

EUROPEAN IT BUDGETS  
HIDDEN SERVICES SPENDING  
REVEALED

INPUT

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# EUROPEAN IT BUDGETS

## HIDDEN SERVICES SPENDING REVEALED

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**Information Services Programme—Europe**  
(MAP)

***European IT Budgets—Hidden Services  
Spending Revealed***

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## Abstract

This study puts individual product and services market trends into the context of overall IT spending by European organisations.

With the European market for IT apparently approaching saturation, this study identifies those areas in which there are still major opportunities for vendors to win new services business.

It compares the IT spending patterns in four major countries with those of Europe overall. Key industry sectors are also analysed to show the relative size and growth of IT budgets.



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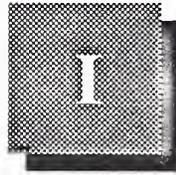
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## Introduction

This report is produced as one of a series of reports in INPUT's Software and Services Planning Services for the Computer Software and Services Industry in Europe.

The report is designed to assist vendors in assessing market opportunities beyond the customer's normal IT budget for external software and services spending.

As the IT market gets saturated, many new vendor opportunities are being found, which are funded outside existing purchasing budgets.

### A

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## Scope of the Report

This report reviews and analyses expenditure on software, services and maintenance markets within the context of total spending on IT in Europe and forecasts the likely growth areas to 1997.

The report assesses trends for the following seven components of the average IT budget, which have been built into INPUT's composite IT spending model for Europe:

- Computer equipment products
- Equipment services
- Software products
- Software services
- Communications products and services
- Other facilities
- Internal staff

*Computer equipment products* includes all mainframe, mid-range, PC, workstation, network, and peripheral hardware.

*Equipment services* is a standard INPUT delivery mode comprising equipment maintenance and environmental services such as installation and cabling.

*Software products* includes application software and systems software products extracted from four INPUT delivery modes: turnkey systems, application software products, system software products and systems integration; with all the supporting services elements or hardware removed.

*Software services* comprises the service elements of all the non-hardware INPUT delivery modes—processing services, turnkey systems services, applications software products support, systems software products support, professional services, network services, systems operations and systems integration services.

*Communications products and services* includes expenditure on telephone and data services, leased lines and switching equipment. Data network interfaces and value-added network services (VANs) are excluded (but included elsewhere) as they are normally counted as part of computer systems.

*Other facilities* covers the provision of office space, other equipment such as copiers, heating, lighting, furniture, vehicles, etc.

*Internal staff* are the human resources associated directly with employees developing, operating, supporting and managing information systems, excluding those staff who would be classified as end users and those who are on a short term contract (normally counted as a professional service within software services).

Expenditure on capital investments have not been separated from revenue expenses in this report. Both are incorporated in the estimates given for INPUT's model of annual spending on IT. The term budget should not be taken too literally as for the data refers to the total composition of IT spending within a country. In most cases, between 10% and 50% of this spending does not appear in any "IT Budgets".

Spending details are also provided for the following key industry sectors in the major countries:

- Discrete manufacturing
- Process manufacturing
- Transportation
- Retail distribution
- Wholesale distribution
- Banking and Finance
- Insurance
- National government

Full details of the delivery mode and industry sector definitions used by INPUT are given in the document, *INPUT Definitions, 1992*.

Software and services continue to attract widespread vendor attention. This report should be read in conjunction with other INPUT reports in order to identify key market and product trends, vendor strategies and opportunities.

## B

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### Methodology

This report is based principally on European research activities conducted by INPUT during 1992 and on reports published on this market by INPUT and others over the past two years:

- A vendor research programme of over 500 interviews with key software and services vendors across Europe.
- Another 1,200 vendor and user interviews across all European market sectors to determine budget trends and opinions.
- INPUT's continuous analysis of the delivery modes and vertical industry sectors comprising the computer software and services market.
- INPUT's research programme into the customer services and user satisfaction in the European market place.

Additionally, INPUT's extensive library and database of information relating to the software and services industry were used.

## C

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### Report Structure

The remaining chapters of this report are structured in the following way:

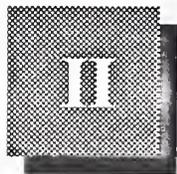
- Chapter II is an executive overview offering a concise summary of the contents of the report.
- Chapter III describes INPUT's assessment of the dimensions of the main constituent components of the European IT spending internally and externally. A number of key industry sectors are also analysed.
- Chapter IV describes INPUT's assessment of IT spending internally and externally in France, Germany, the United Kingdom and Italy.
- Appendix A is the forecast database used throughout the report.

**D****Related INPUT Research Programmes and Reports**

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The following reports contain detailed analysis of key market sectors, offering commentary and recommendations for vendors active in Europe.

- *Computer Software and Services, Europe 1992-1997*
- *European Software and Services, Discrete Manufacturing Sector, 1992-1997*
- *European Software and Services, Process Manufacturing Sector, 1992-1997*
- *European Software and Services, Transportation Sector, 1992-1997*
- *European Software and Services, Distribution Sector, 1992-1997*
- *European Software and Services, Banking and Finance Sector, 1992-1997*
- *European Software and Services, Insurance Sector, 1992-1997*
- *European Software and Services, National Government Sector, 1992-1997*



## Executive Overview

### **A** **Spending on IT Services is Largely Hidden in Other Budgets**

The switch of IT spending from equipment to software and services has been more dramatic than previously thought. It also reveals that there is plenty of potential for further growth if outsourcing could deliver its promises of lower cost and greater flexibility/profit. A total of \$315 billion was spent on IT in 1992 with just over half of it being on computer products and services. The remaining half was spent on staffing and supporting resources.

INPUT has produced a model of the components of IT spending for the major European countries that reconciles its analysis of vendor revenues with an analysis of users' IT budgets.

Acquisition of computer equipment now represents only 20% of the average user's IT spend. Software products add another 8% to costs. Equipment and software services represent 25%. Internal staff with supporting facilities and communications costs represent the other 47% of expenditure on IT.

End user costs associated with staff using information system applications are not included. Exhibit II-1 shows the relationship between the budget components.

The surprise is the relatively large size of the services element. IT management questioned by INPUT and other researchers normally quote under 10% of their budget as allocated to services. However, analysis of vendor revenues across Europe show a different picture.

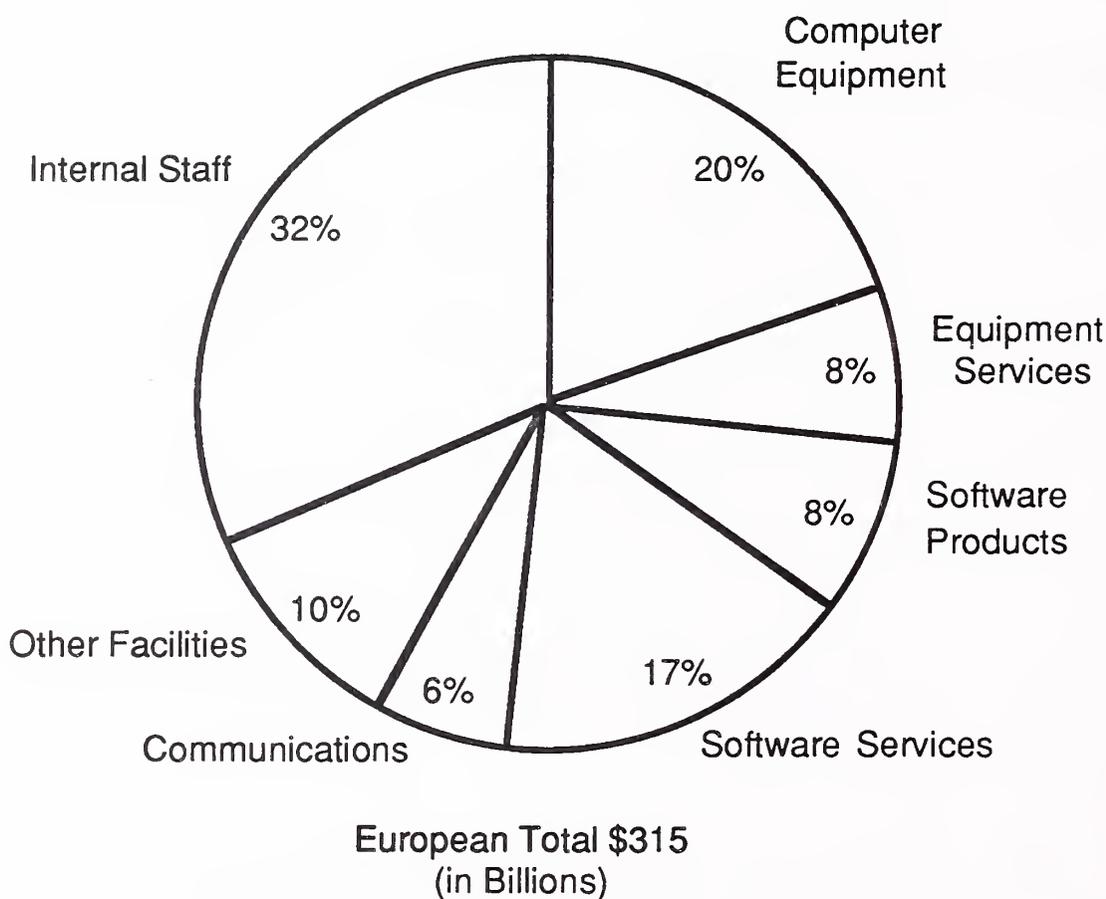
The main reason for this discrepancy is that services are very often accounted for within a special project—which itself may not be funded totally from within the IT budget.

The following exhibits summarise the IT spending in Europe from three perspectives:

- On what products and services it is spent
- Which countries lead spending
- Which industry sectors lead spending

EXHIBIT II-1

**Total IT Spend by Major Budget Component, Europe, 1992**



INPUT's conclusion from this analysis is that:

- A client's demands for professional services of all types cannot necessarily be judged by the size of the planned IT services budget.
- IT services can be sold to meet new demands for special projects even when the formal budget appears to have been fully allocated.
- Vendors should be seeking to win at least twice as many services business from a client as the client admits formal budgets.

The second conclusion from this study is that the trend to outsource IT functions could support a doubling of the market for software services with only a 20% reduction in internal staffing costs. In other words, there is plenty of room for continued dramatic growth in software services if customers could be persuaded that outsourcing offers cost reduction, profit improvements and more rapid response to change.

