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IT Sourcing Trends In The Current Market

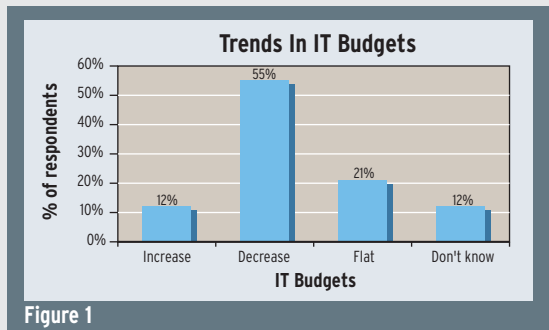
Mired in the midst of the worst financial crisis of the past 50 years, financial services firms are scrambling to batten down the hatches. With cost cutting not so much a trend as a necessity, firms are trimming budgets everywhere—Information Technology (IT) being no exception. Our assessment is that IT budget cuts will be significant and will likely continue for much of 2009. It is also our belief that cost-cutting efforts will result in a jump in the use of global IT sourcing, as well as a significant shift in sourcing strategies. This article provides an in-depth, survey-backed view of emerging IT-sourcing trends, including the key drivers, focus areas, risks and challenges of global sourcing.

This survey was conducted with sourcing professionals dealing with financial services clients.

Key Drivers For IT Sourcing—From Discretionary Spending To Transaction-Based Pricing

Discretionary spend is being put on hold and there is an increased focus on value for money. Strategic initiatives have been stalled in many cases to accommodate compliance and regulatory related opportunities. With fiduciary pressures mounting, companies are trimming IT budgets.

About 76% of the respondents indicated that their IT budget has either decreased or remained flat (see Figure 1) in the past year. In the majority of cases where there has been a decrease in budget, about 15% of respondents project alarming IT budget cuts of over 50%.

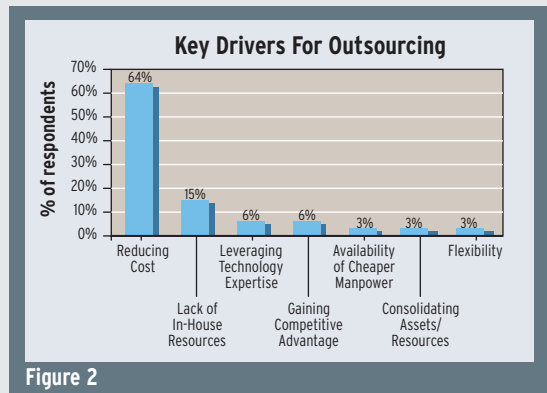


With tighter budgets, financial services firms are looking to extract maximum savings from their IT services vendors. Not surprisingly, a significant shift to outcome-based and transaction-based pricing models is under way.

Both pricing models transfer risk to vendors and provide more flexibility and scalability to companies. With the strong focus on business value and cost reduction there is also an increased emphasis on risk-reward and gain-sharing mechanisms.

Companies are demanding more transparency in pricing and there is an increase in blended rate pricing expectation. Companies that have been traditionally biased to “time and material” arrangements are now slowly moving towards fixed-price deals.

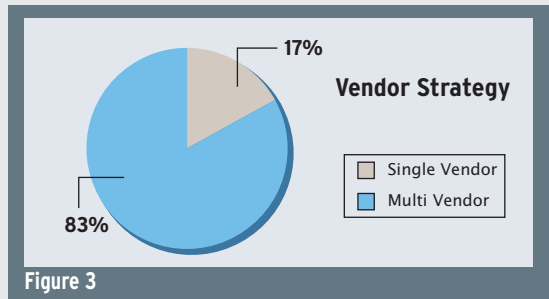
This heightened attention to price reflects an overarching trend in the IT sourcing space: Cost reduction is the most important factor driving sourcing decisions. In fact, companies are going to focus on cost savings almost exclusively when making sourcing decisions for IT services (see Figure 2). A couple of years ago, time to market, expansion of market share and leveraging technology experience were some of the issues that drove IT spending and outsourcing decisions, but these factors have been relegated to the background in the current economic climate.



Under the recent circumstances, about 64% of respondents indicated that reducing cost is the primary driver for outsourcing. The second most important driver is the lack of in-house resources. The number of respondents who stated other reasons for outsourcing was significantly lower.

As competitive pricing and a focus on risk/reward moves into the forefront, a multi-vendor approach continues to drive the sourcing strategy at most firms. In fact, close to 83% of

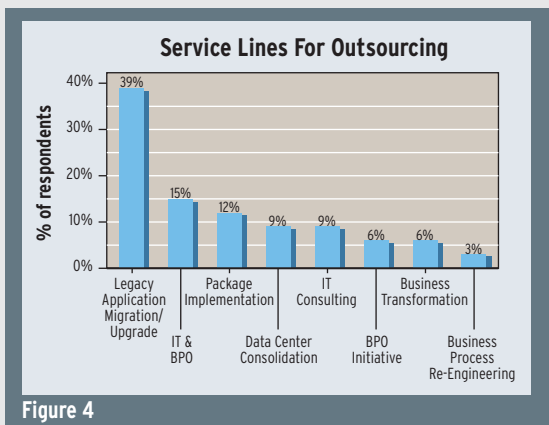
respondents surveyed preferred multi-vendor sourcing over a single-vendor approach (see Figure 3).



