3 Keys to Business Cost Optimization Success

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By Analysts Srinath Sampath

Initiatives: Executive Leadership: Strategic Cost Optimization; IT Cost Optimization, Finance, Risk and Value

Despite overwhelming evidence that effective cost management supports enterprise performance, many organizations have not established consistent frameworks, cross-functional collaboration and clear measures of success. Executive leaders should use this research to increase their effectiveness.

Overview

Key Findings

- Effective cost management is achievable and correlates with positive business performance. Organizations that had effective cost management (defined as successful achievement of predefined targets) pre-COVID-19 are 1.4 times more likely to see their enterprise key performance indicators (KPIs) positively impacted in the face of the disruption caused by the global pandemic.

- Most organizations underperform on the three key success factors that drive effective cost management. Consistent use of cost frameworks across functions, clearly defined measures of success and cross-functional collaboration on cost management contribute to effective cost management.

- Consistent cost framework use remains important, but patchy. Organizations that use a cost management framework consistently across functions are less likely to report a budget cut/cost cut in response to the 2020 crisis, and more likely to achieve their cost management goals.

- Clear definition of success is important, but missing in most organizations. Organizations that define clear measures of success for their cost management initiatives are 2.6 times more likely to succeed at them. Only 48% of respondents say they define clear measures of cost management success. While 66% are using predetermined currency savings as a KPI, only 39% are able to achieve their targets.

- Cross-functional collaboration on cost optimization is sporadic. Functional silos are among the top hurdles facing cost management success. Inter-functional collaboration scores vary by function: Finance scores high marks, sales lags the most. Common-framework usage unsurprisingly correlates with high collaboration among functions. Enterprises with better cross-functional collaboration are 1.5
times more likely to report better performance across several enterprise performance areas through the crisis.

**Recommendations**

Executive leaders should build critical capabilities that enable cost optimization success by:

- Creating a shared understanding of cost-to-value relationships by harmonizing cost categorizations across the organization.
- Defining cost management success measures by establishing clear targets, cascaded consistently across the enterprise, whether in the form of savings goals, or better yet, increasing cost productivity/yield.
- Identifying and addressing areas of poor cross-functional collaboration by standardizing cost management frameworks across functions and creating a community of practice with cross-functional representation.

**Survey Objective**

Gartner surveyed more than 300 executives involved in enterprise-level cost management activities at organizations ranging from midsize to large enterprises in order to understand:

1. What they were doing to manage business costs precrisis, and whether or not they were succeeding at it
2. How they were managing business costs in response to the crisis
3. What their cost prognosis was for the near future as the world starts to look forward to the “new normal”

**Data Insights**

In 2020, organizations around the globe were tested on their cost management capabilities as revenue streams slowed or vanished for many. Some reacted by slashing costs across the board while others were more strategic about where to cut. The unprecedented crisis made many organizations change their approach to cost management — shifting between cost cutting, optimizing for spend and optimizing for value. Gartner's analysis found that the organizations that were effective at pre pandemic cost management were 1.4 times more likely to see positive business performance through the crisis (see Note 1, Figure 5). But what made them effective cost managers in the first place? Upon digging deeper into the data, we found that there were three key success factors that drove organizations to be successful at cost management, and that many organizations continue to underperform in these areas.

**Consistent Cost Framework Use Remains Important, but Patchy**
Cost management framework: A set of cost categorizations that are formally used in budgeting, target setting and reporting on costs.

Only 35% of organizations use the same cost management framework consistently across different functions (see Figure 1). Almost two-thirds of organizations either don’t use a cost management framework at all, or use multiple frameworks across different functional areas.

Figure 1: Usage of Cost Management Frameworks

Usage of Cost Management Frameworks

- 35% Yes, the entire organization used the same cost management framework consistently
- 57% Cost management frameworks used differed by functional areas
- 8% There was no framework used to manage costs

n = 312, all respondents, excluding not sure
Q: Prior to the COVID-19 pandemic, did your organization consistently use a framework for cost management?
Source: 2020 Gartner Business Cost Optimization Through a Crisis Study
744932_C

Larger organizations are more likely to use cost management frameworks consistently (see Note 1, Figure 6). Out of global enterprises (revenue of $5 billion or more), 46% say their entire organization used the same cost management framework consistently. This number goes down to 33% for large
enterprises (revenue in the range of $1 billion to less than $5 billion) and to 23% for midsize enterprises (revenue in the range of $250 million to less than $1 billion).

