Summary Report on the 3rd Annual Globalization of Services Conference

Held on December 7 and 8, 2007

by

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Introduction

On December 7 and 8, 2007, the Third Annual Globalization of Services Conference organized by Rafiq Dossani and Martin Kenney was held at Stanford University. This was a unique conference because, in addition to eighteen senior corporate presenters, nine academics attended the first day and then gathered on the second day with three corporate attendees to discuss the outcomes of the first day. The conference attendance was 116.

This report is divided into two components: The first component discusses the lessons from the conference. The second component reports on feedback we received by email from participants and attendees. A notable point, from discussions with participants and their feedback, is that this conference is becoming viewed as an important event for senior industry representatives to discuss critical, albeit non-confidential, elements of corporate strategy with industry colleagues in a way that is not possible in the usual industry conferences. In the latter, industry representatives tend to discuss industry trends and their own firms' achievements rather than corporate strategy. On the other hand, the Stanford event provides them with a forum in which they can air corporate strategy with the expectation that they will receive serious feedback both from industry colleagues and academics. Apart from the academic and corporate benefits, a consequence of this uniqueness is that the organizers fully expect that the record sponsorship received this year from nine organizations will continue and enable the conference to be self-funding.

The keynote speaker, the president of Satyam America (Satyam is the fifth largest Indian IT firm) noted that a key trend driving the business was that technology enabled more and more remote delivery of services in a way that went beyond writing code. The primary function he was referring to was the design function, such as designing aircraft interiors, construction, and medical instrumentation. These were amenable to substantial remote design work using 3-D and other remote visualization tools.

Despite this, the industry was seeing substantial growth in centers located close to clients. The reasons were several: cultural differences, the need to access government, and to be close to clients. On the last-named, it was not just proximity to understand client requirements but also to provide the client with innovative solutions that they could witness close to their area of operation. This suggests that the industry is moving from the OEM to the ODM phase.

In the first two sessions, the industry representatives explored two issues regarding information technology systems integrators (ITSIs). The first was the development of a global footprint on the part of the Indian ITSIs, and the developed-world MNCs' response. What is plain is that the Indian firms are rapidly establishing new delivery centers around the world and in other low-wage nations. The global reach is necessary as they sign contracts with large MNCs demanding global support. The leader among the Indian ITSIs is TCS, which has aggressively expanded its footprint in Europe, Latin America and East Asia and is shortly to consolidate its American operations in a 1000-person operation in Cincinnati, Ohio. Wipro, a leader in providing R&D services, has announced a similar strategy. Infosys and Cognizant, being more focused on serving the U.S. market from India, lagged

TCS in recent revenue growth despite a similar concentration in BFSI. However, in the past year, they have also been expanding delivery operations outside India. Capgemini, the largest European ITSI, has expanded its Indian operation through hiring and acquisitions. Capgemini's acquisitions of Indian firms made were for the purpose of facilitating its penetration of U.S. markets. In other words, a strong presence in India was a strategy for penetrating the U.S. market. The final interesting outcome of the sessions was that the American ITSIs, particularly IBM, face difficulty in mobilizing their still unparalleled global footprints to offer services globally. To take the case of IBM, many of the IBM operations in developing nations

such as Mexico, Brazil, etc. were meant to service the domestic market. This gave IBM an edge in building out services for the domestic market and strong local leadership teams. However, unlike the Indian ITSIs, whose globalization was designed from the start to serve global clients from India, IBM is now converting these global operations to become global delivery centers. In other words, the global footprint that should be an IBM advantage is an asset that is still to be fully utilized. It should be noted that IBM's presence in India was built to address both domestic and global markets. Over the last 15 years IBM Global Services India has developed a comparable size and scale to the top Indian IT Services firms and has excelled in the domestic arena.

The second question was whether the Indian ITSIs have developed a new business model whose impact on the U.S. ITSIs could parallel the experience of the U.S. Big Three automakers when challenged by superior Japanese rivals. This was not directly answered at the conference. However, the following evidence indicated that competition from the Indian ITSIs was still in the ascendance. First, in terms of their relative standing in the top league of ITSIs, the Indians were perceived by both their western competition and their clients as having arrived. In several areas,

such as financial trading platforms, large-scale contract research and banking software implementation, it is Indian firms who are looked upon as setting the industry standards. Whereas, for example, IBM, as earlier noted, was not yet fully able to effectively leverage its global presence and scale, while the Indian firms appeared to be able to do so. This shows that more than one Indian firm is able to manage scale for global delivery, whereas their western rivals are struggling in this respect. Even those who have developed large footprints in India, such as IBM, Capgemini, and Accenture (the latter two have their single largest workforce in India, while, for IBM, India contains their second largest workforce after the US), have not yet fully managed to do so. This suggests that the Indian firms are not confined to just using their lower labor costs as their competitive advantage. How they do this needs further inquiry. The ability of Infosys to derive value from optimizing SG&A costs through globalization was noted to be one such advantage.

