



### Expert Update

February 20, 2026

### ***Sustaining margins to remain a challenge***

#### Quick Pointers:

- Expect 20-50% deflationary impact on traditional IT services
- Legacy modernization and data readiness for AI may offset revenue loss in the near term, but put margins at risk

*We recently hosted an IT expert to understand the AI impact on labor-intensive revenue models, run by IT services and BPM companies. They anticipate that, sooner or later, revenue models will have to shift to outcome or output-based constructs. Complex areas like platform engineering, AI implementation and agentic deliveries would be more relevant vs. downstream activities, even the ADM service lines would witness a sharp deflationary (30-40%) pressure. As a result, delivering business outcomes becomes less resource-intensive and less dependent on large engineering teams. The IT expert anticipates 20-50% deflationary impact (overall) coming through reducing process complexity and turnaround time. However, large part of this deflationary impact for IT services would be offset by: (1) building AI-ready infrastructure, (2) undertaking model and API development/customization, and (3) creating an agentic automation ecosystem, which are a multi-year consulting and engineering cycle. For BPM companies, in the near term, their revenue might bump up temporarily due to rising AI implementation demand, but sustaining the same would be challenging, as existing automations are replaced by intelligent agentic workflows.*

*Despite IT services companies being relatively well positioned to offset the deflationary revenue pressure, sustaining margins could be a challenge as: (1) the deal to delivery ratio is likely to shrink, (2) reducing entry barriers would increase competition from AI-native vendors, and (3) enterprise plumbing activities would fetch relatively lower margins, thereby impacting the overall margin mix. We believe the companies that drive active engagements in high-end complex activities and anchor proprietary platforms & agentic workflows to the enterprise ecosystem, would be able to arrest margin pressure. However, shrinking deal sizes would require more boots on the ground to drive revenue stability, which in turn could put further pressure on margins.*

**Rapid shift in business model:** Post-Y2K, IT services providers have consistently moved up the value chain, with each technology wave expanding scope and adding incremental layers of work. AI marks a structural break: rather than creating additional layers, it compresses efforts across all layers reducing team sizes, shortening project cycles, and weakening traditional FTE-based pricing models. Consequently, the industry is transitioning from scale-driven growth to capability- and IP-led competition, introducing structural margin pressure despite sustained demand.

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**Business risk to traditional IT services:** AI-led productivity is structurally deflationary for traditional IT services. GenAI and agentic automation are compressing efforts across the SDLC and enterprise workflows (30–40% productivity gains; in select use cases, up to ~90% resource compression), leading to lower ADM volumes and shorter project durations. The industry could face a 20–50% deflationary impact depending on client IT maturity. While revenue may remain supported by new AI-led work creation, margin sustainability, not topline growth, emerges as the primary structural risk.

**New opportunities to offset impact on traditional services:** Data readiness is emerging as the next large services opportunity as enterprises must modernize documents, APIs, legacy architectures, and knowledge repositories before scalable AI deployment, creating a multi-year consulting and data engineering cycle. In parallel, new revenue pools are forming across AI infrastructure enablement, model integration, custom enterprise AI applications, and broader automation ecosystems. While these adjacencies can partially offset the structural erosion in traditional ADM services, they are likely to operate at comparatively lower margins.

## Key takeaways

- AI has materially simplified output generation—users can now issue a text or voice command, and the system will execute the backend workflow end-to-end, including code generation, data retrieval, validation and orchestration. This removes much of the manual effort previously required across development and operations, significantly lowering process complexity and turnaround time. As a result, delivering business outcomes becomes less resource intensive.
- Barriers to entry have materially declined as AI enables smaller, highly skilled teams to deliver outcomes that previously required large-scale offshore delivery models. As a result, mid-sized firms and niche AI-native players can credibly bid for large transformation programs, intensifying competitive intensity and pricing pressure—even as the cost of specialized AI talent increases.
- The traditional FTE-linked pricing construct is structurally weakening as enterprises pivot toward outcome- and value-based commercial frameworks. This shift decouples revenue from headcount growth and creates sustained margin pressure across vendors, particularly those reliant on labor-arbitrage models.
- AI is reducing SaaS stickiness by materially lowering integration complexity and customization effort. With GenAI and agentic frameworks enabling rapid configuration, orchestration, and extension of core systems, enterprises are increasingly reassessing the traditional buy-and-integrate model. The build-vs-buy equation is shifting as organizations leverage AI agents to develop custom internal applications tailored to specific workflows, reducing dependency on SaaS platforms and increasing vendor churn risk.

- BPO and RPA-heavy players face elevated disruption risk as automation transitions toward intelligent, agentic workflows capable of handling end-to-end processes with minimal human intervention. While near-term demand may rise from AI implementation, redesign and transition programs, the steady-state revenue pool is at risk of compression as automation reduces transaction volumes and FTE intensity.
- Across segments, hi-tech enterprises are materially ahead in AI readiness given sustained prior investments in digital and data infrastructure; consequently, they have already captured a significant share of productivity pass-backs from service providers. Within BFSI, large banks and capital markets clients are more advanced relative to insurance players in AI adoption. As a result, these relatively mature segments are likely to see lower deflationary impact, whereas less mature verticals could experience sharper deflation as AI infrastructure adoption scales.

## Analyst Coverage Universe

Sr. No.	Company Name	Rating	TP (Rs)	Share Price (Rs)
1	Coforge	BUY	2,150	1,636
2	Cyient	Hold	1,070	1,109
3	Fractal Analytics	BUY	1,260	900
4	HCL Technologies	BUY	1,910	1,667
5	Infosys	BUY	1,900	1,391
6	KPIT Technologies	Hold	1,090	1,047
7	L&T Technology Services	Hold	4,070	4,244
8	Latent View Analytics	BUY	630	457
9	LTIMindtree	Hold	6,000	6,407
10	Mphasis	BUY	3,480	2,800
11	Persistent Systems	BUY	7,360	6,343
12	Tata Consultancy Services	BUY	4,040	3,240
13	Tata Elxsi	Hold	5,500	5,793
14	Tata Technologies	Hold	660	651
15	Tech Mahindra	Accumulate	1,860	1,671
16	Wipro	Hold	260	267

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<b>Buy</b>	: > 15%
<b>Accumulate</b>	: 5% to 15%
<b>Hold</b>	: +5% to -5%
<b>Reduce</b>	: -5% to -15%
<b>Sell</b>	: < -15%
<b>Not Rated (NR)</b>	: No specific call on the stock
<b>Under Review (UR)</b>	: Rating likely to change shortly

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