Sectoral Assessment Report: Indian IT/Technology Sector

Executive Summary

The Indian IT/Technology sector is experiencing profound polarization as it navigates a complex transition from legacy services to AI-driven digital transformation. Recent data reveals a bifurcated landscape where mid-cap firms demonstrate robust growth through AI-enabled solutions and strategic M&A, while Tier-1 giants face margin pressures and slower revenue growth. Simultaneously, structural tailwinds in data center infrastructure and sovereign AI initiatives are creating new growth vectors independent of traditional IT services. The sector faces significant regulatory headwinds from U.S. visa policies and proposed legislation, but domestic policy initiatives and data center expansion are mitigating these pressures. Current trends indicate a fundamental shift in competitive dynamics rather than sector-wide stagnation, with AI adoption creating both disruption and opportunity across different segments.

Core Thesis Confrontation

Growth Believer's Optimistic Case

The Growth Believer perspective emphasizes structural tailwinds driving sector resilience. Key arguments include:

- **AI as productivity multiplier**: Infosys reported 55% of its $3.8B TCV in Q1 FY26 came from AI-led transformations, with AI agents delivering 5-15% productivity gains. Tech Mahindra expanded EBIT margins +56 bps QoQ through "Project Fortius" offshoring and AI implementation.
- **Mid-cap momentum**: Coforge delivered +9.6% QoQ USD revenue growth and +53.6% YoY, while Persistent Systems achieved +2.8% QoQ and

+21.8% YoY growth. These firms are leveraging AI platforms (Forge-X, AI training data services) to capture market share.

- **Data center expansion**: India's colocation capacity is projected to quintuple from 1.7 GW to 8 GW by 2030, requiring $63B in combined facility and server capex. S&P Global estimates India will become the second-largest data center electricity market in Asia-Pacific within two years.
- **Policy tailwinds**: The IndiaAI Mission awarded 34,371 GPUs by mid-2025, with state-level policies like Maharashtra's AVGC-XR Policy (₹3,268 crore outlay) and Odisha's IT Policy creating domestic talent and compute infrastructure.

Cynic's Risk Assessment

The Cynic perspective highlights structural challenges and deflationary pressures:

- **Revenue deflation**: AI is projected to carve out ~20% of existing IT services revenues by FY30, particularly in high-margin segments like application management and BPO. Global IT services CAGR is throttling to 1.5-3% (CY24-29), dragging India's IT coverage to 3.8% CAGR (FY25-28).
- **Regulatory headwinds**: U.S. H-1B visa fee hike ($100,000 one-time fee) triggered a ~3% Nifty IT drop on September 22, 2025. Proposed HIRE Act could impose ~25% tax on foreign services payments, threatening onsite delivery models.
- **Talent cost pressures**: Attrition spiked +160 bps QoQ to 18.2% at Happiest Minds and +250 bps at Tech Mahindra, inflating talent acquisition costs by 10-15% YoY despite flat Tier-1 headcount growth (TCS +0.8% YoY, Infosys +0.1%).
- **Client spending retrenchment**: Enterprises are optimizing existing budgets rather than greenlighting new IT spend, with retail, auto, and consumer verticals showing flat-to-negative QoQ growth.

Dialectical Resolution

The debate reveals fundamental convergence on AI's disruptive impact but divergence on its net effect. Both sides agree that:

- AI adoption is accelerating across the sector (97% of key accounts adopting AI per Cognizant's Q2 CY25)
- BFSI verticals remain the strongest growth driver (+5-7% YoY across major players)
- Tier-1 and mid-cap performance is diverging significantly

However, they fundamentally disagree on whether AI creates net value:

- Growth Believers view AI as a productivity multiplier that enables margin defense and new revenue streams (e.g., AI training data services)
- Cynics see AI as a deflationary force that erodes traditional revenue pools while creating new competitive threats from U.S. AI platforms

The sector is not experiencing uniform stagnation but rather a Darwinian reallocation where agile players capture value from AI integration while legacy models face pressure. The data center infrastructure boom represents a structural growth vector largely decoupled from traditional IT services dynamics.

Sector Fundamentals Analysis

Revenue Trends

- **Tier-1 vs Tier-2 divergence**: Tier-1 firms show muted growth (TCS -0.6% QoQ, Wipro -1.6% QoQ, HCLT +0.3% QoQ), while mid-caps demonstrate stronger performance (Coforge +9.6% QoQ, Persistent +2.8% QoQ). Top-six IT firms averaged -2.5% to +2% CC QoQ in Q1 FY26.
- **Vertical performance**: BFSI remains the strongest vertical (+5-7% YoY across Infosys, Coforge, Persistent), comprising 30-40% of sector revenues. Retail, auto, and consumer verticals show flat-to-negative QoQ growth.

