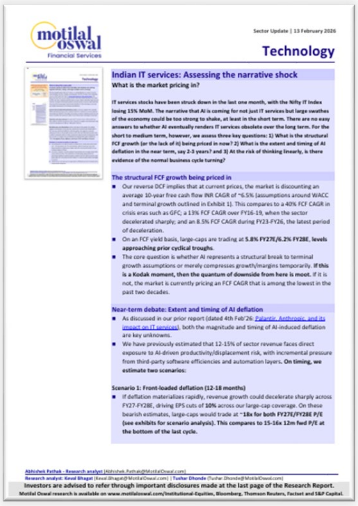
Technology


Sector Update | 13 February 2026

Technology

Indian IT services: Assessing the narrative shock

What is the market pricing in?

IT services stocks have been struck down in the last one month, with the Nifty IT Index losing 15% MoM. The narrative that AI is coming for not just IT services but large swathes of the economy could be too strong to shake, at least in the short term. There are no easy answers to whether AI eventually renders IT services obsolete over the long term. For the short to medium term, however, we assess three key questions: 1) What is the structural FCF growth (or the lack of it) being priced in now? 2) What is the extent and timing of AI deflation in the near term, say 2-3 years? and 3) At the risk of thinking linearly, is there evidence of the normal business cycle turning?

The structural FCF growth being priced in

- Our reverse DCF implies that at current prices, the market is discounting an average 10-year free cash flow INR CAGR of ~6.5% (assumptions around WACC and terminal growth outlined in Exhibit 1). This compares to a 40% FCF CAGR in crisis eras such as GFC; a 13% FCF CAGR over FY16-19, when the sector decelerated sharply; and an 8.5% FCF CAGR during FY23-FY26, the latest period of deceleration.
- On an FCF yield basis, large-caps are trading at **5.8% FY27E/6.2% FY28E, levels approaching prior cyclical troughs.**
- The core question is whether AI represents a structural break to terminal growth assumptions or merely compresses growth/margins temporarily. **If this is a Kodak moment, then the quantum of downside from here is moot.** If it is not, the market is currently pricing an FCF CAGR that is among the lowest in the past two decades.

Near-term debate: Extent and timing of AI deflation

- As discussed in our prior report (dated 4th Feb'26: Palantir, Anthropic, and its impact on IT services), both the magnitude and timing of AI-induced deflation are key unknowns.
- We have previously estimated that 12-15% of sector revenue faces direct exposure to AI-driven productivity/displacement risk, with incremental pressure from third-party software efficiencies and automation layers. **On timing, we estimate two scenarios:**

Scenario 1: Front-loaded deflation (12-18 months)

- If deflation materializes rapidly, revenue growth could decelerate sharply across FY27-FY28E, driving EPS cuts of **10%** across our large-cap coverage. On these bearish estimates, large-caps would trade at **~18x for both FY27E/FY28E P/E (see exhibits for scenario analysis). This compares to 15-16x 12m fwd P/E at the bottom of the last cycle.**

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Thoughts from the disruptors

We are on the road, meeting AI-native founders to understand where the value in IT services could migrate

In seeking answers to both the long-term future and the near-term outlook on the sector, we are going on the road and meeting founders of enterprise AI and AI-native companies to understand the disruption argument. **In this regard, we recently met Sayandeb Banerjee, Co-founder and CEO of MathCo: a Bengaluru- and Chicago-headquartered enterprise AI company with ~USD80m in revenue**. MathCo offers data engineering, advanced analytics, and agentic AI solutions; key partnerships include Snowflake and Databricks. Sayan is an industry veteran with over 25 years in data and analytics - across GenPact and Mu Sigma - before finally founding MathCo in 2016. **Our conversation spanned five themes:** (1) where is the value that is eroding from IT services migrating to; (2) whether AI is a cloud-style multiplier or divider for system integrator revenue; (3) incumbent SI moats; (4) the mid-tier and niche analytics competitive positioning; and (5) the T&M to outcome pricing transition. **Three durable themes emerged: domain context remains a moat, AI implementation services will see a clear J-curve, but timing is uncertain**, and the cloud analogy for AI could be flawed. Key questions and answers below.

