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THOMAS J. DELONG

Infosys (A): Strategic Human Resource Management

How do you feel when you look around and realize that 80% of your colleagues have been in the company for less than 24 months?

— an Infoscion

On November 13, 2003, the HR leadership team led by Hema Ravichandar, head of human resources for Infosys Group, left the conference room with a mixture of excitement and apprehension; a feeling that, they decided dryly, was familiar after a strategy meeting with the chairman and chief mentor of the Infosys Group, Narayana Murthy, and the CEO, Nandan Nilekani.

The cofounders had set a new and aggressive milestone for the HR group, the latest in a long line of challenging goals that had been set for them. By 2007, the cofounders wanted HR to ensure that Infosys was on the Top Ten lists of both Best Performing companies and Best Employers. It sounded innocuous enough to an outsider, but this HR team knew better. To the best of its knowledge, no large organization had ever been able to achieve this distinction because of the tension inherent between the need to control costs for financial performance and the spending required for employee satisfaction.

As the team walked back from the meeting, they were reminded of the painful and humbling experience in 2003 that had made Infosys sharply aware of the difficulties ahead as it transitioned from a small to a large company.

The decade since Ravichandar joined Infosys in 1992 had been a heady one for both the Indian software industry and Infosys. From March 1993 to March 2003, Infosys had a compound annual growth rate of 65%, and its revenues had jumped from US$5 million to US$754 million (**Exhibit 1**). As it had grown, it had added people at an equally impressive rate, from 250 employees in 1992 to over 15,000 in 2002.

Infosys had always recognized that its employees, or "Infoscions," were at the heart of its impressive success. It had been one of the first Indian companies to grant stock options to its employees—making, the legend goes, millionaires out of peons during the dot-com stock market boom. It had been ranked No. 1 in the Business Today Best Employer Survey both in 2001 and 2002.

Professor Thomas J. DeLong, Jaya Tandon (MBA 2005) and Ganesh Rengaswamy (MBA 2006) prepared this case. HBS cases are developed solely as the basis for class discussion. Cases are not intended to serve as endorsements, sources of primary data, or illustrations of effective or ineffective management.

So it came as a rude shock when in 2003, Infosys toppled from the Best Employer List in the same Business Today Survey. The results caused great commotion in the industry, and reams of newsprint were devoted to analyzing the "downfall" of the poster child of the Indian software industry.

As Infosys continued its heady growth, the HR leadership needed answers to prevent crises like this one from recurring. But there was no beaten path to tread and no role model to follow.

The Birth of Infosys: 1981

Narayana Murthy was born on August 20, 1946. He was the son of a schoolteacher and was one of eight siblings. He grew up in a typical Indian middle-class environment, which placed great emphasis on education and values.

The 1950s and 1960s were the heyday of socialism in India, and Murthy was attracted by the socialist idea of equality. The government had control of the "commanding heights" of the economy and had put protectionist policies in place. The reigning idea was to manage the economy so as to redistribute wealth and remove inequality.

After graduation, Murthy took a job in Paris and found himself in middle of the student revolution. He was surprised to find that the French regarded wealth creation as a superior way to remove inequality as compared with wealth redistribution. When his work in Paris was completed, he hitchhiked back to India over the next year, living on the $450 he had saved. His travels through Eastern Europe showed him the realities of communism, where instead of happy comrades and an efficient state, he found repression and an often-frightened populace. He was even briefly imprisoned in Bulgaria over espionage charges.

These experiences led him to become, in his words, "a socialist in my heart but a capitalist in my mind," with two main beliefs: first, the job of the government is not to create wealth but to foster its creation by providing the necessary environment and infrastructure; second, every human being needs incentives to move forward, whether in the form of money, recognition, or fame.

Murthy returned to India in 1974 and spent two and a half years in the public sector, followed by four years at a start-up software firm, one of the many that had come to fill the void created when the Indian government had nationalized the economy and foreign software firms left India.