Organizations that used the same cost management framework consistently across functions were:

- More likely to experience stronger cross-functional collaboration on cost management
- Less likely to report a budget cut/cost cut in response to the COVID-19 pandemic
- More likely to achieve their cost management goals prepandemic

Based on these trends, using consistent frameworks across functions seems like a significant driver of cost management success, yet only 35% of the surveyed organizations do it. This should serve as a wakeup call for the rest.

Recommendations:

- Create a shared understanding of cost-to-value relationships by harmonizing cost categorizations across the organization.
- Evaluate initiatives based on a systematic approach that weighs several factors such as potential benefit, customer impact and degree of organizational risk.
- Determine the extent to which business leadership is committed to supporting identified cost optimization initiatives.
- Execute on the stated cost optimization efforts by delivering the results and communicating the efficiency outlined in the initiative's business case.
- Engage peers and budget analysts in the process of identifying and prioritizing cost optimization initiatives.

Recommended research:

- Prioritize Your Cost Optimization Initiatives Using Gartner's Decision Framework
- Use Gartner's IT Finance Frameworks to Drive Successful IT Finance, Value and Cost Programs

Clear Definition of Cost Management Success Is Important, but Missing in Most Organizations

It's hard for organizations to know they've succeeded at their cost management initiatives unless they set some measurable goals. Yet, only 48% of the respondents strongly agree that they had clear measures in place to track the success of their cost management initiatives (see Figure 2).
Figure 2: More Than Half Don’t Have Clear Measures of Success Assigned to Their Cost Management Initiatives

**More Than Half Don’t Have Clear Measures of Success Assigned to Their Cost Management Initiatives**
Percentage of Respondents Who Had Defined, Clear Measures of Cost Management Success

![Graph showing percentage of respondents with clear measures of success](image)

n = 314

Q: Thinking about your organization’s cost management initiatives prior to the COVID-19 pandemic, to what extent do you agree or disagree with “We had clear measures put in place to measure the success of our cost management initiatives”?

Source: 2020 Gartner Business Cost Optimization Through a Crisis Study 744932_C

That slim minority, however, was 2.6 times more likely to succeed at cost management compared to those who didn’t have clear measures of success in place. In terms of metrics actually used, the most popular measure of success (at 66%) was considering the achievement of specific currency saving targets (for example, cutting $1.5 million in costs over a six-month period) as a win. Yet, even by that standard, only 39% say they were successful (see Figure 3). That rate of success is lower still for other measures of success used. Yet, the popularity of the “cost cutting” metric is also a symptom of how organizations often pursue cost reduction to the detriment of business performance optimization.
Figure 3. Metrics Used to Assess Cost Management Success

Other interesting data point to consider:

- Organizations that consider the sustainability of cost improvements as part of evaluating success were more likely to anticipate cost increases (instead of decreases) over the next 12 months.

Recommendation:

- Move beyond rudimentary cost-to-revenue and raw cost-savings metrics to track metrics such as operating leverage that tell you the value of cost management initiatives.

Recommended research:

- Measuring IT’s Yield to Balance IT Cost Optimization: The Gartner Cost Value Matrix
Cross-Functional Collaboration Is Sporadic and Messy

Functional silos that create misaligned incentives toward cost management were quoted among the top three challenges, preventing the achievement of cost management goals pre-COVID-19 (see Note 1, Figure 7). Since our respondent population included representatives of different functional areas, we asked them about their perceptions of their collaboration on cost management with other peer functions. Figure 4 highlights the large variance in those perceptions across various functional pairings.