What does this mean for IT services? We believe the industry will take some time to find a new equilibrium — be it deflation, new pricing models, or client expectations:

Where is the IT services value erosion actually going?

- There is genuine real-term revenue compression. The cost of delivering an outcome has fallen sharply; **these savings are currently being extracted almost entirely by enterprise buyers through productivity demands** and vendor price pressure.
- Model providers — Google, Anthropic, OpenAI — are not yet the economic winners. They are still absorbing heavy infrastructure costs and actively subsidizing enterprise adoption: discounted token costs and, in some cases, direct services co-investment. **Example:** a hyperscaler may commit USD100m in services spend alongside an enterprise Gemini rollout just to ensure the deployment succeeds.
- This is not an equilibrium. **As token costs normalize (trajectory is structurally downward) and model providers reduce subsidization, the value pool will need to be shared across enterprises**, model providers, and service ecosystem participants.

AI vs. the cloud cycle: multiplier or divider?

- Cloud migration was effort-intensive by design — moving petabytes from on-prem to cloud was a 500-person-team exercise for 18 months; the volume of effort was the product. **AI compresses that same migration to perhaps 50 people. The services revenue pool on any given workload shrinks even if the addressable universe expands.**

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- The old SI piggybacking model — first on SAP, then Salesforce/Pega, then AWS — is structurally challenged. Hyperscalers in the cloud era were broadly indifferent to services revenue; **model companies (Anthropic, OpenAI, and Google) are actively pushing to capture a larger share of the value they enable**.
- Platform strategies differ materially. Palantir is explicitly platform-only — exits services after year one (Palantir engineers are priced at ~USD1m/year); **MathCo is generating meaningful follow-on services revenue on Palantir stacks at multiple client sites. Google remains partner-ecosystem oriented;** AWS historically tried to capture services revenue directly via ProServe. Anthropic and Google appear to understand they need qualified partners for enterprise execution at scale, suggesting partner economics will not be zero but structurally smaller than the cloud-era equivalent.
- **Our prior analysis estimated 12-15% of sector revenue faces direct AI-driven displacement risk** (see our report dated 27th Feb'26: Making sense of the Anthropic product launches); the AI-as-divider dynamic suggests that even the "implementation multiplier" assumption embedded in the bull case needs revisiting.

Context moats: real but eroding faster than the market appreciates?

- **Context — deep knowledge of enterprise systems, processes, and data — is the central variable in enterprise AI ROI. SIs and BPM firms have genuine defensibility here:** decades of accumulated process and systems knowledge that a pure AI-native firm cannot replicate overnight.
- However, AI is democratizing context acquisition: what previously required five senior architects to map (data schemas, process flows, and system interdependencies) can now be generated by foundation models in hours.
- MathCo ran a B2B collections transformation for a client with no native domain context — **AI-generated schemas substituted for the gap that would previously have disqualified them. This was not possible 12-18 months ago**.
- Enterprises are also finding a way around the moat: buyers are increasingly willing to run PoCs with smaller, more agile vendors.

MathCo's positioning: decision intelligence

- MathCo's fundamental positioning is business-problem-led, not technology-led — a distinction that is becoming more valuable.
- **The entry point is always the business outcome (marketing spend optimization, pricing transformation, collections efficiency), not the tech stack. This consulting-with-data mindset is an edge over firms** that enter from the infrastructure or platform side and work upward.
- The company has deliberately stayed out of the infra layer — no system builds, no large-scale infrastructure work. Its stack runs from data engineering (staging data from SAP, Workday, and Salesforce to Databricks, Snowflake, or native cloud, with data quality and governance layered in) through to algorithm development (predictive modeling, forecasting, and optimization) and outcome delivery.

