COVID-19 Drags 2020 Spending Outlook to Minus 5%. IT spending is now projected to decline by 5% in 2020. This according to the latest survey data and analysis by ETR. While the drop represents a 900 basis swing from 4% consensus growth entering 2020, tech spending remains bifurcated with some suppliers and sectors showing significantly [...]

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IT spending is now projected to decline by 5% in 2020. This according to the latest survey data and analysis by ETR. While the drop represents a 900 basis swing from 4% consensus growth entering 2020, tech spending remains bifurcated with some suppliers and sectors showing significantly stronger spending momentum than others.

In this Breaking Analysis we bring in ETR’s Direct of Research, Sagar Kadakia to examine the following:

- Update the current market forecast
- Discuss the relative outlook by industry
- Drill into several sectors including security, cloud, collaboration and IT consulting

Key Highlights

- COVID-19 Drags 2020 Spending Outlook to Minus 5%.
- Hard hit industries expect budget declines i.e. airlines, entertainment, energy, etc. Industries showing relative strength include government, healthcare and IT/telco.
- The market for IT suppliers is notably bifurcated. Those suppliers well-positioned have clear cloud plays with SaaS models, WFH plays and modern cloud native stacks. Legacy on-prem vendors appear to be hardest hit and selected cyber security players stand out from the crowd.
- The big three U.S. cloud platforms, Azure, AWS and GCP show strong spending momentum with Azure showing the strongest velocity.
- Collaboration and productivity software players are not all well-positioned. Survey data suggests leaders like Dropbox, Box, Slack and some others are seeing higher than normal replacement rates.
- Microsoft Teams appears to be the winner in the collaboration space, especially within larger organizations, while Slack comes under fire.
- Counter to recent market reports, IT services, consulting and outsourcing will see notable declines based on survey data with more than 1,200 CIOs and IT practitioners.
- Possible negative implications for IBM Red Hat.

Forecast now Calls for a 5% Decrease in 2020 IT Spending

As we’ve reported previously, the chart below shows the declining sentiment over the course of the latest survey - which took place at the height of understanding the Coronavirus impact in the U.S. The survey includes the responses of 1,200+ CIOs and IT professionals. Note that ETR conducted event analysis after each cited milestone to measure the declining sentiment.
Breaking Analysis: COVID-19 Drags 2020 Spending Outlook to Minus 5%

The key point here is that if you isolate on the more recent survey responses, taking into account the more recent sentiment, the data suggests that a 5% decline is the most likely scenario at this time. Understanding that this is a fluid situation that we will be updating regularly throughout the year.

Here’s ETR’s Sagar Kadakia explaining this data in more detail.

**Industry Impact is Significant Across the Board**

The chart below shows the relative impact of COVID-19 on spending by some of the hardest hit industries. The X-Axis depicts the Net Score (spend velocity) relative to the survey three months ago (S/S Delta) – so really reflecting change in sentiment from early Q1 2020. The Y-Axis shows Net Score from twelve months ago (Y/Y Delta).
Breaking Analysis: COVID-19 Drags 2020 Spending Outlook to Minus 5%

Industries Impacted by Self-Quarantine & COVID-19

Across the board in these sectors we’re seeing declines in spending sentiment. Some points on this graphic:

- Retail is obviously getting hit hard but at the same time it is bifurcated. For example, Amazon has hit all time highs during this crisis and Target’s April online sales increased by more than 200%.
- Airlines are very uncertain at this point with total lack of visibility on demand. Larger airlines like Singapore Air or the big US and European airlines have the backing of wealthy governments. But some of the smaller names that live on the edge could be in big trouble.
- In our last Breaking Analysis we discussed the impact of MPLS networks and the migration to SD-WAN having an impact on Telco.
- Healthcare has really been hit with the need to purchase additional equipment to prepare for COVID-19. At the same time the stoppage in elective surgeries will likely hurt the industry. Pharma could catch a tailwind if vaccines are brought to market but vaccine efficacy has always been a risky business proposition. Government help will be required.
- Financials are down right now but as we’ve stressed before, liquidity is good and banks we think will emerge strong. Our data suggests that while cautious, banks continue to invest in tech.
- Energy remains a big concern with exposure to high yield credit risks. Oil prices dropped below $0 this month and unlike many industries, when oil production is shut down it’s not as productive when turned back on. So producers sometimes would rather keep producing assuming demand will come back. But there’s no headroom on storage capacity.

