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Flat Chance

As companies keep IT spending in check, executives have to make some hard choices about what they can live without.

Vincent Ryan, CFO Magazine
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As IT director of NYK Business Systems Americas (a unit of Tokyo-based NYK, a global container-shipping company), Kurt Schubert has a list of things he'd like to do, and a list of things he needs to do.

He may have to forgo both.

Even essential projects, such as shoring up the redundancy and availability of NYK's custom applications, or developing a new disaster-recovery plan, now look like extravagances. The executive management of parent company NYK is asking for cuts across the board in next year's IT budget. Schubert is in a tough spot: instead of allowing the IT director to improve system availability, the 2010 budget could actually worsen it if the budget forces him to cut support staff for key applications.

Many CFOs and CIOs face similarly difficult scenarios and constraints as they look ahead to 2010. After nearly two decades of continuous increases, IT budgets have finally proved that they aren't immune to market forces. According to research firm Computer Economics, 2009 will mark a holding pattern for IT capital budgets, which will match 2008 levels, and for IT budgets as a percent of revenue, which will remain at an average of 1.5%. A report from Goldman Sachs is more grim: it says U.S. IT spending will fall by more than 10% this year.

Those figures may represent a bottoming out. Or maybe not. Goldman Sachs projects IT spending to rise 2% globally in 2010, but estimates that U.S.-based buying will contract by nearly 1%. Forrester Research is more optimistic, seeing an 8% increase in 2010 IT spending, a level reminiscent of the glory days of the dot-com boom.

As they finalized their budgets in October, however, CFOs and IT executives sang a different tune. IT spending will be flat to down for 2010, they say. And capital investment in IT will be almost nonexistent — only the most necessary of projects are winning approval for next year from executive management and boards of directors.

"We don't have any major needs to expand our network or do any big software projects; we have completed most of our major infrastructure projects over the last three years," says Brad Buss, CFO of Cypress Semiconductor. "And we expect to hold head count relatively flat over the next year."

Unkindest Cuts

Capital investment is on the back burner at companies of all sizes. At Baptist General Convention of Texas, a religious organization that supports the ministry work of churches, universities, and hospitals, the IT budget for 2010 has been cut by 10%. Director of IT Dave Lyons supports 280 PC users. He has changed a couple of staffers from full-time to part-time and plans to refresh fewer PCs next year than scheduled.

But those savings are offset by having to buy seven or eight new servers and paying more for software contracts. "Since the ministry has to run lean, I want to be there with them. But at the same time we can't go below a certain level and provide the services we have to provide," he says. Lyons would love to buy an e-mail marketing server because the current service he uses is not integrated, but that's out of the question.

NYK Business Systems Americas, which serves a much larger company, will also have a smaller budget in 2010, calculating in already-announced head-count reductions in application support and a drive to save on server infrastructure. "There is not a lot of capital spend," Schubert says.

Other companies may be investing, but not in discretionary projects. Nick Caplanson, CFO of Norwich, Connecticut-based Dime Bank, is due to deliver the community bank's IT budget later this month, and when he does, it will reflect a "loosening up of the purse strings — just a bit."

But whatever modest increase there may be owes something to timing: when the financial-services meltdown hit in 2008, the community bank postponed projects it had budgeted for in its 2009 tech-spending plan. Now some of them may finally get funding, but the proposed new outlays for 2010 hardly represent a return to normal levels of investment.

Dime will spend more on software licensing and maintenance to support an expanded user population resulting from the opening of a new branch. In addition, the bank will roll out a fraud- and security-detection system next year, which it deems necessary due to an industrywide increase in bank fraud that has coincided with the recession. The new system can be justified by its focus on keeping losses low, protecting customers, and helping Dime maintain high ratings during regulatory exams, Caplanson says.

Priority Areas

Where else might companies plan to spend their limited IT allocations in 2010? The release of Microsoft's Windows 7 operating system could lift spending on PC hardware and software, says Andrew Bartels, an analyst at Forrester Research. "For many companies, it's time to buy new PCs," he says, "because they have desktop computers that are three and four years old."

