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Acknowledgements

ScotlandIS and 9-20recruitment would like to thank everyone who took part in this year's Scottish Technology Industry Survey for their invaluable input, providing feedback on the operating environment in 2010, and their forecasts for 2011.

The Scottish Technology Industry Survey provides a barometer of the health of the digital technology industry. An essential element of the Scottish economy, catalysing productivity improvements, innovation and service delivery across Scotland, digital technologies, comprising software, telecoms, and IT services, are extremely valuable, employing more than 100,000 people in Scotland. Of these, over 60,000 are directly employed in the supply side of the industry, with the balance providing in-house expert technology skills within other industries.

The Scottish supply base comprises more than one thousand digital technology businesses delivering products and services, at home and abroad, from world class products for major corporations, to specialist services enabling smaller businesses to improve productivity and reach global markets, and in-house technology developments for corporate functions.

This report analyses the survey data by industry characteristics, business dynamics, market forecasts, and employment and skills factors. The survey was carried out by ScotlandIS in January/February 2011. The survey analysis was undertaken by ScotlandIS, and 9-20recruitment. ScotlandIS is particularly grateful to 9-20recruitment for their continued support for the survey.

I very much hope you find this report useful. Please do contact the ScotlandIS team if you have any questions about the survey, or would like further information.

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Your business is yours to build or let wilt. Every decision that matters to you is your decision, so make it wisely and question every time you criticise others for the state of your business. Yes, there is plenty of luck and chance, but every day is an opportunity to achieve great things.

Stuart Roebuck, ProInnovate Ltd

Key Messages

The Scottish Technology Industry Survey provides an annual health check for the information and communication technology sectors.

Industry Optimism, Tempered with Reality

- 63% of those surveyed are optimistic or very optimistic about the outlook for the year ahead.
- Of those surveyed, 54% reported a rise in turnover during 2010.
- The vast majority of companies (79%) expect sales to grow this year and only 11% expect sales to decline.
- Smaller businesses (200 employees or less) are the most optimistic about sales growth, expecting to increase their sales figures by up to 20% while very large companies anticipate growth to be in single figures.
- Cash flow continues to be a challenge for companies.
- Work in the public sector market is expected to fall sharply this year, Financial Services has regained its position as the top sector for new business opportunities.

Employment Growth

- 63% of companies plan to increase headcount this year. Of these, one in ten expect to increase staff numbers by more than 20 in 2011.
- Permanent employees rather than contractors are the preferred option for the majority of respondents, in particular for sales and marketing and infrastructure and support functions.
- Demand for Graduates has recovered strongly.

International Opportunities

- Europe is becoming an increasingly important market with over 40% of respondents selling in Europe and 30% selling to the United States.
- Of the 60% of businesses who are not currently exporting, one in three report plans to do so.
- Of those looking to open up international markets, the United States is the most popular (43%), followed by Europe (25%) and Australia (16%).
- Of those already exporting, Europe is the most popular potential new target market (23%), followed by Asia (22%).

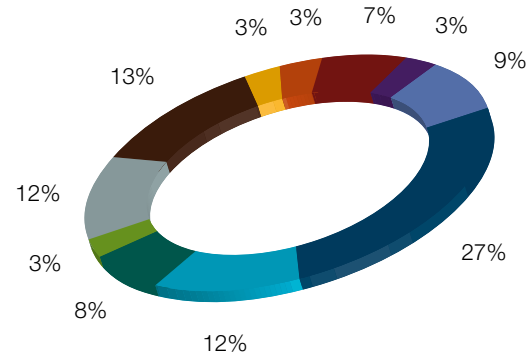
Our Respondents

Respondents provided information including the location of their company headquarters, company size, year of formation, source of capital, and their particular areas of expertise.

Primary Business Area

There is no definitive way to segment digital technologies easily, as many businesses undertake a broad range of activities. We therefore asked respondents to select the sector which most closely matches their main business.

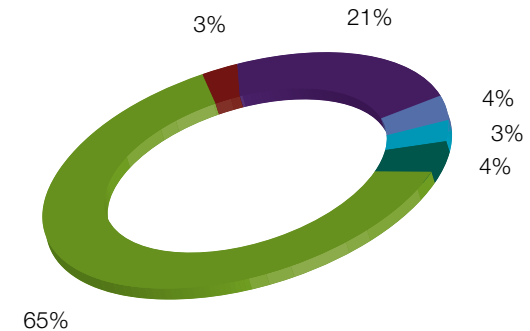
The 'top five' sectors are software solutions & services (27%) e-commerce & web development (12%) IT business consultancy (8%) services to technology (12%) and Application Development (9%).



Product Development

We asked those respondents who indicated their main business to be in software and IT services whether they are also working on product development.

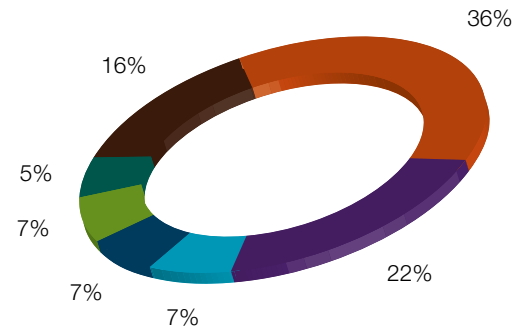
71% confirmed they do have products under development. The majority of these businesses are in software solutions and services, followed by application development businesses.



Company Size by Employment

Survey respondents broadly reflect the wider industry, and the distribution of employment.

Whilst large and very large companies account for 35% of respondents, the majority (65%) are small and medium size companies (SME's) with over half of these employing fewer than 35 people.



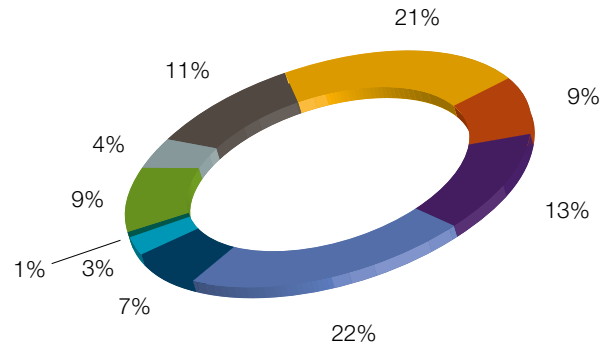
- 1 - 10 Employees (36%)
- 11 - 35 Employees (22%)
- 36 - 65 Employees (7%)
- 66 - 200 Employees (7%)
- 201 - 500 Employees (7%)
- 501 - 1000 Employees (5%)
- 1000+ Employees (16%)

Company Size by Turnover

Like last year, respondents were asked to indicate turnover levels.

The two biggest groupings remained companies in the one million to five million range and those with less than £250,000 turnover.