In 1981, he and six other employees quit their jobs and against the advice of their families and friends, founded their own venture—Infosys. In the words of Murthy, "we were long on energy and enthusiasm but short on capital." They started Infosys on $250 borrowed from their spouses. The people who seemed happiest at his starting Infosys, Murthy recalled later, were his ill-wishers, because they fully expected him to fail.

The Early Years of Infosys: 1981–1991

The Vision

From the start, Murthy and his six colleagues shared a vision of creating wealth in a legal and ethical manner. Moreover, they all came from conservative middle-class backgrounds and wanted to create a company "of the professional, by the professional, and for the professional," as opposed to the kinds of firms that had dominated the Indian corporate landscape—the too personal family-owned and -run companies, and the too impersonal multinational corporations.

In the words of Nandan Nilekani, the youngest cofounder and current CEO, they wanted to build a company that "was professionally owned and professionally managed, with good corporate governance, good employee management, and good ethics. We wanted a firm that promised a fair deal to all its stakeholders—shareholders, employees, and customers alike."

The Hard Reality and Near Death

Getting Infosys off the ground turned out to be a difficult undertaking in the intensely bureaucratic and regulated environment of the 1980s. For example, it took Infosys 12 months and 15 visits to Delhi to get permission from the government to import a computer, and one year to get a telephone line. Issue of foreign exchange for travel abroad was controlled through the Reserve Bank of India. All of these constraints meant longer lead times in executing business. This was not good news for Infosys, whose vision was to become a "global company."

By 1986 Infosys still had only one client, hampered in its sales efforts by the restrictions placed by the Indian government on opening sales offices outside India. In 1989, things became worse when the U.S. government placed new restrictions on the number of B1 visas it issued each year, affecting Infosys's ability to send its employees to customer locations in the U.S.

At that point the company almost dissolved. Believing that Infosys was a "small unknown company with no brand equity" and was as good as dead, one of the cofounders left to pursue opportunities on his own in the U.S.

The remaining cofounders held a marathon emergency meeting. Reminisced Nilekani: "For a long time, we lamented how hard it was to do business and debated the best course of action to take now. A consensus seemed to be emerging that it would be best to sell the company or dissolve it."

Keeping Hope Alive

Nilekani continued:

> Narayana Murthy, who had been quiet throughout the discussions, now spoke up. He said he was confident that the company was going to succeed and that he would be happy to buy out any of the others who wanted to leave. There was silence for some time, and then Nandan spoke up. "If you are staying on," he said, "then I am in it with you." One by one, every one of the other cofounders changed their views and decided to stay on. As we pledged to redouble our efforts, Murthy admonished us, "let this be the last time we talk about selling the company."

Murthy recalled later that he had had no money to back up the offer he had made, and no idea where to get it if even one of the cofounders had taken him up on his offer. However, he had tremendous faith in the strength of their team, their shared values, and their ability to make Infosys successful.

Economic Liberalization

Although the founders decided to stay together, they also recognized the need for a drastic change in strategy. This renewed internal impetus was serendipitously followed by an external booster—the liberalization of the Indian economy—which set the stage of dramatic success.

In 1991, faced with an imminent economic meltdown sparked by a balance-of-payments crisis, long running fiscal deficit, high inflation, and dangerously low foreign reserves, the Indian government launched a program of economic liberalization, which dismantled the "license and permit raj" and significantly opened up the Indian economy. The software industry benefited in numerous ways. It became much easier to travel and open offices abroad, and to hire foreign consultants. Current account convertibility and 100% ownership of high-technology companies was allowed. Government-dictated pricing of new equity securities was eliminated and in 1993, Infosys tapped the Indian capital markets for its IPO.

The Move from Body-Shopping to Offshoring

The founders' initial vision for the company had been "offshoring"—i.e., performing work within India for foreign clients, thereby taking advantage of the lower labor costs of software professionals in India. But, in line with the rest of the industry, 90% of the work that Infosys did was based on "body shopping," which involved sending Indian IT professionals to the client site abroad, a considerably more expensive proposition. Motivated by its near-death experience to re-examine its strategy, Infosys became one of the leaders among Indian firms to refocus its work from onsite "body shopping" to offshore development centers (ODCs). Offshoring implied that the software firm, rather than the client, would control the project, a risk that clients had been hesitant to take so far. To instill confidence in clients, Infosys became more quality- and process-focused in its approach to software development. This ensured that the product quality was more stable and less risky to offshore clients.

