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10 Rules to Rapidly Reduce IT Spend

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In an uncertain and pressurized economic landscape, organizations often face the challenge of realizing immediate IT cost savings. This research features 10 short-term cost-cutting rules that can help CIOs achieve their targets and minimize the impacts on business operations.

Additional Perspectives

- Summary Translation: 10 Rules to Rapidly Reduce IT Spend (24 April 2024)

Overview

Key Findings

- In times of economic challenge, organizations often cut costs without a clear understanding of the potential consequences and risks associated with implementing savings targets within a pressured time frame.
- Most IT departments lack a formal approach in implementing rapid cost-cutting measures across their department.
- The risks of reactive cost cutting are often not well-defined, quantified or effectively communicated, leading to poor decision making. This can have unintended consequences in the longer term and drive potential disruptions.

Recommendations

CIOs seeking to rapidly cut their costs as part of their cost optimization approach should:

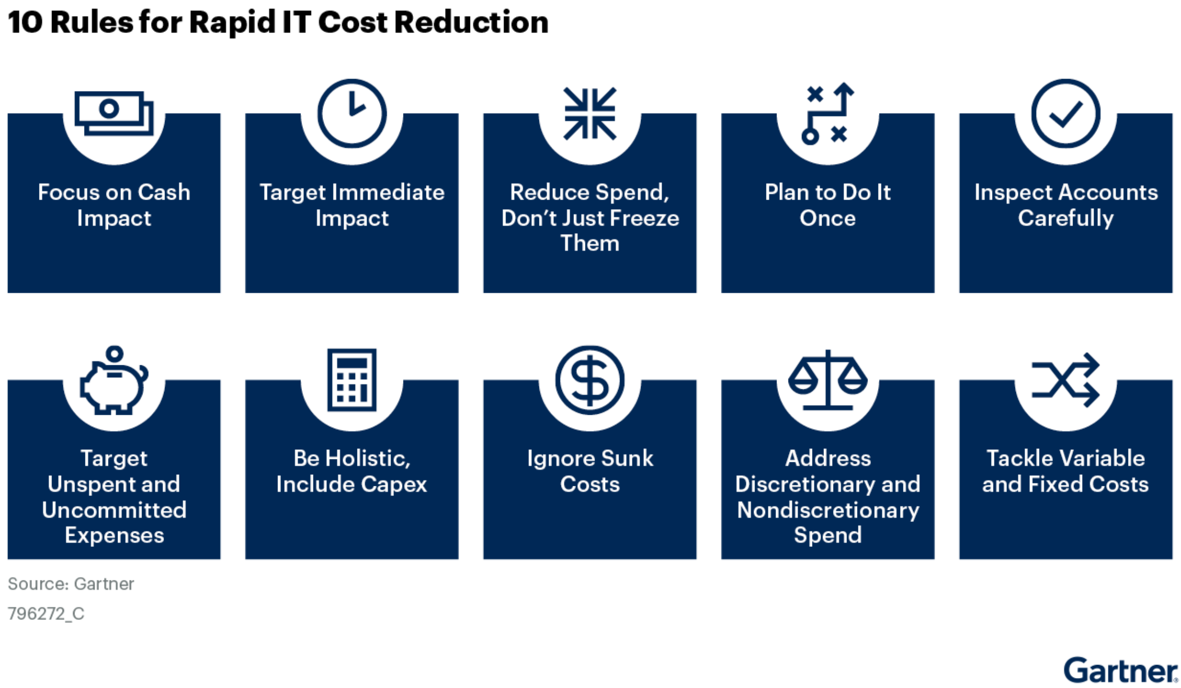
- Establish your cost reduction fundamentals by defining the specifics of the cost savings targets and the time frame for implementation.
- Apply Gartner's 10 rules of IT spend reduction to determine the types of actions, expenses and categories that will have the most immediate and/or largest impact.
- Map out plan to eliminate, reduce or suspend spend, and communicate it internally to IT, the business units (BUs) impacted and the CFO/CEO driving the reductions.
- Minimize the long-term disruptions of cost cutting by clearly defining and assessing the potential consequences and risks associated with cutting costs in relation to supported business outcomes.