Businesses turning over less than £1M account for 42% of all respondents.

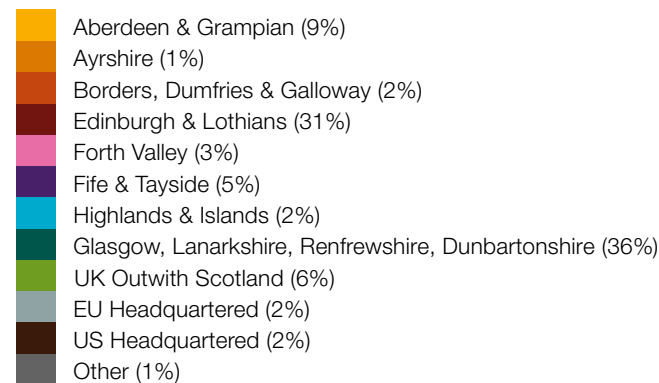
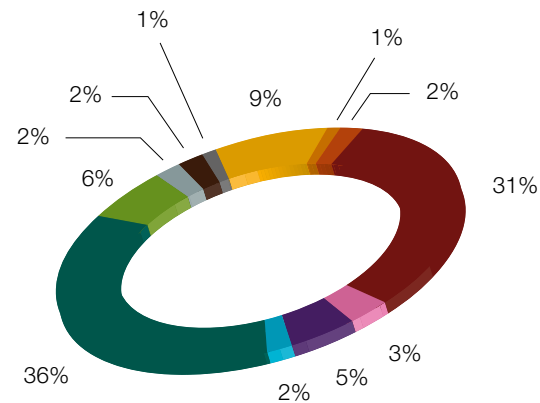


- £0 - £250k (21%)
- £250k - £500k (9%)
- £500k - £1M (13%)
- £1M - £5M (22%)
- £5M - £10M (7%)
- £10M - £15M (3%)
- £15M - £20M (1%)
- £20M - £50M (9%)
- £50M - £100M (4%)
- £100M+ (11%)

Our Respondents cont.

Location of Company Headquarters

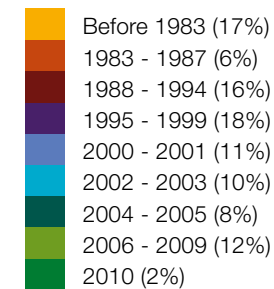
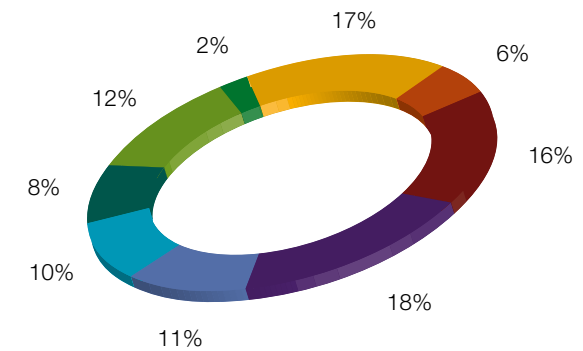
The vast majority (88%) of this years respondents have their head quarters in Scotland, with 75% of the total sample located in the central belt, in line with the geographic distribution of the wider industry. A detailed breakdown of respondents' company headquarters location is shown below.



Year Company Was Formed

The ICT sector benefits from a high rate of start-ups. Over 40% of our sample companies have been in business less than 10 years, and 13% were formed in the last 5 years.

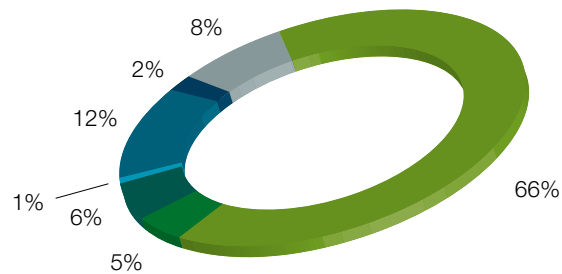
Just under half of companies formed before 1983 are very large organisations.



Sources of Company Funding

Respondents were asked how their businesses are funded. Over half are funded from founders' capital, with the vast majority (85%) of these being smaller companies (under 65 employees)

11 % of respondents are funded by a mix of angel or VC funding. Whilst services companies are often able to fund growth through retained profits, product companies tend to be more capital intensive and generally need external funding.



Listen to advice from people from other types of business - every little helps.

Graeme Duncan, MD, Xtreme Business Solutions Limited

Live within your cashflow whatever it is.

Pete Mowforth, CEO, INDEX International

Listen to what customers are telling you, **especially** if they are telling you something you didn't expect or don't want to hear.

David Stewart, CEO, Critical Blue

Focus on growing the business, developing the product, and delivering service.

Aydin Kurt Elli, CEO, Lumison

Reflections on 2010

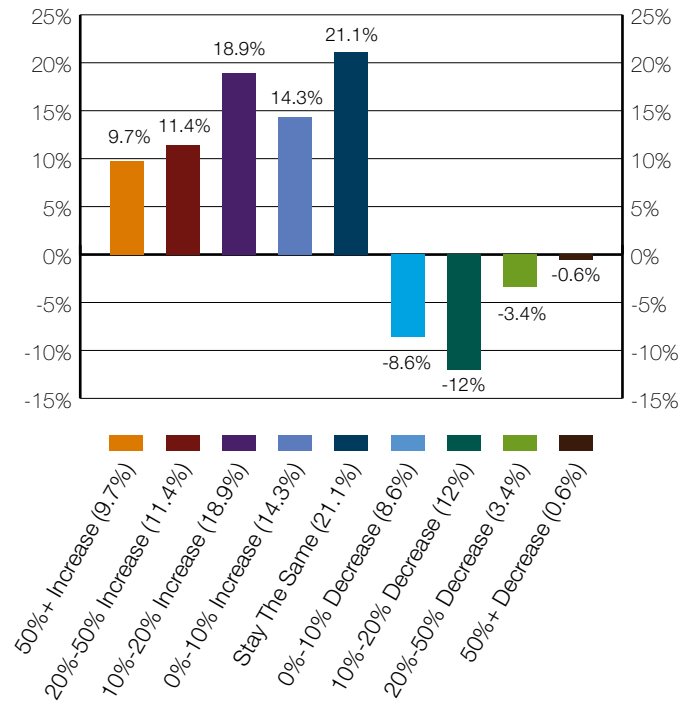
Respondents started 2010 with a degree of quiet confidence, notwithstanding the complex operating environment, with many business forecasting they would be able to maintain or grow business volumes. With most finishing close to budget and profit margins under slightly less pressure, it appears their confidence was not misplaced.

This year respondents were asked to share their aspirations as regards global markets. The results suggest many companies are seriously interested in exploiting international opportunities.

