

## Robust Growth in the Indian Services Sector Over Next One Year: KPMG survey

The spring 2008 KPMG Business Outlook Survey, which surveys around 1,400 service sector firms across the BRIC region (Brazil, Russia, India and China), highlighted continued confidence regarding business prospects for the next twelve months. Although the overall net balance of firms forecasting growth of activity (+58.0) was down on that registered last autumn (+65.7), it was still indicative of buoyant optimism.

Around 60% of panellists anticipate a rise in activity at their company during the coming year, compared with just 2% that expect a decline. Positive sentiment was most widespread amongst Indian firms.

Service providers are confident that revenues will rise over the coming year, with 61% predicting an increase. Higher new orders, improving market conditions and the introduction of new products were cited as the main factors likely to support growth of revenues. The principal threats to revenues were perceived to be intensifying competition, rising input costs and weaker economic conditions.

Volumes of new business placed with BRIC service providers are expected to rise at a marked pace over the coming year. Growth of new work is anticipated at 58% of companies, while less than 3% forecast a fall.

Company profitability at BRIC service providers is predicted to increase strongly over the next year, with well over half of survey respondents anticipating a rise. Indian firms were the most optimistic regarding profits.

Higher profits are set to underpin increased investment in capital, with a net balance of +39.9 companies predicting growth of capital spending over the next twelve months. However, this was down from +47.3 last autumn, mainly reflecting a marked softening of optimism in Brazil.

Higher workloads are predicted to support a robust pace of job creation across the BRIC nations. Around 37% of service providers anticipate growth of employment, with Russian and Indian firms the most upbeat.

Outsourcing is also expected to increase, with a net balance of +24.0 firms forecasting a rise in bought-in services.

Over half of BRIC service providers forecast annual growth of their total operating costs to accelerate over the next twelve months, citing dearer raw material prices, staff salaries and outsourcing costs. Inflationary expectations were particularly elevated in Russia.

In response, companies are set to raise their own charges at a faster pace, with over a third of panellists expecting a rise in annual growth of average tariffs. Reflecting the trend for input costs, Russian firms predicted by far the sharpest acceleration.

Perhaps surprisingly, panellists reported that the availability of credit to their companies had improved compared with the situation prior to the financial market turmoil which commenced last summer. Approximately 38% of companies stated that this was the case, with only around 8% of

firms noting a deterioration in credit availability and just 2% reporting that their business was being constrained as a result.

However, the cost of credit was widely reported to have risen since the start of the credit crunch, with 47% of companies signalling higher borrowing costs and less than 8% noting a decrease.

**Commenting on the latest survey findings, Ian Gomes, Chairman of KPMG's New and Emerging Markets Group, said:**

*'Confidence in the BRIC service sector remains buoyant according to the latest survey findings, suggesting that rapid economic expansion is set to be maintained in 2008 and into 2009. Companies expect fast-growing demand for services to support higher levels of activity, while strongly rising revenues and profits will be ploughed back into investment in capital.'*

*'Although still elevated, optimism was mildly down on that recorded in the last survey conducted in autumn 2007, reflecting concerns over a slowing global economy and heightened inflationary pressures. Nevertheless, the overwhelming feeling amongst companies is that business opportunities remain plentiful as domestic demand in the respective BRIC economies expands apace.'*

## **NATIONAL SURVEY FINDINGS**

### **BRAZIL**

Brazilian service providers remain confident that service sector activity will continue to expand over the coming year, according to the latest findings from the BRIC Business Outlook Survey. Around 57% of firms anticipate growth of activity - though this was down from 81% in the last survey conducted six months ago.

Higher levels of activity are set to be underpinned by an expected increase in new work received. Approximately 55% of companies predict a rise in incoming new business, compared with just under 3% that forecast a decline.

Higher expected workloads are set to lead to a rise in the value of outsourced work. Around 23% of companies predict an increase in outsourcing, against 9% that expect a fall.

Business revenues are widely predicted to rise over the course of the next twelve months, with around 53% of panellists anticipating an increase. Survey respondents stated that new order growth, improving economic conditions and the introduction of new services were the factors most likely to support higher revenues.

Over 51% of companies anticipate an improvement in their profitability during 2008 and into 2009. This was despite a predicted acceleration in input cost inflation, with approximately 40% of firms expecting sharper annual growth of total costs.

Pricing power is set to remain strong enough to pass on part of the rise in costs to clients in the form of higher output charges. Around a third of companies expect annual inflation of tariffs to strengthen over the coming year.