Introduction

In uncertain economic environments like today, organizations face the challenge of achieving immediate IT cost savings. Business and market pressures often dictate that this takes place in a rapid or immediate fashion, requiring more of a "cost cutting" approach. Despite the urgency, Gartner recommends that organizations take a structured and programmatic approach to strategic cost management that includes an ongoing cost reduction discipline (see Executive Essentials: Develop a Strategic Approach to IT Cost Reduction, Optimization and Investment).

When faced with immediate or short-term pressures, CIOs still need to take a thoughtful approach to cutting costs, ensuring that they strive to mitigate the risks and minimize the long-term impact on the organization. Figure 1 lists the 10 rules of rapid spend reduction that can help CIOs to swiftly reduce IT spend while safeguarding performance in a dynamic business environment.

Figure 1: 10 Rules for Rapid IT Spend Reduction



Analysis

Establish the Cost Reduction Fundamentals

In facing the challenge of delivering immediate savings, it is key to establish and document precisely what the need is, such as the size, timing and type of reduction required. To answer this, it is critical to define the desired outcome, the required time frame to meet it and the approach.

The Outcome/Need

Work with finance leaders to define the outcome(s) that is required in terms of the annual, ongoing or budgetary savings in hard currency figures. These should be definitive cost targets or savings goals calling out the focus area, whether it is reducing operational expenses, minimizing overhead costs or meeting budget/forecast targets.

Timing

After determining the size of the savings required, focus on the time in which they need to be delivered. Emergency cost cutting will typically happen within weeks or months, often six months or less.

Time given to plan cost-cutting exercises is often dictated by time pressure. However, planning should be prioritized, as it will drive the strategy, approach and timing of execution. It will also crystalize the goals communicated to the teams to identify and deliver the savings, and avoid wasted time and effort throughout the execution of the exercise.

The Approach

The combination of the need and the time available to realize the cost reduction determines the approach. CIOs should determine and establish the enterprise's preparedness and willingness to "spend to save." Are there funds that can be invested to deliver significant savings? Is there time to achieve this? While spending to save or investing for growth are rarely options for rapid reduction outcomes, they should not be dismissed out of hand.

10 Rules for Rapid IT Cost Reduction

Following are the 10 rules for rapid IT cost reduction that can be used to assess your reduction options:

1. **Focus on Cash Impact —** Target those items that will have a real cash impact. Don't focus time and effort on noncash accounting treatments on the impacts of depreciation or amortization. Savings in SaaS or infrastructure as a service (IaaS) costs have a real cash impact, as opposed to reducing on-premises software licenses or owned assets like hardware. For owned assets, options for sale and lease-back can also realize real cash savings.

2. **Target Immediate Impact —** The more urgent the need to cut spending, the more urgent the need to focus on its immediate impact. Think here in terms of in-year impacts. Eliminate, reduce or suspend items that will impact in one, six or even nine months, not in years. Examples include expenses like SaaS costs incurred and paid monthly or quarterly on a pay-as-you-go basis, rather than annually. While you focus on immediate results, be mindful of the fact that cost-cutting a service in IT may show a reduction in IT's financial numbers, but may simply push the cost elsewhere in the organization if the business unit disagrees with the cut and reinstates or funds the service itself. In the long term, this could lead to an increase in shadow IT and badly managed IT costs (which will likely be brought to the CIO's attention in the near future).