Offshoring was the best way to overcome the obstacle presented by the U.S. government's visa restrictions, and thus, as K. Dinesh[1] said, "Infosys' management had decided to convert a threat (the U.S. visa issue) into an opportunity." This evolved into a system of project management known as GDM (Global Delivery Model), which divided projects into components to be executed independently and concurrently, both at the client site and at remote development centers.

Infosys: 2000–2004

Narayana Murthy summarized the transitions Infosys had gone through: "Yesterday, we moved from being a Bangalore company to an Indian company with a Bangalore base. Today, we are moving from being an Indian company with global reach to a global company headquartered in India."

Moving up the IT Value Chain

Traditionally, Infosys, as others in the Indian software industry, had focused on the lower end of the IT value chain—i.e., IT implementation and IT management, which involved implementing solutions that had already been designed, and/or simply maintaining the implemented systems.

[1] One of the cofounders of Infosys.

However, over time Infosys moved toward providing higher-end value-added services including IT strategy and IT design. This shift meant that Infosys's competitive set[2] moved from IT outsourcing firms such as TCS and Wipro in India or Keane and EDS in the U.S., to bigger firms like Accenture and IBM. In the words of a marketing executive:

> IBM and Accenture provide higher value-added services and end-to-end solutions but are concentrated in certain geographies. Infosys provides a greater proportion of lower-end services but spans more geographies with its Global Delivery Model. Clients don't want to choose between getting end-to-end solutions and lower costs. They are demanding that their suppliers have both, so both types of firms (at either end of the spectrum) are frantically moving to close the gap they each have, so they can become the preferred supplier to the client. Accenture is trying to add offshoring and GDM, and Infosys is trying to get into consulting and end-to-end solutions.

It was an open question as to who would win, and people were sharply divided into two camps. Doomsayers were of the opinion that Indian IT firms did not have the kind of brand identity necessary for firms to trust them with larger consulting projects. But Infosys begged to differ. As the head of a business unit noted: "It is easier for us to add a thin layer of consultants to our global model than for global consulting firms like IBM and Accenture to recreate the entire offshore offering and the GDM. Also, it is a disruptive model for them because all their offshore work will come at the expense of their onsite work and existing employees."

Improving Brand Equity

At the same time, Infosys knew that improving its brand equity was one of its most urgent and challenging tasks. Murthy explained his vision for the kind of brand equity he hoped Infosys would one day have:

> I changed my car recently and bought a Toyota Corolla. My driver is from the rural areas. He can read Kannada but not English. I asked him after a few days how the car was behaving and he says to me, "you know, these Japanese cars are extraordinary." That's the kind of brand equity we need to build. When a junior programmer in the U.S., a clerk in a corporation in the US who doesn't come in contact with us, when you ask him how is your software behaving and he says, "you know, these Indians, they build extraordinary software"—that is brand equity. The beauty is that the most peripheral person must feel the impact.

Infosys was taking a number of initiatives to accomplish this goal. For example, it became the first Indian company to list on the NASDAQ (on March 11, 1999). But it admitted the task was not easy. Murthy felt that the answer lay in drastic differentiation: "We have to continuously differentiate from all our competitors. Ideally, we need to change the playing field or if we can't, then we need to change the rules of the game. Own the rules of the game so that everybody else is playing by our rules."

People Philosophy

From the time Infosys was founded in 1981, the founders had always tried to ensure that the firm was the Best Employer or Employer of Choice for potential employees.

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[2] A set competitors within a specific region or industry.

