

Best Practices to Drive Cost and Value Optimization in IT Management

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Effective management of the IT budget is an essential capability for all CIOs. This research provides an overview of best practices to maximize the IT organization's contributions to business success.

Key Findings

- Enterprises often don't achieve the desired results from cost optimization initiatives due to poor prioritization, poor execution, and lack of clear accountabilities for results.
- Most organizations have already virtualized, consolidated and eliminated underutilized assets. These approaches are still valid, but must be supplemented with new strategies such as demand management.
- Many organizations fail to get the maximum benefits from their IT budget management initiatives because they do not drive them wide enough and deep enough to embrace business cost and value optimization.

Recommendations

CIOs:

- Baseline IT costs. Use Gartner's ITBudget tool assessment as a source of comparative data to assist IT and enterprise leaders with fact-based decisions on IT spend.
- Adopt a tiered approach to IT cost cutting, shifting the focus from simply optimizing IT costs to optimizing business costs.
- Increase IT financial cost transparency to make better joint business and IT decisions.

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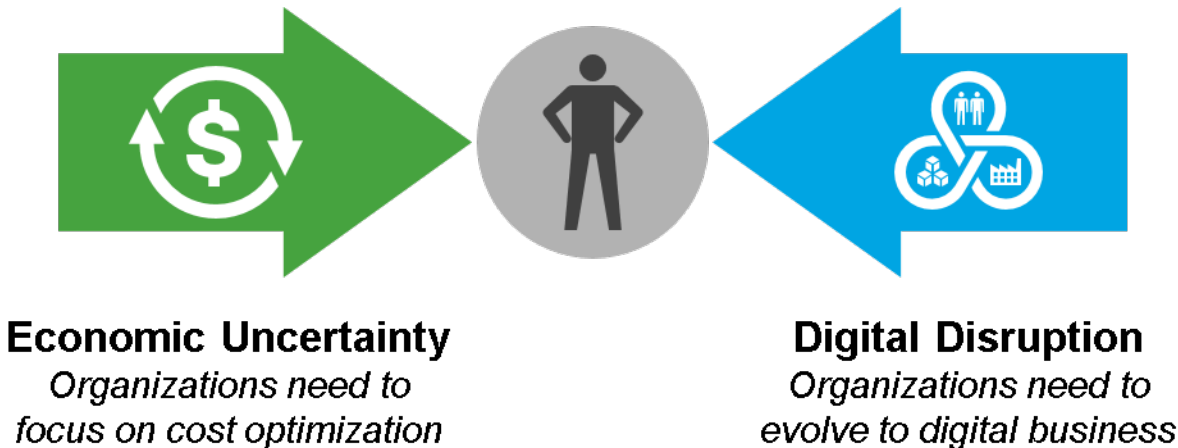
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Analysis

Managing the IT budget effectively is a critical capability for CIOs, and is a prerequisite for maximizing the IT organization's contributions to business cost optimization.

Figure 1. 2016 Economic Landscape Presents Challenges and Opportunities



Source: Gartner (March 2016)

In an increasingly digital world, the effective selection, deployment and management of diverse technologies is critical to business success. Many of our clients have delayed making the necessary

investments to fund digital business; the economic uncertainty further threatens their ability to make these investments (see Figure 2 and Note 1).

Figure 2. Cost Optimization in the Age of Digital Business



Source: Gartner (March 2016)

Cost optimization in the age of digital business means organizations must use a mix of IT and business cost optimization for increased business performance, while preparing for digital futures. Simply cutting the IT budget and taking an approach of waiting until the economic environment is more favorable to make digital investments is a risky approach.

During the past five years, Gartner has helped hundreds of organizations manage their IT budgets; this has resulted in the enterprise driving the maximum amount of business value for its IT investments. This research identifies the best practices that have proved to be most useful in managing IT budgets. Gartner recommends you begin your IT cost optimization program by focusing firstly on:

- IT procurement — Get the best pricing for your IT purchases.
- Cost savings within IT — Improve efficiency of IT processes.
- Joint business and IT cost savings — Simplify business services.

