. The silver lining is that India's exports of software and IT-enabled services have proved resilient. However, such exports face new threats that should not be underestimated.

The US and UK, which are worst hit by the global crisis, account for 81% of India's exports of computer software and IT enabled services (ITES). Moreover, the largest chunk of Indian IT exports are to the banking and financial sector, which are the worst hit globally.

Yet, early results for Indian IT companies in the January-March quarter suggest only a marginal sales decline over the previous quarter, and substantial growth over the last year. The immediate future of IT is very uncertain. Yet NASSCOM, the apex body of the IT industry, makes bold to project export growth of 30% over the next two years.

A World Bank paper, 'The Resilience of Services Trade', by Aaditya Matto and Ingo Borchert highlights how resilient global trade in services has been even as trade in goods

has plummeted. In February 2009, US imports of goods fell 33%, but service imports fell only 7%. In that month, US exports of goods fell 21% but service exports fell only 6.5%. A similar pattern shows up for countries across the globe.

A range of business and professional exports are actually growing. US data show that imports of professional and business services are actually up 7%, and exports up 10%. This lends credence to NASSCOM's optimism.

Why are IT exports relatively resilient? First, the global credit crunch has hit manufacturers much harder than service providers. Trade credit dried up for goods after Lehman Brothers collapsed last October, but trade credit for IT exports was little affected. Electronically-delivered business services need less trade finance than goods shipped by sea. Manufacturing companies have substantial debt that needs to be rolled over, and this has posed problems to manufacturing companies like Tata Motors and Hindalco. But IT companies like Infosys and TCS are cash rich and have no debt at all. Finally, a significant part of IT exports are sales by Indian branches/subsidiaries of MNCs to their parent firms, and this trade is not finance-dependent.

In recessions, unsold inventories of manufactures pile up, forcing production cuts till the inventories are liquidated. But services

cannot be stored, and do not suffer inventory-driven collapses of demand. Consumers can easily postpone the purchase of durable goods like cars, but corporations cannot postpone purchases of outsourced services like book-keeping and call-centres. US companies can indeed postpone purchases of software products, but not of software services that are essential for business. Finally, NASSCOM hopes the recession will result in even more IT offshoring. In particular, MNCs with existing facilities in India may transfer more work. Borchert and Matto find that such intra-corporate purchases have continued growing at 10%, even as purchases from outsiders have declined to almost zero.

However, this happy picture is marred by protectionist threats, such as the Buy America provisions of recent US laws. Back in the technology bust of 2001, states like New Jersey enacted laws to maximize local procurement of IT services, but these had loopholes, rendering them largely ineffective. But the US mood is much nastier now. Sallie Mae, a company managing \$180 billion in government-backed student loans, is moving 2,000 jobs from India and the Philippines back to the US, although this will raise its wage costs by \$35 million.

The US government has thrown lifelines to several struggling corporations, with im-

plicit or explicit directives to keep jobs within the US and not outsource. In the insurance industry, a sick giant taken by the government, AIG, has reduced outsourcing, while solvent rivals like AXA have not. In the auto industry, outsourcing has been significantly reduced, in some cases by 50%. This owes something to cost-cutting, but may also reflect the desire of auto firms seeking government rescues to keep on the right side of US public opinion on offshoring. The US government has acquired preferred stock in more than 200 banks and financial companies. It may convert much of this into equity, giving it a majority or near-majority stake. This will surely be followed by government directives to slash outsourcing and increase jobs in the US.

Finally, the recession is now certain to become a Great Recession, if not a Great Depression. Dozens of corporations are going to go bust, and the dying companies will obviously no longer outsource operations to India. Indeed, bankrupt US companies may fail to pay Indian service exporters for services already rendered. This may affect the resilience that IT exports have shown so far.

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