**Figure 4: Cross-Functional Cost Management Collaboration Matrix**

### Cross-Functional Cost Management Collaboration Matrix

Percentage of Respondents Rating Their Cost Management Collaboration as High

<table>
<thead>
<tr>
<th>A's perception of collaboration with B</th>
<th>Finance n = 39</th>
<th>Supply Chain n = 36</th>
<th>IT n = 40</th>
<th>Customer Service n = 32</th>
<th>Marketing n = 40</th>
<th>Sales n = 37</th>
<th>Human Resources n = 40</th>
<th>Operational Roles n = 40</th>
</tr>
</thead>
<tbody>
<tr>
<td>Finance</td>
<td>69%</td>
<td>83%</td>
<td>81%</td>
<td>65%</td>
<td>65%</td>
<td>78%</td>
<td>74%</td>
<td>0%</td>
</tr>
<tr>
<td>Supply Chain</td>
<td>55%</td>
<td>-</td>
<td>58%</td>
<td>42%</td>
<td>54%</td>
<td>54%</td>
<td>46%</td>
<td>55%</td>
</tr>
<tr>
<td>IT</td>
<td>51%</td>
<td>42%</td>
<td>-</td>
<td>68%</td>
<td>48%</td>
<td>30%</td>
<td>68%</td>
<td>55%</td>
</tr>
<tr>
<td>Customer Service</td>
<td>50%</td>
<td>31%</td>
<td>62%</td>
<td>48%</td>
<td>44%</td>
<td>44%</td>
<td>56%</td>
<td>56%</td>
</tr>
<tr>
<td>Marketing</td>
<td>47%</td>
<td>31%</td>
<td>55%</td>
<td>32%</td>
<td>-</td>
<td>58%</td>
<td>38%</td>
<td>40%</td>
</tr>
<tr>
<td>Sales</td>
<td>43%</td>
<td>33%</td>
<td>53%</td>
<td>43%</td>
<td>54%</td>
<td>-</td>
<td>32%</td>
<td>38%</td>
</tr>
<tr>
<td>Human Resources</td>
<td>50%</td>
<td>42%</td>
<td>60%</td>
<td>50%</td>
<td>45%</td>
<td>54%</td>
<td>-</td>
<td>50%</td>
</tr>
<tr>
<td>Operational Roles</td>
<td>67%</td>
<td>75%</td>
<td>66%</td>
<td>59%</td>
<td>51%</td>
<td>41%</td>
<td>65%</td>
<td>-</td>
</tr>
</tbody>
</table>

n varies, excluding not sure

Q: How would you rate the level of alignment and collaboration between your function and each of the following functions in support of cost management?

Source: 2020 Gartner Cost Optimization Through a Crisis Study 744932_C

On aggregate, finance functions enjoy a favorable perception in the minds of their peer cost management executives. Sales and marketing functions share the dubious distinction of being perceived as the worst cost management collaborators. Organizations must drill deeper to understand which functions absolutely must collaborate and make sure those collaborations are shaping up smoothly. For example, supply chain and human resources need a better relationship if the former manages temporary labor contracts. Temporary labor can be a huge source of cost, but they’re not always under the ambit of HR. Similarly for marketing and supply chain, given how much of marketing spend is on outside agencies, you would want to see supply chain really leaning in to help with good procurement practices.
Other interesting data points to consider:

- Organizations that use a common cost management framework consistently across functions are more likely to experience higher cross-functional collaboration scores.
- Enterprises with better cross-functional collaboration were 1.5 times more likely to report better performance on indicators of enterprise performance through the crisis.

Recommendations:

- Identify the key cost management issues within your organization that depend on effective cross-functional collaboration.
- Assess the interfunctional collaboration strengths and weaknesses.
- Design a plan moving forward to improve the interfunctional collaboration where necessary.
- Create a community of practice with cross-functional representation around cost optimization strategies.
- Standardize the cost management frameworks used across different business functions.

Recommended research:

- How Important Are Cross-Functional Cost Optimization Teams for Business?
- CIOs Should Prepare Now for Financial Discussions With CFOs and C-Suite

Additional Research Contribution

Cristina Gomez, Piers Hudson, Geraint John, Angela Kreiter, Bryan Kurey, Ewan McIntyre, Randeep Rathindran and Sanil Solanki

Evidence

The 2020 Gartner Business Cost Optimization Through a Crisis Study was conducted to understand how organizations’ cost management practices before and during the COVID-19 crisis allowed them to be ready for the rebuilding phase into the “new normal.”