This could be seen as far back as 1991, when liberalization of the economy, with its manifold benefits, also brought a potentially fatal threat in the form of competition from multinationals, which had started setting up bases in India. Infosys's management addressed the compensation challenge by ensuring that its employee salaries were in the top 10%–15% of salaries offered by companies in its peer group. In addition, in a major departure from the practices of other Indian firms, Infosys began issuing stock option warrants, which vested over a period of five years, to its employees. To counteract the second pull of multinational corporations on potential employees, Infosys invested a substantial part of the proceeds from Infosys's IPO in relocating Infosys to its 80-acre campus at Bangalore, replete with extensive dining, residential, entertainment, and state-of-the-art technological facilities as well as ample green space and areas for recreation.

Over the years, Infosys had developed a deep understanding of employee relations. An HR manager explained, "There are three ways in which we add value to the employee: learning value-add through training, emotional value-add through the work environment, and financial value-add through compensation and benefits."

The Challenge of Developing the "Infoscion"

Emotional Bonding

Infosys recognized that an employee would only be as committed to the firm as the firm was committed to its employees and it attempted to demonstrate its own commitment in a number of ways. The head of Employee Relations described their efforts:

> First, we always keep our doors open informally besides having a formal Grievance Resolution mechanism. Employees do not always like to take issues to formal mechanisms and it's important we recognize that. Second, we provide a lot of support during emergencies. For example, there was an employee who went into a coma and had to be put on life support. The firm supported the employee's family for the two years that he remained in that condition. Third, we have created a very effective health platform. We discovered that because of the nature of the occupation, health was a not a priority for most people. So we created a platform call HALE (Health Assessment and Lifestyle Enrichment) and offered our employees health checkups, yoga classes, stress audits, and professional counseling among a diverse set of programs on company premises. Fourth, to enable an employee to pursue areas of interest, we created hobby, cultural, and sports clubs, which organize events every week—such as learning to dance or a Beatles' fan evening—so people can have a life beyond work.

Yet, employee discontent was on the rise. With the company's rapid growth and its number of employees skyrocketing, the disparity of expectations across the employee hierarchy had become very complex. Until the early 1990s, Infoscions received employee stock options at a purchase price of 5% of the fair market value. Coming from modest middle-class upbringings, most of them reaped rewards beyond their wildest imaginations. The next generations of Infoscions had similar expectations but were sorely disappointed when the SEBI (the Indian equivalent of the SEC) required Infosys to issue future ESOPs at 85% of fair market price.

There were two other troubling factors with the company's growing size: (1) As Infosys became more process-oriented and started leveraging its experience to perform repeatable projects, employees realized that they were being deprived of the creative and technical ingenuity that had been inherent in their work during the initial years. (2) Employees thought the organization was becoming more impersonal and that some of the perks of the initial years were being repealed.

Creating Fun and Community Empathy at the Workplace

The HR group at Infosys attempted to address employee discontent by trying to make the workplace more fun and meaningful. The average employee age at Infosys was a mere 26 years, and most of these professionals had recently left college and joined Infosys as their first job. Aware that they were still in a stage of transition from academic to corporate life and would appreciate a more college-like environment, Infosys HR focused on facilitating a sense of fun in the workplace through events like DJ nights, quizzes, intellectual debates, and dances. Infosys also gave its employees the opportunity to have a greater and more meaningful impact on the world. Every development center at Infosys had an Employee Social Services group, which helped out in the local community. Participation was purely voluntary and did not have to be monetary in nature; employees could devote their after-work time to projects such as providing outreach to street children or volunteering at old-age homes.

Values and Value Champions

It was well known that the founders of Infosys had strongly articulated values and tried to practice them during every interaction. As the company started scaling up across multiple locations, Infosys articulated the core values it believed in and wanted every employee to adhere to through the acronym "C-LIFE": Customer delight, Leadership by example, Integrity & Transparency, Fairness, and Pursuit of Excellence.

Infosys went to great lengths to instill these values in its employees and to ensure that employees were supported in their efforts to follow them. Explained a senior HR executive: "We try to inculcate these very early. People who join the company are trained by senior leaders and then we have lots of refresher sessions. We want everyone to be Value Champions, people who communicate values to others—newcomers, colleagues, juniors—by their own examples.