2010 Sales Compared to 2009

2010 continued to provide a challenging market environment for businesses. Respondents reported mixed results: whilst 54% of respondents reported an increase in sales compared to 2009, 21% reported static sales and 25% saw sales fall in real terms.

As in last year's survey, growth was seen across the whole spectrum of company size, but those reporting growing by more than 50% were predominantly smaller companies (under 65 employees).

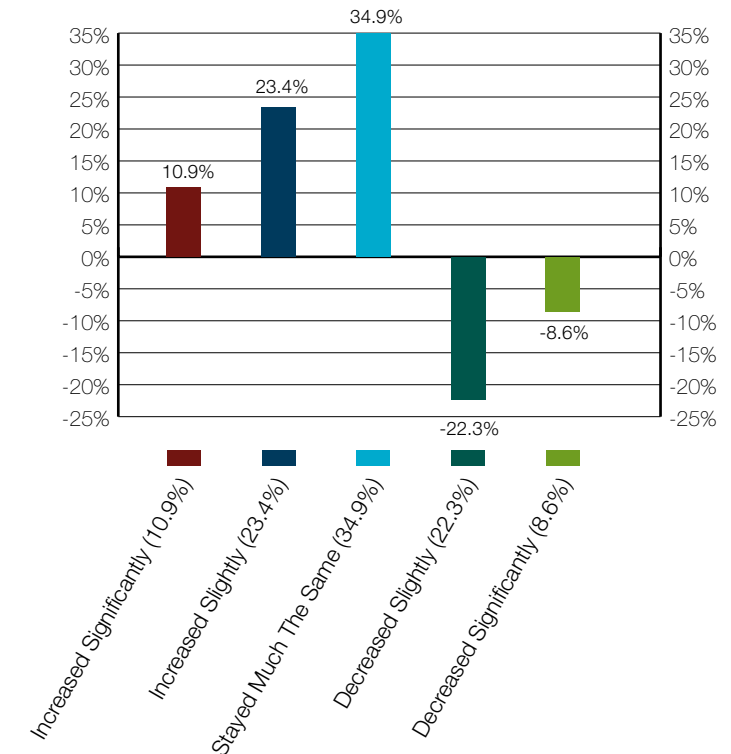


Actual Sales Compared to Budget

Respondents were asked how their actual sales for 2010 compared to their forecasts at the beginning of the year.

The vast majority (81%) reported actuals close to budget. A further 11% saw actuals significantly ahead of budget and 9% reported a considerable reduction in actual sales. Whilst companies reporting sales near to or more than budget were across the whole size spectrum, those experiencing sales significantly less than forecast were predominantly very small businesses.

One in five were at the extremes, reporting a significant difference from their original forecasts.

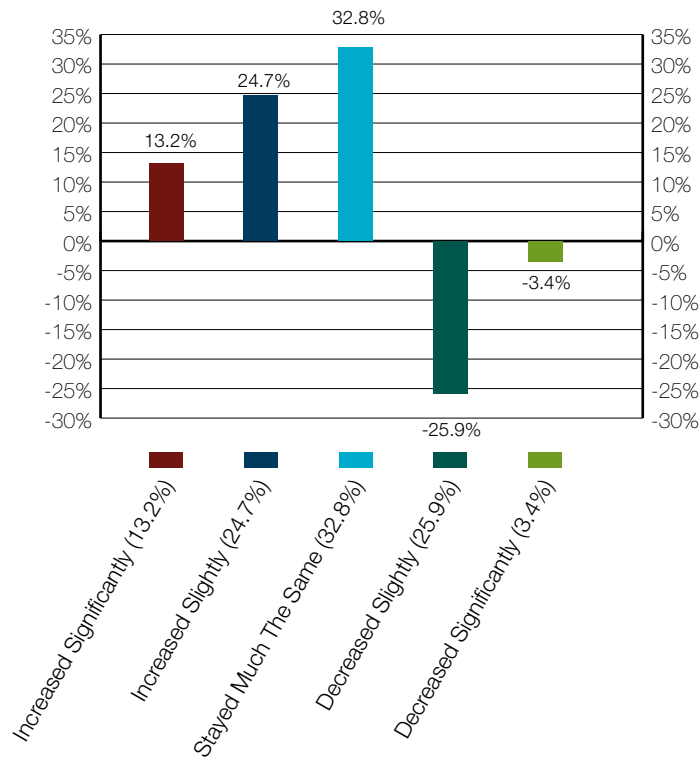


Profitability

The pressure on profit margins seems to have eased slightly in 2010. Whilst 38% of respondents report increased margins (down 3% on 2009), a further 33% (up 8%) indicate that profit margins have been maintained.

This trend was reflected in the number of respondents reporting reduced margins, which fell from 34% in 2009 to 29%.

These results seem independent of company size.



Geographic Markets

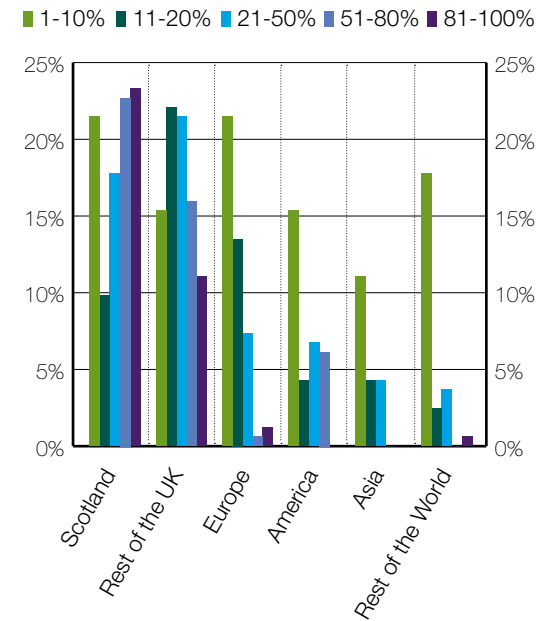
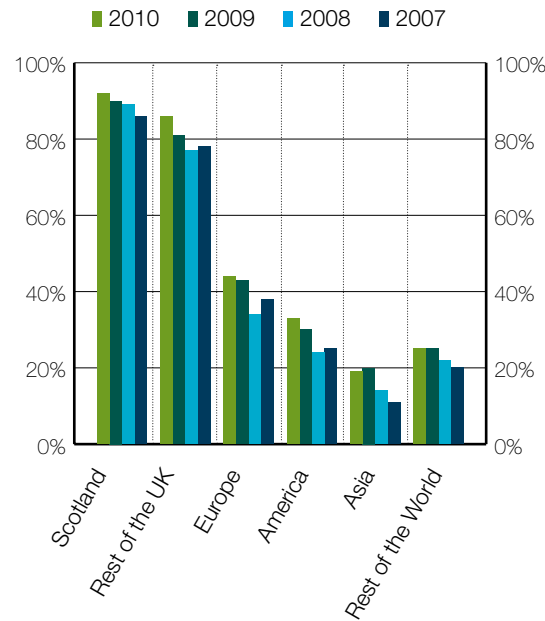
The Scottish ICT industry has traditionally serviced a wide range of geographic markets, but with a heavy reliance on the home markets in Scotland and the rest of the UK. However exports have been gradually increasing with a steady expansion into overseas markets.