Case study: how AI has changed traditional data engineering

- Every enterprise AI initiative requires data to first be moved from source systems (SAP, Workday, and Salesforce) into a central staging environment - a data warehouse or lakehouse on Databricks, Snowflake, or native cloud. This process — extract, transform, load (ETL) — has been the backbone of enterprise data work for decades.
- **Traditionally, ETL was a headcount-intensive exercise. Depending on data volumes and system complexity, a pipeline build could require teams of 50-100 engineers over several months,** writing transformation rules and validating data quality. It was a natural home for large SI teams billing on T&M.
- Agentic ETL changes this fundamentally. An AI agent autonomously maps source schemas, identifies transformation rules, flags data quality issues, and builds the pipeline — with higher precision and a fraction of the human effort. **MathCo has built this into its NucliOS platform; when presented to a buyer running a traditional ETL program**, the cost differential opens the commercial conversation immediately.
- A second structural shift is happening alongside the effort compression. Traditional ETL staged data into SQL tables, which worked for dashboards but is poorly suited to how AI models reason. **Knowledge graphs and semantic layers are now the required foundation — and building these requires exactly the business-problem-first thinking** that MathCo is oriented around, rather than a purely technical approach.

Different types of outcome-based models and the impact of deflation

- Deflationary pressure is strongest wherever pricing still signals labor input. **Any proposal that references headcount — explicitly or implicitly — invites the buyer to demand the same output with fewer people. T&M-based pricing is structurally vulnerable; this is not a cyclical phenomenon.**
- Sayan drew a distinction that the market always confuses. Outcome-tied pricing: scope and price are defined around a business output and delivery milestones — not headcount. Outcome-contingent/gain-share pricing: fee as a function of actual performance improvement achieved (e.g., "improve collections by X%, share Y% of the upside").
- **Most large SIs saying "we're moving to outcome pricing" mean the former; gain-share is a materially different and harder commercial model** — very few firms are genuinely doing it at scale.
- Gain share will survive, but implicit outcome-based (which is still headcount dependent) will decline too.

Other points of discussion — J curve, AI model progress, and conclusion

- On the J-curve — unequivocal yes. **Enterprise AI at scale requires significant upfront investment in context before ROI materializes. Generic foundation models are irrelevant to an enterprise**; real ROI begins only when enterprise-specific contextual knowledge is fed in.
- Was Opus 4.6 a turning point? No single model release is a true inflection point — progress so far is a continuum, and the market periodically overreacts to individual versions. Some of the positioning by model companies amplifies this — it is partly a marketing dynamic, not purely a capability step change.
- **Over the next 2-3 quarters, we will monitor:** (a) pricing commentary in managed services deals — any explicit mention of outcome-linked structures in large-cap results; (b) AI-native partnership announcements involving Indian IT vendors and evidence of short-cycle AI-led deal wins (refer to Exhibits 5 to 7).

