

2007 Asia Pacific IT Market Predictions

December 18, 2006

IT Market Opportunity: Bulletin

INTRODUCTION

This Springboard Research document presents an analysis of key trends in the Asia Pacific IT market in 2006 along with a preview of the top ten trends that Springboard believes will shape the regional market in 2007. The analysis is based largely on Springboard's continuous tracking of the major trends and developments in the Asia Pacific IT markets. However, we also interviewed CIOs from some of the leading companies in the region, executives with leading IT vendors, and assessed publicly available information on countries, IT companies, products, technologies and services in the region to provide additional inputs.

2006: KEY TRENDS AND CURRENT LANDSCAPE

In 2006, the overall economic buoyancy in the Asia Pacific region, especially in China and India, continued to drive the IT market forward. There were some political and social risks to the market – such as the coup in Thailand and continued North Korean threats – but in general macro market conditions were sound for strong market performance.

Enterprise spending was boosted by the growing sophistication of Asian companies in the Large Enterprise and Small and Medium Business (SMB) segments, who increasingly view IT as a vital part of their organizational success. In addition, multinational firms continued to direct investments toward the Asian market, which also boosted spending across the region.

In our review of 2006, our analysts assigned awards for the key dynamics they deemed most noteworthy. Results are highlighted in Table 1 below, followed by background on each selection.

TABLE 1: 2006 MARKET AWARDS

Award	Selection
IT Buzzword of the Year	SOA
IT Trend of the Year	Software as a Service
Asian IT Market of the Year	India
Asian IT Company of the Year	Lenovo
Acquisition of the Year	HP / Mercury Interactive

Source: Springboard Research, 12/2006

SOA – IT BUZZWORD OF THE YEAR

The IT buzzword deemed most prominent in 2006 was clearly SOA. In IT media, product developments, acquisitions, CIO initiatives and elsewhere, SOA was everywhere to be seen and heard across Asia in 2006. Some in the market wrote SOA off as nothing more than a second incarnation of a prominent buzzword from years past – Web Services – while others raised it up as a savior for all that ails IT systems across the region. Whatever

one's view, SOA was clearly the buzzword that could not be escaped throughout the year.

SOFTWARE AS A SERVICE – IT TREND OF THE YEAR

We believe the IT trend of the year was Software as a Service, or SaaS. Following in the footsteps of successful SaaS firms such as Salesforce.com, software vendors of all types grappled with how to best offer SaaS capabilities in their products. From our interviews with leading international software firms throughout the year, it became apparent that most are still trying to understand how to respond to the trend and protect traditional sources of revenues as SaaS upstarts emerge as new threats. Everyone, however, acknowledged the long-term staying power of SaaS in Asia Pacific.

INDIA – ASIAN IT MARKET OF THE YEAR

India has always been viewed as a promising IT market for the long term, but present day revenues did not always match the promise or population. However, that started to change in 2006 as vendors in all market segments persistently identified India as one of their largest and fastest-growing markets in Asia. Eclipsed by China for the past decade, India was increasingly mentioned in the same context as its larger counterpart throughout the year. In our view, India crossed an important milestone of credibility and legitimacy in 2006 as a dominant regional IT market.

LENOVO – ASIAN IT VENDOR OF THE YEAR

After Lenovo's acquisition of IBM's PC business there were many questions about the Chinese vendor's ability to integrate such a large and globally focused American company. Although some questions remain, Lenovo has put many of those doubts behind it and has become increasingly visible and integrated. The company has posted profitability and is increasingly focusing on its global operations with effective branding and marketing campaigns. As such, we have selected Lenovo as our Asian IT Company of the Year.

HP / MERCURY INTERACTIVE – ACQUISITION OF THE YEAR

HP's US\$4.5 billion acquisition of Mercury Interactive gave a significant boost to the vendor's software business, which has struggled to generate solid performance on a consistent basis. In addition to its scale, we selected this deal as our acquisition of the year because it positions HP to benefit from a key trend we expect to impact the market in 2007 and beyond: SOA.