The graph below shows data for the last four years, indicating a continuing trend to move into export markets.

Over 80% of respondents have some business in the rest of the UK – the first “export” market for many.

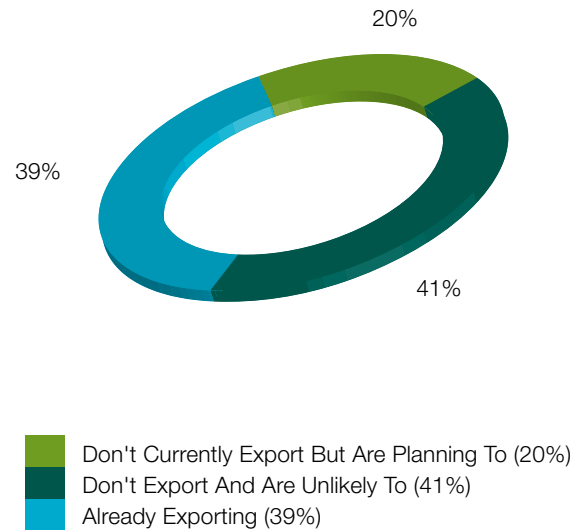
Europe is an increasingly important market with over 40% of respondents having some European sales. 30% of respondents sell to the United States. There is a strong correlation between these figures, with 70% of companies reporting European sales also selling to the US.

The left hand graph below shows the year on year growth in export markets; the graph on the right shows the spread of geographic markets respondents supply, and the percentage of their business these markets account for in 2010.



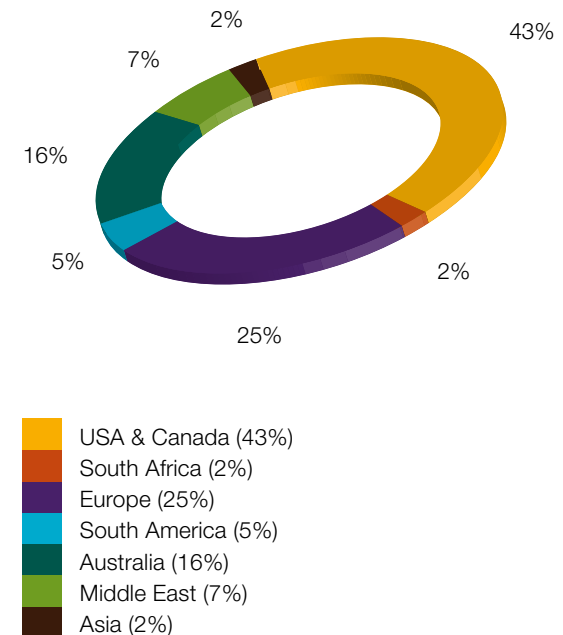
International Aspirations

With the increasing economic focus on export markets we asked respondents to indicate whether they currently sell overseas, or are considering doing so. Of the 60% of businesses who are not currently exporting one in three are planning to do so.



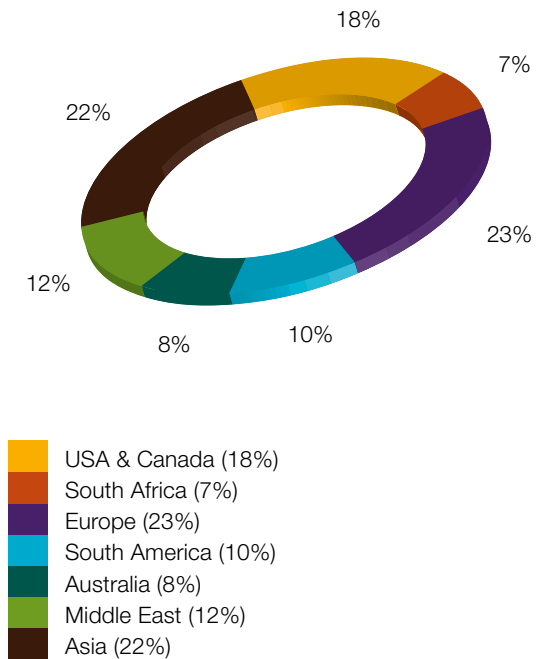
Prospective Markets for New Exporters

We asked respondents who are considering international markets which geographies they are looking at. Responses indicated a wide range of prospective geographies as shown in the graph below, with the US market dominating (43%), followed by Europe (25%) and Australia (16%). Asia with its enormous emerging markets trails in at merely 2%, which suggests that those new to exporting are cautious about their ability to access Asian markets.



Prospective Markets for Existing Exporters

Companies already exporting were asked to indicate new geographies they hope to break into. Again a wide range was indicated as shown in the graph opposite. 23% see Europe as offering considerable potential and 22% indicated Asia as a target market, suggesting experienced exporters are less concerned about the issues of selling to Asia.



Don't ignore the growing market opportunities in the US and BRIC economies.

David Cairns, Executive Chair, Prismtech

Be flexible and adaptive to change, look across border to seize opportunities to counteract challenging market conditions at home, productise where possible!

Callum Sinclair, Legal Director, DLA Piper

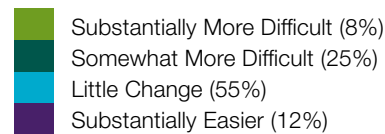
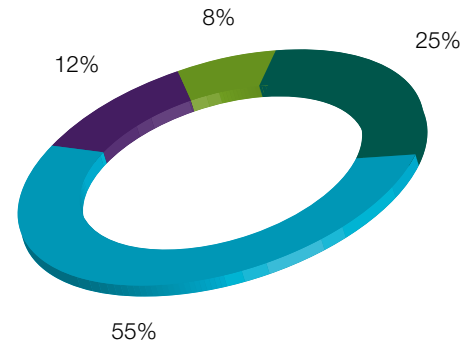
Financial Environment

With a continuing shortage of working capital facilities available from the retail banks, we asked respondents to share the impact on cash and sources of finance. The industry seems to be able to finance 'business as usual' from operations, but those seeking start up or expansion finance report mixed experiences.

Cashflow

With cashflow challenges being reported by many industries over the last couple of years, we asked respondents how cashflow had been impacted in 2010.

Responses are very much in line with 2009, with the breakdown between the various categories remaining fairly steady.