Interestingly, 27% of respondents operating with a large number of vendors are looking to consolidate—generally to three or four preferred vendors. As a whole, the multi-vendor trend is more pronounced in situations involving large deals. Often the work is segmented and sourced from multiple vendors in order to spread the risk.

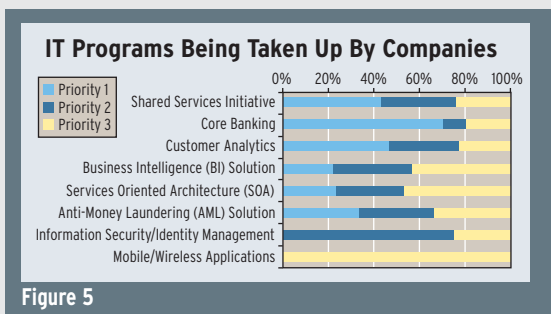
Key Strategies In IT Sourcing—From Outsourcing To Integrated Offering

Though price remains the dominant issue, companies are also beginning to focus on generating long-term value from outsourcing—their emphasis shifting from tactical cost reduction to sustainable, continuous business process improvement. Our survey revealed that in addition to outsourcing ADM services, companies are increasingly looking at integrated IT & BPO offerings as a key outsourcing focal point (see Figure 4).

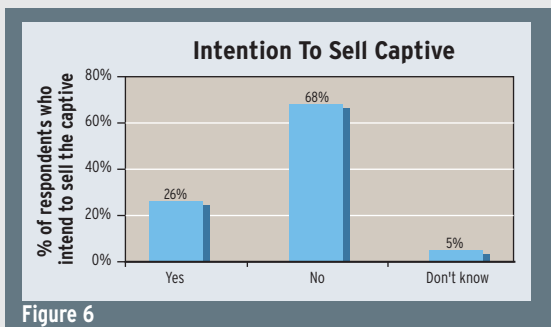


Package implementation, data center consolidation, and IT consulting are the other service offerings gaining traction. However, there has been a rapid decline in the percentage of ADM services outsourced. Only 39% of the respondents have indicated legacy application migration or upgrade as their top outsourcing priority.

Core banking renewal is emerging as the major priority, followed by shared services initiatives and customer analytics (see Figure 5). Banks are increasingly finding that in order to sustain growth under the current economic and regulatory environment the right core banking system must be implemented.



Location continues to remain a major factor when formulating an IT sourcing strategy. Apart from India being the most favored location for outsourcing, companies in the US have identified Mexico as the next favored location due to time zone and geopolitical reasons. Only 18% of the respondents see China as one of the preferred locations for outsourcing. The other locations that companies have indicated a likelihood to outsource include (in order of preference) Eastern



Europe, Philippines, Toronto, Brazil, Argentina, Russia, Spain and Costa Rica. Captive outsourcing remains prevalent. About 68% of respondents associated with captives have indicated that these will not be sold (see Figure 6).

Around 32% of respondents indicated that investment will be higher—continuing to strengthen the captive program, with the end goal of expanding the service involvement of the captive. Some of the companies are looking at having all vendors work under an India-India Master Services Agreement that carves out a separate rate structure for India based operations.

Risks And Challenges In IT Sourcing

Data security and the quality of resources of the vendor seem to be the risks with the highest priority as perceived by companies (see Figure 7).

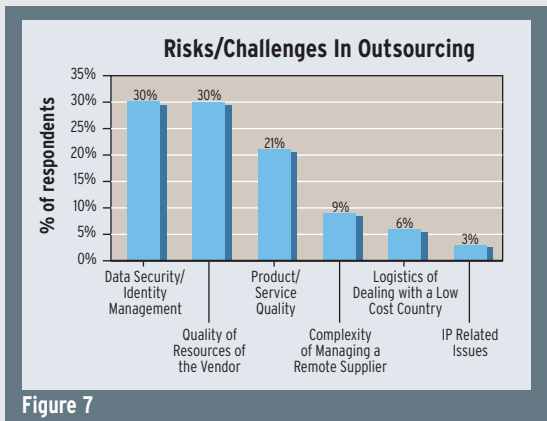


Figure 7

Other risks and challenges cited include unions, loss of control on outcomes and knowledge, impact to employee-friendly image and estimation transparency. A majority of our respondents, about 88%, have indicated that they have not seen any impact due to political and social factors on their outsourcing decisions.



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Conclusion

Tough times call for tough measures. Financial services companies will continue to cut IT budgets into the near future. To get the most bang for their IT-buck, these companies are increasingly turning to IT outsourcing. Though cost is the main focus, companies continue to shift away from ADM as the primary reason for outsourcing. IT & BPO integration, package implementation and data center consolidation are all initiatives gaining momentum. Core banking is one of the key priority focus areas, and banks plan to manage IT projects with a multi-vendor strategy, usually involving captives.

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