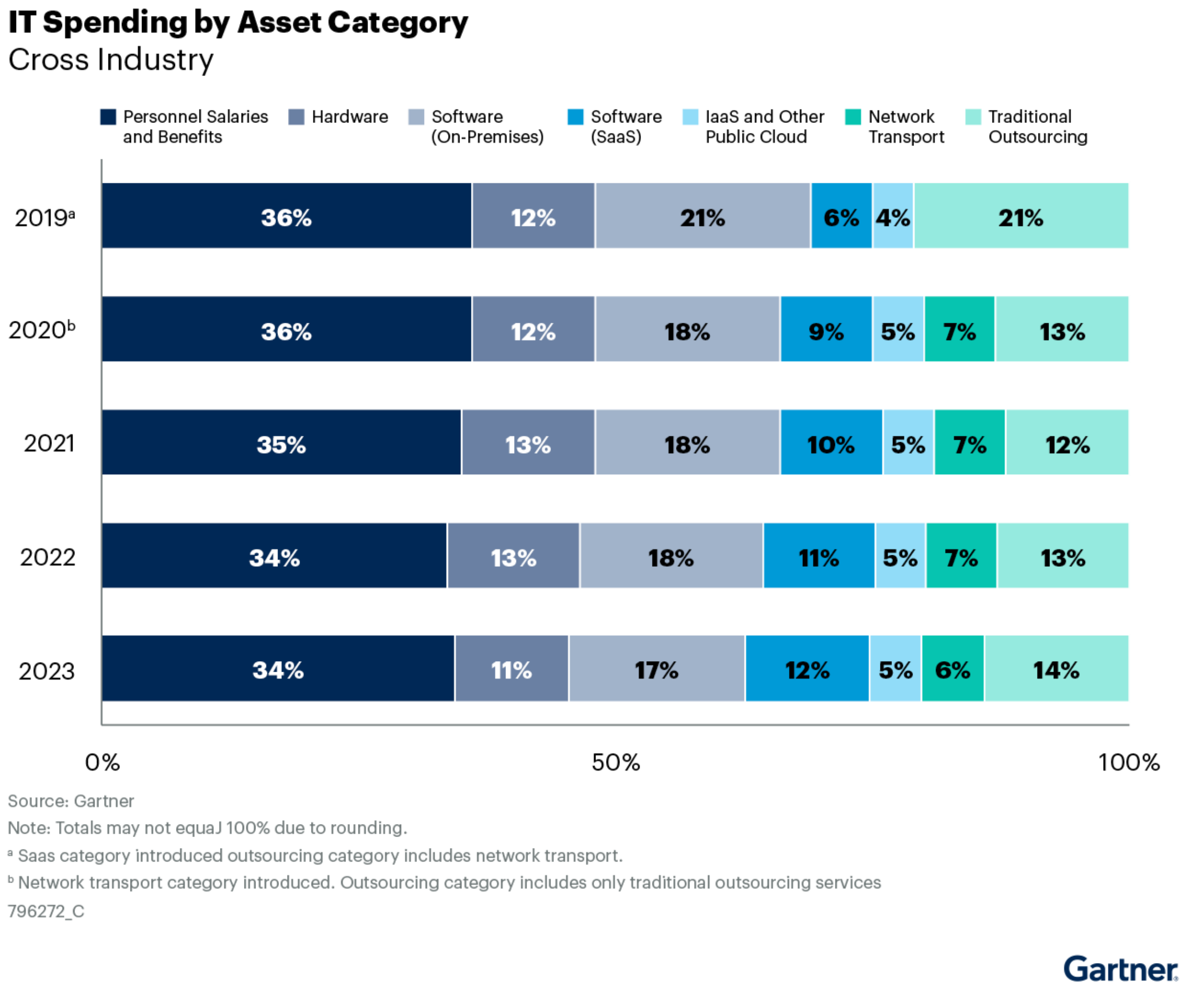
3. **Reduce Spend, Don't Just Freeze Them —** The focus here needs to be on costs that can be truly reduced or completely eliminated, not just frozen out for the current period, to reappear again down the line. While freezing costs can help with immediate cut-off of cash outflow, it might not address the underlying issues causing unnecessary spending.

4. **Plan to Do It Once —** Most organizations don't cut deep enough the first time, so they need to revisit and do it again. This creates a destructive and unproductive cycle of uncertainty, effort and lost productivity.

Don't assume that making small cuts across all IT functions is better than making one or two large reductions. Managing and communicating the risks and impacts of one or two significant changes is preferable to subjecting the IT function to a "death by a thousand cuts." Therefore, cut or reduce "hard" enough the first time, and only do it once. This is particularly relevant in IT personnel or staffing reductions (see Optimize Your IT Staffing Levels in 3 Steps), where cycles of ongoing reductions can be particularly dangerous due to their negative effect on morale, trust and brand.

5. **Inspect Accounts Carefully —** Define the cost base, both in terms of the profit and loss, and the balance sheet. Work with your IT finance or finance partner to obtain a holistic view of expense level detail, such as expense accounts and key balance sheet accounts, including expense accruals and prepayments. Use this view to identify specific cash reductions in operating expenditure (opex) and capital expenditure (capex) costs, which will immediately impact reported financials. Use Gartner's IT spend asset categorization (see IT Key Metrics Data 2024: Industry Measures — Cross-Industry Analysis) as a framework for obtaining this view (see Figure 2).