Other key trends of 2006 according to our analysts and market interviews are outlined below:

- **Expansion to Tier 2 and Tier 3 cities pursued as a key growth strategy for IT vendors in Asia Pacific:** A strong focus on expanding geographic footprints led IT vendors aggressively expand their office and channel networks in smaller cities across several countries. IT vendors like IBM, Intel, HP, Dell, Oracle, SAP and Sun benefited from expanding to new markets and profited from demand from new emerging centers of business and economic activity.

- **SMB focus boosted in 2006 as vendor programs become increasingly effective:** Almost all leading IT vendors increased their focus on the SMB space across the region, especially in China and India. Despite dominating the business universe in the region and contributing around 35% to the IT spending in Asia, the segment has largely remained underserved. 2006 was different from that perspective as IT vendors vied with each other to focus on geographic expansion, launching new products and modifying existing ones to better suit SMB needs. Key players also initiated partnerships and even created new SMB-focused business units in order to more aggressively tap the market segment. HP, Oracle, Dell, EMC, SAP, Hitachi and Microsoft were among the leading vendors who launched major partnership initiatives for SMBs. Geographically, Oracle and HP were among the vendors who focused significantly on expanding to Tier II and Tier III cities in China and India. These SMB-targeted initiatives showed positive results for many of these vendors.
- **Vendors enhance and expand vertical industry capabilities beyond finance, telco and public sector mainstays:** There was an increased focus on verticals like retail, healthcare, media and entertainment and education in 2006, even as finance, telecommunications, manufacturing and government continued to be most vendors' largest sources of business. The dynamism and growth in these verticals resulted in significant business for vendors from these segments. In fact, healthcare emerged as one of the fastest growing verticals in the region.
- **Small and Mid-Market customers increasingly turn to outsourcing and managed services, as average services deal sizes drop:** There was a renewed focus on services in 2006. While outsourced IT and managed services remained favorites mainly with large and upper-mid market customers, SMBs also started showing interest in these services. The year saw many early adopters from a segment in which most enterprises are still far off from realizing the value of the services. A key trend in the services market during the year was shrinking deal sizes and the emergence of small niche service providers. Large vendors, particularly IBM, launched service solutions especially targeted at small and mid market customers.
- **Focus on public service delivery drives government investments in IT:** Growth in the government segment was driven by major investment initiatives taken by governments across the region to improve their IT infrastructure in order to more efficiently deliver public services and also improve their own organizational efficiency. Government organizations in Australia, China, Hong Kong, India, South Korea and Singapore made significant investments in IT during the year. The Public Sector also emerged as one of the leading adopters of SOA in 2006.

2007: TOP PREDICTIONS

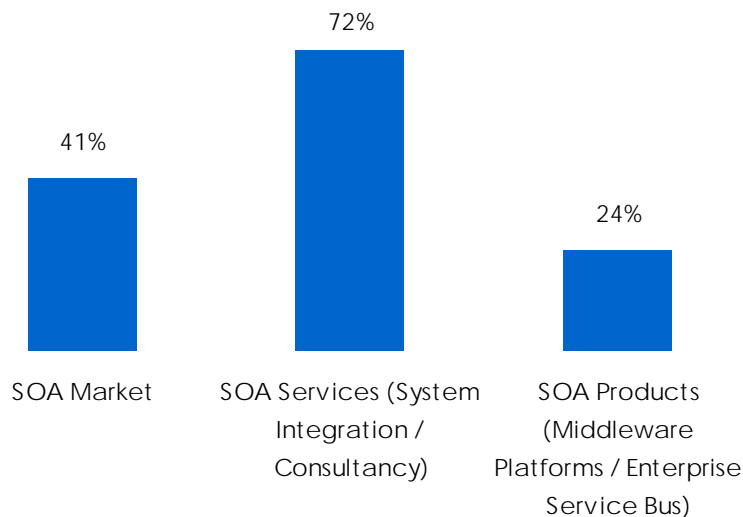
Even as new investments in technology, products and services will continue to change the IT landscape in enterprises across Asia Pacific, Springboard Research expects CIOs to focus on two key goals in 2007 --- doing more with less and making IT more agile and aligned to business needs. So any new technology, application or services they evaluate must appear to meet these goals before being considered for deployment. With that in context, Springboard Research presents here a preview

of top 10 trends that will shape enterprise IT in 2007 besides significantly impacting the business of IT in the region.