The Gartner ITBudget tool (see gartner.com/itbudget) enables CIOs and IT leaders to generate enterprise-specific IT spending metrics comparisons against their industry to support measurement programs that are recurring, ongoing, driven, strategic, systematic and informed. Baseline metric comparisons include IT spending as a percentage of revenue, operational budget, IT spending per employee, IT staffing levels and the distribution of IT spending by IT domain and resource categories — to name but a few.

Results from that tool representing over 2,000 surveys with analysis across 21 industries are presented in "IT Key Metrics Data 2016: Executive Summary". It reports that average IT spending represents 3.3% of revenue and 4.3% of total operating expenses. The results can identify areas

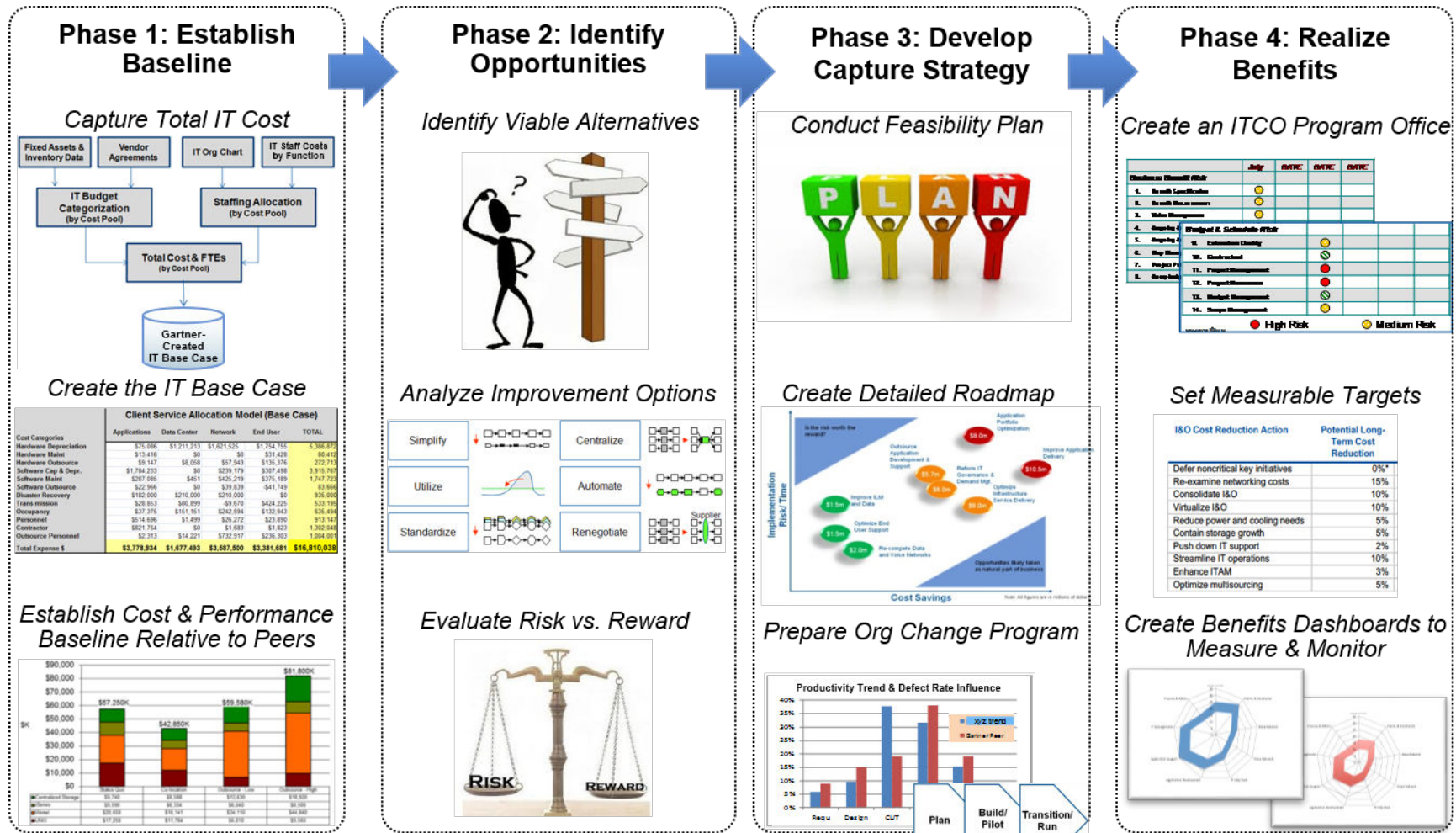
where there are benefits from cost optimization and, often equally important, identification of areas that should be left alone from further cost optimization focus.