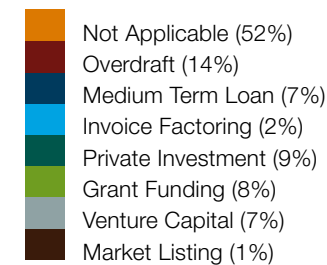
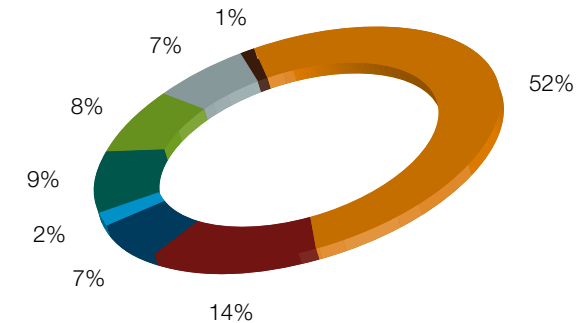


Sources of Additional Finance

Respondents were asked how they would source additional finance during 2011. Just over half (52%) indicated they don't anticipate the need for additional facilities, up from 47% in 2010.

Of those that might look for further finance, 21% indicated they would seek retail bank funding; (overdraft facilities (14%) and medium term loans (7%)).

A further 16% would chose either private investment (9%) or venture capital (7%). This compares with 23% in 2010.

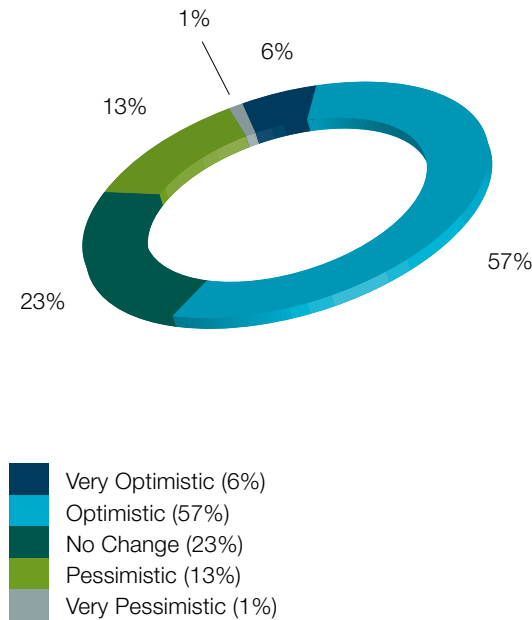


Looking Forward to 2011

The survey results highlight the industry has firm growth targets for 2011, but these are tempered by a recognition of the uncertain economic conditions in many markets.

Outlook for 2011

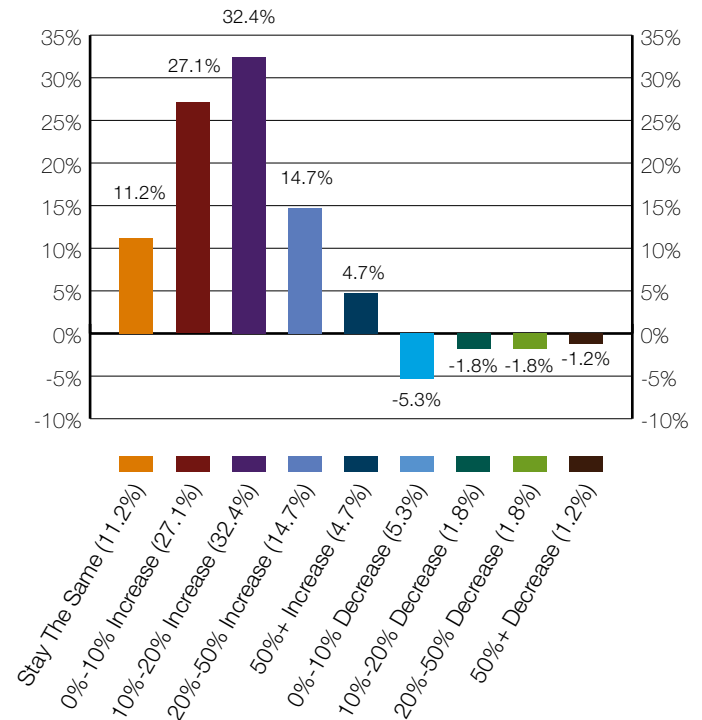
We asked respondents to share their views on the outlook for 2011. 63% indicated they are optimistic or very optimistic, down 9% from last year's figure of 72%, which could suggest a more pragmatic approach to growth is being taken by the industry. This is reinforced by 23% indicating no change (up from 17% in 2010) and a slight increase in the numbers who are pessimistic, up from 10% to 14%, perhaps underlining the uncertainty of the year ahead.



Projected Sales

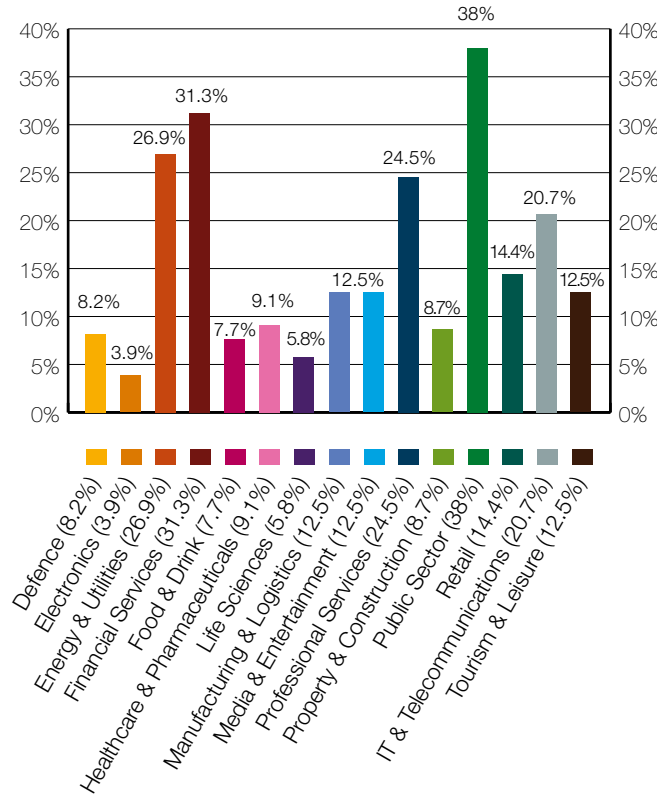
Respondents continue to demonstrate an appetite for growth in 2011, with a total of 79% indicating they expect to build additional sales during the year.

Breaking this down by company size smaller companies (up to 200 employees) expect to be able to increase sales by 10 - 20% on average, whilst very large companies (over 500 employees) anticipate growth will be in single figures.