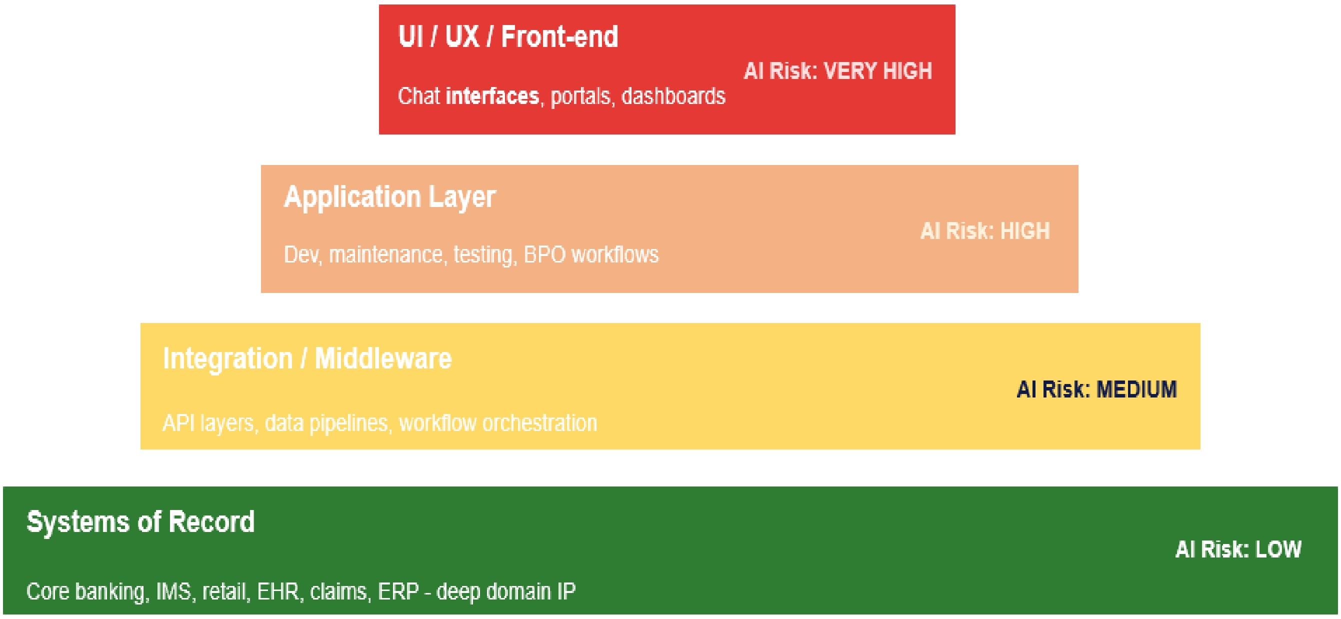
Our view on IT services

- The 4QFY26 results have done little to allay fears of disruption in the sector — **we expect most large-cap revenues to decelerate in FY27, a clear sign that deflation seems to be picking up**, and it may get worse before it gets better.
- The technology remains in flux, and it is difficult to expect clarity in the short term.
- **The two key variables we highlighted earlier remain unresolved:**
  (1) Timing and extent of AI deflation, and
  (2) Timing and scale of AI-led revenue opportunities.
  While deflation is becoming incrementally visible, evidence of large-scale, revenue-accretive AI deals remains limited and skewed toward smaller, short-cycle engagements.
- **We have consistently argued that context (enterprise systems, data, process knowledge) is the core defensibility of IT services (refer to Exhibit 1). This still holds, particularly in brownfield environments where AI deployment is complex**. However, AI is reducing the cost of context replication, lowering entry barriers for AI-native firms and compressing incumbents' pricing power over time.
- Our analysis of API calls for Claude and token usage for OpenAI reveals two key things: 1) software engineering is ground zero for AI invasion – 50% of all API calls target software engineering, and 2) **AI is currently being used only by cloud-first/AI-native enterprises. Of the top 20 token users for OpenAI, 90% are new-age companies**. This indicates that AI is easier to deploy in greenfield environments (see Exhibits 2 and 3).
- Near-term, value capture remains skewed toward AI enterprises, with IT services vendors absorbing pricing pressure, keeping growth visibility constrained.