#1: IT VENDORS WILL SEE SERVICE-ORIENTED ARCHITECTURE GUIDING A LARGER PERCENTAGE OF THEIR CUSTOMERS' IT INVESTMENTS

Riding on success stories from 2006, SOA will see greater adoption in Asia Pacific in 2007. Creating more agile information systems and making better use of existing infrastructure will continue to be the leading factors boosting SOA adoption in Asia Pacific. An increased awareness of SOA coupled with the ever-increasing pressure on CIOs to link IT investments to business benefits, provide less complex services, and lessen the cost of development and deployment of new applications and services will encourage more organizations to invest in SOA. As we had predicted earlier in the year, the SOA market in Asia Pacific will grow 41% in 2007 in the region. A significant portion of this growth will be contributed by SOA related system integration and consultancy services.

FIGURE 1: SOA REVENUE GROWTH IN ASIA PACIFIC – 2007



Source: Springboard Research, 12/2006

Whether organizations embrace the term SOA or not, they will continue to look at ways to integrate their IT more effectively with their business goals and in the process also focus on dissolving IT complexities. Given that, we expect SOA to steadily spread its influence throughout Asian enterprises in 2007 and in the process fundamentally alter the way IT systems are operated and managed.

#2: VIRTUALIZATION WILL MATURE AND COME INTO ITS OWN IN 2007, DRIVING CHANGES IN HARDWARE AND SOFTWARE PRICING MODELS

Very much like SOA and SaaS, the drive of 'doing more with less' will be central to the virtualization drive in business enterprises in 2007. Despite the advantages, virtualization has not always been a smooth ride for organizations. Organizations that go for it often face new management and performance issues, and vendors have been building unrealistic expectations of benefits from virtualization. We believe that in 2007 virtualization will be one of the hottest technologies in Asia with greater

technology maturity and fewer unrealistic expectations. Virtualization will be hot with servers, storage and applications. We expect virtualization to not only impact the IT systems of enterprises but also the bottom line of IT vendors who will be forced to rework their hardware and software pricing models as the trend becomes more pervasive.

#3: ORGANIZATIONS WILL SEE A SHARP INCREASE IN THEIR FOCUS ON NETWORK-FRIENDLY APPLICATIONS

Our interviews with prominent CIOs indicated optimizing network performance will be a key goal for them in 2007. This will fuel the demand for applications that are less complex, do not consume too much bandwidth and do not add to network complexity. There will be more urgency for thinner bandwidth optimized ERP, CRM and SCM applications in organizations that are expanding to new markets and geographies. On the other hand, CIOs will increasingly seek solutions to bridge the divide between network capabilities and demands of enterprise software. Applications are typically not optimized for enterprise networks and are often inflexible to the needs of enterprise software thereby affecting application performance. Moreover, there is a big divide between those concerned with running and managing the network and those developing and procuring applications. As such, we expect CIOs to focus as much on network optimization as on application development and procurement. Nevertheless, CIOs will continue to prefer applications that are easy to configure and use by business users so that they can function without much intervention by the IT department. This will be one of key factors driving many organizations to consider SaaS (Prediction #5).

