

The performance of the Computer Software Industry for the third quarter of 2016 was respectable. For the most part, the larger enterprise software vendors continued making progress in the cloud arena. That said, the financial results continued to be somewhat constrained by the transition to the service orientation of the cloud. Meanwhile, adverse currency translation due to the relative strength of the U.S. dollar remained, but was less pronounced than in 2015.

On average, the stock price performance of this industry in the three months since our mid-August review registered a modest advance, versus the more moderate losses inked by the major market benchmarks. That said, of the 23 companies included in our industry, only 12 saw their shares move forward in the interim. Moreover, there was a wide variation in the group's stock performance, indicating little consistency in investor support. On a year-to-date basis, the price performance of the Computer Software Industry remains well within the range recorded by the major indexes, though a few stocks included here have not yet recovered from the declines experienced in the months of January and February.

As it stands now, most forecasts suggest that spending on computer software and related services should stay on an upward trend in 2016, reflecting the secular move to cloud architecture.

Notwithstanding the uneven prospects for global economic expansion, we remain cautiously optimistic on the prospects for the larger enterprise software vendors.

#### A Brief Review Of The Third Quarter

Most software vendors reported strong growth from products and services aimed at cloud computing and cloud architecture. Although the cloud is becoming a larger part of their respective revenue streams, investors are still very interested in the sale of traditional software licenses and services. On point, the so-called on-premise systems may well remain in place for some time yet, as enterprises transition their organizations to cloud-based architecture. In this regard and on a constant-currency basis, contracting activity in the on-premise arena continued to generally register modest improvement in the third quarter. Nonetheless, the long-term prospects for growth from traditional software sales remain rather muted, in our view.

Meanwhile, in keeping with the more recent quarterly reports, financial results from large enterprise software vendors for the September period were much less affected by the relative strength of the U.S. dollar, as some stability seems to have been established in the currency markets, at least for the time being. That said, for the most part, software vendors continued to offer forecasts for growth based on constant currency, with investors taking this in stride while looking forward to the fourth quarter and 2017. At this writing, assuming the dollar does not strengthen appreciably, currency translation effects should remain less of a burden, with the prospect that they may turn neutral in 2017.

#### An Update On The Economic Landscape

The outlook for economic growth in the United States has improved slightly since we published our last review in August. At 2.9%, the initial read on GDP for the third quarter provided a bit more optimism, as increased

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consumer spending on services related to housing and healthcare more than offset declines in residential housing investment and in spending by state and local governments. As it stands now, the GDP performance in the first nine months suggests that economic expansion in the United States may increase at a 2.0% rate, or more, through next year.

Meanwhile, business investment remains on a recovery path in Europe, though other advanced economies are tracking forward faster in this regard. Nonetheless, the improvement is being fostered by better demand, favorable profit expectations, and declining uncertainty, all of which should be positive for large enterprise software vendors. Indeed, many reported good sales activity from Europe in the third quarter. Elsewhere, the slowing pace of expansion in China is always of interest, given the size and scope of its economy.

#### Software And Related Services

Although the latest outlook for the IT market is for a modest decline (constant currency) this year, software and related services usually track faster than the IT market taken as a whole. This backdrop, when combined with the reality that most corporate businesses are in good financial shape and have the resources to continue investing in enterprise software and related services, suggests that spending on computer software should advance nicely this year. Moreover, corporate interest in software infrastructure and the general realm of cloud services should remain quite active.

#### Industry Trends Remain The Same

The move to cloud architecture, cloud computing, and hosted services is front and center. Indeed, most software vendors should continue benefiting from the interest, as corporations look to leverage storage, applications, security, and processing power via cloud services. Indeed, contract bookings from the cloud are becoming a larger part of the overall software business.

#### 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*