Second, there also was evidence that Indian firms were increasingly securing larger contracts and penetrating the higher value-added areas of system integration. The TCS deal with A. C. Nielsen, which is worth $1.2 billion and encompasses all areas of system integration, is an example. There was general agreement that the rivalry would only increase in intensity and was becoming more global in nature.

The third session included executives from established Silicon Valley and other MNC firms that were building a global R&D footprint. For all of these firms, their largest R&D operations outside the U.S. were located in India. Though all had operations in China, they hestitated in trusting their Chinese operations with key intellectual property. So, for example, Adobe Systems, at this time, did not allow access to their source code from their Chinese facility, while they would allow their

Indian facility such access. Cisco saw India as being their primary base to market Cisco's products and services to emerging economies. This fits in with their global vision of moving to a more services driven model. The Cisco speaker made an often-to-be-quoted statement, that in a six-hour flight from India one has access to 70 percent of the world's population. A startup in the subsequent session, Arada, noted a similar advantage: from the viewpoint of product development, Taiwan and China were closer to India than the US, thus making it easier to undertake post-conceptualization semiconductor work from Bangalore than from Silicon Valley. Nevertheless, in statements to be echoed in later sessions by smaller firms, both SAP and Adobe noted the continuing challenge of developing deep management expertise in India. All of the participants expected their offshore R&D facilities to become of even greater importance in the future. SAP already relies on its developing country centers to be centers of IP creation. However, they recognized the challenges, particularly the problem that multiple offshore sites, while increasing options, increased managerial complexity. As firms in India expand their operational sites in order to access larger labor pools or markets, they have encountered these challenges.

An interesting observation was that the corporate CIO function, which was critical in the days when firms had large in-house IT departments, might be losing its importance. The cause appears to be the rising complexity of the work to be done and the rising ability of outsourcers to manage even the most complex IT tasks with their own personnel.

Sun Microsystems has experimented with dividing overseas work by projects and allocating a global site leader to whom all engineers, no matter where they are located, respond. The speaker from Sun noted that the risks of this model were that this approach tended to sacrifice opportunities

in the local environment, such as selling to the local market, relations with government, developing local partners and accessing the best talent from the universities and building university-industry relations. Where these factors are important, as they have become in Bangalore, a local company champion who conveys company strategies and ensures that the global teams work well from the local site may be a better approach.

The final panel was composed of startups. Two of the firms were startups designing high-end semiconductors. One firm, Arada Systems, was established by a number of Silicon Valley veterans, but it had all of its design operation in India. In the last year it had grown from less than 50 engineers in India to nearly 150 engineers. Arada noted that while operating in Bangalore could mean isolation from both customers and cutting-edge innovation, the quality of documentation was better. The other firm, Infinera, designed products based on Digital Optical networking. It had design operations in Sunnyvale, CA and Bangalore. Though there were difficulties in hiring experienced personnel in India, the operation there was critical for the firm's success and was growing rapidly. GlobalLogic operated as a design contractor for small U.S. electronics firms. In essence, for these small firms GlobalLogic was a contract designer. It argued that the advantage of the small firm in services lay in helping avoid the duplication of non-core functions such as finance and facilities management. The final firm TRG discussed the difficulty it had had getting U.S. and its overseas engineers to work better. This was related to conflicts of interest that arose when American workers were asked to cooperate with overseas engineers for work transfer. When cooperation failed, TRG's solution had been to fire all the U.S. engineers and transfer the entire operation abroad. While this had led to some short-term instability, it ultimately enabled the overseas operations to do all the work at significantly lower costs.   This final panel showed that

offshoring was not only the province of large firms, but that smaller firms were also utilizing the engineering resources in India and other developing countries. All the examples showed the potential of offshored locations and risks to lower-end American jobs.

In this session, it became evident that Silicon Valley's advantage no longer lay in pure software projects. The example of Infinera showed that combining multiple technologies and sciences was key to SV's future. As a senior participant from the well-known VC firm, Kleiner Perkins, noted, every portfolio company that was headquartered in SV leveraged expertise in at least three frontier technologies.