Don't stop optimization by focusing just on that 4.3%, but rather extend your horizons to focus on how IT can contribute to business cost optimization across that other 96% of enterprise spend.

Use the Gartner Four-Phase Process to Manage Your IT Cost Optimization Program

Manage IT cost optimization effectively using Gartner's four-phase process (see Figure 3).

Figure 3. The Gartner Four-Phase Cost Optimization Process



Source: Gartner (March 2016)

Not All IT Cost Optimization Ideas Are Worth the Effort

Potential benefit must be measured to get a sense as to whether the effort might be worth it. Customer impact must be assessed (though not necessarily quantified) to determine if an effort might have large financial benefits, but would create ill will with customers — and thus undermine the value of moving forward. This is especially important in the public sector, where customer impact is often a primary concern of elected officials.

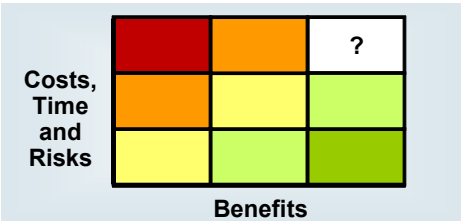
But, in assessing the options, the assessment must also take into account how long it will take to accomplish the reduction, whether the technical and organizational risks are so high that it may not be worth the effort, and whether an upfront cash investment is required to achieve downstream savings. The issues of time, risk and investment requirement may be so severe as to diminish the likelihood of ever achieving any of the desired benefits.

Use a decision framework as shown in Figure 4 to evaluate the opportunities and assess viability (see "Decision Framework for Prioritizing Cost Optimization Ideas").

Figure 4. The Gartner Decision Framework for Prioritizing Cost Optimization Initiatives

For each opportunity generated:

- What's the upside?
- Is it worth the effort?



Potential Benefit:

- How big is the saving if the action is implemented, and how does it affect cash flow?

Business Impact:

- What impact will this have on the business?

Time Requirement:

- Can you capture the savings in this fiscal year?

Degree of Organizational Risk:

- Will your leaders ensure the changes are made?
- Is your organization capable of adapting to the changes?

Degree of IT Technical Risk:

- Is there a risk that the change will undermine the ability of your systems to deliver?

Investment Requirement:

- Does the change require a large upfront investment before savings can be captured?
- Is the organization willing to make an investment at all?

