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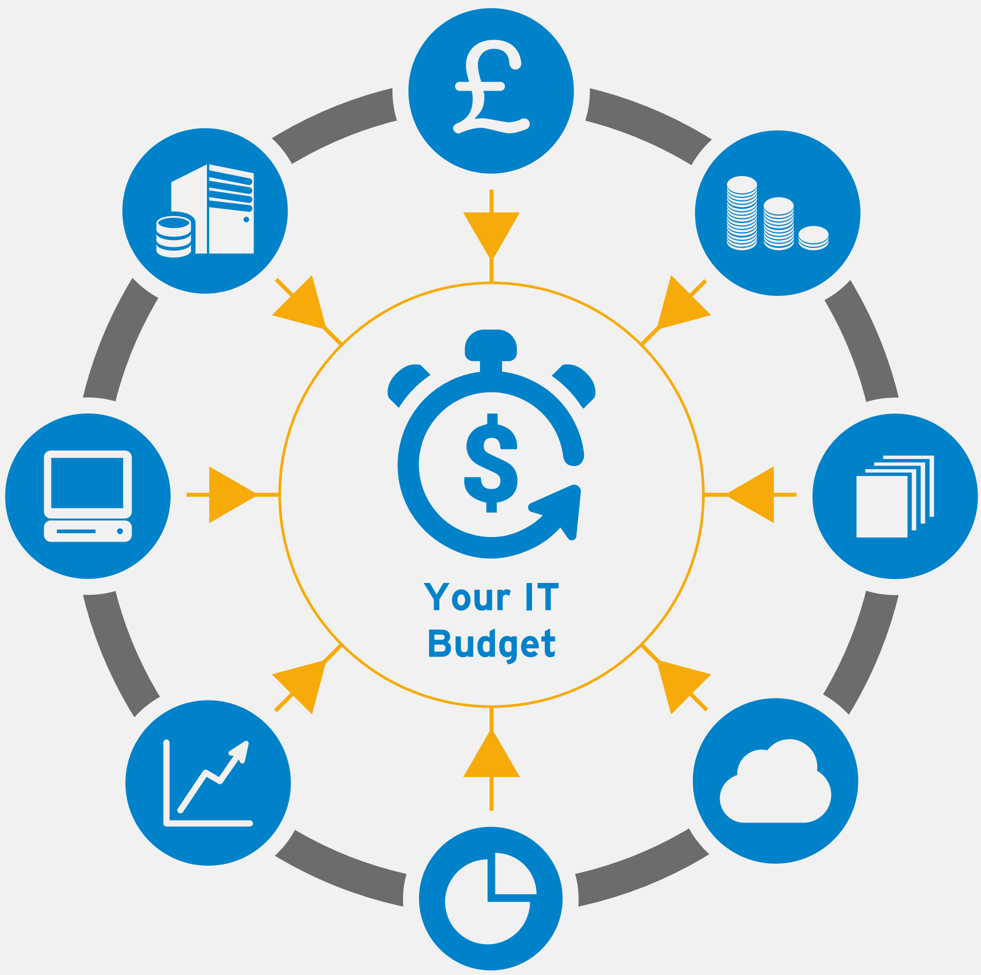
The SmartGuide to...
Choosing between CapEx and OpEx for IT budgets

Developing an efficient IT budget

IT investments are large, expensive and critical to how a business operates and remains productive. So what is the best way to pay for them and get the most value out of your investment? This guide investigates some of the models available and their pro's and con's.



IT Capital Expenditure (CapEx)

The CapEx model is the traditional and conventional method for purchasing IT hardware and infrastructure, allowing your business to depreciate the cost of the investment over the life-span of the hardware. By combining this with leasing and hire purchase options, you can make large hardware investments without severely impacting that year's balance sheet.

There are also tax benefits for businesses looking to invest capital expenditure in areas such as IT systems. The Annual Investment Allowance (AIA) is a type of capital allowance, which offers tax relief at 100 per cent on qualifying expenditure in the year of purchase. In the 2014 Budget, the maximum businesses can deduct from taxable profits is set at £500,000. This pro-rates for short or long periods, and also for periods that span the operative dates and rates of allowance. The AIA allowance presents a good opportunity for businesses looking to make any IT investment as tax efficient as possible.