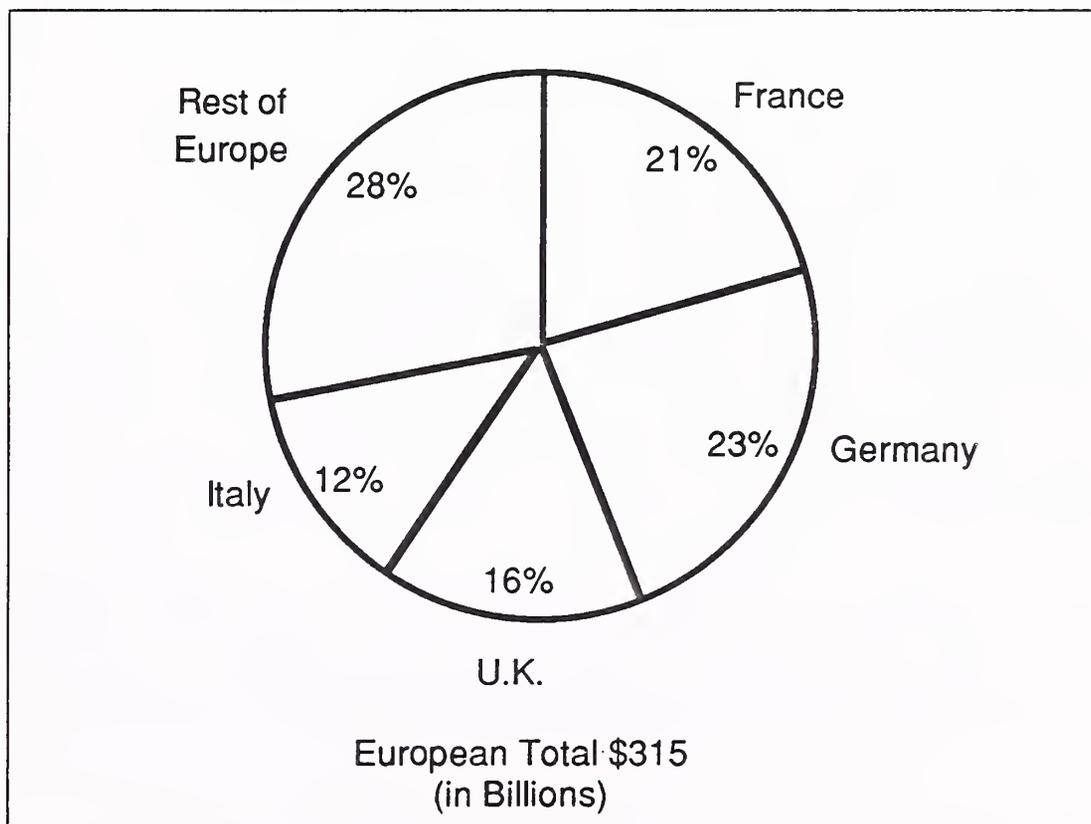
**B**  
**Germany Lags in Services, But Leads in Overall IT Spend**

The pattern of spending on IT varies significantly between the countries in Europe. Exhibit II-2 summarises the relative sizes of each country's spending.

Although France leads by a large margin in its use of software and services, it falls behind Germany when it comes to overall spending due to the German tradition of using heavy in-house IT staff in development and operations functions.

EXHIBIT II-2

**Total IT Spend by Major Country, Europe, 1992**



C

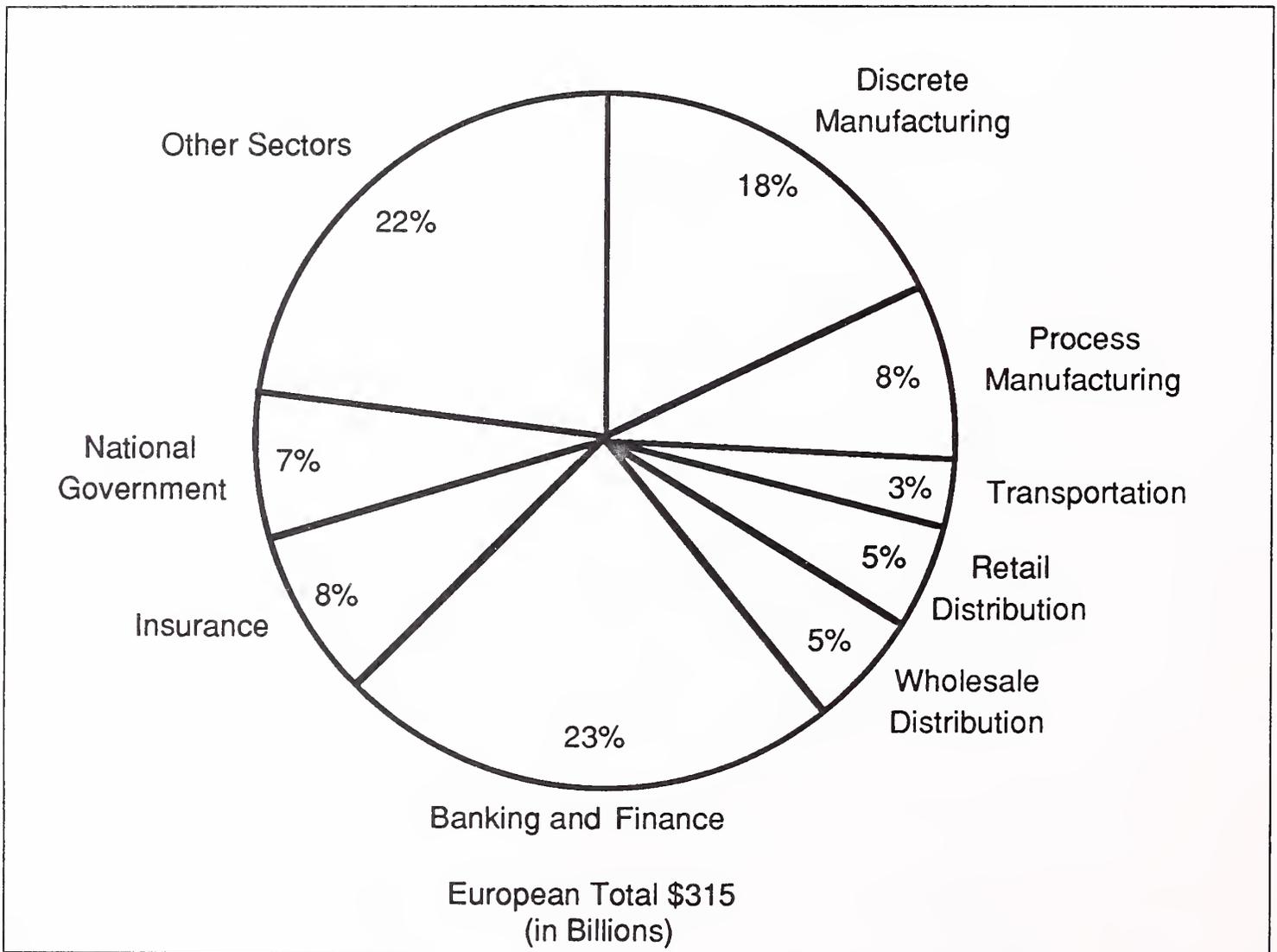
**Banking and Finance Sector Remains the Leading Market**

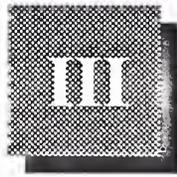
Among the major industry sectors, process manufacturing is expected to offer the most growth opportunities over the next five years. However, banking and finance will continue to be the largest sector, with a heavy dependence on IT as the catalyst for competitive edge, as well as cost constraint.

The pattern of spending around Europe's industry sectors is shown in Exhibit II-3 and expanded upon in Chapter III.

EXHIBIT II-3

**Total IT Spend by Major Industry Sector, Europe, 1992**





## European Market Overview

### A

#### European IT Spending Still Promises Growth for Software and Services

As user spending on IT seems to approach saturation, opportunities for vendors to grow revenues have become restricted to two key activities:

- Winning market share from competitors
- Convincing customers to outsource previously in-house functions

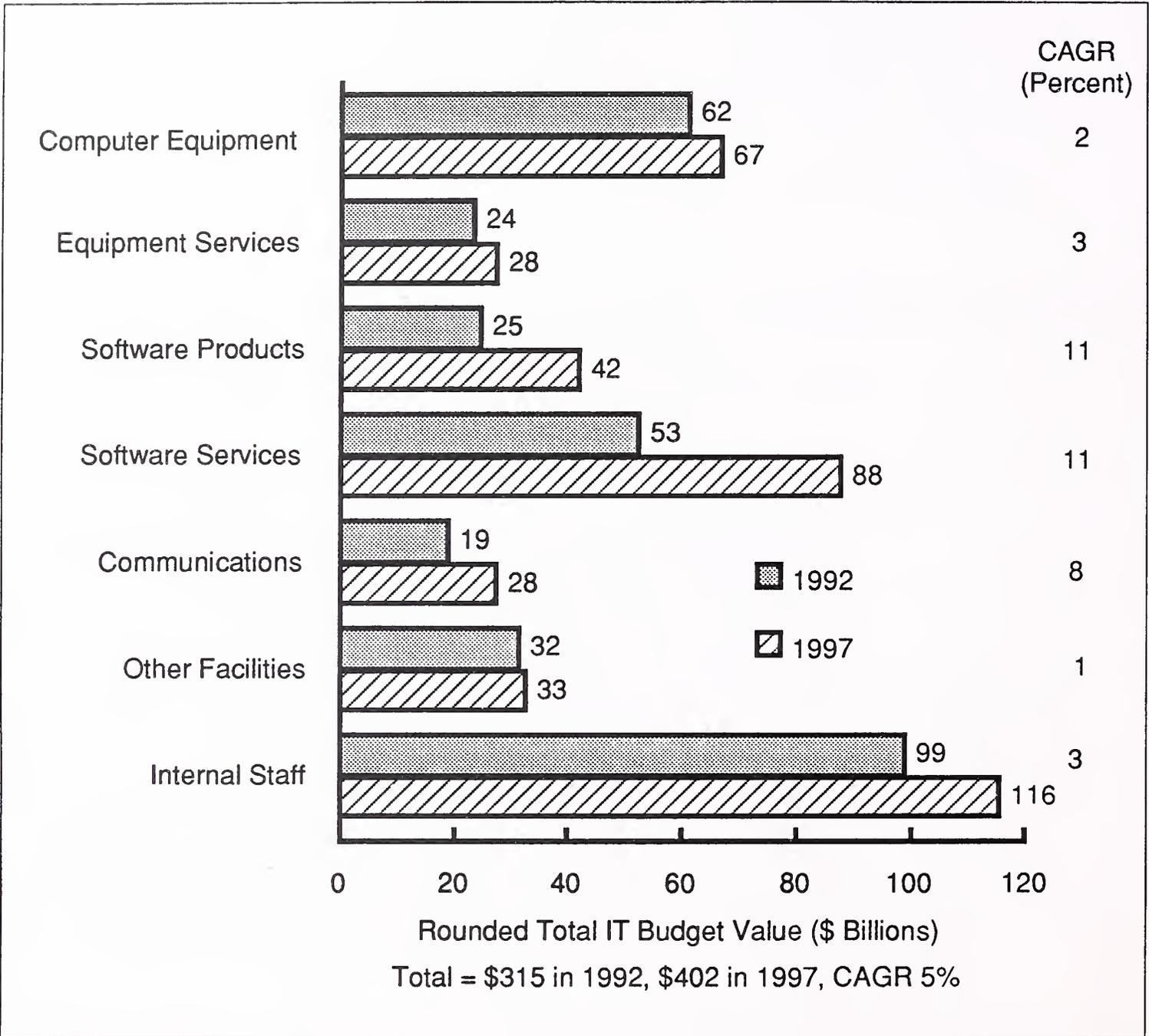
Most of INPUT's research to date has concentrated on the size of the open market and vendors position within each sector. Captive business—in which a vendor is more or less guaranteed business from his parent group—and potential business—such as that currently carried out in-house by the customer's staff—have not been included in market estimates or forecasts. This study provides estimates of the overall market opportunity for vendors by assessing the total in-house and external IT spending of European customers.

All sectors of the IT market have become exceptionally competitive. For many, professional services vendors are concerned about their competition, which has become a priority for the very first time. Many used to boast that their customer's IT department was the only real competition; however, vendors now need to fiercely defend their customer base and become highly focused on their own differentiators in order to expand it.

In order to measure the possible growth for trends such as outsourcing, it is necessary first to understand how the average customer is spending on IT. Exhibit III-1 gives a consolidated European view, dividing the spend between major budget components. Definitions of these components are provided in Chapter I.

EXHIBIT III-1

### Forecast Growth in IT Spend by Budget Component, Europe



Internal staff costs are estimated to account for some 31% of overall spending across Europe—the largest budget component. Computer equipment is the next largest category at 20%, followed by software services at 17%.