The research was conducted online between August and October 2020 among 314 respondents from North America, Europe and APAC, across all industries except government, and in organizations with annual revenue of at least $250 million.

Respondents were screened for involvement in enterprise wide cost management in their organization. The study was developed collaboratively by Gartner analysts and the Primary Research Team.
Disclaimer: Results of this study do not represent global findings or the market as a whole but reflect sentiment of the respondents and companies surveyed.

Note 1: Additional Survey Findings

Figure 5: Likelihood of Achieving Positive Impact on Enterprise Business Performance Areas

Likelihood of Achieving Positive Impact on Enterprise Business Performance Areas

Other drivers include:
- Utilizing reserve budget to avoid making cuts to high-value functions
- Collaboration between functions in support of cost management

Barriers
- Function-level cost/-budget cuts in response to COVID-19

n = 313; all respondents, excluding not sure
Base: Results of driver analysis on achieving top quartile scores on the 0-100 index outcome variable, based on the following question
Q: In the following performance areas, how would you assess the impact of COVID-19 on your enterprise?
Source: Gartner 2020 Business Cost Optimization Through a Crisis 744932_C
Larger Enterprises More Likely to Use Same Cost Management Framework Consistently

Usage of Framework for Cost Management

- Midsize Enterprise ($250M to <$1B) (n = 62): 19%
  - 23%: There was no framework used to manage costs
  - 58%: Cost management frameworks used differed by functional areas
  - 19%: Yes, the entire organization used the same cost management framework consistently

- Large Enterprise ($1B to <$5B) (n = 153): 7%
  - 33%: There was no framework used to manage costs
  - 60%: Cost management frameworks used differed by functional areas
  - 7%: Yes, the entire organization used the same cost management framework consistently

- Global Enterprise ($5B+) (n = 97): 3%
  - 46%: There was no framework used to manage costs
  - 51%: Cost management frameworks used differed by functional areas
  - 3%: Yes, the entire organization used the same cost management framework consistently

n = 312; all respondents, excluding not

Q: Prior to the COVID-19 pandemic, did your organization consistently use a framework for cost management?

Source: Gartner 2020 Gartner Business Cost Optimization Through a Crisis

744932_C
Figure 7: Functional Silos Among Top Hurdles for Cost Management Success

Functional Silos Among Top Hurdles for Cost Management Success

- Growth Takes Priority Over Cost Management: 36%
- Functional Siloes Create Misaligned Incentives: 34%
- Short-Termism in Cost Management Initiatives: 34%
- Business Complexity Drives Up High Costs: 33%
- Market Conditions Prevent Competitive Pricing From Suppliers: 31%
- Lack of Data Quality and Granularity: 30%
- Perceived Risk to Quality, Service or Growth: 26%
- Allegiance to Periodic Uniform Budget Reductions: 19%
- Regulations and Other Legal Constraints: 19%
- Limited Current Capabilities for Adoption of New Operating Models: 18%
- Insufficiency of Resources: 17%
- Other: 1%
- None of the Above: 0.3%

n = 314; all respondents
Q: What were your company's top three challenges associated with achieving cost management goals (before the COVID-19 pandemic)?
Source: Gartner 2020 Gartner Business Cost Optimization Through a Crisis 744932_C

Recommended by the Author

- Manage Risk in Crisis-Driven Decisions From Response Through to Recovery
- Use Gartner’s Business Value Model to Make Better Investment Decisions
- Tool: Cost-Saving Ideas to Optimize Your Spend Reduction Program
- 5 Rules for Sustainable Cost Optimization Across the Enterprise
- Sustaining Cost Efficiency Gains in the Postpandemic Era
- 7 Cost Optimization Errors You Cannot Afford to Make
- Create a Culture of Smart Spending
- How Sydney Water Drives Cost Savings Using a Value-Based Budgeting Model
- Improve Cost Insight Using Multimodel Budgeting
- Near-Term Budgeting Strategies in the COVID-19 Era