The CapEx model may look cheaper, but the overhead costs associated with IT infrastructure can be static, determined at specification and are not always flexible. Hardware, power, cooling and floor space are all examples of costs that need to be specified in advance and cannot be quickly or easily altered. For many businesses the costs and complexity of planning, designing, building and running 'in-house' infrastructure is making outright ownership increasingly untenable, resulting in full or partial outsourcing.

Some businesses are capital constrained, they simply don't have the ability to invest in IT assets. For these companies it makes sense to utilise options such as leasing or cloud solutions that can convert a given investment into an operating expense. In the pursuit of maintaining a lean balance sheet with optimum cash flow, some boards are holding back on new CapEx investments, opting wherever possible to fund projects through an OpEx expenditure instead.

> "Infrastructure-as-a-Service (IaaS) shifts the spending for many IT workloads from CapEx to OpEx.... (it) represents an industrialised offering that provides computing resources on an as-needed basis at a very low price."
>
> Forrester report - 'Sizing the Cloud'

IT Operational Expenditure (OpEx)

Infrastructure-as-a-Service (IaaS) is becoming popular with businesses looking for agile budgets, due to its higher levels of utilisation and a highly standardised infrastructure management process. Essentially your business is able to pay in line with its current IT consumption levels, rather than investing in its own infrastructure that needs to maintain spare capacity earmarked for future growth.

As IT outsourcing solutions have become more popular and (IaaS) providers have matured, some businesses have moved to this model as they look to free up capital by converting large CapEx investments into monthly OpEx costs. The OpEx model is maturing to provide businesses with greater choice and flexibility for reducing data centre costs, mitigating risks, accommodating unforeseen change and gaining access to the capacity needed today, while retaining future flexibility.

By switching to an OpEx model, your business can remove itself from long-term commitments to IT infrastructure expenditure. The financial commitment to data centre resources then becomes the responsibility of your chosen supplier.

Moving to an OpEx model through an IaaS provider also introduces much greater flexibility and efficiency when it comes to the provision of new or additional resources. Other overheads also become the responsibility of the provider instead of your in-house IT department, such as licensing, upgrades, management of hardware suppliers and 24/7 staffing costs.

So what are the main candidates to move to an OpEx cost? An example might be something like a sales forecasting system or CRM system. Using a cloud-based Software-as-a-Service (SaaS) such as Salesforce is a monthly expense, and the service can be dropped anytime in favour of a competitor or in-sourcing your own sales forecasting system. Similarly, networking and desktop computers that you plan to refresh on regular intervals (e.g. every 3 years), because you can lease the equipment on-site as a monthly expenditure.

> “Cloud providers are able to lower server costs 75-80% vs. internal data centers
> UC Berkeley Cloud Computing Paper”

Flexibility is key

Every business should evaluate all options available to them when it comes to hardware investment, some may see the value in investing in hardware as an asset, others may want a pure operating cost that does not impact their available cash flow.

Using a Managed Services Provider (MSP) has become an attractive OpEx model for IT costs over the last decade because using such a supplier delivers on-demand IT infrastructure as a consumable resource to the business. This allows you to scale up and down very quickly and cost-effectively, delivering a lean IT budget that allows your business to be very agile and re-active to change.

The MSP model allows you to provision new, live, IT resources with a simple phone call, adding additional capacity and power within the hour and only ever paying for what is used. The overheads are carried by the MSP and your business benefits from IT resources that can shrink and grow directly with the demands and requirements of your business or your customers.

Which is best for your business?

It comes down to usage. If you choose to invest in your own privately owned IT infrastructure then on paper the total cost may appear lower than a comparable outsourced solution. But in reality your privately owned infrastructure will either be sized to cope with the next 5-10 years of growth, in which case it will be hugely under-utilised for the majority of its lifetime, or it will only be sized for your immediate requirement which will leave it too small to provide the flexibility and economy of scale that your business will need long term.

Ultimately its about finding the best fit for your unique business needs. The options are myriad and thanks to new cloud technologies and maturing service providers, your business has never been in a better position to get the most value out of its IT investments.

Contact us for advice on your IT budget

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