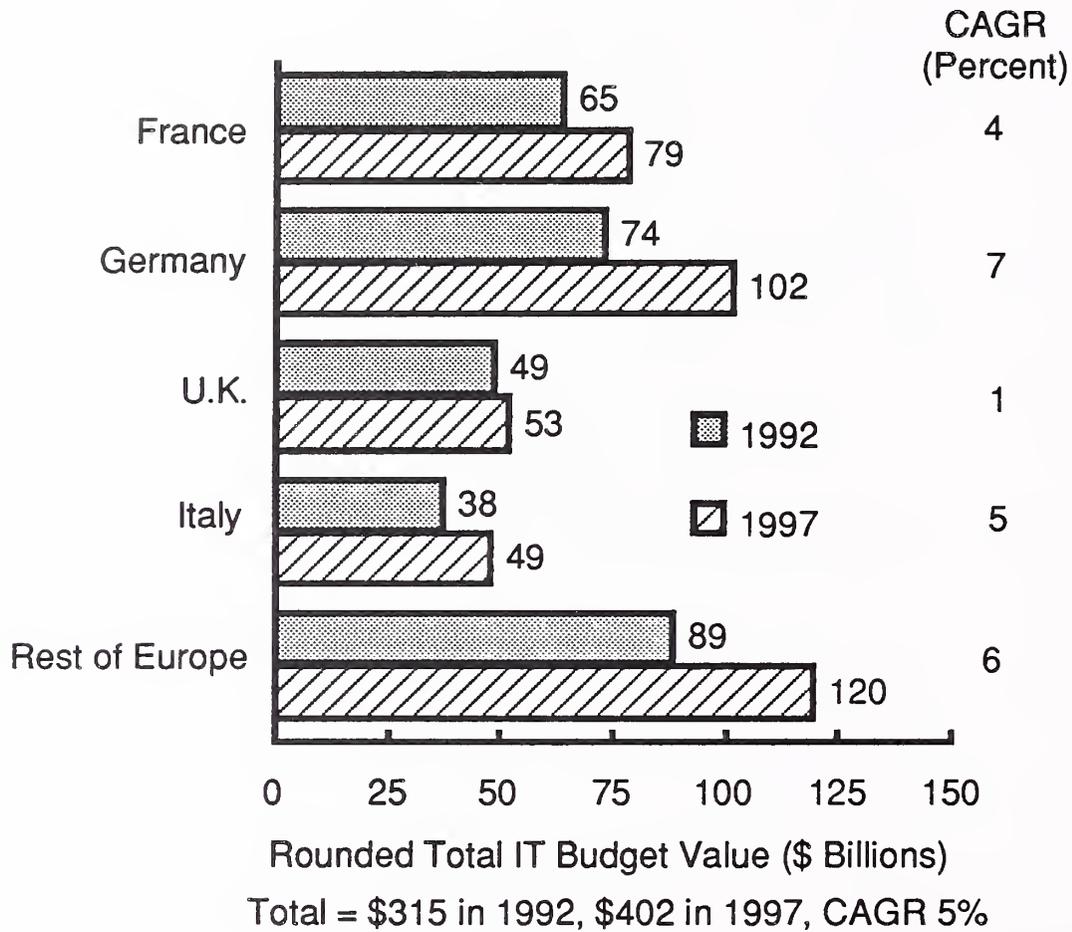
The size of the software services component is surprisingly large compared to that typically attributed by IT management when responding to research questions. IT management's view of their services spending tends to average around the 6% to 8% level. The reason for this wide difference—the 17% figure for software services that resulted from INPUT's rationalisation of user opinion and vendor revenue analysis—seems to be that funding for many software services is found in one-off project budgets rather than in IT department budgets.

This indicates that opportunities to sell software services will always be much greater than each customer's conventional IT budget suggests. INPUT's current forecast for each component will result in software services spending exceeding equipment spending by 1995. The compound annual growth rate (CAGR) assumed for each component is noted against each component category.

Exhibit III-2 shows the variation in overall spending on IT between these countries. Although France leads Europe in terms of spending on software and services, this exhibit shows that by including all IT spending Germany actually has a higher overall investment level than France. This country pattern changes significantly when viewed by industry sector (see later exhibits).

EXHIBIT III-2

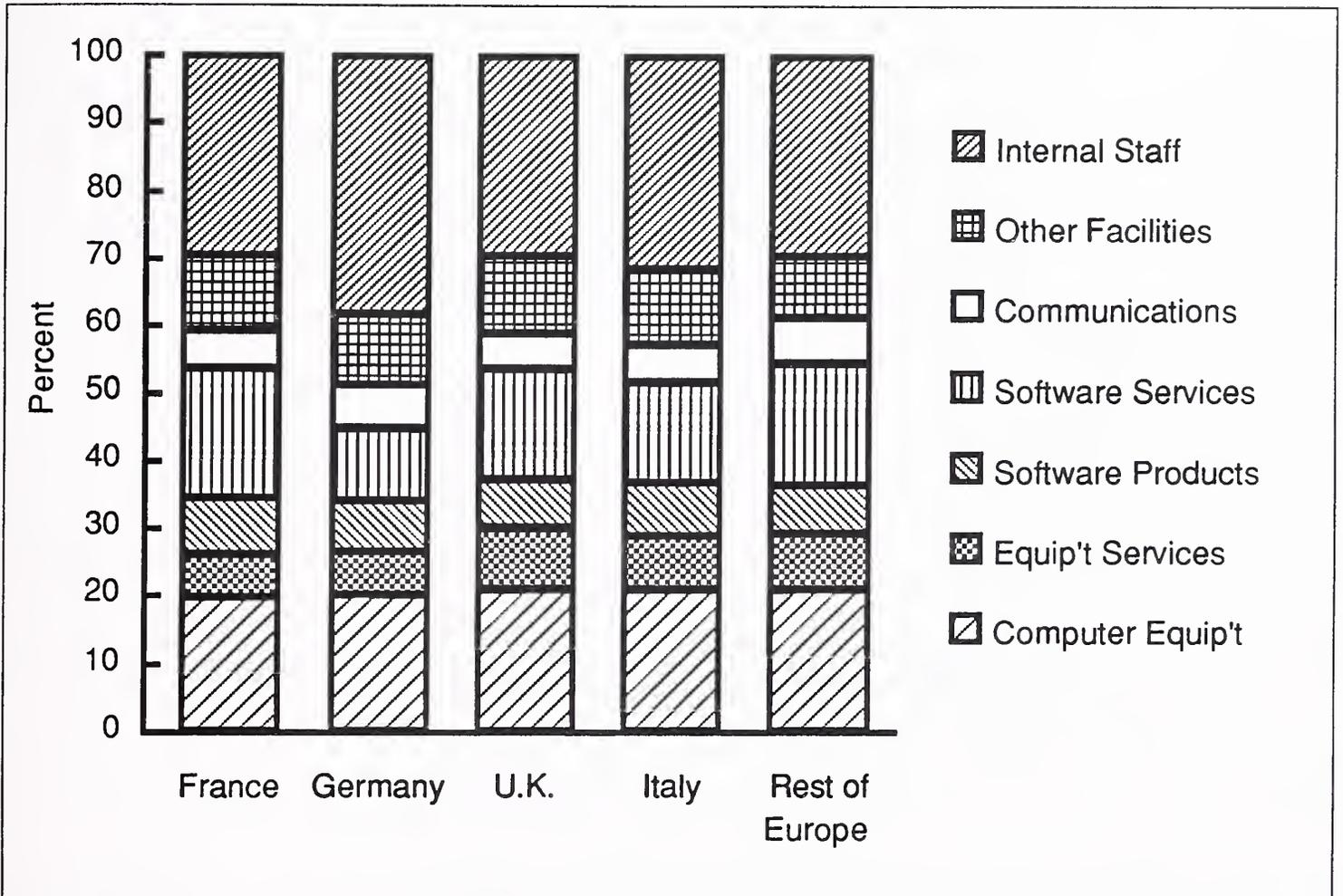
**Comparative Forecast Growth in IT Spend by Major Country, Europe**



The database model from which these charts were produced is given in Appendix A. The European figures are the result of consolidating the data from France, Germany, the U.K., Italy and the remaining regions known as Rest of Europe.

EXHIBIT III-3

### Comparative IT Spend Budget Component by Major Country



Percent of IT Spend on Budget Component	France	Germany	U.K.	Italy	Rest of Europe	Europe
Internal Staff	30	38	30	32	30	32
Other Facilities	11	10	11	11	9	10
Communications	5	6	5	6	7	6
Software Services	19	11	16	14	18	16
Software Products	8	7	7	8	7	7
Equipment Services	6	6	9	8	9	8
Computer Equipment	20	20	21	21	21	21

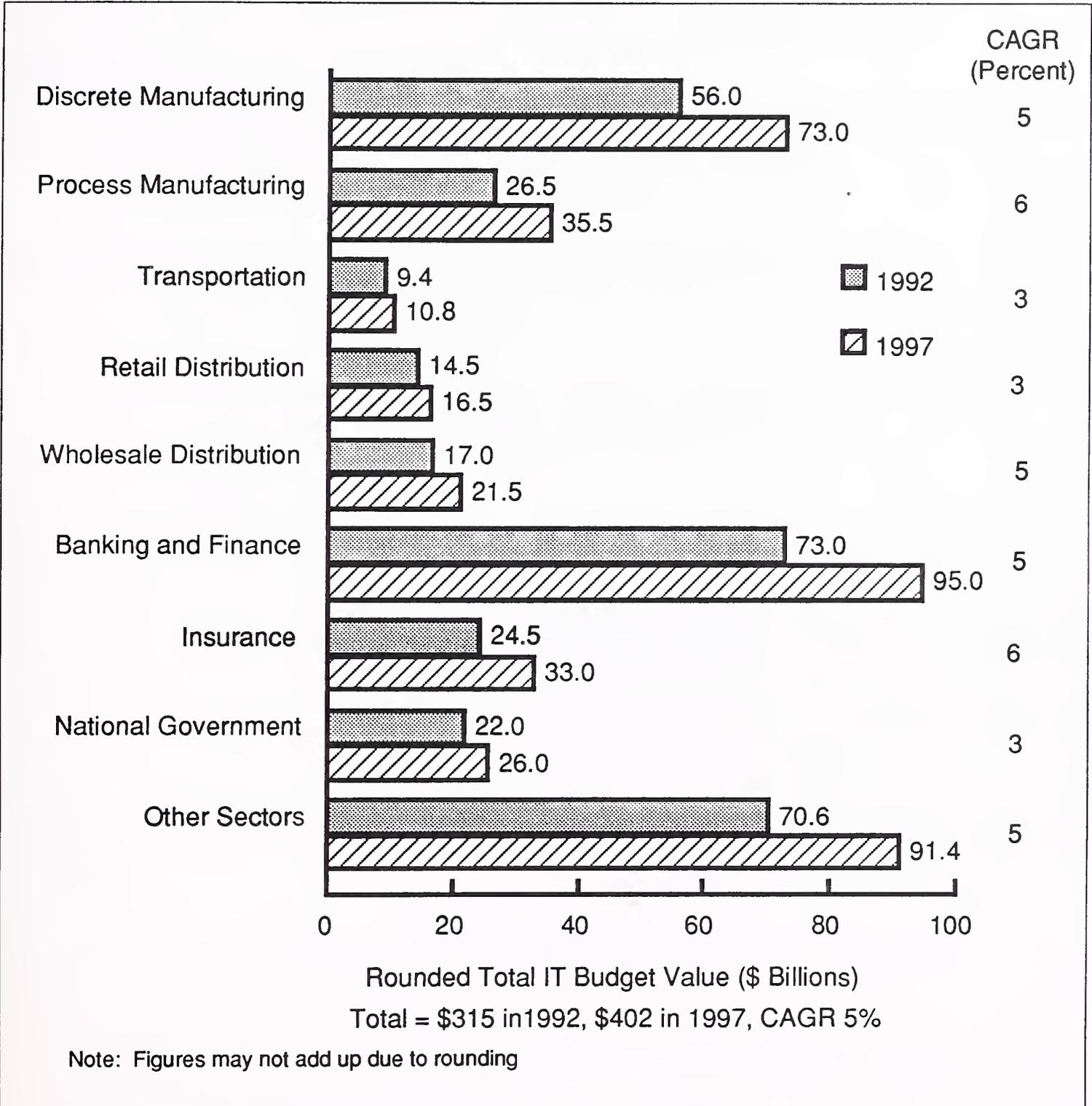
Note: Numbers may not add up due to rounding.