#4: WINDOWS VISTA WILL STIMULATE IT BUYING ACTIVITY, BUT MAINSTREAM ADOPTION WILL BE DELAYED IN 2007

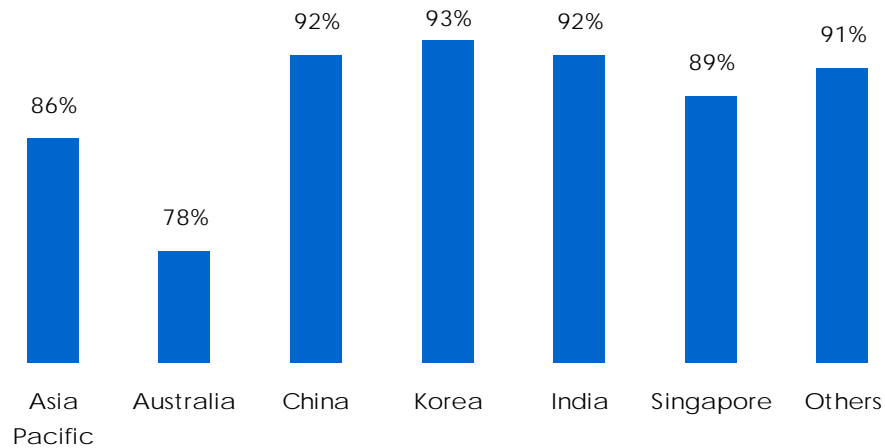
Microsoft's latest big ticket offering will keep users occupied as they begin considering upgrades. While many of the reports on problems and faults with Windows Vista may be exaggerations, CIOs and business users are going to be concerned with facilitating smooth migrations. We believe organizations going in for a Vista upgrade will have to incur extra hardware costs, an expense line item that many of them may not have planned for while budgeting for the upgrade. Many CIOs we interviewed indicated that because a Vista upgrade will entail hardware upgrades as well, many companies are likely to go for Vista only when they have planned a hardware replacement. As such, in spite of Vista's potential to stimulate IT procurement activity, 2007 will see only a slow start to Vista adoption.

#5: SOFTWARE AS A SERVICE WILL SEE SUBSTANTIAL GAINS IN ACCEPTANCE AMONG ASIAN ENTERPRISES

As Asia Pacific enterprises continue to be more demanding with their IT needs, they will increasingly look for external support. A growing number of organizations will focus more on their business and less on IT – a key reason that will fuel the growth of on-demand software services (and other IT services). This is especially true in the Small/Medium business (SMB) space where outsourcing applications has traditionally not been an option. SaaS is stepping in to provide SMBs the ability to leverage world-class, robust applications that they do not have to manage. Enterprises will be more focused on services both internally (and therefore look at SOA to deliver applications as services) and externally (and therefore embrace SaaS and other on-demand services). While this will not translate to an all-out embracing of Software as

a Service across the organization, they will surely be more inclined to adopt the on-demand model for their non-critical operations.

FIGURE 2: SAAS REVENUE GROWTH IN ASIA PACIFIC – 2007



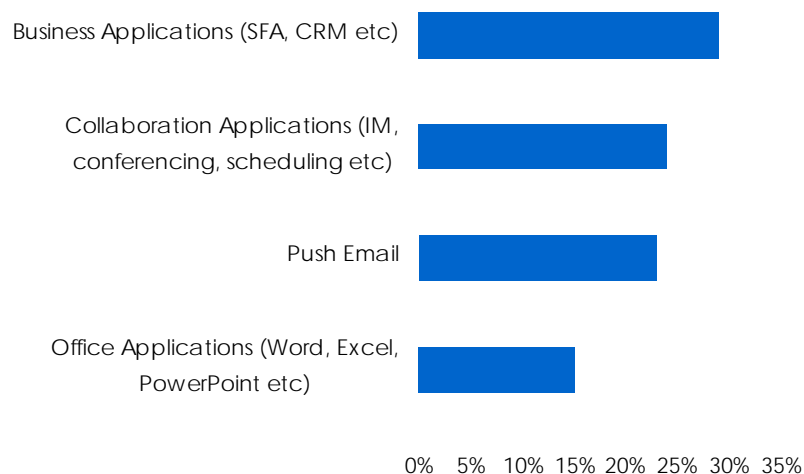
Source: Springboard Research, 12/2006

A major push for SaaS adoption will come from traditional software vendors, especially Microsoft, who will engage SaaS more actively to profit from it. We expect large software vendors to recognize SaaS as a more dynamic element of their business. The onslaught of upstart SaaS vendors and Google offering applications on-demand will force the likes of Microsoft and others to more openly recognize the virtues of the on-demand model. Moreover, we expect 2007 to see the emergence of a number of new partnerships between traditional software vendors, local ISVs, SaaS vendors, and telcos leading to the growth and development of new SaaS ecosystems in the region. The year will also see a number of venture-funded SaaS start-ups in the region.