Brazilian service providers anticipate recruiting additional staff over the next twelve months, although they are less confident of doing so than six months ago. Almost 38% of firms expect to increase staffing levels at their companies, compared with only 6% forecasting workforce cutbacks.

Investment is set to increase in the Brazilian service sector during the next year. Approximately 29% of companies anticipate growth of capital spending.

## **RUSSIA**

The latest findings from the BRIC Outlook Survey show that business optimism in the Russian service sector remains high. Around 62% of firms anticipate growth of activity during the next twelve months, with expansion set to be powered by robust demand and continued improvement of the domestic economy.

Although still high, the overall degree of confidence regarding activity was lower than that registered in the last survey conducted six months ago. Anecdotal evidence suggested that firms were wary of the potential impact of rising input costs and a slowing global economy.

Volumes of incoming new business are widely anticipated to rise, with 64% of companies predicting growth. Consequently, revenues are set to increase at a similarly brisk pace.

Higher workloads are forecast to lead to continued strong job creation in the Russian service sector. Almost half of panellists expect to add to their staffing levels over the coming year, compared with only around 5% planning cutbacks. The amount of outsourced work is also set to increase markedly.

Expectations regarding input price inflation remain extremely high, with over 70% of firms anticipating cost inflation to accelerate. Raw materials, wage bills and business-to-business services are all viewed as likely sources of inflationary pressure.

Russian service providers widely expect to pass on increases in their cost burdens to clients in the form of higher output charges. Over three-quarters of firms anticipate a rise in their tariffs, while fewer than 1% are planning a decrease. Strong pricing power is set to protect company profitability, although confidence over profits is less buoyant than last autumn.

Higher profits are forecast to support continued growth of investment in capital. Approximately 46% of firms expect to raise their capital spending over the course of the next twelve months.

## **INDIA**

Robust growth is anticipated in the Indian service economy over the coming twelve months, according to the latest BRIC Outlook Survey. Over 60% of service providers - the highest of all four BRIC countries - expect an increase in levels of business activity.

Growth of activity is expected to be supported by an anticipated strong rise in volumes of incoming new business. Approximately 56% of all companies forecast an increase in new work, while none expect a fall.

Revenues are also set to rise markedly, underpinned by increased marketing activity, the introduction of new products and entry into new markets. Around 58% of companies expect growth of revenues during the coming year. This is despite widespread concerns over intensifying competitive pressures in the Indian service sector.

Service companies remain optimistic about future profit levels - higher profitability is anticipated at just under 58% of firms. Increased revenues and profits are set to support rising levels of capital expenditure.

**Commenting on the survey findings, Russell Parera, CEO , KPMG in India said, ' The current optimism reflects the unique positioning that India has with its large domestic market, off shoring service capabilities and economic value drivers.'**

Staffing levels are set to rise strongly, with around 41% of panellists forecasting an increase in employment. Despite the resultant likely increase in capacity, companies also expect a greater amount of work to be outsourced.

Inflation of input costs is set to accelerate substantially over the coming year. Almost 43% of firms expect a sharper annual rise in input prices, with salaries, outsourcing costs and raw materials all set to be sources of inflationary pressure.

Reflective of robust demand, firms expect to retain a significant degree of pricing power, and expect to pass on much of the increase in their costs to customers in the form of higher charges. Around 40% of companies forecast a faster annual rise in tariffs over the next twelve months.

## **CHINA**

Further rapid growth is expected in the Chinese service sector during 2008 and into 2009, according to the latest BRIC Business Outlook Survey. Companies widely predict higher levels of business activity, revenues, incoming new work and profits, with strong domestic demand remaining the principal driver of expansion.

Volumes of new business are forecast to rise at around 59% of all Chinese service providers surveyed, compared with just 3% anticipating a decline. Consequently, revenues are set to increase strongly, supporting further marked growth of profits.

Improved profitability is set to underpin investment in capacity expansion, with just under half of panellists predicting a rise in capital spending. Employment is also forecast to increase as firms recruit additional staff to deal with higher workloads.

Companies expect that sharp input price inflation will continue, with around 55% of firms predicting a faster annual rise in costs in twelve months time compared with the present situation. Raw material prices and non-staff costs are deemed as the principal factors set to drive inflation.

Firms expect to pass on a portion of the increase in their costs to clients in the form of higher tariffs. However, with approximately 24% of firms anticipating a rise in output prices, growth of charges is predicted to be well below that of costs.

Companies expect to increase the amount of work they outsource over the coming year. Approximately 18% of panellists predict growth of outsourcing, while less than 2% anticipate a fall.

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