A more detailed comparison of the spending pattern in each country is shown in Exhibit III-3. Here, each budget component is shown as a percentage of the whole (100%) for each country. For example, one can see the strong preference in Germany for employing in-house staff for development rather than using external services. It is also clear that the U.K. has equipment services as a more dominant factor than any other European region.

Exhibit III-4 shows clearly the relative sizes of each industry sector in terms of overall IT spending. Banking and finance sector and the discrete manufacturing sector are far larger than any other sectors. Banking and finance is large because information systems are the fundamental service that the sector offers. Discrete manufacturing is large because this sector is such a huge element of GDP and employment.

EXHIBIT III-4

### Comparative IT Spend Budget Component by Major Industry Sector



This and the following exhibits show the pattern of spending within key industry sectors across the major countries of Europe. These charts can be compared to Exhibit III-2 to judge the relative strengths of each region within a particular sector.

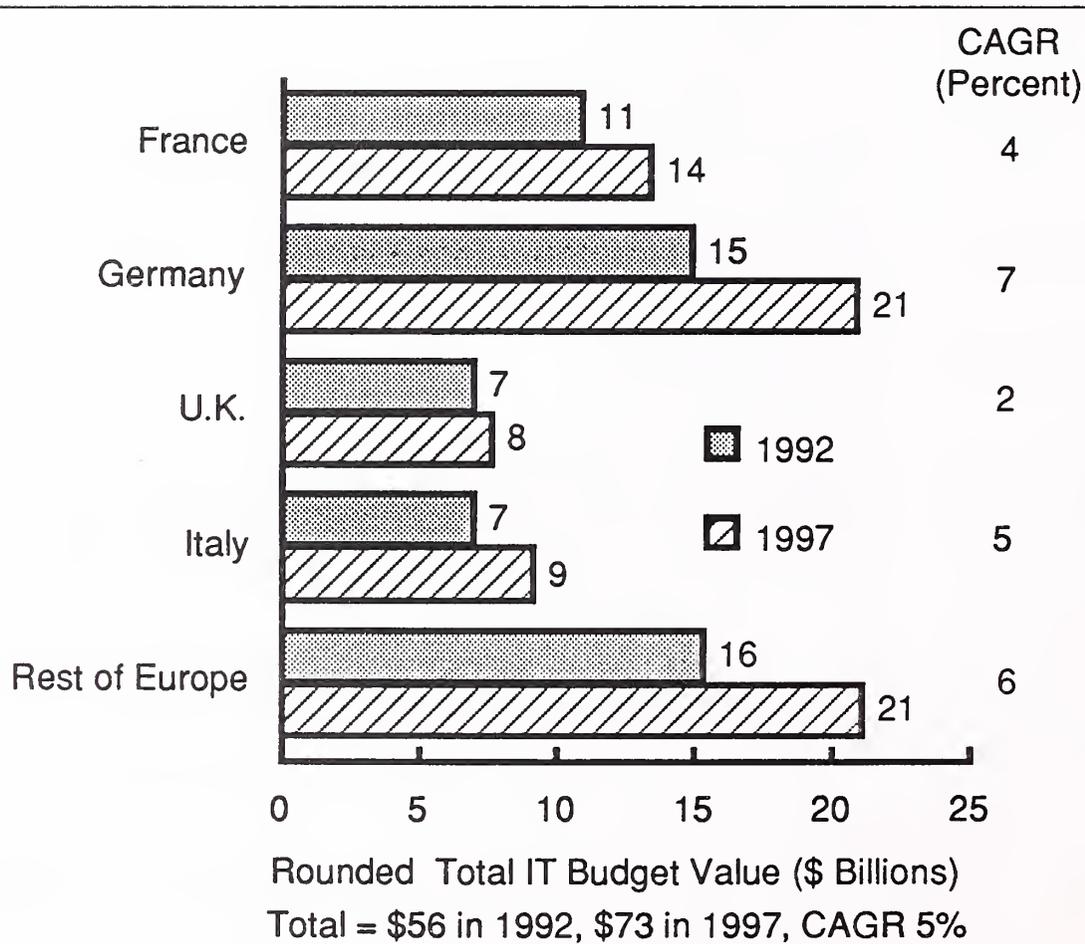
**B**  
**Recession Threatens German Manufacturers**

Germany has the strongest manufacturing base in Europe. The recent downturn in the German economy has not been accounted for in this IT spending database as for INPUT has not yet sufficient evidence to predict the effect on IT budgets. However, it does seem certain that the manufacturing sector will no longer be Germany's star performer.

Exhibit III-5 shows Italy pulling ahead of the U.K. to reach third position in Europe by 1993 in the discrete manufacturing sector.

EXHIBIT III-5

**Comparative Forecast Growth in Discrete Manufacturing IT Spend by Major Country, Europe**

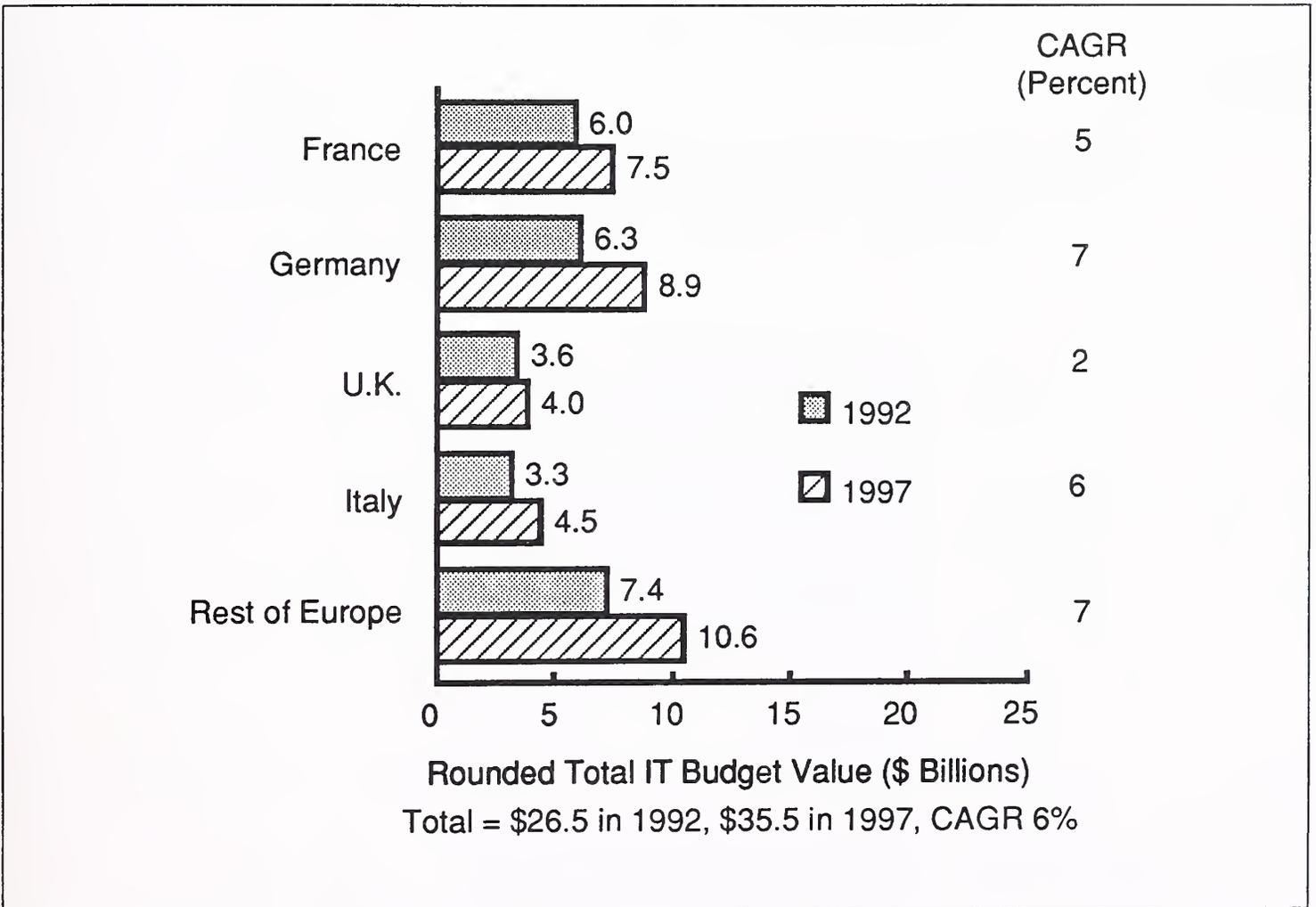


Continuing cuts in the defence sector are having the less effect on manufacturers than expected, but have contributed to limit growth prospects in most countries.

The process manufacturing sector has been less affected by recession with food, energy and pharmaceuticals still exhibiting healthy growth.

EXHIBIT III-6

**Comparative Forecast Growth in Process Manufacturing IT Spend by Major Country, Europe**



C

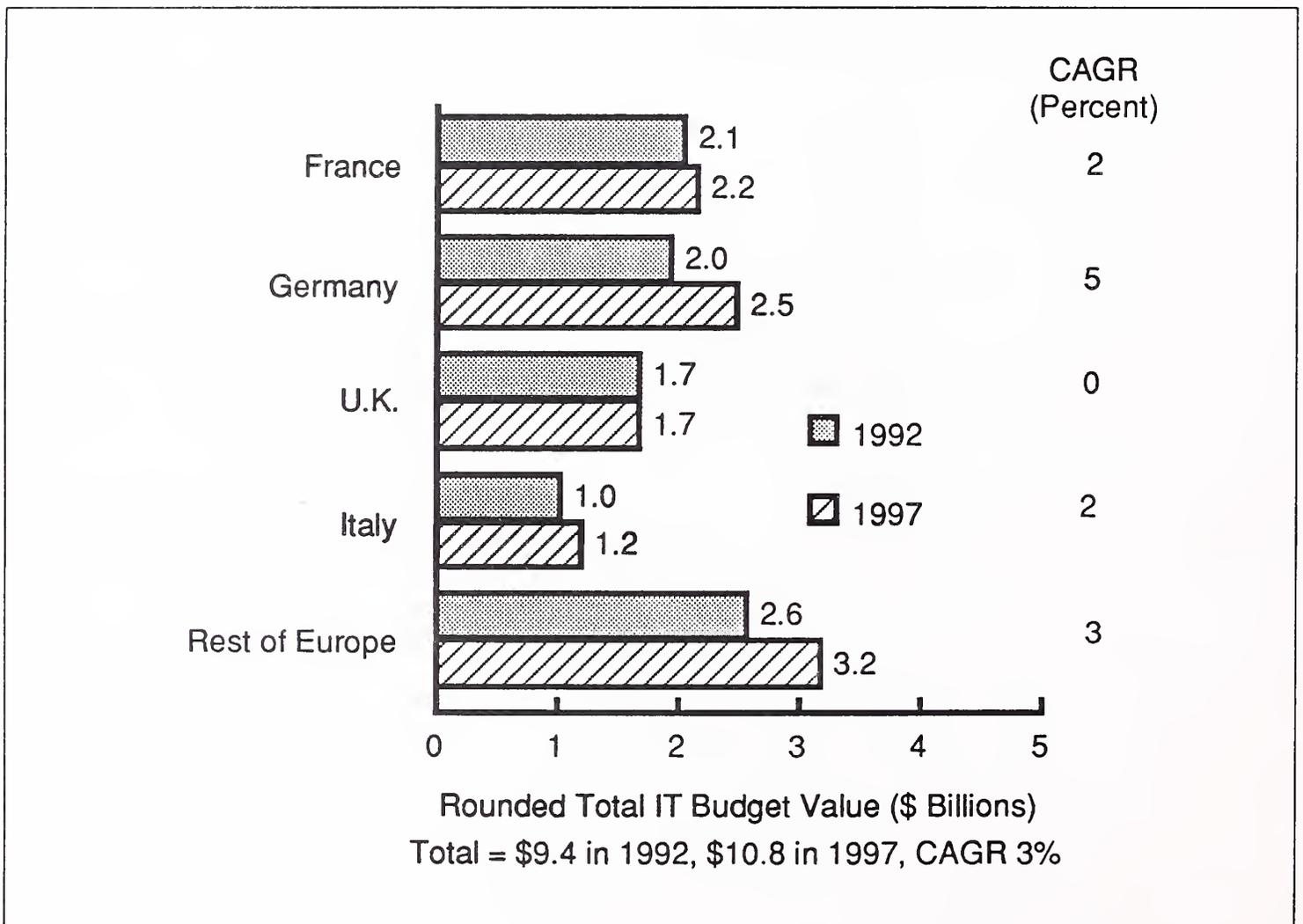
Transportation—Better Services at No Extra Cost