The limitations of India also became evident in this session. India has rapidly become the premier developing country location for undertaking software work at all levels of complexity, but the ability to conceptualize and launch projects and products from India was still weak. This might be because the Indian IT clusters primarily cater to export markets and lack both the expertise in pure sciences and new technologies, as well as knowledge of the more sophisticated local markets. Of course, this should partly change with time and there are signs that in India's most sophisticated markets, such as mobile communications, this is changing; however, the change may not be led by work in the established clusters but could be in locations where market need is acute and where labor and bandwidth are adequate.

The weakness in the Indian educational infrastructure also remains a challenge. Its impact may be seen in the evidence that there are firms like GE that do sophisticated work in India, yet they recruit scientists and technologists from US universities and have them work in India.

Another weakness of the Indian IT industry is that the firms' overseas operations are primarily focused on the old model of selling programming services. Moving up the value-chain requires building centers of excellence in different verticals in the US. The largest Indian firms such as TCS have begun this process and are establishing large campuses in the US, but it is still early days. Some participants, such as from Intel Corporation, noted that the caliber of the US-based teams of the Indian ITSIs usually was well below their Indian HQ.

Post-conference Feedback

<u>Academics</u>

The feedback came from both Sloan Foundation-funded academics and corporate participants. The academics found the conference interesting and useful. For example, Frank Levy of MIT said, "First, thanks again for inviting me to the conference. I really enjoyed it and I think I learned quite a bit."

Manuel Serapio, a professor at the University of Colorado, Denver and whose Center is a sponsor of the Conference sent this email, "Congratulations on an outstanding conference! I learned a lot from the sessions and our roundtable discussion. I really liked the format this year of allowing more time for discussion. It was great to meet faculty colleagues and business leaders/executives. We are very pleased to be a sponsor of the conference. It is always a pleasure to work with both of you. Let's talk early next year about how we could collaborate on the 2008 meeting."

Clair Brown, a professor at the University of California, Berkeley wrote, "Your conference was excellent---key people who were willing to share their knowledge and experience with us. Many thanks for your hard work putting it together, and for including me." Clair's input and the other questions by the academics (Rose Batt, Susan Helper, Cynthia Kroll, and Tim Sturgeon) of the corporate executives were particularly pointed, and the executives remarked as to how interesting it was to have industry-savvy academics involved.

Professor David Finegold, Dean, School of Management and Labor Relation, Rutgers University sent this email, "Thanks for including me in a wonderful conference. Both the industry and

academic discussions were excellent. Think I relished it even more because it gave me the chance to be a faculty member rather than a Dean for a couple of days. I'm now on a flight to Copenhagen and enjoying your book Rafiq. Congratulations to you both and keep up the great work."

Corporate Personnel

The corporate personnel also found the conference valuable. For example, Jeanne Beyer (Vice President, Global Business Development, Objectiva Software Solutions) said that she was "so pleased that I could participate- and I read your book (Rafiq's book was given to all participants) on the way over to China. And what interesting introductions that made in the business class cabin!!!!! Thank you for giving the conference participants a copy and look forward to continuing the relationship." Jeanne has been to all three conferences and was one of the speakers on the second day with the academics.

Harmandir Singh (Vice President - Strategic Relationships, Persistent Systems Inc. and formerly of Cognizant) found the conference valuable. Here is his email to us, "Congratulations - On yet another stellar success of the Globalization series of seminars! Attending the Globalization of services seminar the 3rd year in a row, I can surely say that that it has evolved immensely and has made significant strides in getting industry and academia together to ponder on the challenges and opportunities this wave presents. The takeaways are both insightful and extremely valuable. Many thanks again for having me attend. It was truly an exhilarating experience for me." Harminder Singh is actively involved in managing global relationships for Persistent Systems.

Raj Saxena of Cognizant Technologies wrote: Congratulations on organizing another very successful globalization of services conference!

Jim Gordon of Intel Corporation wrote: I just wanted to thank you again for inviting me to participate in the Globalization Conference last week at Stanford. The topics were relevant to the realities of business I face daily – changing business models and globalization strategies – and helped bring clarity to some of the issues I'm currently confronting. More importantly though, the conversations and connections I was able to have with peers in the industry really added to the whole experience and provided insights that you can't really gain in any other fashion. I look forward to continuing our collaboration in 2008.

Utkarsh Rai of Infinera Technologies wrote: First of all Thanks for the excellent conference. It provided me an opportunity to hear and learn more and also to mingle with many folks.