#6: MOBILITY WILL BECOME A KEY ELEMENT OF ENTERPRISE IT STRATEGY

Despite being on the horizon for many years now, mobility adoption in organizations has not been particularly widespread. Despite a growing number of mobile workers, organizations have little to support them or extract real business value out of mobility. We expect 2007 to be different. As the population of mobile workers continues to grow in the region, we expect Asia Pacific enterprises to adopt a clearer and more long-term strategic approach to the deployment of mobile technologies in 2007. With mobile and wireless technologies becoming more pervasive with the launch of more high speed wireless networks based on WiMax or 4G cellular technologies, it will become increasingly difficult for organizations to keep mobility out of their IT strategies. However, given the personal nature of mobility most organizations will have a tough time managing it in their current IT environment. A major challenge will be the ever-changing behavior of mobile users that are harder to control.

FIGURE 3: MOBILE APPLICATIONS DEPLOYMENTS – 2007



Source: Springboard Research, 12/2006, Based on a survey of 155 CIOs / IT Managers who were asked what mobile applications they will prefer to deploy in the next 1 year

#7: THERE WILL BE AN INCREASE IN THE NUMBER OF PARTNERSHIPS IN THE OPEN SOURCE ARENA

The open source world will see some major changes in 2007. Quite ironically but not surprisingly, many of the significant changes will be driven by initiatives from the proprietary world. We believe that a growing acknowledgement among non-open source vendors about its value proposition will force them to include it in their business strategies. The foundation for this has been laid in 2006 with Oracle announcing its intention to emulate Red Hat's success in the enterprise space. We also expect Microsoft to change its outlook on open source, especially Linux, significantly. It already has acknowledged Linux's growing prominence in the IT infrastructure by working out a collaboration deal with Novell, a Linux and Open Source software vendor. We expect Microsoft to get into more open source partnerships in 2007 with other Linux vendors.

#8: THE SMB SEGMENT WILL CONTINUE ITS MOMENTUM IN 2007, AND INCREASINGLY TURN TO OUTSOURCED SOLUTIONS

Asian SMBs became a more important market segment in 2006 as almost all large IT services and software vendors came up with a more focused strategy to target the segment. We expect this momentum to continue in 2007 and reach a new level – as more products become commodities, IT vendors will target SMBs with an array of outsourced and managed services. We expect SMBs in Asia Pacific to gradually start embracing these services in 2007. Packaging services to suit SMB IT budgets and communicating business value of outsourced and managed services will be two of the biggest challenges that service providers will face with SMBs. However, despite that, as SMBs expand their operations driven by the positive economic climate in the region, we expect a significant number of SMBs to become early adopters of outsourced IT and managed services

#9: INDIAN IT SERVICE PROVIDERS WILL COME UNDER INCREASING PRESSURE FROM MNC PROVIDERS, WITH SOA SERVING AS A KEY EXAMPLE

Top Indian IT services providers, no longer just selling the low cost advantage but much more, will come under increasing pressure from MNC providers, especially in the SOA domain. With much larger SOA engagements and investments in technology, we believe that the likes of IBM, Accenture and HP who have been making the biggest investments in SOA will be better placed to corner the offshore market for SOA related consultancy and services than Indian companies like TCS, Infosys and Wipro. The MNC providers' experience in process automation and better client reference base will work to their advantage. Moreover, the MNCs have been building SOA competency across the spectrum by not just investing in new R&D but also by acquiring companies to fill out their software and service portfolio. However, despite the Indian provider-MNC SOA slugfest, India will emerge as the most significant hub for delivery of offshore SOA services to customers across the globe. The following table lists some of Indian services providers with SOA capabilities and MNCs who have invested in building SOA capabilities in India.