Transportation is a key element in the competitive nature of Europe's supply chains. EDI and the associated electronic commerce are expected to lead the continuing development of such businesses, but with the proviso that such improvements in information flow are implemented without increasing business operating costs.

Exhibit III-6 shows France as the biggest spender in 1992, though the Netherlands and Belgium (within Rest of Europe) dominate spending in the road haulage sector.

EXHIBIT III-7

Comparative Forecast Growth in Transportation IT Spend by Major Country, Europe



**D**

**Distribution—Wholesale Spending Dominates in Europe**

Likening of Exhibits III-8 and III-9 reveals that wholesale distribution budgets are estimated at \$17 billion in 1992, compared to \$14.5 billion in the retail sector. This pattern holds true for all countries except the UK where the retail sector is dominated by very large groups and wholesalers tend to be small to medium sized companies.

Despite leading Europe in the spend on external software and services, U.K. retailers trail behind German retailers in overall spending on IT. Exhibit III-8 also shows the U.K. total IT spending forecast to shrink as outsourcing and cost reductions are implemented.

EXHIBIT III-8

**Comparative Forecast Growth in Retail Distribution IT Spend by Major Country, Europe**

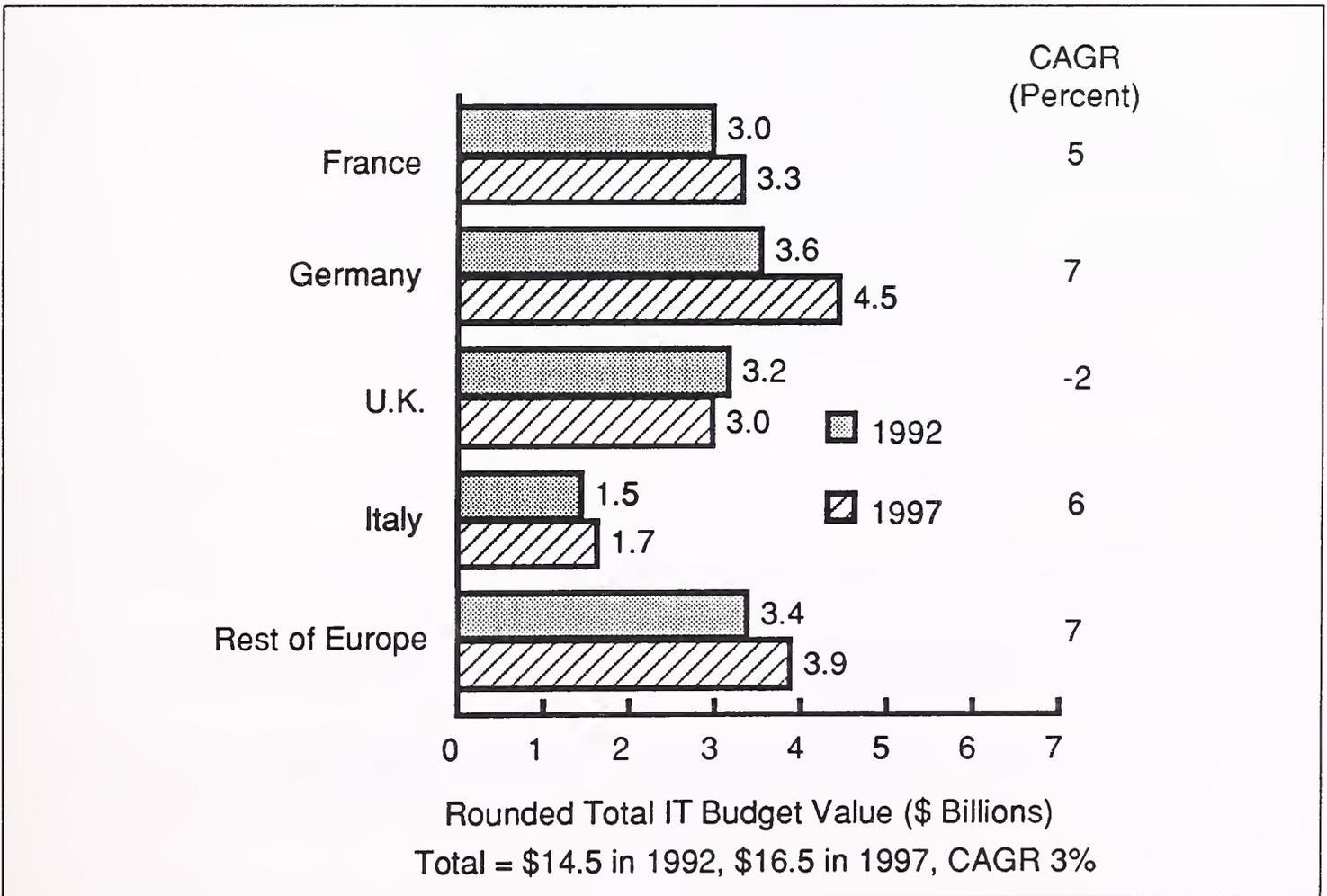
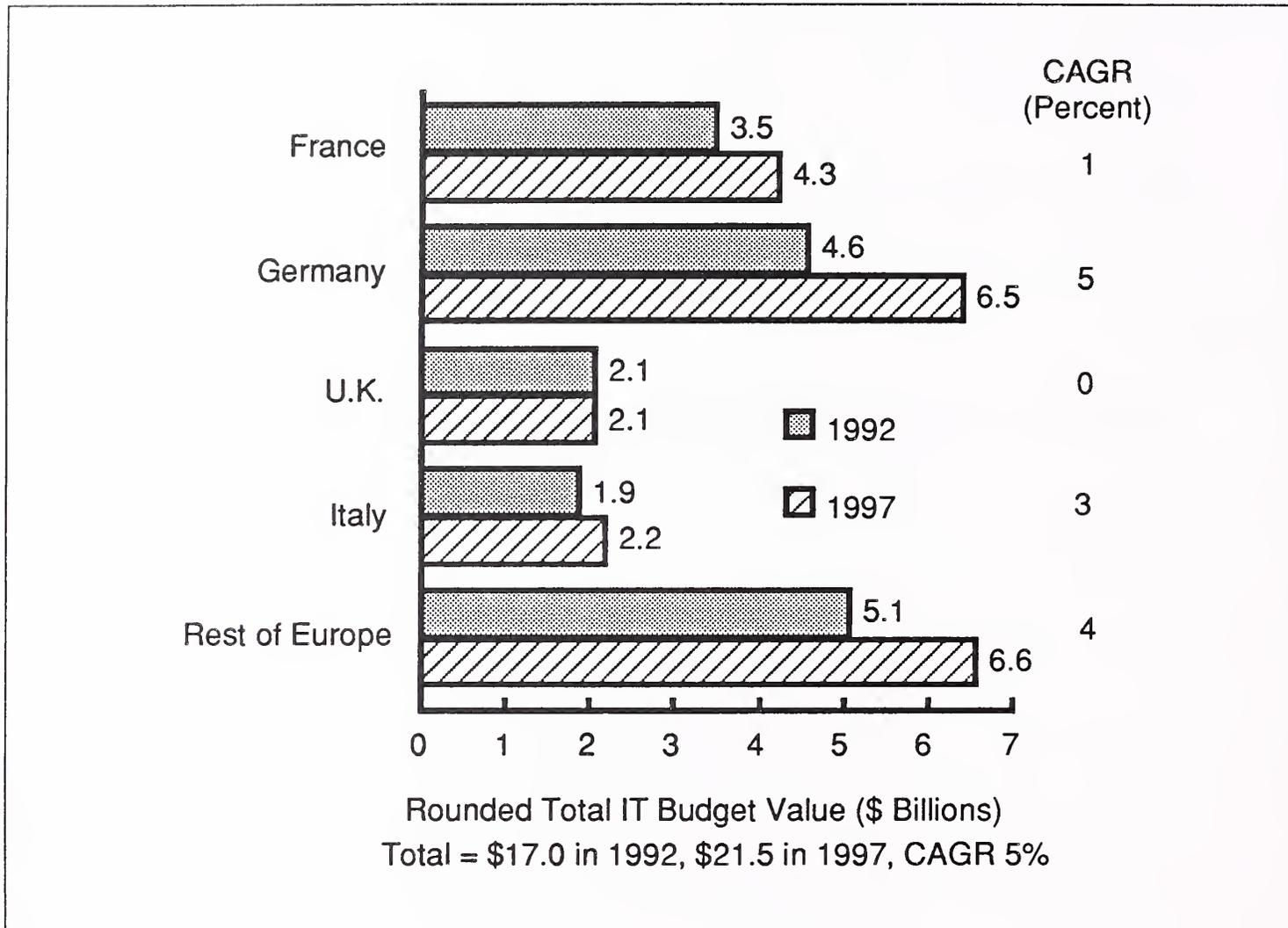