- **Deal momentum**: TCV bookings rose 6% YoY (Kotak July 31), but growth is concentrated in large, strategic deals rather than broad-based demand. Infosys' $3.8B TCV in Q1 FY26 included 55% net-new AI-led transformations.

Margin Dynamics

- **EBIT margin divergence**: Tech Mahindra expanded EBIT +56 bps QoQ to 11.1% through AI-driven productivity and offshoring, while HCLT slipped -171 bps to 16.3%. Infosys edged down -13 bps to 20.8%.
- **AI as margin cushion**: Productivity gains from AI agents (5-15% efficiency improvements) are offsetting client retrenchment in some firms. Coforge widened EBIT +100 bps to 13.2% through integration savings.
- **Aggregate margin outlook**: Projected to flatline at ~20% through FY28 as deflation strikes higher-yield services while growth tilts toward lower-margin consulting & implementation.

Competitive Positioning

- **Mid-cap advantage**: Coforge, Persistent, and Hexaware are gaining market share through agility in AI service-line pivots. Coforge's +28.5% YoY headcount growth and $58M AI datacenter investment demonstrate strategic capacity building.
- **Tier-1 challenges**: Large firms face structural constraints in adapting to AI-driven transformation. Wipro and Tech Mahindra are most vulnerable to revenue deflation, while Infosys and HCLT show relative resilience.
- **Global competition**: U.S. AI firms are deploying predatory pricing (ChatGPT at ₹399/month), while Indian startups remain trapped in application-layer roles piggybacking on foreign LLMs.

Operational Metrics

- **Headcount trends**: Tier-1s show flat or muted headcount growth (TCS +0.8% YoY, Infosys +0.1%), while mid-caps ramp aggressively (Coforge +28.5% YoY, Persistent +7.7% YoY).

- **Attrition rates**: Industry-wide attrition has stabilized at 14-16% (down from 30% in 2022), but specific firms show concerning spikes (Happiest Minds +18.2%, Tech Mahindra +250 bps QoQ).
- **Offshore shift**: Firms are accelerating offshoring (targeting 70% offshore delivery by FY26 end), reducing onsite dependency from 30-40% to mitigate U.S. visa cost pressures.

Key Risk Factors

Regulatory and Policy Risks

- **U.S. visa and tax policies**: H-1B visa fee hike ($100,000 one-time fee) and proposed HIRE Act (25% tax on foreign services payments) threaten onsite delivery models. These could shave 1-2% off FY26 EBIT for firms with significant onsite presence.
- **Data localization requirements**: India's Digital Personal Data Protection Act (2023) and RBI's financial data storage mandate create compliance costs but also drive domestic data center demand.
- **State-level policy variations**: While Maharashtra and Karnataka offer favorable incentives (land subsidies, electricity duty waivers), Uttar Pradesh maintains higher commercial tariffs despite attractive datacenter policies.

Technological Disruption Risks

- **AI-driven revenue deflation**: AI is projected to carve out ~20% of existing IT services revenues by FY30, particularly in high-margin segments like application management and BPO.
- **Foreign platform dominance**: U.S. AI firms are capturing market share through predatory pricing and bundled services (e.g., Perplexity free with Airtel, Gemini Pro bundled), threatening Indian pricing power.
- **Infrastructure bottlenecks**: Data center growth faces challenges with water stress in key urban centers (Mumbai, Bengaluru, Chennai), where high water demand for cooling (25.5 million liters/year per 1 MW load) could cause operational disruptions.

Competitive and Market Risks

- **Vendor consolidation**: Enterprises are reducing supplier rosters, favoring firms that can prove ROI on AI integration. This creates winner-takes-all dynamics where only agile players capture value.

- **Capital intensity**: Data center expansion requires $30B in facility capex plus $33B in server hardware capex, creating financing challenges for smaller operators.

- **Renewable energy dependency**: Data centers require reliable renewable energy procurement, but grid expansion delays and regulatory uncertainty around renewable waivers pose risks to sustainability goals.

Market Outlook and Trends

Sector Trajectory

The Indian IT/Technology sector is transitioning from a homogeneous growth model to a bifurcated landscape with distinct growth vectors:

- **Traditional IT services**: Growth will remain muted (3.8% CAGR FY25-28), with revenue deflation from AI adoption offset by productivity gains and client consolidation.

- **Data center infrastructure**: Expected to grow rapidly, with capacity projected to quintuple from 1.7 GW to 8 GW by 2030. India is on track to become the second-largest data center electricity consumer in Asia-Pacific.

- **AI-native services**: New revenue streams are emerging around AI training data services, cloud migration, and modernization plays, with mid-caps leading adoption.

Emerging Themes

- **Polarization of players**: Tier-1 firms face structural challenges adapting to AI-driven transformation, while mid-caps with agility in AI service-line pivots are gaining market share. Coforge, Persistent, and Hexaware show higher growth potential despite volatility.