But corporate customers typically delay buying Microsoft's latest OS until its durability is proven, so the bulk of that spending might not take place until after 2010. Indeed, Dime Bank will likely do a major network and desktop infrastructure upgrade pending the release and broad acceptance of Windows 7, says Caplanson, but not until 2011.

"Virtualizing" servers by installing software that allows one server to do the work of many is another spending wave that could up the level of investment in 2010. In the next 12 months, IT managers surveyed by Goldman Sachs expect to increase the percentage of installed servers that are virtualized to 54% from 37%.

Schubert at NYK Business Systems Americas is trying to optimize server infrastructure at two North American data centers. "We're trying to replace servers coming off lease with fewer boxes to cut down on maintenance costs," he says.

Funding for technology that addresses regulatory requirements and enhances data security will also trend higher in 2010. "Audits are not going away, and in some cases they are more intense than ever," says Bernie Wedge, leader of the Americas IT risk and assurance practice at Ernst & Young. Automation of governance and compliance processes is likely to pick up as head-count reductions put stress on companies trying to implement and adhere to controls, Wedge says.

Security software and services budgets will grow 4% and 3%, respectively, in 2010, predicts Gartner, outpacing other areas of infrastructure software and services. Implementing and improving processes around data leakage from the corporation will take precedence, Wedge says. "There are so many locations where [network] clients maintain data now, and you have employees downloading information to their BlackBerries. The further away you move data, the weaker the controls get."

A Midyear Bump?

There is a belief that if the economy and corporate revenues pick up, enterprises will raise IT budgets during 2010. That happened after the dot-com bust, but CFOs and directors of IT say this flexibility on the upside is much less likely today.

"The last couple of years we were required to spend *less* than budget [90% in 2009]," says Lyons of Baptist General Convention of Texas. "Based on what the CFO has said, any excess would go into reserves. We wouldn't expect it to go to spendable budgets."

Dime Bank's Caplanson is in a similar situation. The banking company typically builds about 5% contingency for unanticipated items into the IT budget. "But it is rare that we use this contingency, and therefore [we] often come in below budget for the year," Caplanson says. "This year is no exception."

Bartels thinks that enterprises will get out their checkbooks in 2010 largely because they did not overspend on IT during the past three years, despite the cheap cost of capital. "They didn't buy servers, software, and routers like they were going out of style," he says. Thus, the next two years will see "the lid taken off pent-up demand."

That's the bullish view, anyway. Others argue that, at best, the lid will be screwed down a little less tightly.

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Better Budgeting
IT Cost Management for Lean Times

• **When justifying expenditures to the board, speak in business terms.** Since most IT projects hit multiple accounts, managers need to know where the dollars are going from a business perspective (the distinct projects) rather than from an accounting perspective (buckets in the general ledger), says Lawrence Serven, president of XLerant, a budgeting-and-planning-software firm. When the mandate comes down to cut costs, this will also help IT assess the business impact of spending cuts.

• **Go beyond the general ledger and develop service-level costing** for business units, helping them determine what they are spending their IT dollars on, says Eric Berg, vice president of marketing at Apptio, developers of an IT cost-optimization tool. What is the cost per e-mail mailbox? Include all elements — hardware depreciation, software, facilities, labor, and so on. This helps business units weigh alternatives (like cloud computing) to internal IT services, and also lets IT benchmark outlays against others in its industry.

• **Push budgeting and budget accountability deep into the organization,** says Serven. If managers do their own budgets, the results are much more likely to be accurate, since day-to-day spending decisions are in their hands.

• **Keep IT focused on the budget** by developing a bonus payment or a portion of bonuses aligned with effective budget management. Dime Bank is considering just that in its bonus plan for 2010, says CFO Nick Caplanson.

• **Increase visibility into IT operational spending.** About 75% to 80% of the typical IT budget is operational cost, but do the CFO and CIO know what makes up those costs? How do costs compare across data centers, across applications, and across locations? Once cost models are established, the organization can perform "what-ifs." "What if we shut down our New Jersey data center? That's a framework for financially sound decisions," Berg says. — *V.R.*