EXHIBIT III-9

**Comparative Forecast Growth in Wholesale Distribution IT Spend by Major Country, Europe**



**E**

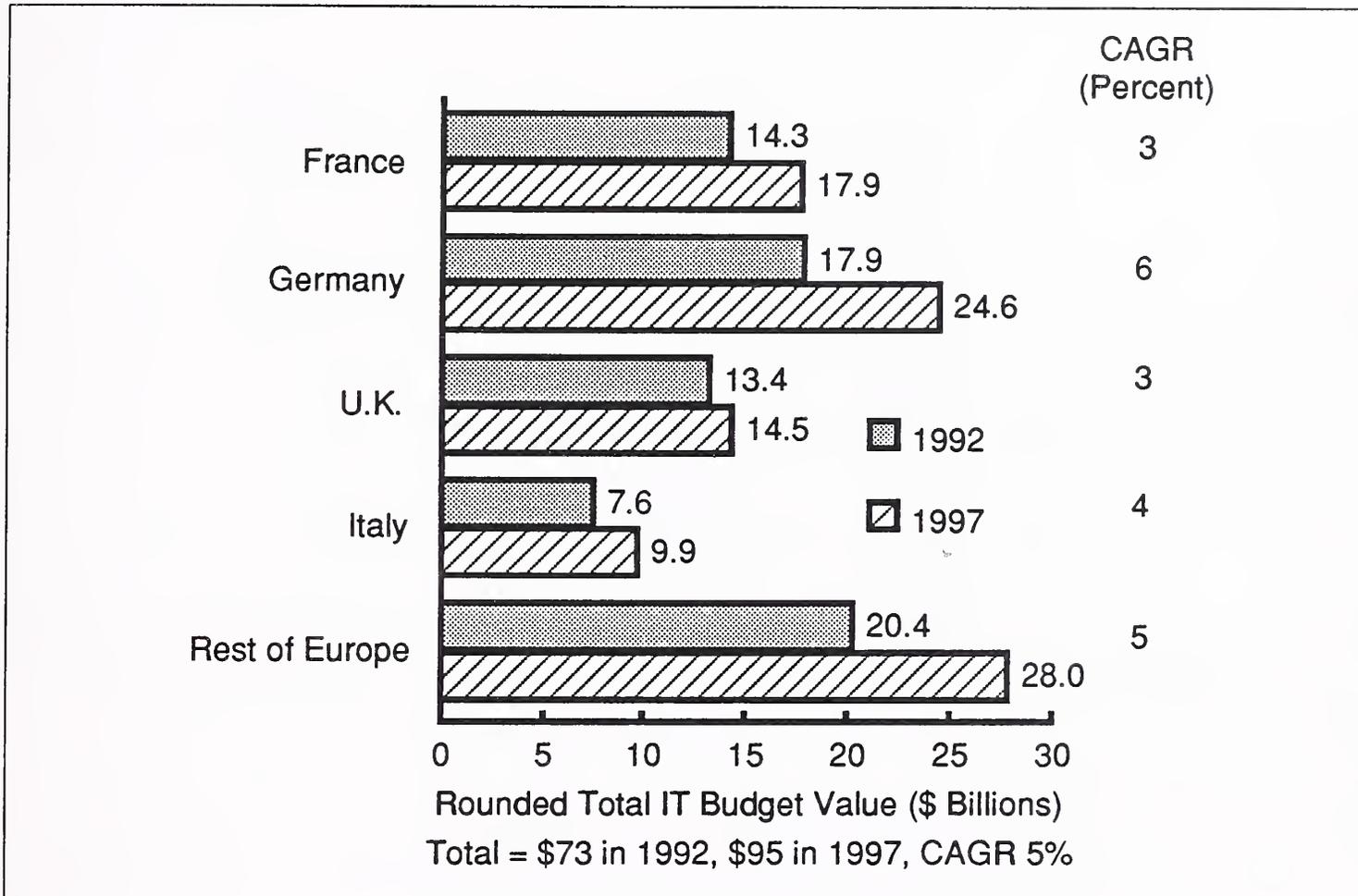
**Banking Rector Remains the Biggest IT Spender in Europe**

Even though the banking sector is going through a crisis of confidence, it is still the largest sector in Europe for IT spending.

The strength of the Deutsche Mark among European currencies seems to be reflected in the size of IT investment in the German banking and finance sector, as shown in Exhibit III-10.

EXHIBIT III-10

### Comparative Forecast Growth in Banking and Finance IT Spend by Major Country, Europe



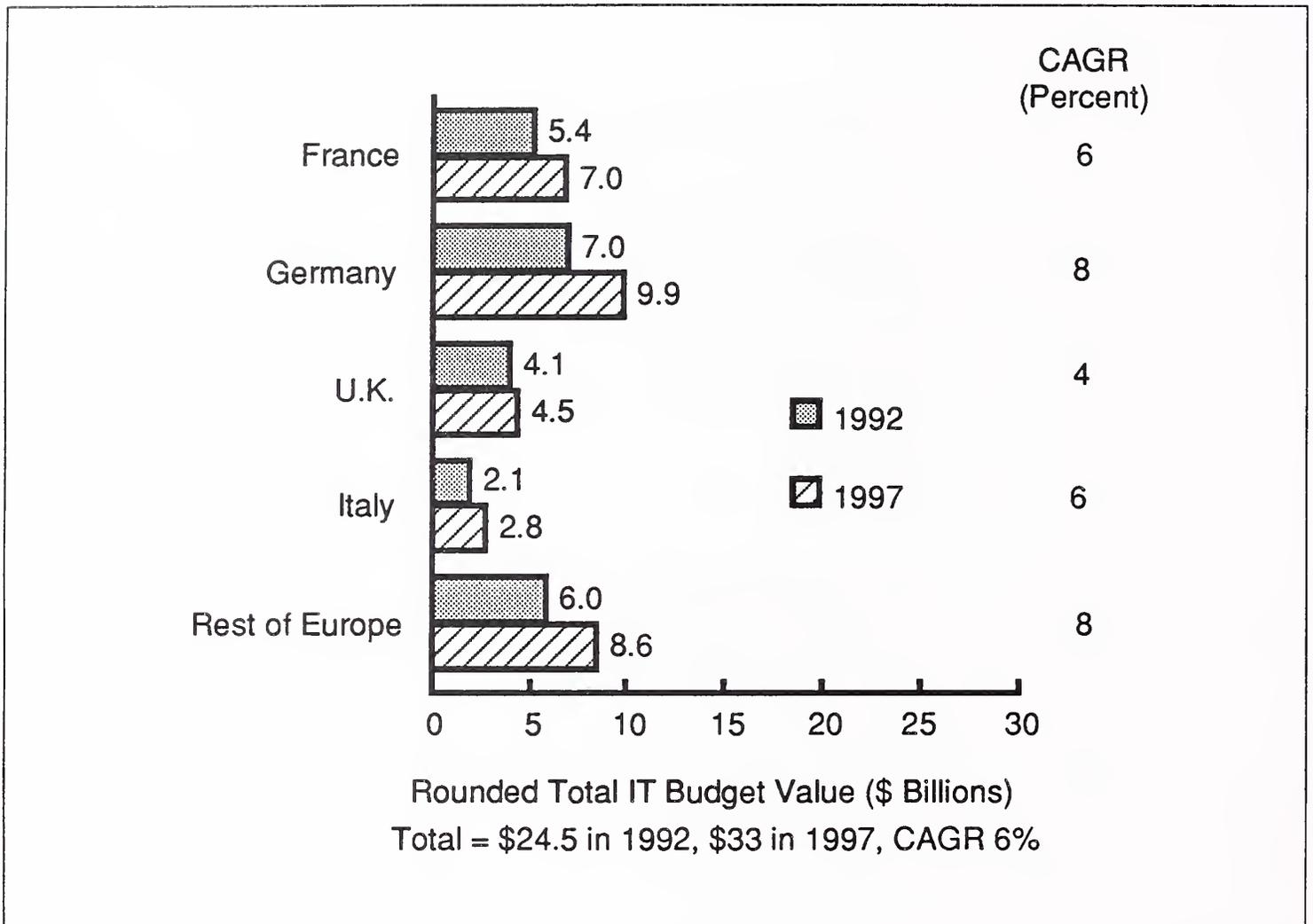
## F Insurance Companies Seek More IT Efficiency

Insurance companies are among Europe's heaviest spenders on IT. Typically, IT budgets represent between 6% and 16% of a company's operating costs. The recent losses being recorded by non-life insurance groups are putting pressure on IT departments to reduce costs.

Exhibit III-11 shows the relative size of annual IT investment in each country.

EXHIBIT III-11

### Comparative Forecast Growth in Insurance IT Spend by Major Country, Europe



## G

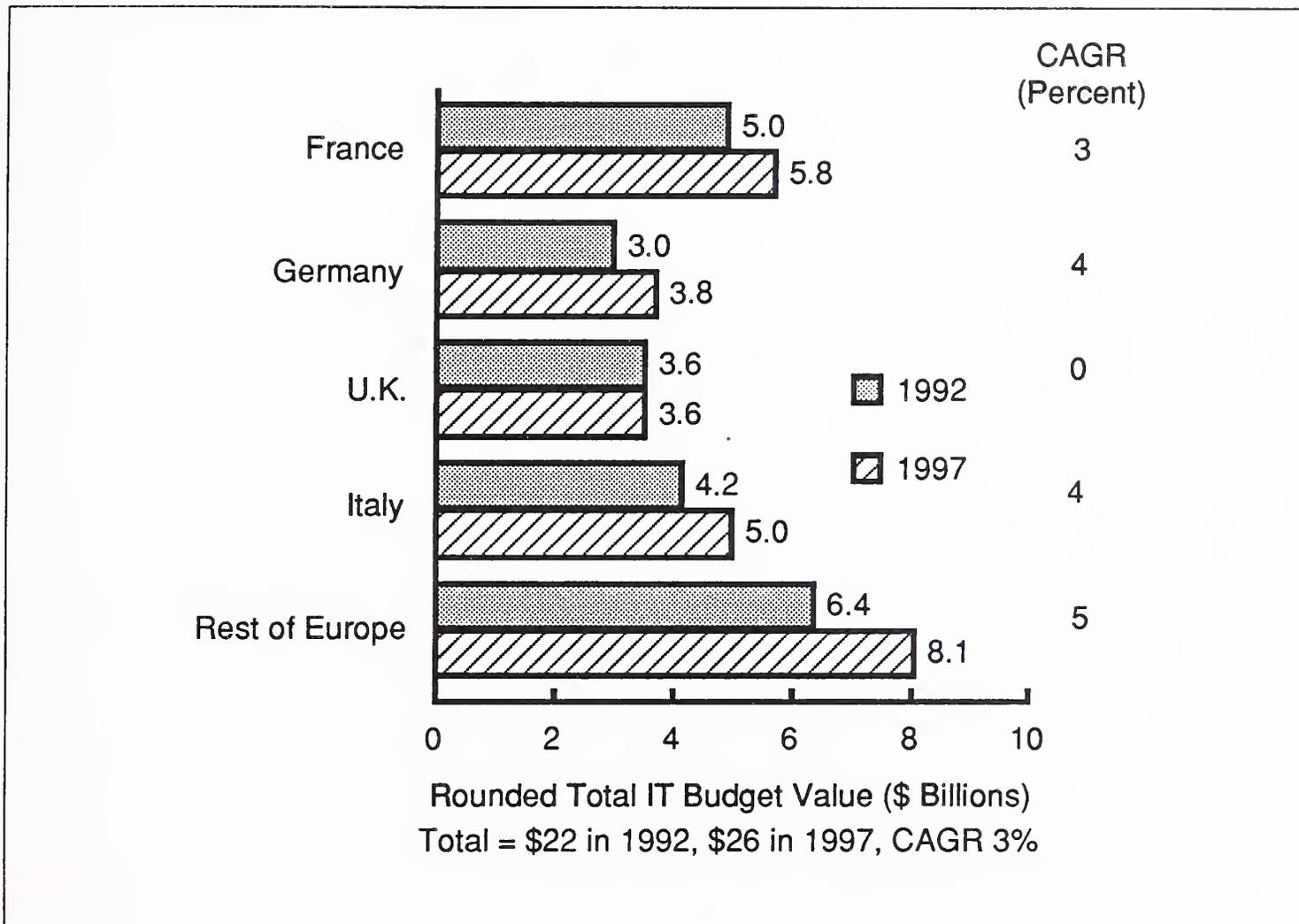
### Government Sector Seeks Infrastructure Efficiencies

Reductions in defence spending have hurt those vendors specialising in this sector, but perhaps not as badly as many had feared. Economic recession is now impacting the whole of Europe, with Germany facing the extra burden of re-developing industry and infrastructure in old East Germany. As a result, the demands for improved efficiency and more responsive operational and administrative systems continue to grow.