Our research on Indian IT and AI:

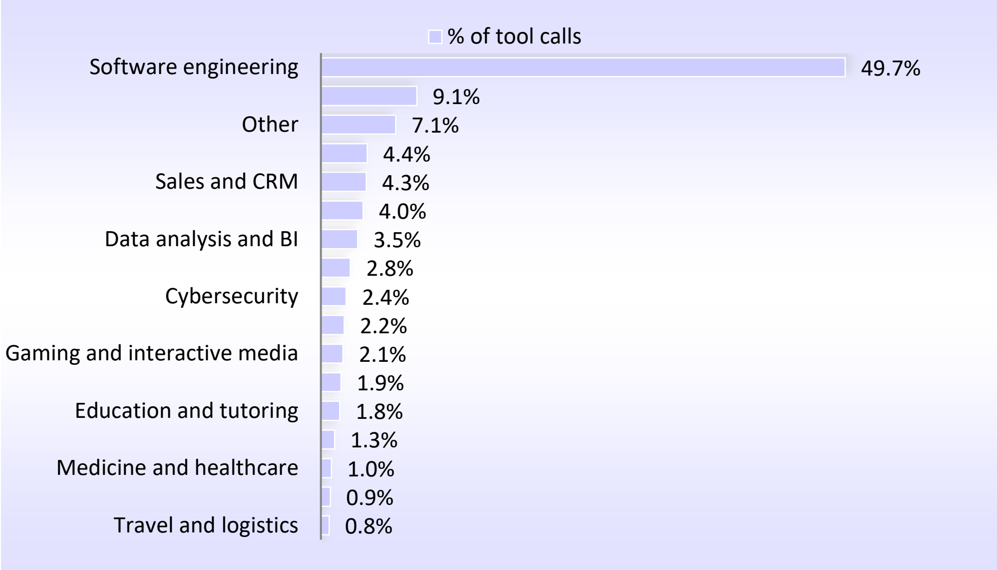
1) Mythos: Unpacking the next Anthropic model release | 8th April 2026
2) Making sense of the Anthropic product launches | 27th Feb 2026
3) Indian IT services: Assessing the narrative shock | 13th Feb 2026
4) Palantir, Anthropic, and its impact on IT services | 4th Feb 2026
7) GenAI and IT Services: The waiting game | 19th Sept 2025
8) Productivity gains and Indian IT – What is the value at risk? | 5th Jun 2025

Exhibit 1: Proximity to systems of record could be a MOAT, whereas UI/UX/Front-end could be at risk of being commoditized



Source: MOFSL

Exhibit 2: Software engineering is ground zero for AI invasion – 50% of all API calls target software engineering



Source: MOFSL Anthropic

Exhibit 3: OpenAI customers who have used 1T+ tokens

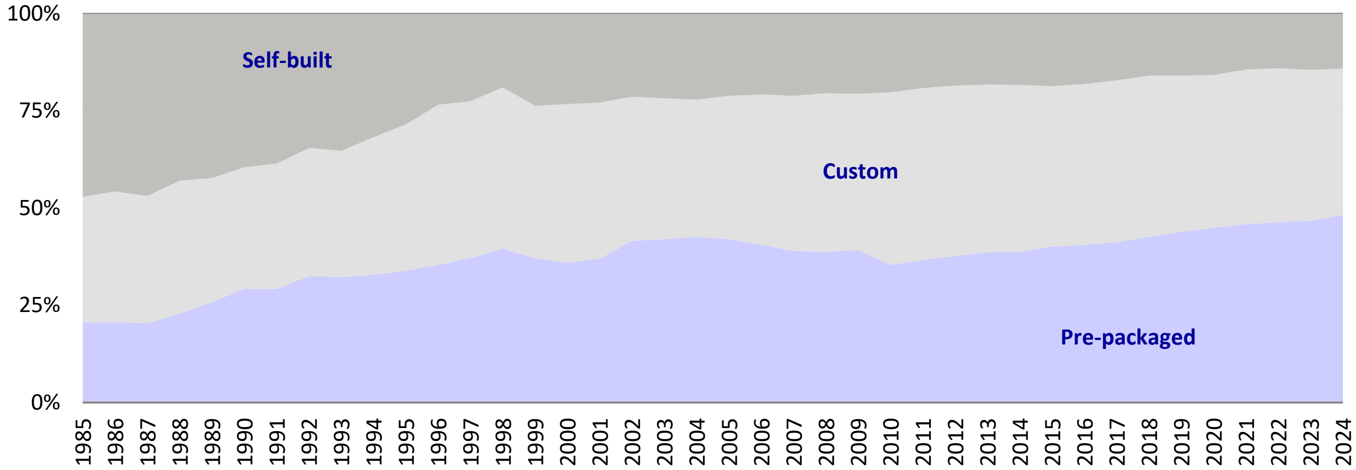
Most of these companies are new age, and enterprises with legacy burdens could need more foundational work before deploying AI at scale