But the execution of C-LIFE remained a challenge across the organization. To maintain the company's value system, it tried to recruit and hire employees based on their potential fit with the company's culture and values. But this became a challenge, as Infosys did not want to be constrained by lack of resources in its pursuit of growth.

Managing Scale and Attrition Risk

Infosys realized the benefits of introducing employees to the Infosys culture right from the start and consequently, had developed an extensive and detailed induction process. It had two types of induction programs. One catered to "freshers"—college graduates who were joining Infosys straight from academic life and for whom Infosys was their first corporate experience. The other program catered to professionals with prior experience, who were joining Infosys from another organization.

In spite of these initiatives, Infosys was facing challenges resulting from its continuing growth. With each passing year, the diversity and disparity of the employee hierarchy was becoming more apparent. Middle managers and senior managers were not in touch with the rapidly changing realities of employees at lower levels. These managers could not understand the frustrations of employees who were doing less interesting work than the managers and had not been richly rewarded by Infosys. Managers also found it hard to practice a very hands-on management approach and struggled to delegate effectively as their responsibilities expanded.

In an almost paradoxical state of affairs, Infosys had to deal with increased employee turnover in the same era in which it was expanding operations. The organizational growth led numerous employees to reflect and realize that work was not as fulfilling as they had hoped. This was simultaneous with the entry of multinational technology firms into India. These firms attracted talent from Infosys and Wipro because of their global brand and better compensation packages. At Infosys, this turnover led to an increase in employee costs because of the need to build up recruiting efforts.

Execution Challenges and Immigration Issues

Infosys also faced challenges executing work efficiently. As the company evolved, clients started to expect greater efficiency and faster turnaround of projects. These demands were accentuated by the economic downturn of 2001–2002. Yet with a constantly growing Infosys employee base, everyone had to be trained on processes, various technologies, quality issues, and customer interaction skills in order to ensure standardized output to clients.

Also, just before the downturn, Infosys had made many job offers across college campuses although it did not have enough projects to keep everyone productive during the downturn. While Infosys did not go back on any of its offers (as did several other firms), Infosys found that the increase in "bench" (resources on company rolls not staffed on any project) caused employee frustration and increased costs for the company.

In the beginning of 21st century, new external realities posed unforeseen challenges. The U.S. government severely reduced the number of visas issued for business purposes (from 195,000 in 1998 to 65,000 in 2004). This put pressure on the business models of bigger players like Infosys and Wipro. For example, Infosys projects typically had a very active onsite (client location) component during the exploratory phase of projects, yet the visa restriction made it harder for Infosys to send employees onsite. Also, onsite experiences were one of the main motivational tools used by senior managers to reward high performers, but it became more difficult to use them as such under the new visa restrictions.

Preparing Infosys for Future Growth: Changes after 2000

In 1999, Infosys was growing at a rapid rate, having doubled in size every 20 months. Its management realized that a large "small" company till now, Infosys was well on its way to becoming a small large company. Recognizing the business imperative to institutionalize and improve productivity, cost-competitiveness, and efficiency, Infosys management decided to implement a series of changes including building a portfolio of core companies and services and reorienting the way people were measured, compensated, promoted, and rewarded.

Managing Portfolio Diversity

Infosys was evolving into a multinational firm with a portfolio of core companies. For example, Infosys's consulting practice was created in order to provide clients with higher-end IT strategy consulting services. Identifying China as a development base and potential market for Infosys services triggered the establishment of a Greater China office. In its quest to provide end-to-end solutions, Infosys also set up a BPO[3] subsidiary called Progeon.

Each of these subsidiaries clearly had cultural and compensation disparities. Managing these differences and employee expectations across subsidiaries was a new challenge for Infosys.

[3] Business process outsourcing.

Variable Pay

Until March 2001, the concept of variable pay applied only to Infosys' senior management, who constituted 2% of Infosys' population and for whom 10%–15% of their compensation derived from an individual-performance-based variable component. After March 2001, variable pay was introduced across the organization, with three components: company performance, unit performance, and individual performance.