Main Markets

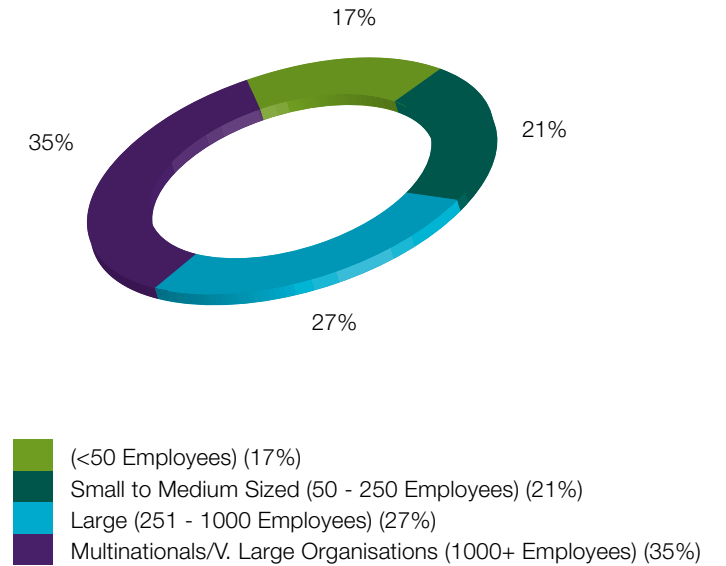
The spread of end markets served by the industry is very broad as illustrated in the graph opposite. Energy & Utilities, Financial Services, IT & Telecoms, Professional Services and the Public Sector are key markets for the industry, with each supplied by more than 25% of respondents.



Customer Profile

Respondents were also asked to indicate the profile of their customers by size. Nearly two thirds of respondents are supplying the enterprise market with only 17% supplying very small companies (ie less than fifty employees)

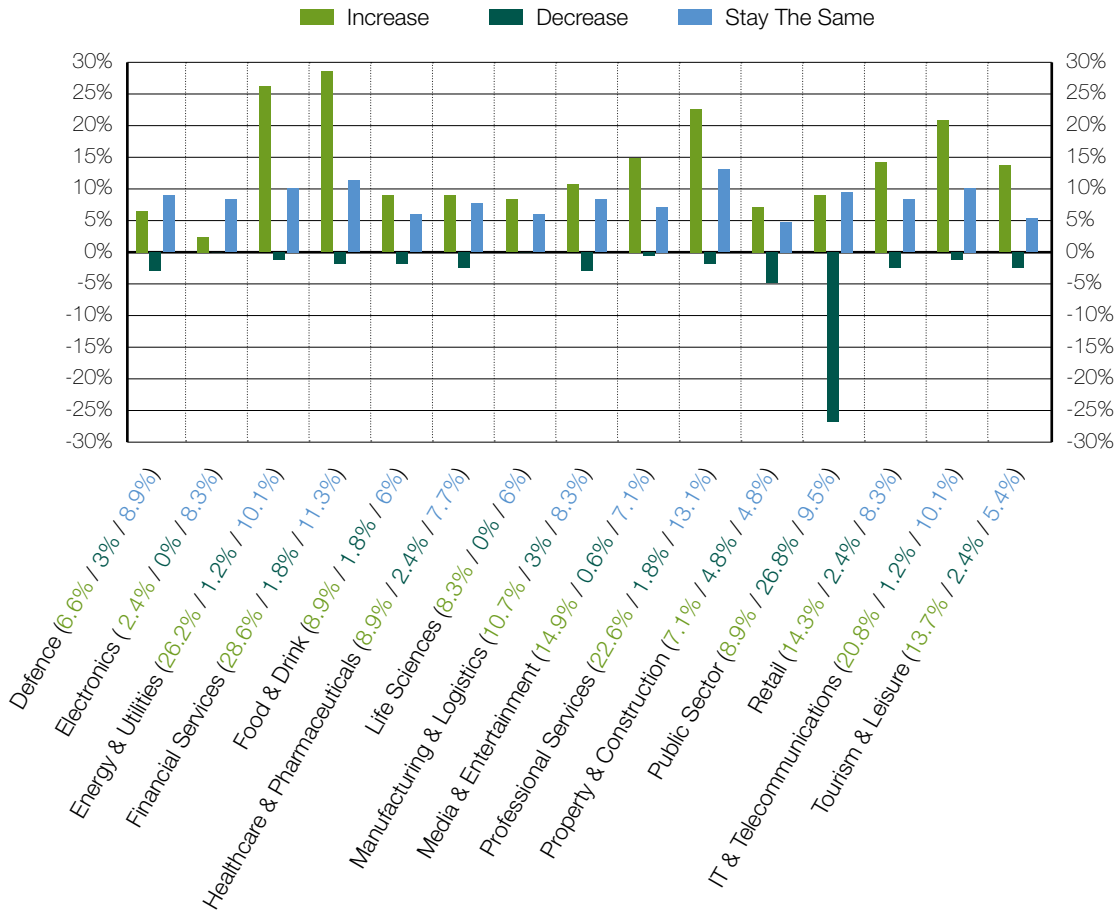
The number of respondents supplying very large companies has increased from 29% in 2010 to 35% this year.



Market Trends

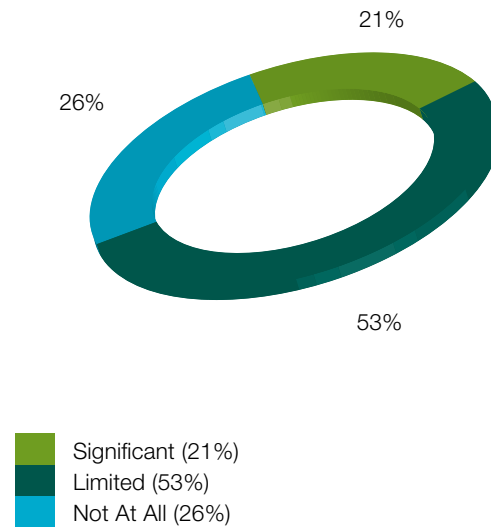
Whilst the key markets of Energy & Utilities, Financial Services, IT & Telecoms, and Professional Services are generally expected to increase in value during 2011, many respondents expect demand in other markets to stay much the same as last year. Unsurprisingly, the public sector market is forecast to experience significant reduced demand during 2011.

The continued recovery of the Financial Services industry is underlined by the growth expected this year. 39% of respondents report financial services as one of their main markets; three quarters of these are expecting demand from the financial services industry to increase.



Impact of Public Sector Cuts

In the light of planned cuts in public sector expenditure across the UK we asked respondents whether they expect these to affect their businesses. Nearly 45% of respondents do some business with the public sector. 21% recognise that the cuts will have a significant impact, with a further 53% indicating they expect the cuts will have a more limited impact.



Be brave to take the right decisions
that may be hard to support now but
will pay back in time.