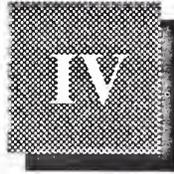
There is significant potential for outsourcing in the government sector, with the U.K. taking a lead in privatising IT departments along with many other departmental functions in order to cut costs.

EXHIBIT III-12

### Comparative Forecast Growth in National Government IT Spend by Major Country, Europe



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## Country Markets

There is wide variation between the major European countries in terms of how the typical IT budget is spent. The following exhibits picture the mix of spending on internal and external resources for France, Germany, the United Kingdom and Italy. The exhibit also shows the forecast growth for each budget component to 1997.

The data from which these charts were constructed are given in Appendix A. The model for each country was produced by INPUT using our own database of research into spending on software, services and maintenance, which has been developed and refined over the past fifteen years.

In addition, desk research has been used to collect other published sources of budget analysis across Europe. Where this has been entirely the result of user surveys there appears to be a significant margin for error in analyses of the basic budget categories. There are two primary reasons for this:

- There can be a very wide interpretation of a category such as software, for instance, it could include custom developed software, rather than being treated as a professional services as it is within INPUT's definitions.
- The IT department's own budget reflects a generally shrinking proportion of most organisations' IT spending—end-user departments are buying their own IT independently so it does not necessarily appear within any so-called company IT budget.

As a result, INPUT finds that user opinion of how much is being spent on IT services is far smaller, as a proportion, than the IT vendors report in their financial results. This discrepancy suggests that most IT managers find a great deal of additional money to spend on services from outside of their IT services budget.