- **Infrastructure-led growth**: Data center expansion is creating opportunities beyond traditional IT services. Electrical/power systems ($10B), racks/fitouts ($7B), and cooling infrastructure (Voltas, Blue Star) represent underappreciated beneficiaries.
- **Policy-driven opportunities**: The IndiaAI Mission ($1.2 billion outlay) and state-level policies (Maharashtra AVGC-XR, Odisha IT Policy) are creating domestic compute capacity and talent pipelines. However, implementation challenges remain around renewable energy procurement and grid expansion.

Key Developments to Monitor

- **U.S. regulatory developments**: Finalization of HIRE Act provisions and potential visa policy changes will significantly impact onsite delivery models.
- **Data center infrastructure progress**: Monitoring of grid expansion for renewable energy and water management solutions in key urban centers.
- **AI adoption metrics**: Tracking of AI-generated code percentages, AI training data service revenue, and productivity gains across firms.
- **State policy implementation**: Effectiveness of Maharashtra's AVGC-XR Policy and Odisha's IT Policy in creating domestic talent and manufacturing capacity.

Recent Trends Synthesis

Recent developments (September 15-22, 2025) highlight the sector's volatility and structural shifts:

- **Market reaction to U.S. policy**: Nifty IT index dropped ~3% on September 22 following U.S. H-1B visa fee hike announcement, with individual stocks declining 2-5% (Persistent Systems down ~4%). YTD performance shows Nifty IT down ~15.6% versus Nifty 50's +7.1% gain.

- **State policy initiatives**: Maharashtra approved AVGC-XR Policy (₹3,268 crore outlay targeting 200,000 jobs), while Odisha Cabinet approved Electronics Component Manufacturing Policy and IT Policy 2025 with increased capital subsidies (25-30%).
- **IndiaAI Mission progress**: Over 34,371 GPUs awarded through two rounds of tenders in 2025, with about half installed as of mid-2025. These GPUs are estimated to provide ~2 TWh of additional annual electricity demand.
- **Industry response**: Indian IT firms are calling for single-window clearance systems for GCCs and startups, while accelerating offshoring strategies to mitigate visa cost impacts.

Areas of Convergence vs. Genuine Disagreement

Areas of Convergence

- **AI adoption is accelerating**: Both sides agree 97% of key accounts are adopting AI, with Cognizant reporting 30% of code AI-generated in Q2 CY25. Indian firms are implementing AI productivity tools across delivery models.
- **BFSI vertical strength**: Both acknowledge BFSI as the strongest growth driver (+5-7% YoY across major players), comprising 30-40% of sector revenues.
- **Data center expansion**: Both recognize India's data center capacity will quintuple to 8 GW by 2030, with S&P Global projecting India to become the second-largest data center electricity market in Asia-Pacific within two years.

Genuine Disagreements

- **Net impact of AI on revenue**: Growth Believers see AI as a productivity multiplier creating new revenue streams (AI training

data services), while Cynics view it as a deflationary force eroding ~20% of existing revenues by FY30.

- **Sustainability of mid-cap growth**: Growth Believers see mid-cap momentum as scalable and indicative of sector leadership, while Cynics view it as volatile outliers in a fundamentally weak sector.
- **Regulatory impact severity**: Growth Believers believe offshore pivots and domestic policies can mitigate U.S. visa costs (1-2% EBIT impact), while Cynics see proposed HIRE Act as a fundamental threat to business models.

Meta-Analysis: What the Recent Data Reveals

The recent data reveals a fundamental transformation rather than simple growth or decline. The Indian IT/Technology sector is experiencing a Darwinian reallocation where:

- **Structural bifurcation is occurring**: Traditional IT services face headwinds while data center infrastructure and AI-native services create new growth vectors. The sector is not monolithic but consists of distinct growth engines.
- **Policy is becoming a critical differentiator**: Domestic policies like IndiaAI Mission and state-level incentives are creating competitive advantages for firms that align with sovereign compute and talent development goals.
- **Data center growth is decoupled from IT services**: The $63B capex for data center infrastructure represents a structural growth vector largely independent of traditional IT services dynamics, with 95% of capacity increase coming from leased facilities.
- **Competitive advantage is shifting to agility**: Firms that can rapidly pivot to AI-enabled solutions (Coforge, Persistent) are gaining market share, while legacy models face pressure from both AI disruption and regulatory changes.

The sector's trajectory is not about overall growth or decline but about which players can successfully navigate the transition from legacy services to AI-driven digital transformation while capitalizing on

infrastructure-led growth opportunities. The data center expansion and sovereign AI initiatives represent structural tailwinds that could offset traditional IT services challenges, creating a more complex but ultimately resilient ecosystem.