Andrew Campbell

People and Skills

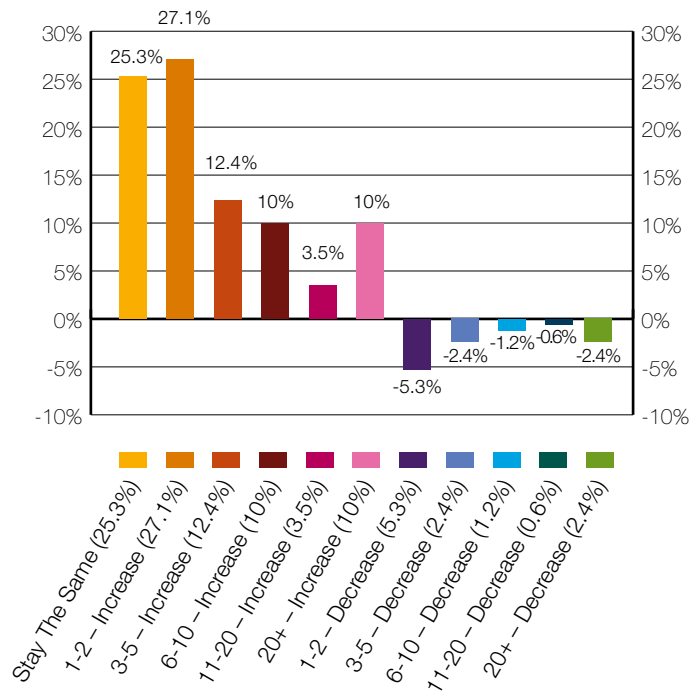
Respondents were asked for their views on employee numbers and how they would expect these to vary throughout the year, as well as which skill-sets they anticipated having the greatest demand for.

Encouragingly, like last year the majority of companies in the sector (63%) have indicated that they are expecting staff numbers to grow in 2011.

Changes to Employee Numbers

The sales growth forecast by respondents is reflected in the anticipated demand for additional staff. Whilst 25% expect to maintain current staffing levels, 63% expect to increase headcount.

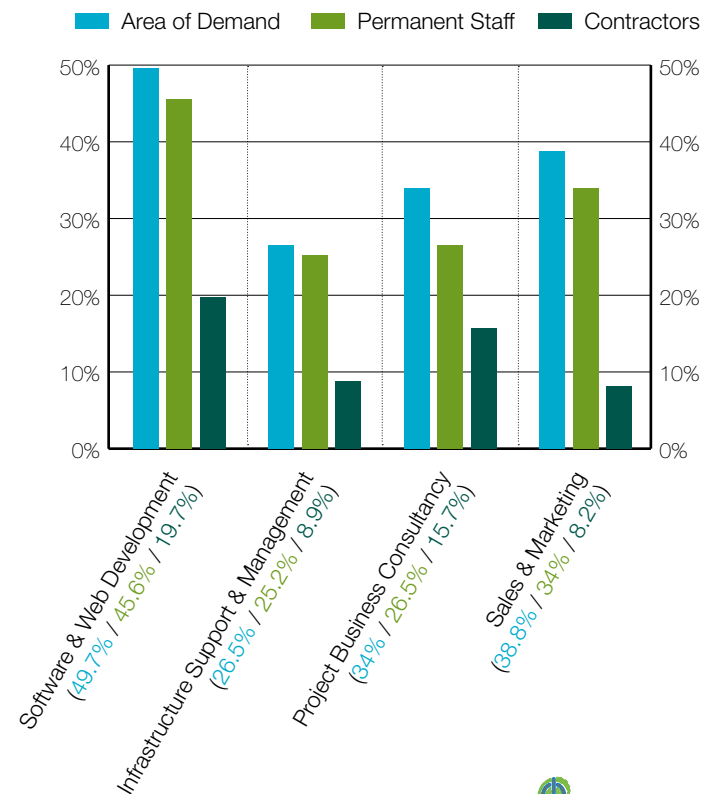
Nearly a quarter (23%) of respondents are planning to recruit more than 5 new members of staff. Encouragingly, one in ten companies are expecting to increase staff numbers by more than 20 during 2011, with half of these being larger, blue chip organisations.



Greatest Demand in 2011

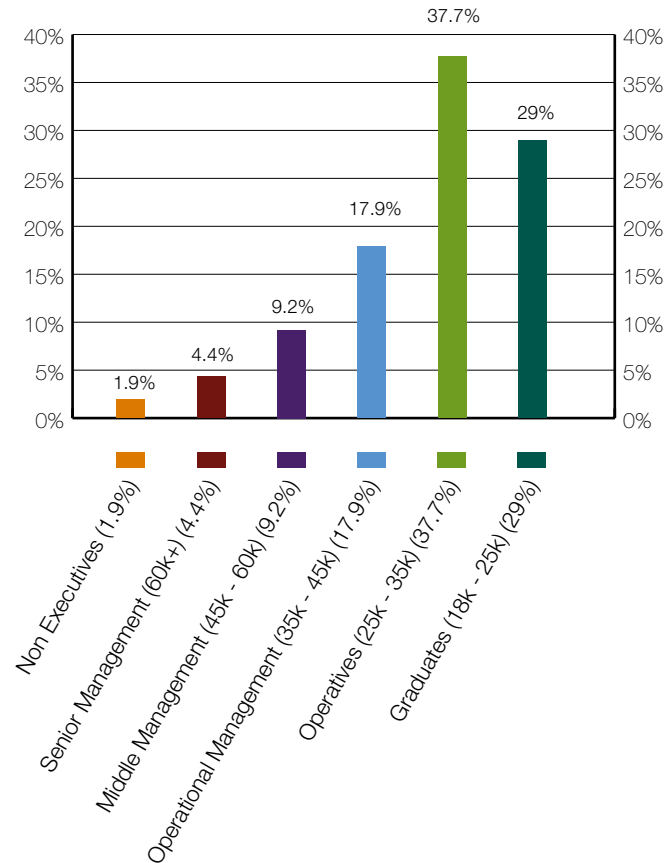
Companies indicated that Software & Web Development (50%) together with Sales & Marketing (39%) are the most in demand skill-sets.

Permanent employees rather than contractors are the preferred option for the majority of respondents. Permanent staff are particularly in demand for sales & marketing and infrastructure & support functions.; however, companies are more likely to use contract staff for software and web development, and project business consultancy roles.



The Level of Jobs in Demand

There is less of a focus on the Operatives skillsets (£25k - £35k) than last year (down from 45% to 38%) however this area continues to remain as the front runner, with graduates the second highest on the list. More promisingly we're starting to see more companies looking to fill positions at the middle management level.



Spread your net wide when looking for the best people.

Phil Murray, CEO, Petrotechnics

Specialise. It makes it easier to do a good job, train staff and earn referrals from happy customers.