Figure 2: IT Spending by Asset Category



6. **Target Unspent and Uncommitted Expenses —** Look for unspent (or uncommitted) expenses to achieve rapid savings. Unless payments (or commitments) can be recovered, or prepayments returned, the most immediate impact will come from unspent or uncommitted payments. Evaluate contracts/commitments for renegotiation/termination clauses.

7. **Be Holistic, Include Capex —** Typically, opex is the first reduction to be sought, but capex, representing 22% [1] of the average IT budget, can also be reduced. Capex reduction can be achieved by either consolidating data center assets to reduce redundancy or by avoiding expensive hardware refresh by extending equipment life span. While capex reductions could lead to reduced opex spend, for example, by avoiding new license or support costs, on the flip side, support costs or licenses for current assets may need to be increased.

8. **Ignore Sunk Costs —** Past spend, or spend that has already been made, are "sunk costs." Sunk costs are irrelevant and should not influence your decisions about whether to continue or discontinue a project. While this holds true from a rapid-reduction standpoint, it's important to assess the gain from stopping future project payments relative to the potential benefit of completing the project.

"In-flight" projects can be stopped midway for rapid savings. However, CIOs need to be aware of the fact that, in some cases, the savings may be less than the potential benefit that can be derived from the project delivered. These can be the hardest to evaluate, but a blind rule of cutting all future project spend can be dangerous. Projects should be continued if they will deliver tangible benefits to the organization within the window available or if they cannot be restarted later. Assess the entire change portfolio through the lens of: do it, dump it or delay it.

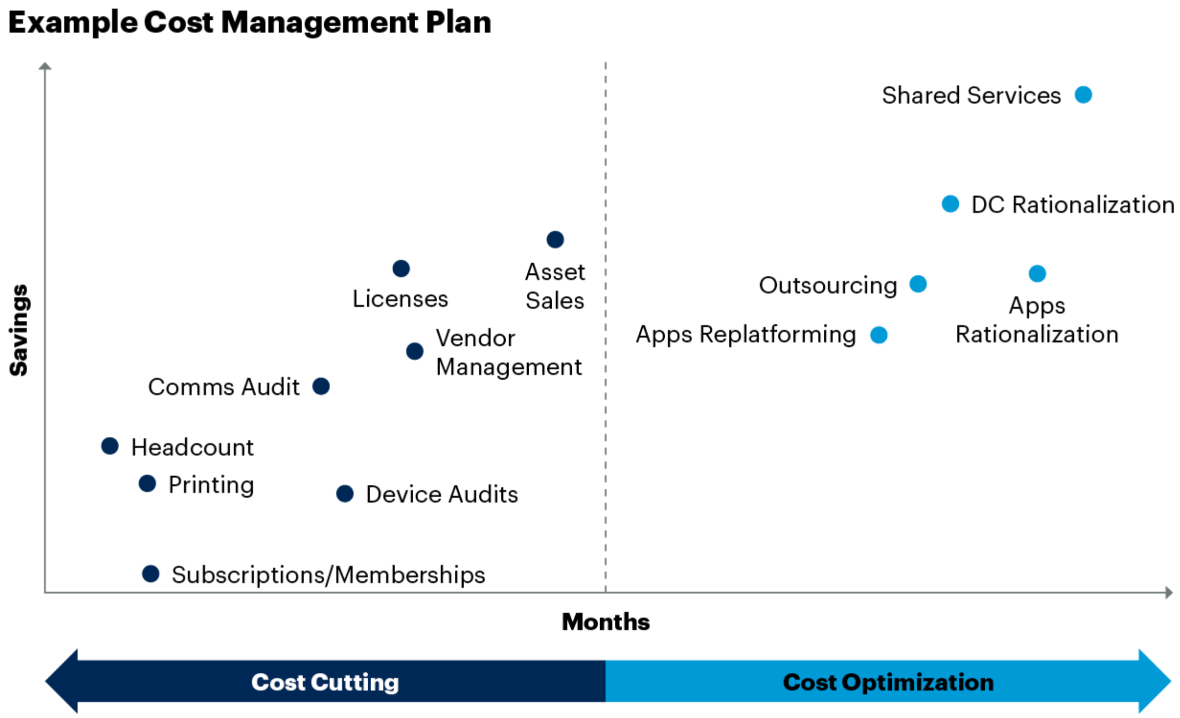
9. **Address Discretionary and Nondiscretionary Spend —** Baseline your run costs and the cost of maintaining opex, and list out the distinction from "grow and transform" initiatives. Run costs are critical to the functioning of the business. Cutting nondiscretionary spend, such as delaying noncritical hardware upgrades, renegotiating service contracts and optimizing software licenses, is recommended for reducing expenses without compromising core operations. While the discretionary spend in the change category which is tied to business growth and transformation can be an easy target for cost reduction, it is important to assess the overall impact on the organization's financial and strategic objectives (see Split the Business Value of IT Story Into Run and Change Narratives).

