



# TO MAKE ZERO-BASED BUDGETING WORK, CHANGE BEHAVIOR

By Karin von Funck, Mark Austin, Donat Wunderlich, and Christina Schenk

**O**VER THE PAST 12 months, the COVID-19 crisis has forced business leaders to double down on cost management, ensure liquidity, and scrutinize budgets. Apart from prompting short-term contingency measures—such as cutting back on marketing budgets or IT projects—the lockdowns have spurred cost reductions. Just consider the dramatically lower spending on travel that has accompanied the shift from physical meetings and events to virtual ones.

Although hopes remain high across the business world that the pandemic crisis will end soon, heightened volatility and uncertainty are undoubtedly here to stay. This raises a number of critical questions: How do companies rethink their resource allocation and budgeting process going forward? How can they preserve the tactical savings they have captured over the past year? And how can they harness and translate COVID-related behavioral changes into sustainable savings— and avoid the cost creep that invariably occurs when cost-cutting programs become fixtures?

There is a highly effective way to change how companies manage cost: through zero-based budgeting (ZBB). This clean-slate, bottom-up approach to resource allocation enables companies to reset their cost base and cost structure so they can redirect funds to advance the company's strategic priorities. But like any other major change effort, transforming a company's approach to costs requires effective change management.

Moving to ZBB involves adopting a new way of thinking that permeates the entire organization. To succeed, a ZBB implementation must do more than tackle the mechanics of new processes, policies, and systems. Above all, it must instill a new mindset and new behaviors. By modifying the incentives that shape their organizational context, companies can change their mindset, foster new behaviors, and unleash the enduring power of ZBB.

## A Clean Slate

ZBB is not just another line-by-line budgeting method. In fact, at bottom, it is not a

method at all. Rather, it is a philosophy that infuses a culture of cost consciousness and new ways of working throughout the organization. ZBB emphasizes differentiating between high-value-added and low-value-added spending so that companies can allocate resources to projects and processes that deliver the most value.

Although ZBB is not new, introducing a ZBB program could not be more timely. The pandemic has led to economic, health, and social devastation, but it has also created an unprecedented opportunity to reassess how businesses operate. The crisis has challenged many core beliefs, and employees have exhibited a newfound openness to fundamental changes in their ways of working. We hear this from company leaders across industries:

*“People have not only proven they’re able to work effectively and efficiently at home—they like it.”*

*“When it comes to spending, everything is on the table. There are literally no sacred cows left.”*

*“We’re asking our sales people: do you really need to be out in the field and with the customer at all times?”*

As a business-driven program, ZBB requires leadership from the top. It is not a cost optimization program led by finance or procurement. The business side of the organization spearheads joint discussions with functional experts, systematically reviewing the terms and prices they’ve negotiated. More important, participants challenge current spending patterns, processes, and demand, asking such essential questions as, “Is it worthwhile to spend our resources on this, and can we reduce our consumption or service level?”

## Creating the Right Context

The goal of a ZBB program is to ensure that every employee adopts an owner-operator mindset toward spending, questioning the value of everything that is funded and treating company money and

budgets as if they were their own. That means, of course, that a ZBB program must be implemented company-wide and treated as an ongoing effort—a continuous cycle. It requires a consistent taxonomy of costs that provides an organization-wide view of actual cost categories (such as travel, facility management, and marketing expenses). Managers can then map these costs directly to the activities where they are incurred. The point of doing so is to challenge budgets and spending from the bottom up in order to assess whether they support business priorities.

The traditional approach to budgeting does not encourage such practices. Typically, decision making occurs from the top down, and the primary bases for allocations are past performance and power centers, rather than enterprise strategy and future needs. Traditional budgeting has fostered deep-seated behaviors such as sandbagging to preserve a unit or department’s budget allocations for the following year, or doling out incremental changes year after year instead of questioning the actual budget as a starting point.

Since such behavior is usually a rational response to a company’s internal dynamics, the company must create the right context if it is to overcome that behavior. Specifically, the company needs to orient itself so that it is in individuals’ self-interest to behave in the desired new ways. Successful ZBB programs take this into account, creating an environment that makes cost-conscious, strategy-focused behavior both rational and desirable to all.

## Seven Critical Actions to Instill ZBB Behavior

Through BCG’s extensive client work and research on change management, we’ve identified seven key context dimensions through which companies shape their environment, and thus behaviors and mindset. These dimensions are interconnected and mutually reinforcing, so by adjusting the structures and mechanisms within the dimensions, companies can effect deep and lasting change.