TABLE 2: SOA INVESTMENTS IN INDIA BY VENDOR

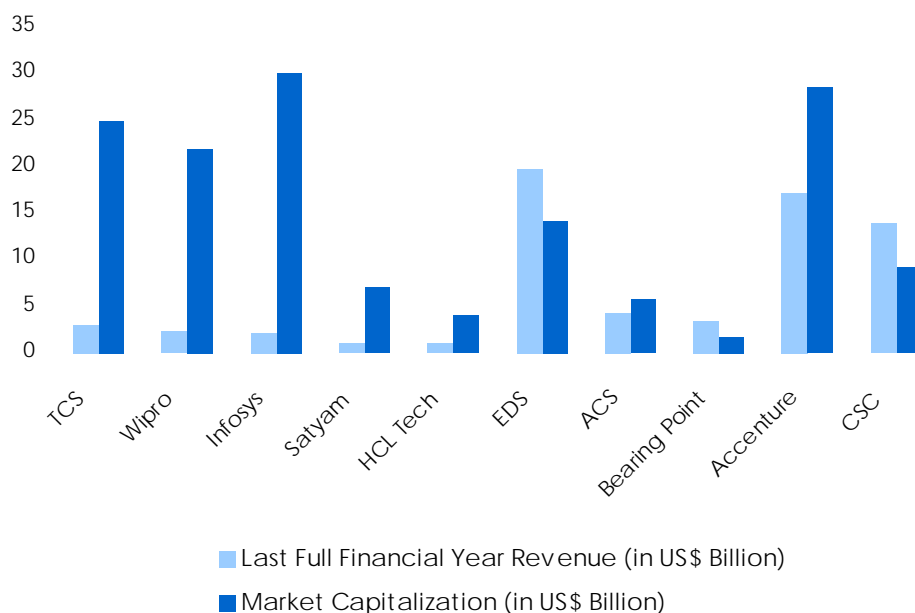
Leading Indian IT Services Providers with SOA Capabilities	MNC Vendors with SOA Competency/Excellence Centers or SOA Related Investments/Plans in India
TCS	HP
Wipro	IBM
Infosys	Sun Microsystems
Cognizant Technologies	Accenture
Satyam Computer Services	BEA Systems
HCL Technologies	WebMethods
Patni Computer Systems	

Source: Springboard Research, 12/2006

#10: INDIAN IT SERVICE PROVIDERS WILL BE MORE AGGRESSIVE WITH ACQUISITIONS, WITH ONE MAJOR TIE-UP EXPECTED BEFORE THE END OF THE YEAR

New competitive pressures, including the urgency to increase the depth of offerings, will force Indian IT companies to develop more aggressive acquisition plans in 2007. While some of the Indian companies like TCS and Wipro have been regularly acquiring companies, they have not focused on large acquisitions. We expect this trend to change in 2007. Even as Indian companies become more aggressive in acquiring service providers with strong bases in Latin America and Eastern Europe, we expect Indian service providers to team up with private equity investors and other funds for big ticket acquisitions in the US as well in 2007. The business environment of some of the large US vendors will make them easier acquisition targets for Indian companies.

FIGURE 4: REVENUE AND MARKET CAPITALIZATION OF INDIAN AND US IT SERVICES COMPANIES



Source: Company Data / Springboard Research Estimates / Market Capitalization as of December 2006 / Annual Revenues for last full financial year / All figures in US\$

CONCLUSION

Building on the key trends of 2006, the Asia Pacific IT market is expected to exhibit healthy growth and dynamism in 2007. The overarching trend shaping enterprise IT investments will be the drive to make IT systems increasingly agile, manageable, cost-effective and virtual. Technologies and strategies that are built around this key dynamic will be well placed for success in the year to come.