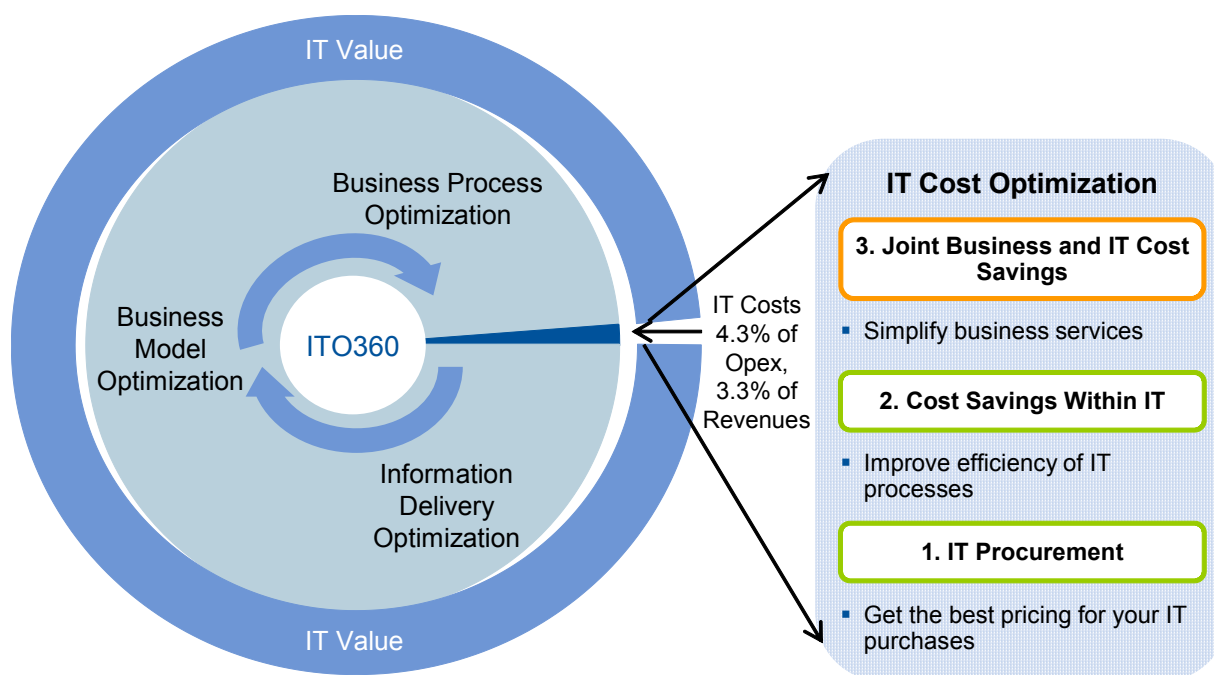
	Small	Medium	Large
Potential Benefit:	Small	Medium	Large
Business Impact:	Negative	None	Positive
Time Requirement:	>18 months	6 to 18 months	<6 months
Degree of Organizational Risk:	High; staff redundancies, and re-engineering of processes and structures	Moderate; limited changes in roles, structures, and processes	Low; no staff reduction, nor changes in organization and processes
Degree of IT Technical Risk:	High; impacts OS, DB, middleware, and applications	Moderate; impacts few components of the architecture	Low; little more than "moving boxes"
Investment Requirement:	High	Moderate	Low/None

Source: Gartner (March 2016)

Take a Holistic Approach to Shift Focus From Costs to Value

The next step in the process is to shift the focus from costs to value, by taking a 360-degree approach, which involves using IT to maximize business outcomes through increased digitalization of business processes, information delivery and business models (see Figure 5).

Figure 5. A 360-Degree View of IT Cost Optimization



Source: Gartner (March 2016)

IT costs only represent 4.3% of the average organization's expenses, although it varies enormously by industry, so the biggest opportunities to reduce overall business costs are outside of IT. In fact, investments in IT generally lower business costs. Our work on optimizing business costs touches many areas, including business process management (BPM) and business process outsourcing (BPO), supply chain optimization, information management and the Internet of Things (IoT).

General Framework

These Gartner tools and research provide a general framework for managing IT cost optimization:

- Gartner ITBudget tool — Leverage the ITBudget tool to generate a comparison of your overall IT spending metrics and identify areas for improvement (see gartner.com/itbudget).
- "IT Key Metrics Data 2016: Executive Summary" — This research contains enterprise-level IT investment, cost and staffing metrics, as well as business productivity ratios for 21 vertical industries, collected throughout 2015 from a global audience. It provides an overall summary of the Gartner IT Key Metrics Data (ITKMD): Key Industry Measures published research.