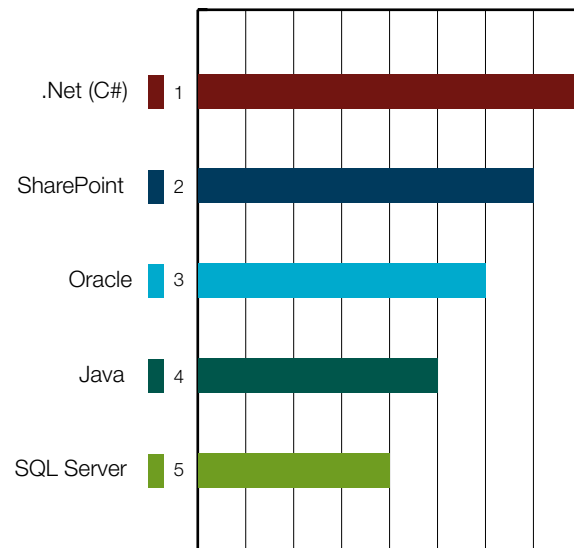
Mark Griffiths, MD, Codify

Stick to what you do best, differentiate from the rest and employ good people.

Martin Mutch, CEO, Rocela

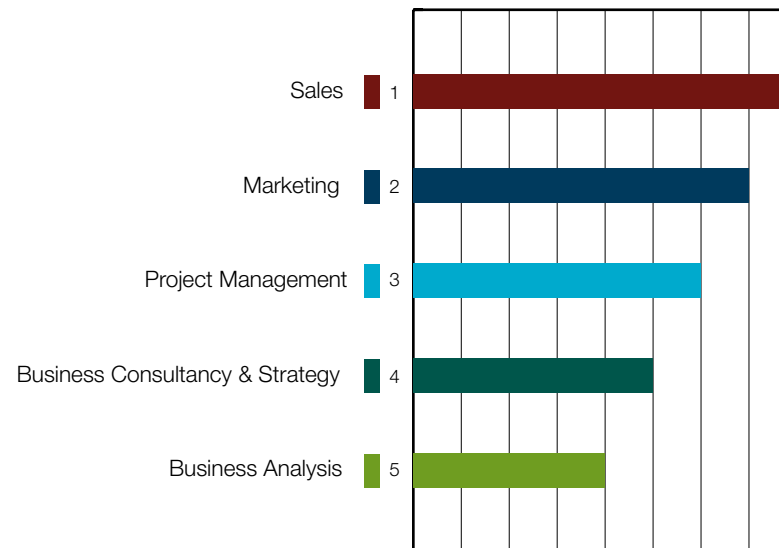
Top Technical Skills

.Net (C#) is the clear leader this year in the demand for technical skills. Notable changes include SharePoint moving from the 5th position to the 2nd, and Oracle which did not appear in last year's top 5, advancing to 3rd place. It's interesting to note that last year's leader, 'Web2.0 Marketing' is nowhere to be seen in this year's top 5.



Top Commercial Skills

Whilst in the past there has been a stronger emphasis on defining the separate elements of the sales lifecycle, this year respondents have reverted to core sales and marketing skills with 29% projecting these to be the most in demand. Interestingly, Business Consultancy and Strategy has appeared in the top 5 for the first time with an increase also evident in the demand for Project Management and Business Analysis skillsets.



Employment and Skills Commentary

In this, our 6th year of supporting the Scottish Technology Industry Survey it's great to see the sector is continuing with an upward, albeit conservative growth pattern for 2011.

Top sectors to look out for

Whilst showing signs of returning to the spotlight in 2010, Financial Services has now firmly regained its position as the top sector for new business opportunities amongst Scotland's technology companies. Oil and gas, another winner in the last few years also continues to provide a clear continued opportunity in 2011. A strong agile approach to be able to adapt to market conditions seems to be essential in dealing with the challenges of public sector cuts, with 54% of respondents indicating that they don't expect the cuts to have an impact on their business.

Demand returns for senior posts

It is good to see an increase in the importance of middle management, evident amongst survey participants. The surge in demand for Project Management and Business Analysis roles indicates the industry is benefiting from renewed investment, with new projects coming online. This in turn will create further activity in the operative and graduate markets. Encouragingly Software and Web Development is expected to be the biggest area of interest, continuing Scotland's historic reputation for innovation.

It is evident that companies who have recently been reacting to individual positions on an ad hoc basis are now planning their resource management on a 3-6 month timeframe which is a positive step forward, reflecting the confidence of Scotland's technology decision makers. Recent announcements of significant new jobs from a number of industry players is very encouraging.

Appetite for .Net continues to surge

.Net appears to be the framework of choice amongst the Scottish market, as it once again appears as the top runner for the most in-demand skill. Other notable changes include SharePoint which jumped from its position of five last year to its new position at number two and Oracle which didn't even appear in last year's top five moving straight into number three.

Wendy McDougall

Managing Director

9-20 recruitment

Technology Industry Viewpoint

Scotland's digital technology industries are a vital element of the Scottish economy, adding more than £4bn in GVA annually.

It is therefore great to see a continued appetite for growth amongst respondents to this year's Scottish Technology Industry Survey.

Challenging times

The last few years have provided a complex operating environment for most industries. Scottish digital technology businesses, including the software, telecoms and IT services sectors, have been able to combine careful cost control and continued service delivery, to maintain market share, and grow sales over this period.

2010: Reflections

For 2010 over half of our respondents report an increase in sales from the previous year, with a further 20% maintaining sales at 2009 levels. On the other hand one in four reported a drop in sales, underlining just how difficult trading can be.

Members report longer sales cycles, slower decision making and postponements of some projects within a number of end markets, all of which contribute to business uncertainty.

A positive outlook

Looking forward, the economy in 2011 looks no less challenging with continuing uncertainty in a number of markets and conflicting economic indicators. Respondents to the survey appear realistic about these factors, but nonetheless most companies are still confident they can achieve further growth during the year.

This steady year on year growth is beginning to have an impact. Whilst many respondents are small and medium sized businesses (SME's), we are seeing the emergence of a group of larger sme's, many of whom are extending their markets overseas, and taking advantage of international opportunities.

Going International

For the first time this year we asked respondents whether they are selling overseas, and if so which international markets they sell in. Many of the companies surveyed are already exporting to a broad range of countries with Europe, followed by the US, ranking first and second in terms of international sales.

Many other companies are looking to enter export markets, taking advantage of the opportunities global markets provide. The United States is the most attractive export market for most new entrants, with Europe a close second.

Unsurprisingly, companies who already have a successful track record in trading internationally, are confident of their ability to open up new markets, and see Europe and Asia as offering the greatest potential.

Conclusion

Overall, this year's survey indicates quiet optimism across the industry, and a continued focus on growth.

Polly Purvis
Executive Director
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