EXHIBIT IV-1

**Forecast Growth in IT Spend by Budget Component, France**

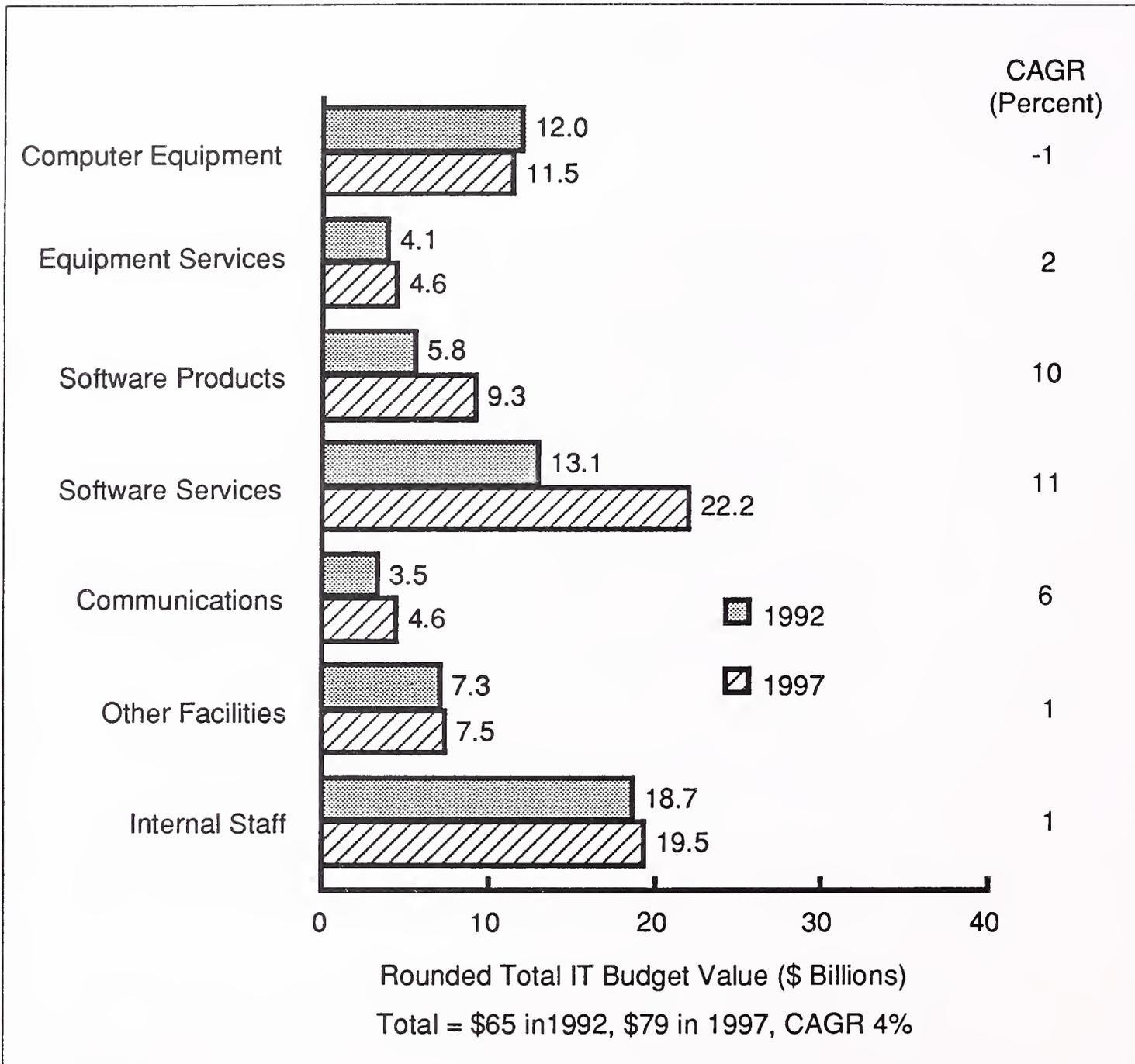


EXHIBIT IV-2

### Forecast Growth in IT Spend by Budget Component, Germany

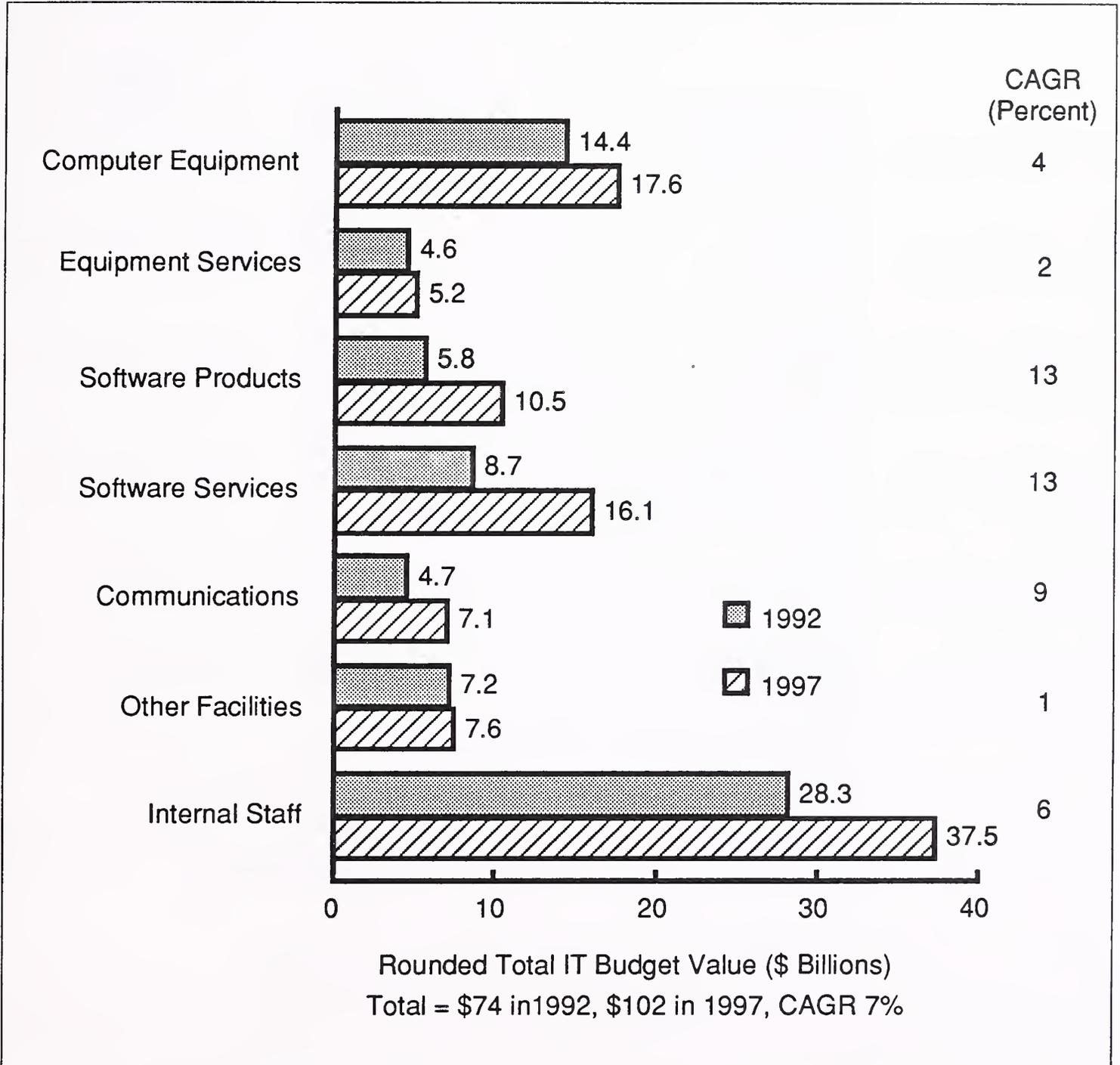


EXHIBIT IV-3

### Forecast Growth in IT Spend by Budget Component, United Kingdom

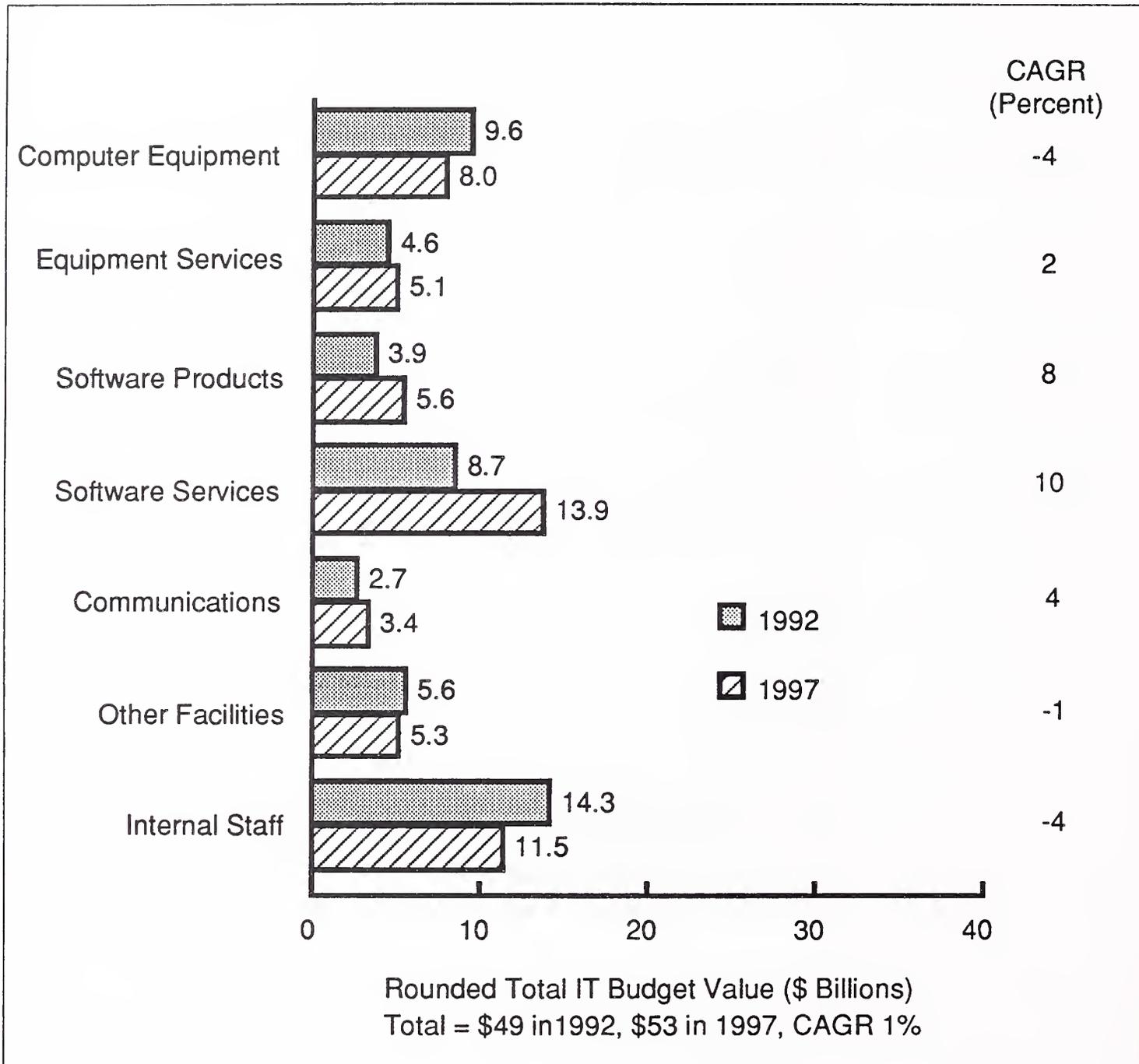
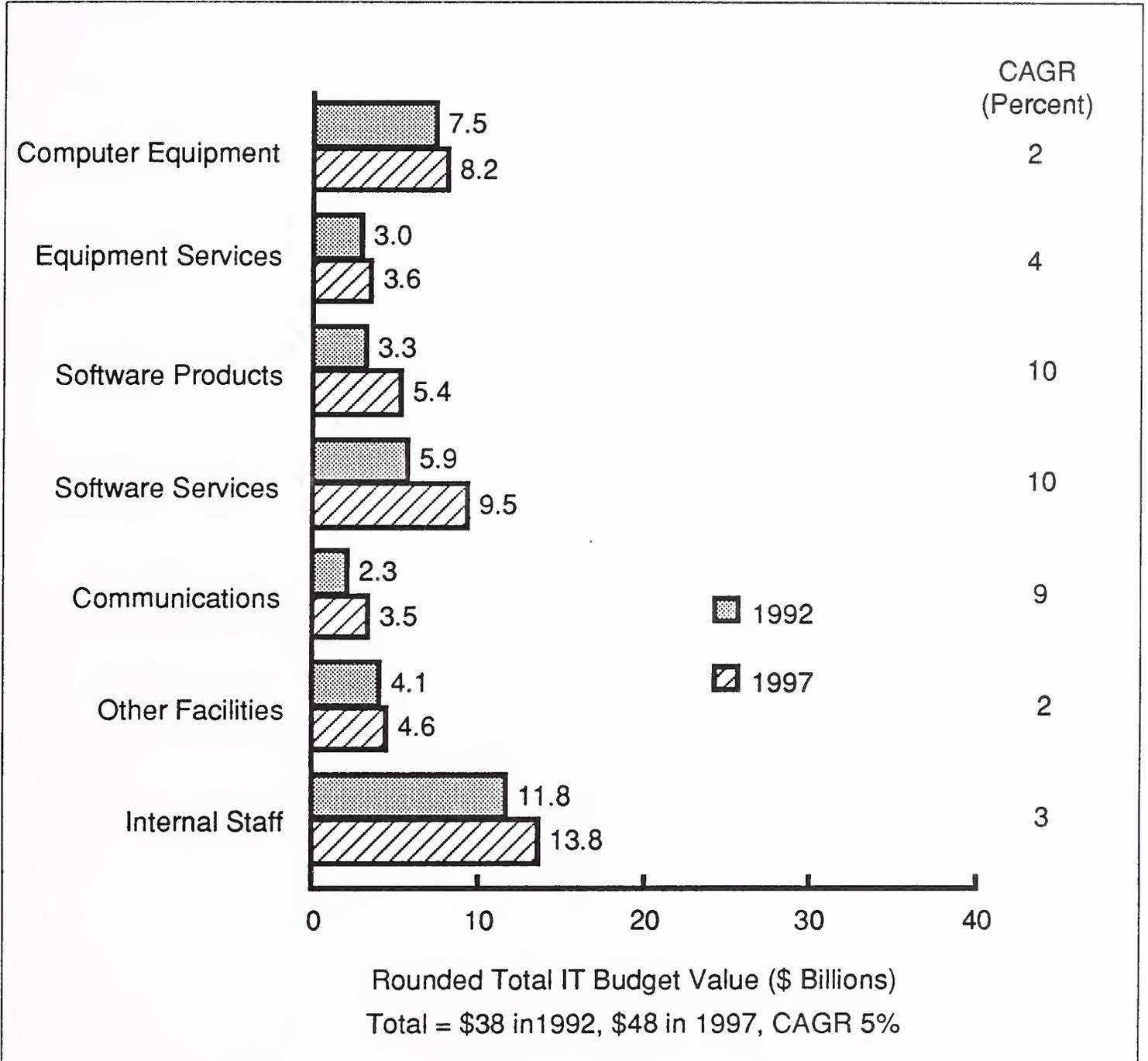


EXHIBIT IV-4

**Forecast Growth in IT Spend by Budget Component, Italy**



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## Appendix—Forecast Databases, IT Spending, Europe, 1992-1997

EXHIBIT A-1

### IT User Budget Forecast Database, Europe (Revised December 1992)

Budget Element	\$ Million (Rounded)								
	1991	1991 1992 Growth (%)	1992	1993	1994	1995	1996	1997	1991 1997 CAGR (%)
Computer Equipment	62,300	-1	61,700	62,000	62,800	64,100	65,500	67,300	2
Equipment Services	23,300	2	23,700	24,400	25,100	25,900	26,600	27,700	3
Software Products	22,600	11	25,000	27,700	30,500	33,800	37,800	42,100	11
Software Services	48,300	10	52,900	57,900	64,000	70,700	78,900	88,000	11
Communications	18,100	7	19,400	20,800	22,300	24,000	25,900	27,900	8
Other Facilities	31,700	1	31,900	32,100	32,200	32,500	32,700	33,000	1
Internal Staff	97,100	2	99,400	102,300	105,300	108,500	112,200	115,900	3
<b>Total IT Expenditure</b>	<b>304,000</b>	<b>4</b>	<b>315,000</b>	<b>327,000</b>	<b>343,000</b>	<b>359,000</b>	<b>380,000</b>	<b>402,000</b>	<b>5</b>

## EXHIBIT A-2

### IT User Budget Forecast Database, France (Revised December 1992)

Budget Element	\$ Million (Rounded)								
	1991	1991 1992 Growth (%)	1992	1993	1994	1995	1996	1997	1991 1997 CAGR (%)
Computer Equipment	12,470	-4	12,030	11,740	11,580	11,450	11,330	11,530	-1
Equipment Services	4,000	2	4,070	4,170	4,270	4,360	4,460	4,580	2
Software Products	5,230	10	5,750	6,250	6,830	7,510	8,360	9,310	10
Software Services	11,950	9	13,050	14,560	15,980	17,860	19,960	22,160	11
Communications	3,280	6	3,490	3,690	3,900	4,110	4,360	4,610	6
Other Facilities	7,140	2	7,260	7,300	7,360	7,390	7,450	7,510	1
Internal Staff	18,530	1	18,730	18,920	19,110	19,110	19,310	19,500	1
<b>Total IT Expenditure</b>	<b>62,740</b>	<b>3</b>	<b>64,670</b>	<b>66,600</b>	<b>69,500</b>	<b>71,430</b>	<b>75,290</b>	<b>79,150</b>	<b>4</b>

## EXHIBIT A-3

### IT User Budget Forecast Database, Germany (Revised December 1992)

Budget Element	\$ Million (Rounded)								
	1991	1991 1992 Growth (%)	1992	1993	1994	1995	1996	1997	1991 1997 CAGR (%)
Computer Equipment	14,210	1	14,410	15,000	15,530	16,120	16,840	17,630	4
Equipment Services	4,510	3	4,640	4,770	4,870	4,970	5,070	5,230	2
Software Products	5,100	14	5,790	6,510	7,370	8,220	9,310	10,490	13
Software Services	7,760	12	8,680	9,800	11,050	12,430	14,080	16,120	13
Communications	4,340	8	4,670	5,070	5,530	5,990	6,510	7,110	9
Other Facilities	7,240	0	7,240	7,300	7,370	7,430	7,500	7,570	1
Internal Staff	26,970	5	28,290	29,930	31,580	33,550	35,530	37,500	6
<b>Total IT Expenditure</b>	<b>70,390</b>	<b>5</b>	<b>73,680</b>	<b>78,290</b>	<b>83,550</b>	<b>88,820</b>	<b>94,740</b>	<b>101,970</b>	<b>7</b>

## EXHIBIT A-4

**IT User Budget Forecast Database,  
United Kingdom  
(Revised December 1992)**

Budget Element	\$ Million (Rounded)								
	1991	1991 1992 Growth (%)	1992	1993	1994	1995	1996	1997	1991 1997 CAGR (%)
Computer Equipment	10,530	-9	9,590	8,830	8,460	8,080	7,990	7,990	-4
Equipment Services	4,610	0	4,610	4,660	4,740	4,830	4,940	5,090	2
Software Products	3,570	8	3,850	4,140	4,420	4,700	5,170	5,550	8
Software Services	8,270	5	8,650	9,210	10,150	11,090	12,310	13,910	10
Communications	2,630	4	2,730	2,820	2,910	3,100	3,200	3,380	4
Other Facilities	5,730	-2	5,640	5,550	5,450	5,360	5,360	5,260	-1
Internal Staff	15,040	-5	14,290	13,630	13,060	12,500	11,940	11,470	-4
<b>Total IT Expenditure</b>	<b>50,380</b>	<b>-2</b>	<b>49,440</b>	<b>48,870</b>	<b>49,250</b>	<b>49,620</b>	<b>50,940</b>	<b>52,630</b>	<b>1</b>

## EXHIBIT A-5

**IT User Budget Forecast Database,  
Italy  
(Revised December 1992)**

Budget Element	\$ Million (Rounded)								
	1991	1991 1992 Growth (%)	1992	1993	1994	1995	1996	1997	1991 1997 CAGR (%)
Computer Equipment	7,610	-1	7,520	7,610	7,650	7,830	8,000	8,170	2
Equipment Services	2,960	1	3,000	3,130	3,220	3,350	3,430	3,570	4
Software Products	2,960	12	3,300	3,650	4,000	4,430	4,870	5,430	10
Software Services	5,300	11	5,870	6,430	7,000	7,700	8,610	9,480	10
Communications	2,090	8	2,250	2,460	2,670	2,930	3,200	3,500	9
Other Facilities	4,090	1	4,130	4,220	4,260	4,390	4,520	4,610	2
Internal Staff	11,570	2	11,830	12,170	12,520	12,960	13,390	13,830	3
<b>Total IT Expenditure</b>	<b>36,520</b>	<b>4</b>	<b>37,830</b>	<b>39,570</b>	<b>41,300</b>	<b>43,480</b>	<b>46,090</b>	<b>48,700</b>	<b>5</b>

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