- "IT Key Metrics Data 2016: Index of Published Documents and Metrics" — The Gartner ITKMD research series contains over 2,000 IT investment, cost, staff and performance metrics covering five topic areas and 96 documents. This document provides a comprehensive list of all documents and metrics published in the series, and contains direct links to each.
- "Toolkit: Spend Less, Drive More Value — The Gartner Approach to IT Cost Optimization" — This Toolkit provides a tutorial presentation and a workshop framework to kick-start IT cost optimization initiatives.
- "Toolkit: Use Gartner's 2016 IT Key Metrics Data to Optimize IT Costs" — CIOs and IT leaders should leverage Gartner's 2016 ITKMD to identify potential areas of cost optimization. This Toolkit organizes key metrics from nearly 20 reports, enabling you to create a fact-based approach to analysis of unit cost and staffing to help identify cost optimization opportunities.
- "Managing Cost Optimization Primer for 2016" — Cost optimization is more art than science, and a dynamic capability where one size does not fit all. IT organizational strategies and tactics will and should be different to take advantage of seemingly unlimited and unique opportunities to be found for motivated CIOs and IT leaders.
- "The Gartner Top 10 Recommended IT Cost Optimization Ideas, 2016" — Gartner has advised hundreds of organizations on IT cost optimization during the past several years. Here, we highlight 10 ideas we most frequently recommend to CIOs and IT leaders.
- "IT Cost Optimization Should Be an Ongoing Discipline" — All organizations attempt to optimize IT costs, but those that do it best focus on cost optimization as an ongoing discipline and not as a one-off exercise. Here, we reveal best practices used by these organizations' IT leaders to optimize IT costs.
- "The Ongoing Opportunity for IT Cost and Value Optimization, 3Q15 Update" — Technology evolution continues to provide new ways to reduce IT costs and to extract increasing business value. Gartner offers IT leaders a four-stage framework for prioritizing IT cost and value optimization initiatives, along with continuous research on the subject.
- "IT Metrics: A Critical Evaluation of Decentralized IT Spending and Digital Enterprise Readiness" — This research provides CIOs with insights into the pitfalls of decentralized IT spending, and offers strategic advice for the centralization of that spending.

IT Procurement

Get the best prices for your hardware, software and services. Every day Gartner analysts provide specific actionable advice for clients in these areas. Procurement is often seen as the starting point for IT cost optimization, because it can result in short-term cash savings. Gartner research provides guidance on getting the best pricing for IT purchases, best practices for contract negotiations and renegotiation, T&Cs, selection of service providers, alternative delivery and acquisition models, and other issues related to procurement of IT services:

- "How to Budget, Track and Reduce Public Cloud Spending" — Companies that use public cloud infrastructure as a service (IaaS), such as Amazon Web Services or Azure, can face

unexpected costs. This research provides best practices for tracking and better managing cloud spending, to avoid unforeseen costs.

- "Why Aren't You Using ITAM to Achieve Total Cost Optimization?" — IT asset managers are uniquely positioned to achieve total cost optimization with their detailed overview of IT asset costs. Without this total cost of ownership, IT decision makers are more likely to make budgeting errors, miss savings targets and see higher overall costs.
- "Cost Optimization Secrets: Strategic Sourcing and Vendor Management Realign Costs and Protect Revenue" — Overspending can be reduced, but significant savings are only achieved by restructuring costs through strategic change. Strategic cost optimization depends heavily on successful market intelligence, as well as planning and execution by sourcing, procurement and vendor managers.
- "IT Asset Management and Procurement Are Key to Successful Cost Optimization and Cloud Adoption" — Organizations are challenged to select, manage and optimize the IT investments that support and drive business outcomes. Executives managing IT assets, procurement and vendors can use this research to understand and address the key challenges they face around the cloud and cost optimization.
- "IT Services: One of the Highest Opportunities for Savings Given It's One of the Largest Sources of IT Spending" — Spending on IT services is one of the largest components of enterprise IT spending categories. Thus, IT services often represent the highest opportunity for cost savings, optimization and new markets. We examine the implications and strategic imperatives regarding the use of IT services.
- "Toolkit: Follow 10 Steps for Better IT Services Sourcing Decisions" — Business changes fast, and sourcing struggles to keep up. This research provides 10 steps for making better sourcing decisions in light of a dynamic business.
- "Toolkit: Best-Practice Guidelines for Assessing Outsourcing Contracts" — Organizations often leave the elements of a contract to their providers. This Toolkit provides best practices for sourcing managers to choose the appropriate elements from their outsourcing deals.
- "Best Practices: Saving Costs Through Outsourcing and IT Services" — Enterprises often outsource to cut costs, but fail to assess how outsourcing will achieve these savings. Businesses need to analyze the sources of savings to achieve sustained long-term benefits.
- "Minimize IT Financing Risk and Exploit Cost Optimization Opportunities Through Gartner's IT Financing Framework" — IT procurement managers struggle to reduce the risks and costs of financing IT assets, while maintaining the flexibility that IT and the business demand. Use this research in collaboration with IT finance to synchronize your assets' useful, financial and economic lives and identify lowest-risk financing.
- "What to Consider Before Cancelling Your ERP Vendor's Maintenance Agreement and Switching to Third-Party Support" — Cost pressures force ERP leaders to look at alternatives to costly, annual ERP maintenance fees. This research provides best practices to switching to third-party support.

