

# Executive Summary

# BDO Seidman 2009 Technology Outlook

## BDO SEIDMAN TECHNOLOGY PRACTICE

BDO Seidman, LLP works with a wide variety of technology clients, ranging from multinational Fortune 500 corporations to more entrepreneurial businesses, on myriad accounting, tax and other financial issues.

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*These findings are from the BDO Seidman 2009 Technology Outlook Survey, which examined the opinions of 100 chief financial officers at leading U.S. technology companies in the software, hardware, telecommunications, Internet and IT services sub-sectors. The survey was conducted in January of 2009.*

The first quarter of 2009 has been marked by continued stock market losses, rising unemployment and a general sense of foreboding about the future. In stark contrast to 2008, the BDO Seidman 2009 Technology Outlook Survey of chief financial officers (CFOs) at leading U.S. technology companies revealed predictions of reduced sales revenues and reports of restructuring and workforce reductions. However, the CFOs continue to see work as companies look to streamline their operations and advance innovation, starting with their technology tools and departments.

In addition, the study measured CFOs' thoughts regarding changes in financial reporting standards, shareholders' say on pay, M&A activity, security, corporate responses to the financial crisis, capital issues, international outsourcing and more.

### 2009 Projections

Less than a third (30%) of CFOs at leading U.S. technology businesses forecast increased sales revenue over last year. This compares to early 2008 when almost three quarters (73%) of CFOs felt optimistic about sales revenue, predicting an increase in sales revenue over 2007. This year, thirty-seven percent forecast decreased sales (up significantly from six percent in 2008), and one-third (33%) predict flat sales (up from 15% in last year's survey). The average sales loss forecast is fifteen percent among those CFOs predicting a decrease in total sales revenue this year.

A majority (55%) of the CFOs cite a necessary economic rebound in the United States as the greatest driver of growth in the industry in 2009. Recent reports from Washington suggest we will

see this rebound begin in 2009 and continue into 2010. Thirteen percent indicate that increased IT budgets, followed by the demand for green technologies and solutions (12%), will be growth drivers. These were followed still by international growth (10%), consumer demand for innovative personal technology (8%) and the web 2.0 boom (2%).

### Challenges and Responses to the Financial Crisis

In 2009, concerns about how to grow are replaced by concerns about how to survive. In 2008, the ability to recruit and retain talent (38%) was seen as the greatest challenge for the coming year. However, this year the percentage dropped by over two-thirds, as only twelve percent believe that the ability to recruit and retain talent is the greatest

challenge for 2009. CFOs cite managing risk (39%) as their greatest challenge in 2009 (up from 23% in 2008), followed by access to capital (33%), which is over double the fifteen percent of CFOs who cited that as a challenge in 2008. Foreign competition (8%, down from 9% in 2008) and financial reporting and corporate governance (8%, down from 14% in 2008) rounded out the challenges.

As a response to the financial crisis, almost two-thirds (61%) of CFOs state that their company has restructured operations, including reducing their workforce. Following that, CFOs cite that they have reassessed revenue collection methods (43%) and reassessed the valuation of assets (43%). Only three percent of the CFOs said that their company reorganized or sought governmental protection (including bankruptcy protection) last year.

### **M&A Activity Cautiously Continues**

Consistent with the 2008 survey findings, CFOs anticipate that merger and acquisition activity in the tech sector will pick up in 2009 (43%, up from 41% in 2008). However, more than twice the percentage of CFOs this year believe that M&A activity will decrease (35%, up from 17% in 2008) and twenty-two percent (down from 42% in 2008) believe M&A activity will stay the same.

According to these CFOs, the primary drivers behind acquisitions in today's technology market are expanding market share (40%, up from 26% in 2008) increasing revenue and profitability (34%, down from 37% from 2008), acquiring technology assets (12%, down from 24% in 2008), increasing distribution channels (10%, up from 4% in 2008) and geographic coverage (4%, down from 6% in 2008).

Almost three quarters (72%) of the CFOs say that the Financial Accounting Standards Board Statement 141(R) on business combinations (that will change accounting rules related to in-process R&D, contingent consideration and merger expenses) will not reduce merger and acquisition activity in the technology sector once it becomes effective.