Here’s Sagar Kadakia’s take on the industry outlook.

Best-of-Breed Security Firms Capitalize on the WFH Pivot

The chart below shows Net Score or spending momentum in the security sector. The data compares the
most recent April survey results (yellow bar) with April ‘19 (gray bar) and the Jan survey (blue bar).

Security, a remote workforce reveals best-in-breed … and may lead to permanent changes

While almost all suppliers show declines from January results, many are showing accelerated momentum from a year ago, including Twistlock (Palo Alto), Crowdstrike, Sailpoint, Okta, etc. As we’ve stressed the playing field is bifurcated with those companies positioned well for cloud, SaaS, remote workers and mobile security tend to have strong momentum while others are seeing decelerating spend velocity.

Sagar Kadakia adds color in this video clip.

**Downturns have been Friendly to Cloud**

In 2008/2009, we reported that we were entering the next phase of cloud computing. Whereas early cloud was about startups and tire kickers, the 2008 downturn saw CFOs embrace a rapid shift from CAPEX to OPEX. When we came out of the financial crisis organizations realized the power of cloud computing and cloud’s decade-long bull march began.

We believe the end is nowhere near as organizations dabbling in digital transformation and cloud-first mantras now see cloud as a mandate to business flexibility.

The slide below shows Net Scores or spending velocity for the Big Three cloud players.
**Key Points:**

- While AWS, Azure and Google momentum converged coming into 2020, Microsoft has regained the top spot in Net Score.
- All three cloud platforms have very strong spending momentum with well over a 60% Net Score compared to many others in the data set. Volume cloud in the U.S. remains a three-horse race between the companies that can spend the CAPEX required to scale.

*Sagar Kadakia: “Cloud is a three-horse race...”*

We’ll see over time how this plays out. As we’ve pointed out many times, the AWS market numbers are clean and easier to track. But the strong momentum in the surveys for Microsoft is undeniable.

**Collaboration: Not Rosy for All Vendors**

The world has reported on Zoom’s ascendency and in previous Breaking Analysis segments we’ve commented on the tailwind that work from home has given this space. But as shown in the data below, it’s not all good for all vendors – again the bifurcation story.
This chart compares a mix of productivity and collaboration players. It shows the three survey samples we mentioned earlier but it focuses on replacement rates for the vendors. Note that many are seeing double digit defections from their platforms – one in five for Dropbox – while the rightmost players are looking strong.

As Sagar Kadakia points out in this clip, if you’re not doing well now with the work from home pivot it could spell trouble. Note that the three vendors showing the top defection rates, Dropbox, Box and Slack currently have a combined $25B market cap.

**Teams Gaining Traction in the F500**

Collaboration is another area where Microsoft is winning with Teams. The chart below focuses on the Fortune 500 and asks what percentage of your organization is using Teams today and what’s the outlook twelve months from now.
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The following key points are noteworthy:

- Seven percent of respondents say Teams is penetrated through their entire organization today and that figure is projected to rise to 20% in twelve month.
- Looking twelve months forward, only 10% of respondents say that their organization will be less than 20% penetrated in twelve months.
- The midpoint average of 40.2% today is expected to grow to more than 67% in 2021.

Sagar Kadakia explains further.

**Slack Could be under Fire**

The chart below shows the same view as the previous Teams drilldown with a focus on Slack.
Key Points in the data:

- Today, 3% of F500 organizations deploy Slack across the company and that is projected to remain flat.
- Today, 33% of F500 organizations say Slack has penetrated more than 50% of their organization and that figure is expected to drop to 24% by 2021.
- The percentage of F500 respondents using Slack in less than 10% of their organization is expected to grow from 24% today to 35% by next year.

As Sagar Kadakia points out, Slack is a seat-based model and less users means less revenue, which spells potential trouble ahead for Slack.