The variable-pay philosophy was designed with the intent of better aligning the Infoscions' and Infosys's interests. This implied that if Infosys improved its performance over time, the Infoscion would be better rewarded, and similarly, during a downturn the pain would be mutually shared. This variable pay program also helped reinforce the company's high-performance work ethic; variable pay created an earning potential that was much higher for a better employee than for an average one. This helped Infosys compete more effectively in the war for talent with multinational corporations that were offering higher packages. But this compensation change received mixed reaction from employees. Some were skeptical of the company's intentions, given the way variable pay was defined, and thought it was a way for the company to reduce compensation costs.

Broad-Banding

Infosys undertook an elaborate competency-modeling exercise for all roles within its organization structure, and collapsed 15 layers into 7 bands. The rationale for moving toward a role-based organization was twofold. As a senior HR executive explained:

> First, an employee would know exactly what his/her role was as well as the role he wanted to move to. And therefore, he/she would see the gap between the two, and the gaps in his/her skill set that s/he needed to fill to achieve the move. Second, broad-banding let us create an equitable framework for people-related decision-making. We attached a numerical worth to each role based on its contribution to business and value-add. So now it was possible for us to compare jobs between, say, finance and HR. Each role therefore had an equity attached to it. This facilitated career planning and also introduced objectivity to the process. It wasn't the department head's call now, it was coming through a scientific process of job evaluation.

Broad-banding was the tipping point at which employee dissatisfaction and discontent at Infosys reached its peak. Rapidly changing HR policies bred confusion among employees and managers alike. Middle and senior managers were made responsible by HR for communicating these changes effectively to employees, but some managers were unsure of certain aspects of the change and could not face the scrutiny of employees. This fostered misinformation and rumors, which led to further discontent and lack of trust between some employees.

Promotion Policy

Infosys had always linked promotions to parameters such as individual performance and seniority; it now also linked promotions to the needs of the organization. The policy clearly stated that promotions now depended on three factors: individual performance, the individual's abilities to fulfill the next role, and (a new addition) the existence or need of that particular opening within the organization. The rationale behind the new promotion policy was twofold: it ensured that performance and not seniority would be the criterion for promotion, and that there would be no "fat" in the organization's layers.

The Fall from Grace

Always recognized for its path-breaking HR practices and considered a model employer, Infosys was ranked highly in 2001 and 2002 on Best Employer lists. Then, in a shock to the entire industry and especially to Infosys, it fell off the Best Employer's list in 2003. Its own internal employee satisfaction survey showed dissatisfaction.

Rapid Retrenchment on Employee Satisfaction

Realizing that something had gone wrong with their organization, Infosys's management scrambled to solve the mystery of the fall. They realized that the changes initiated since 2001 and many more effected in 2002 and 2003 had had an unintended impact in de-emphasizing the traditional culture of Infosys—its small-company feel and collegial environment, where processes and policies were flexible and customized to individual needs. Infosys also had to deal with problems of managing expectations and communication within a large organization. Employees were doubtful about the impact of the changes—for example, how the variable pay mechanism or the new promotion policy worked in practice. They were also unclear about the rationale behind these changes, all of which appeared to boost the company at the expense of employees. Ravichandar and her team knew something needed to be done to recapture the hearts of Infoscions, but they were not sure where to begin.

Exhibit 1 Infosys Financial and Employment Information

Year	Revenue (US$ million)	Net Income (US$ million)	Employees
March 2003	$753.81	$194.87	15,356
March 2002	545.05	164.47	10,738
March 2001	413.85	131.95	9,831
March 2000	203.44	61.34	5,389
March 1999	120.96	30.35	3,766
March 1998	68.33	13.86	2,605
March 1997	39.59	8.64	1,705
March 1996	26.61	6.82	1,172
March 1995	18.3	3.5	918
March 1994	9.6	2.6	637
March 1993	5.01	1.2	410

Source: Compiled from Hoover's, Inc. data and Infosys annual reports.