	Company		Company
1	Duolingo	16	HubSpot / Dashworks
2	OpenRouter	17	JetBrains
3	Indeed	18	Delphi
4	Salesforce	19	Decagon
5	CodeRabbit	20	Rox
6	iSolutionsAI	21	T-Mobile
7	Outtake	22	Zendesk
8	Tiger Analytics	23	Harvey
9	Ramp	24	Read AI
10	Abridge	25	Canva
11	Sider AI	26	Cognition
12	Warp.dev	27	Datadog
13	Shopify	28	Perplexity
14	Notion	29	Mercado Libre
15	WHOOP	30	Genspark AI

Source: MOFSL, OpenAI

Exhibit 4: **Share of US enterprises' spend on software:**

US enterprises shifted from self-built to packaged software over the last three decades; self-built software now comprises ~14% of total US software spend vs. 35-40% earlier



Source: Bureau of Economic Analysis; MOFSL

Exhibit 5: Strategic partnerships with Anthropic

Date	Service Vendor	Program Type	Brief Description
			Partnership with Anthropic
Oct-25	**IBM**	Strategic partnership with Claude	❖ Claude will be integrated into select IBM software products, starting with IBM's new AI-first products.
Oct-25	**Salesforce**	Strategic partnership with Claude	❖ Expanded partnership to make Claude a preferred model for Salesforce's Agentforce platform,
Oct-25	**Deloitte**	Strategic partnership with Claude	❖ Anthropic's largest enterprise AI deployment to date; available to more than 470,000 Deloitte people.
Nov-25	**Cognizant**	Strategic partnership with Claude	❖ Anthropic to roll out Claude to 350,000 employees and embed Claude to accelerate coding tasks, testing, documentation, and DevOps workflows.
Dec-25	**Snowflake**	Strategic partnership with Claude	❖ USD200mn agreement to make Claude models available on the Snowflake platform to more than 12,600 global customers
Dec-25	**Accenture**	Strategic partnership with Claude	❖ This partnership focuses on scaling Claude adoption, training ~30,000 professionals, positioning Accenture as a premier AI coding partner, and deploying Claude Code to accelerate enterprise software productivity.
Feb-26	**Infosys**	Strategic partnership with Claude	❖ The collaboration will begin in telecommunications with a dedicated Anthropic Center of Excellence to build and deploy AI agents tailored to industry-specific operations.

