Plan Conservatively for 2016

RFG Perspective: 2016 looks to bear a strong resemblance to 2015, but has the potential to be worse. The U.S. GDP growth most likely will again be in the two percent range with low to no inflation. The worldwide GDP growth will likely be less robust and in many of the key countries it will be flat or negative. A strong dollar and weak oil prices will keep inflation down and slow job growth, too. Business and IT executives need to plan accordingly and ensure purchases, resources and staffing can be flexibly adjusted to support the changes of the economies and potential volatilities of the markets.

The U.S. economy grew almost four percent in the second quarter, according to the government's second update on how fast the nation's economy expanded during the spring quarter. This was a major jump from the first quarter's 0.6 percent growth. This history plus the projected growth for the second half of the year leads to economists' predictions of full year growth in the 2.0 – 2.5 percent range for the year. Thus, for the last six years the U.S. economy will have grown on average less than two percent per year. Not robust enough to generate strong revenue growth or real job growth year-over-year. That said, this is the good news.

The economies in Western Europe are struggling to stay out of recession while the BRICS (Brazil, Russia, India, China, and South Africa) are contracting, stagnating, or struggling to keep the engines of growth going. The other nations are not faring well either. Midyear projections from global economic prognosticators believe 2016 will be slightly better than 2015. But they are starting to hedge their bests as economic conditions since their last pronouncements have worsened. Thus, RFG believes 2016 may not be as strong as this year, especially outside of the U.S.

Other Indicators

The collapse of the global crude oil market, which is down almost 50 percent since last year at this time, is negatively rippling through the world economies. For consumers oil-based products are less expensive but the impact to governments, banks, and those producers tied to the market has been severe. In most oil-producing countries the governments (which own the oil firms) are under water and will not escape for years to come, given current projections of constrained oil prices. This is bad news and could result in destabilization of the countries over time.

Russia is experiencing outflows of cash continually and is struggling to balance its political desires against revenues, which are commodity based. Brazil is no longer a beacon of economic growth but a stumbled giant dealing with high inflation and government corruption. India cannot seem to get its regulatory grip out of the way of economic growth while China's growth continues in a downward spiral (although still a decent five to six percent). Lastly, South Africa will enter a recession if it experiences another quarter of contraction. Thus, companies looking for the BRICS to be their engines of growth will be sorely disappointed.

The strong dollar will not help either. Outside the U.S. the nations are hoping that they can devalue their currencies for an economic advantage. This may help temporarily but when companies look at it from a constant dollar basis, the news will not be good.

Wages are not growing either. There is little inflationary pressure or market tightness (except in some areas of IT) to push wages up. On the other hand, there will be pressure on organizations from the regulatory agencies as more and more rules and regulations keep being created. The net result is internal costs will go up as a percentage of revenues.

IT and Procurement Implications

RFG expects 2016 budgets to be constrained for companies not experiencing rapid growth. Marketing budgets are likely to be down, which means the IT budgets derived from CMO expenditures will likely take a hit. IT executives can expect another year of "do more for less" across the board. Executives need to re-evaluate staffing and determine where globally resources need to be located, as well as whether the resources should be from internal staff, contractors, outsourcers, or just moved to cloud providers. IT executives will have to carefully construct merit increase and hiring/attrition plans to conserve expenses.

In terms of acquisition of hardware and software IT and procurement executives should be leasing (or renting) unless the firm's model advocates capital expenditures vs. operational expenses. This will reduce CapEx and allow the company to better utilize capital. Moreover, in today's environment leasing will prove to be less expensive overall, if done correctly, especially since most companies of good standing will be able to take advantage of the low interest rates currently available today and through next year.

Regardless of whether or not one leases or purchases, IT and procurement executives should be moving to volume purchases. This should be the case whether one is acquiring materials all at once or staggered over one to three years. Executives should negotiate pricing based on the maximum potential purchase amounts but without any guarantees of minimum quantities. Most suppliers in the slow-growth markets will be more than willing to negotiate on these terms.

Summary

Executives need to tighten their seat belts for another tough year. RFG and other studies show that 60 to 70 percent of operational budgets are wasted every year. Done appropriately IT executives can continue to slice costs without impairing their ability to deliver and meet commitments. Moreover, some of the savings initiatives can be self-funding and can prime the pump for future cuts, automation, and process improvements.

RFG POV: The IT budgets for 2016 should be constructed in such a way that IT executives can easily and rapidly respond to changes in the economy and volatility in the markets. This requires executives move conservatively and refrain from spending ahead as much as possible. While 2016 seems to be just one more year "of the same," for many IT and procurement executives implementing the strategies defined above are a major change. Business and IT executives should develop fiscal year budgets that can be implemented and continually monitored and revised to support the needs of the business.

Additional relevant research and consulting services are available. Interested readers should contact Client Services to arrange further discussion or interview with Mr. Cal Braunstein, CEO and Executive Director of Research.