Despite the disruption caused by the coronavirus pandemic, the performance of the Computer Software Industry since our early-February review was respectable on a comparative basis. From a financial and operating perspective, the larger enterprise software vendors continued finding fertile ground in the cloud arena in the March period. To wit, the overall margin on gross profits was again less constrained by the transition to the service orientation of the cloud, as software companies are increasingly enjoying the scale economies in their cloud businesses. We note here that *CloudFlare, Inc.*, an operator of a cloud-based platform supplying a broad range of network services, is making its debut in *The Survey* this week.

Meanwhile, the stock price performance of our Industry in the three-month interim since our last report was impacted by the sharp decline recorded by the equity market over the 33-day period ending March 23rd. Nonetheless, the group's loss of 5.7%, which essentially matched that of the NASDAQ Composite, was relatively mild compared with the decline of 12.1% registered by the S&P 500 Index. Looking a little deeper, though, of the 29 companies included in our group, only eight saw their shares rise in price, with the largest moves being associated with the smaller companies in our Industry.

As it stands now, forecasts by industry analysts (Gartner) suggest that spending on computer software and related services is likely to decline some 7.3% in 2020, reflecting the economic recession that is to follow in the wake of the coronavirus pandemic. This figure differs markedly from the 10.9% growth that had been estimated at the beginning of the year. That said, those software companies that are in the process of moving their business to the cloud and cloud services should fare better than others in the software sector.

A Brief Look At 2020

Most software vendors should continue finding good growth from products and services aimed at cloud computing and cloud architecture this year. This business is largely subscription-based, allowing customers to pay for the software and services over the life of the contract or on a by-use basis. By comparison, the traditional perpetual license agreement requires a large up front payment for the use of the license and possibly training, with an annual fee for maintenance. The cloud is becoming a larger part of many vendors' respective revenue streams, but perpetual licenses are still an important factor.

Meanwhile, our sense is most software vendors have the financial wherewithal to withstand the challenges posed by the economic recession that is unfolding even as the problems associated with the coronavirus begin to subside. Nonetheless, some of their customers may find the going more difficult, causing them to conserve cash and reduce spending on software and services. Still, the flexibility of the cloud and subscription services may be seen in a positive light by those having to pare budgets, particularly when compared with the initial capital outlay for a perpetual license agreement. Such a juxtaposition may act to enhance the move away from traditional software purchases and to those based on the cloud and cloud services.

An Update On The Economic Landscape

The outlook for economic expansion in the United States has changed markedly since our February review, when many forecasters where looking for a continuation of the growth that had been established. To wit, the employment picture was bright, and it appeared that the drag from the trade war with China was easing. With a turn of a card, the coronavirus pandemic relegated those forecasts to the dustbin, with the economic outlook for the months ahead quite uncertain. The optimistic view is that the downturn will be quite sharp, but limited in extent, with the potential for progress holding forth as 2021 begins. Still, the economic dislocation that may have been caused by the lockdown orders issued by state governors is not yet known, and the recession may become a drawn-out affair. Assuming that the recovery from the economic downturn moves apace in the months ahead and does not become extended, companies operating in this Industry should experience calmer waters as 2021 begins.

Software And Related Services, Industry Trends

Although the overall outlook for spending on software and related services for 2020 has taken a turn for the worse, we are currently taking the optimistic view that business will improve next year. Still, much depends on the extent of the economic recession that will follow in the wake of the coronavirus pandemic. The long-term picture is much less uncertain and brighter, in our view. On point, most corporate businesses are likely to continue investing in enterprise software and related services, suggesting that overall spending on computer software should progress nicely in coming years. In this regard, the move to cloud architecture, cloud computing, and hosted services will remain central, underpinning the growth that we envision.

Conclusion

There is a broad spectrum of companies in the Computer Software Industry, offering a wide range of products and services. Subscribers should consult individual company reports before making new commitments.

Charles Clark

Computer Software

RELATIVE STRENGTH (Ratio of Industry to Value Line Comp.)

Index: June, 1967 = 100