Cost Savings Within IT

A priority for many IT organizations is to identify opportunities to reduce baseline IT costs, not just move them to another budget center. Where IT organizations focus is where they will be successful with costs savings. Gartner provides specific cost-saving opportunities by technology and service area, ranges or specific percentages of savings that are typical, things you have to do to achieve these savings, alternatives to the current status quo, and pros and cons related to possible cost-saving actions:

- "Synchronize Bimodal IT and Cost Optimization for the Best Outcomes" — Cost optimization techniques differ between Mode 1 and Mode 2. This research looks at these differences and offers several best practices.
- "Don't Use ERP Rules of Thumb When Costing Projects" — Organizations must spend adequate time costing ERP projects, or they may face surprising and unexpected costs. Gartner provides best practices for costing ERP projects, and overcoming the challenges of using "rules of thumb."
- "10 Absolute Truths for Costing IT" — CIOs often find it challenging to determine the cost of IT. This research provides CIOs with insights for better costing IT.
- "Spend Wisely With a Three-Layer Strategy for IT Cost Optimization" — This research outlines an approach to cost optimization that starts with categorizing IT costs using a three-layer analysis to ensure that cost reductions are made in the right places.
- "IT Cost Optimization Round 2: Strategic Shifts and Doing Less With Less" — The continuing economic turmoil has helped many enterprise leaders understand that "business as usual" is not enough to meet additional cost optimization requirements. Major change and a fresh evaluation of management practices and assumptions are required to meet the challenges of 2011 and beyond.
- "How CIOs Can Improve Processes to Manage Expenses and Identify Opportunities" — Many organizations lack the IT asset management and financial processes to analyze variances properly and determine their budgetary impact. CIOs can use the best practices in this research to develop robust processes to determine the financial effect of variances and unforeseen operational changes.
- "Get Your IT Service Model Right by Optimizing IT's Operations and Outcomes" — IT organizations seeking to optimize their performance must optimize the two key components of their service model (the operating and delivery models), and develop the necessary synergy between them. This research explains how to choose and combine those components.
- "Six Steps to Rationalize IT Service Costs With 'Just Enough' Service Levels Based on Business Value" — A best practice for effective IT service management is to review SLAs for "just enough" service levels to rationalize IT service costs based on business value. Integrate service-level management, business relationship and demand management processes.
- "Use IT Organization Staffing Ratios to Plan and Validate Organizational Changes" — Cost pressures and changing business structures force many CIOs to restructure and downsize, or

even deliver agility and growth, fast. They need clear principles for setting the number of management layers and the span of management control in the IT organization.

- "Getting Started and Realizing Benefits From Lean" — "Lean" is an important and proven management technique. CIOs can exploit it in a number of ways, albeit each with limitations, and bring together existing and emerging disciplines to create more of an integrated and holistic approach to delivering IT services.
- "Market Guide for IT Financial Management Tools" — IT financial management tools can help IT leaders better understand their spending. This Market Guide looks at the market for these tools, and covers a number of representative vendors.

Joint Business and IT Cost Savings

To make lasting and substantial changes in the cost structure of IT, organizations ultimately have to move beyond asset optimization and incremental improvements in the IT environment and seek to simplify IT's business services and reduce the volume of demand. When CIOs begin to look at joint business and IT cost savings, they — along with their business leader counterparts — consider how the enterprise manages demand for IT; how it governs the use of IT; how it manages the life cycle of IT-enabled business assets; and how it applies IT to generate value. Here, the decisions become more challenging, and involve issues such as applications rationalization, chargeback and the consolidation of services. These efforts are generally several years in the making, and often require investments to generate long-term savings. As a result, most organizations are still target-rich environments when it comes to joint business and IT cost savings. Gartner provides specific guidance on implementing cost-saving technologies in conjunction with the business that may include investments to reduce cost long term, or alternatives to current technologies:

- "Developing a Financial Transparency Roadmap" — Financial transparency can build the credibility of IT leaders. This research helps IT leaders assess their current states and take several other steps toward establishing a financial transparency roadmap.
- "Define IT Optimization to Drive Business Outcomes Instead of Efficiency Gestures" — CIOs who successfully reach cost- or budget-cutting goals, using only tactical methods, are often surprised by larger requests for more cuts. Such budget appeasement can be harmful to an enterprise. Influencing business outcomes must be the higher goal of optimization enabled by IT service portfolios.
- "Avoid Damaging Key Business Capabilities When Cost Cutting" — Business capabilities are difficult to build. Avoid inadvertently damaging the ones that are most valuable to your future business when looking for cost-cutting opportunities.
- "Optimize IT Investing With an All-Purpose Governance Portfolio" — One of the most important functions of high-performing governance is to optimize spending and investments across the entire enterprise portfolio. This research suggests a portfolio model that CIOs can use to help optimize this process.

- "10 Absolute Truths for Optimizing the Value of Investments Requiring IT" — Gartner provides CIOs with 10 points of advice for getting the most from IT investments. Advice covers areas such as managed change and attributing responsibility for project success.
- "IT Chargeback as a Tool for Cost Optimization" — Chargeback for IT services will change from a tool to demonstrate business value back to a punitive tool for expense allocation and efficiency during times of economic uncertainty. The demands of IT cost optimization will dictate future chargeback program utility and relevance.
- "Use EA Business-Outcome-Driven Analysis to Identify Cost Optimization Opportunities" — Economic uncertainty and a slow recovery drive enterprise architects to find more cost reduction opportunities and help optimize budgets. Applying business-outcome-driven EA best practices will help strike the right balance between business value and cost management.
- "Use EA Business-Outcome-Driven Analysis to Optimize IT Costs Without Losing Key Capabilities and Services" — Economic uncertainty will continue to pressure organizations to reduce IT costs, but boards and CEOs will still demand profitable revenue growth. Enterprise architects tasked with IT cost optimization must take a surgical approach to avoid destroying critical capabilities needed for growth.

Business Cost Optimization

IT and business cost optimization is a complex initiative that relies heavily on IT management disciplines, such as financial management, service management and portfolio management. Business cost optimization should ensure that their underlying capabilities in IT management are up to the task.

- "Cost Optimization in the Age of Digital Business" — Many organizations are already behind the curve in terms of funding digital business. An economic slowdown further threatens organizations' ability to make these investments. CIOs should be proactive about IT and business cost optimization to fund digital business.
 - "How to Shift the Focus From IT Cost Cutting to Business Optimization" — This research describes practical steps CIOs can take to move from a never-ending focus on cutting the IT budget to optimizing IT's contributions to business performance.
 - "ITO360: Break Through IT Cost-Cutting Barriers to Optimize Business Performance" — As enterprises adopt digitalized strategies and business models, CIOs must rethink the optimization of IT value. IT optimization from a 360-degree perspective (ITO360) maximizes business outcomes through greater digitalization of business processes, information delivery and business models.
 - "Flipping IT Financial Thinking to Prepare for Digital Business" — This research looks at how the enterprise's transition to digital business requires CIOs to establish a new relationship with financial risk and uncertainty.
- "CIOs Should Follow the Money to Succeed in Digital Business" — Digital business requires business leaders to revisit how they budget. This research looks at the financial impacts of digital business and offers related best practices.

- "Successful Approaches to Business Process Improvement" — This research provides examples of how enterprises are approaching investments to improve business processes.
- "Cost Optimization Through Improving Business Processes" — CIOs are promoting the message that focusing on improving processes through structured redesign before technology implementation can deliver better business outcomes.
- "Enterprise IT Maturity, 2014: CIOs Are Seen but Not Heard" — Gartner examines its ITScore Maturity Assessment data from 2010 to 2014, analyzing for CIOs the true state of affairs and overall enterprise maturity in deploying, sustaining and strategically leveraging IT. CIOs can use these findings to build a healthier and more effective IT organization.

Note 1 Cost Optimization in the Age of Digital Business

Cost optimization in the age of digital business means organizations must use a mix of IT and business cost optimization for increased business performance, while preparing for digital futures.

Evidence

Gartner analysts have been assisting clients manage their IT budgets effectively ever since Gartner was founded. This research collection is based on the thousands of interactions that have occurred over the last few years.

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