**IT Consultancies, SIs and Outsourcers: Expect Software Demand**

CIOs in hard hit industries tell us that they’ve brought spending to a halt on most large projects. They say some strategic digital transformation projects will continue but an obvious place for companies in hospitality, airlines, retail, healthcare, restaurants and other hard hit businesses is to put the brakes on project work.
Breaking Analysis: COVID-19 Drags 2020 Spending Outlook to Minus 5%

The above data shows Net Scores or spending momentum for seven large SIs and consultancies. Note the yellow bar comparing the most current survey data with three months ago (blue) and last April (gray). Notably, IT consulting looked strong entering the year for Deloitte, EY and Accenture but virtually all consultancies are showing dramatic declines in spending momentum in the most recent survey.

Key Points:

- Significant deceleration in spending momentum for IT services
- In a recent ETR COVID-19 drilldown survey, 25% of respondents said they were completely freezing new IT projects or deployments.

Watch and listen to Sagar Kadakia’s commentary on this topic.

**Implications for IBM Red Hat**

IBM reported that Red Hat revenues grew 20% in the first quarter of this year. That’s pretty healthy but the forward looking data in the ETR surveys suggest there’s a slowdown coming.

Around 60% of IBM’s revenue comes from professional services. As we reported last year when IBM completed its Red Hat acquisition, the near term priority for IBM was to drive OpenShift deals through IBM’s consulting and services organization as a platform to modernize a substantial number applications in the IBM customer base.

The good news for IBM is that it has hit its goal of making Red Hat accretive to free cash flow in its first year under IBM. We’ve always been confident that this would happen given IBM’s visibility on its modernization pipeline and its services prowess.

But IBM, like many companies, has suspended earnings guidance due to lack of clear visibility on its earnings. In its latest earnings call, CFO Jim Kavanaugh stressed that IBM’s services business is substantially annuitized – more than 80% for IBM Global Business Services (GBS - strategy consulting, application integration and management services) and 95%+ for Global Technology Services (GTS -
outsourcing and infrastructure support services). But each quarter this percentage comes down.

**IBM’s Key KPIs**

When asked about key indicators IBM is watching, CFO Kavanaugh said:

> Arvind and I are looking at daily...what’s happening to the rate and consumption of our backlog, what are clients doing around projects, around offerings, what’s happening to our utilization, our chargeable billable rates, our price realization. Each of those are fundamental KPIs that we’re looking at in this environment right now, to the health of the indicator around a services based business.

IBM understands that the near-term health of its business, including its ability to meet its second Red Hat financial goal – i.e. make Red Hat accretive in year two – is heavily tied to its services performance and these metrics.

Longer term, as we’ve reported previously, Arvind Krishna wants to return IBM to growth and he plans to do that, in part, with more of a technology-led story.

We’re watching this closely. It could be a rocky few months or quarters for IBM. The upshot is Arvind Krishna will get a “COVID Mulligan” and have some breathing room to rebound.

**Next Week: Part II - More Sector Drill-Downs**

We’ll continue digging into the survey data and plan to focus on infrastructure, analytics data stores, software, automation (e.g. RPA) and other sectors, so please tune in for that.

Watch the full video analysis:

Remember these episodes are all available as [podcasts wherever you listen](#).

Ways to get in touch: Email david.vellante@siliconangle.com | DM @dvellante on Twitter | Comment on our LinkedIn posts.

Also, check out this [ETR Tutorial we created](#), which explains the spending methodology in more detail.

Watch this week’s full video analysis:
David Vellante is co-CEO of SiliconANGLE Media, as well as co-founder and Chief Analyst at The Wikibon Project, the world’s leading open source technology research community. Dave is a long-time tech industry analyst, entrepreneur, writer and speaker. As co-host of theCUBE – “The ESPN of Tech,” Vellante has interviewed over 5,000 experts since 2010. He is also a co-founder of CrowdChat, an angel funded startup based in Palo Alto using big data techniques to extract business value from social data. Prior to these exploits, Dave founded a CIO consultancy and spent a decade growing and managing IDC’s largest business unit. He lives in Massachusetts with his wife and four children where he is active in town activities including serving as the president of his town’s local “Kiddie Sports” association. Dave holds a B.S. in Applied Mathematics from Union College.

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