### **Still Seeking Capital**

Just over one-third (34%) of the CFOs expect their businesses to seek additional capital in the coming year, up from twenty-seven percent in 2008. More interesting, the CFOs cited private equity (56%) as their chief source to raise capital, up from thirty-three percent in 2008. In fact, almost three-quarters (73%) of CFOs at public companies in the technology sector will focus on private equity to secure capital in the coming year. Less than a third (31%) cited debt, and public equity (9%) finished last.

Nearly one-third (32%) of the CFOs cite working with an investment banker as the best action a technology company can take to identify and procure capital in the coming year, followed by over a quarter (28%) who feel the best method is to work directly with a private equity firm. Eighteen percent name pursuing an M&A opportunity, attending industry conferences and networking (15%) and citing international sources (7%) as other attractive ways to seek and secure capital in 2009.

### **IFRS vs. GAAP**

As the Securities and Exchange Commission (SEC) adjusts the timeline for moving all U.S. public companies to International Financial Reporting Standards (IFRS) from the U.S. Generally Accepted Accounting Principles (GAAP),

only one-fifth (21%) of CFOs indicate that their company would adopt the standards early, if given the opportunity.

Businesses are becoming more receptive to IFRS, but more than half (57%) still feel GAAP provides better revenue recognition rules for technology companies over IFRS. This is down from sixty-nine percent of companies who felt GAAP provided better quality revenue recognition rules when queried last year.

When asked if the switch from GAAP to IFRS will make U.S. companies more competitive with international firms, the majority (71%) indicate that there will be no impact on competitiveness. Less than a quarter (24%) say that the switch will make U.S. companies more competitive with international firms, and only five percent say that the switch will make them less competitive. This compares to early 2008 when less than half (49%) of the CFOs thought that international companies reporting financial results using IFRS have a competitive advantage over U.S. companies filing under GAAP.

### **Executive Compensation Disclosure**

The vast majority (89%, up from 69% in 2008) of CFOs indicate that their company does not allow shareholders to vote on their executive compensation plans, compared to only eleven percent (down from 31% in last year's survey) that do. Moreover, only one-third (34%, down from 61% in 2008) of the CFOs personally feel shareholders should have a say on executive compensation plans in 2009.

The survey also asked the CFOs about the adjustments their companies are likely to make to equity compensation

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in the coming year, and found that less than a quarter (24%) of technology businesses will offer replacement grants, fourteen percent will re-price options and six percent are planning to eliminate options for employees.

## Security Concerns

Despite the influx of identity theft cases with retailers and creditors in the past year, only ten percent of CFOs at technology companies indicate that their company had an external hacking or breach during the past year. This was followed by intellectual property infringement (7%), identity theft (5%) and misappropriation of assets (3%) as the most common security incidents.

External hacking or breaches (38%) is seen as the most potentially harmful security-related issue, followed by intellectual property infringement (32%), misappropriation of assets (18%) and identity theft (12%).

## Outsourcing & International Operations

Nearly two-thirds (62%) of CFOs say that their companies outsource services or manufacturing. However, the survey results point to a likely decline in international outsourcing in 2009: twenty-two percent say the United States is the outsourcing destination they are most likely to consider in 2009, compared to sixteen percent for China and thirteen percent for India. Another nineteen percent report no interest in additional outsourcing.

The most common non-U.S. locations for outsourcing are India (50%), Southeast Asia, including the Philippines (31%, down from 50% in 2008), China (19%, down from 46% in 2008), and Western Europe (19%).

When asked what **one** location they might consider for outsourcing in the future, the CFOs most frequently cite the United States (22%), followed by

China (16%), India (13%), Southeast Asia, including the Philippines (7%), Latin America (7%), Western Europe (6%), Canada (5%) and Eastern Europe (3%).

Of those outsourcing, the most common functions being off-shored currently are: manufacturing (54%), IT services and programming (46%), research and development (35%), distribution (35%) and call centers (35%).

Less than half of the CFOs (42%) indicate that they have operations outside the U.S., compared to nearly double that amount (79%) last year. Nearly a third (29%) of respondents say their primary concern regarding international growth is an uncertain business or political climate. About a quarter (26%), cite international business and tax regulations, with twenty-one percent citing currency risk, fourteen percent intellectual property risk and exploitation, and 10% training of international employees as their primary concern.

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