Source: Company, MOFSL

Exhibit 6: Strategic partnerships with OpenAI

Date	Service Vendor	Program Type	Brief Description
Jun-25	**HCL Tech**	Strategic partnership with OpenAI	❖ HCLTech will embed OpenAI models (ChatGPT Enterprise & APIs) across its platforms (HCLTech AI Force, AI Foundry, industry accelerators) and customer solutions to drive large-scale enterprise GenAI adoption.
Jul-25	**Globant**	Strategic partnership with OpenAI	❖ Aim is to combine OpenAI's advanced models with Globant's digital engineering & AI delivery to build responsible, enterprise-wide AI transformations (agentic apps, language, translation, commerce, etc.)
Oct-25	**Salesforce**	Strategic partnership with OpenAI	❖ OpenAI to integrate frontier AI models into Agentforce 360 platform, aiming to deliver enterprise-grade AI tools to a wider range of businesses and regulated industries.
Dec-25	**Accenture**	Strategic partnership With OpenAI	❖ As part of the agreement, Accenture will equip tens of thousands of its professionals with ChatGPT Enterprise so the firm can leverage it in consulting, operations, and delivery work and help OpenAI scale its capabilities to enterprises.
Feb-26	**TCS**	Strategic partnership With OpenAI	❖ Tata Group employees will get access to Enterprise ChatGPT, accelerating innovation and productivity. In addition, TCS will leverage OpenAI's Codex to boost software engineering outcomes.
Feb-26	**Capgemini**	Strategic partnership (Frontier Alliance)	❖ Founding member of OpenAI Frontier Alliance; focus on enterprise AI deployment, agent workflows, and transformation
Feb-26	**Accenture**	Expanded partnership (Frontier Alliance)	❖ Part of Frontier Alliance with focus on enterprise-scale AI integration + deployment
Feb-26	**Boston Consulting Group**	Strategic partnership (Frontier Alliance)	❖ Strategy + enterprise AI transformation partner under the Frontier platform
Feb-26	**Mckinsey & Company**	Strategic partnership (Frontier Alliance)	❖ AI strategy + workflow integration partner for enterprise adoption
Apr-26	**Infosys**	Strategic partnership With OpenAI	❖ Infosys will combine OpenAI's technology with Infosys Topaz Fabric, its purpose-built, composable, and open agentic services suite, to help customers move from AI experimentation to practical, responsible deployment.

Source: Company, MOFSL

Exhibit 7: Some of the enterprise AI, LLM, and AI Agents/Tools partnerships by leading IT services companies

Company	Partner/Startup/AI Platform	Type of Collaboration/Focus	Brief Description
Accenture	**Palantir Technologies**	Expanded Strategic Partnership	❖ Launch *Accenture Palantir Business Group* to drive AI/data solutions for clients and co-develop large-scale AI/data deployments.
Cognizant	**WRITER (agentic AI platform)**	Strategic Partner for AI Agents	❖ Deploy domain-specific AI agents using WRITER's platform for enterprise use cases in regulated sectors.
EPAM	**Cursor**	Strategic Partnership	❖ Build & scale AI-native engineering teams and accelerate enterprise adoption of generative AI workflows.
Globant	**Faros AI (engineering intelligence)**	Strategic Startup AI Partnership	❖ Collaborate to accelerate agentic AI-based projects and software engineering intelligence workflows.
Capgemini	**Mistral AI**	Generative AI Model Platform Partnership	❖ Partner to bring cutting-edge generative models into scalable enterprise solutions (esp. regulated industries).
Capgemini	**C3 AI (Enterprise AI)**	AI Application Platform Expansion	❖ Extend partnership to deliver enterprise AI applications using the C3 AI suite in various industries.
Infosys	**Cognition (Devin, AI software engineer)**	Strategic AI agent / autonomous engineering collaboration	❖ Infosys and Cognition are collaborating to scale Devin, an AI software engineer/agent, across Infosys' internal engineering ecosystem and global client engagements, integrating it with Infosys Topaz Fabric to accelerate software delivery productivity, reduce modernization timelines, and boost developer efficiency.
TCS	**AMD**	Strategic collaboration	❖ Partnership to accelerate enterprise AI adoption, focusing on GenAI, hybrid cloud, and high-performance computing through co-developed, industry-specific solutions.
Cognizant	**Cognition**	Strategic Partnership	❖ Partnership with Cognition to help enterprises apply AI to SDLC work at scale. Unlike traditional coding assistants that suggest code, Devin can take on end-to-end development tasks independently, planning, executing, and validating work across complex systems.
Infosys	**Cursor**	Strategic collaboration	❖ Infosys will set up a Center of Excellence to drive AI-native software development by combining Cursor's AI-assisted coding tools with its Topaz Fabric, helping clients modernize and scale systems faster and with better quality.

Source: Company, MOFSL

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