10. **Tackle Variable and Fixed Costs —** Fixed costs are expenses that remain constant, regardless of activity or volume, for example, office rent, subscriptions and payroll. For fixed costs, focus on elimination. Variable costs change with activity or volume, for example, communications, contractors and consumables. For variable costs, the focus can be on both reduction through consumption management and elimination.

Map and Communicate Your Plan to Eliminate, Reduce or Suspend Spend

There are many categories or types of spend to target or consider when looking for rapid spend reductions. The objective in rapid reductions is the balance of both time to reduction and the size of the reduction. Figure 3 shows an example of a cost management plan, differentiating between cost-cutting and cost-optimization activities where time may allow for bigger initiatives with greater savings impact.

Figure 3: Example of a Cost Management Plan



Source: Gartner
Note: Example Only — Not a Benchmark
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CIOs can refer Tool: Decision Framework for Emergency IT Cost Cutting to map cost savings in the short term across common technology areas such as applications, infrastructure, staffing and resources, end user/service desk and management/change activity. For each action/activity, identify and document the expected saving, timing and any investment required to achieve the saving. Once a detailed cost reduction plan is developed, the next step is to communicate the plan transparently with the internal stakeholders (see How to Communicate Value in the Languages of IT, Finance and Business Outcomes).

Define and Mitigate the Risks

As part of developing a rapid reduction plan, it is critical to define and mitigate, as far as possible, inevitable and accompanying risks. It is essential that a process for risk management is undertaken to ensure that the CIO, IT organization and business unit do not find themselves walking blindly into the potential consequences of the cost-cutting activities. If business unit leaders and their staff fail to grasp how the initiative will impact their day-to-day activities and operations (such as decreased productivity or product time to market), then the initiative may prove both unpopular and unsuccessful. Use Tool: Gartner's Top IT Cost Optimization Ideas to:

- **Define** the financial benefit, investment, business impact, time required, and organizational and technical risks each action/initiative will pose to the organization.
- **Assess** the level of risk that senior leadership is prepared to accept, tolerate or manage. This may differ from "normal" circumstances if cost and time pressures driving the cost reductions are high.
- **Mitigate** risks wherever possible. Don't ignore risks, but accept that not all of them can be mitigated in full, and be prepared for that eventuality. If the risk materializes, consider the negative impacts on the cost-cutting exercise, as well as on morale and culture.
- **Communicate** risks, plans for mitigation or risk-realization impacts. Communicate these internally to IT and to the affected business units. As cost targets are met and reported to senior leadership, so should the impacts, risks and implications. Lack of proper communication will distract employees, create unnecessary speculation about the organization's future and result in reduced productivity. Both employees and stakeholders may become resistant to changes, making cost cutting all the more challenging.

Conclusion

Even when faced with immediate cost pressures, CIOs need to take a thoughtful approach to cost cutting, ensuring that they mitigate the risks and minimize the long-term impact on the organization. Cost cutting can be a difficult exercise for CIOs, but a tight focus on the saving outcomes and the timing to get there will pay dividends. It is essential to balance short-term gain with long-term risk for the preservation of critical functions and strategic objectives.

Evidence

[1] IT Key Metrics Data 2024: Industry Measures — Cross-Industry Analysis

[2] When Cutting Costs, Don't Lose Sight of Long-Term Organizational Health, Harvard Business Publishing (Harvard Business Review)

Document Revision History

10 Rules for Rapid IT Spend Reduction - 4 November 2019

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