**Ensure that the executive team leads the way.** Effective change flows from the top, and this truth applies with full force to ZBB programs. Leaders must personally advocate for ZBB and explain what ZBB is and why the company is adopting it. They must convey the necessary changes in mindset and the new rules and guidelines to promote more efficient spending. Informal meetings and gatherings are effective venues for CEOs and CFOs to communicate these points.

Leaders cannot treat the ZBB implementation as merely a project to be managed. Instead, they must consistently and rigorously demonstrate the appropriate behaviors. Freeing up costs often involves some pain, so leaders should set an example by publicly making their own sacrifice. For example, to signal their commitment, executives might suspend travel privileges for senior managers or cancel an expensive company offsite.

**Demonstrate that ZBB is more than just another cost-cutting program or tedious budgeting exercise.** Often, employees initially perceive ZBB to be purely a cost-cutting effort. For a ZBB program to succeed, people must understand how it ties directly to the organization's core strategy. Beyond redirecting resources more usefully and boosting profitability, ZBB can play an integral role in modernizing the organization—for example, by freeing up funds to build new digital capabilities or bring strategic activities in house, such as competitive reviews of marketing agencies or customer journey audits.

In addition to explaining how the ZBB program serves the company's overall strategy, leaders should explain how and where they intend to reinvest the money. By openly communicating what benefits ZBB will deliver and how it will advance the organization's vision and agenda, leaders can build critical support for it.

**Expand accountability to foster fresh perspectives.** Traditionally, companies have organized budgets by function, department, or business unit, even though

the spending for many categories of cost extends throughout the enterprise. To optimize costs, it's essential to break through organizational silos to get an enterprise-wide view of actual expenses. With ZBB, the company designates cost category owners (CCOs) to manage each cost category. The CCO challenges budget owners, bringing a fresh perspective that enriches budget discussions. But rather than dictate the outcome, the CCO works with budget owners to promote and track savings. Besides helping to clarify the expense picture, this approach broadens accountability.

As the person with accountability, the CCO has the support of senior leaders and sets guidelines and policies (such as spending thresholds above which approval is needed). The CCO role also provides internal benefits by offering opportunities to share best practices, spread new ideas, take advantage of volume discounts, and negotiate more favorable deals.

It is common for senior managers to be skeptical about the CCO role at first, thinking of it as having someone watching over their shoulder. But the healthy friction that results can change opinions. At one client organization, the same managers who initially resisted the idea turned out to be the most active CCOs when they took on the role.

**Promote prompt, fact-based decision making.** Transparency lies at the heart of ZBB. It gives management a basis for making objective, better-informed decisions, rather than relying on gut instinct, politics, or sheer habit. It enables them to more accurately balance tradeoffs and determine whether the return is worth the money. Companies will find it easier to track and trace the impact of their budget decisions—and ensure rigorous implementation. And the insight that they gain into where the money is going enables companies to reverse the burden of proof at budget-setting time.

Instead of an approach in which the controlling function argues against allocating a

certain amount (and all too often lacks the data to back up its argument), the budget owner makes the case for the expenditure by providing proof of its value. Over time, as defending costs on the basis of return and value becomes ingrained behavior, decision making becomes faster and more efficient. Conflicts over budgeting decisions can be resolved quickly.

**Embed ZBB into the company's systems, IT, and processes.** As we've said, a successful ZBB program depends on there being a clear view of how much the company is spending on every given item, and by whom. As a result, financial tracking must reflect a cost-category perspective across organizational units, as well. And this, in turn, means that the organization must embed cost transparency in its systems and technology tools.

As a first step, companies should update their chart of accounts and their accounting rules to consolidate expenses by cost category. One important aspect of this effort involves ensuring that no one buries expenses under "miscellaneous" or "other" account headings. By using existing systems—and without adding complexity or bureaucracy—companies can develop reports that they can generate automatically to pinpoint any budget deviations quickly. Other useful tools include a marketing-mix tool to help optimize media spending and a quick-quoting tool to use in small-scale market research projects.

But embedding ZBB in systems and tools is not enough. Companies must also ingrain ZBB in key management processes, including the regular dialogues between CCOs and budget owners about budget deviations and delays in implementing savings measures (for example, delays caused by the protracted renegotiation of a contract).

**Incentivize the desired behavior.** Companies can foster a ZBB mindset and behavior among employees through their performance management processes, KPIs, and rewards and recognition programs. Companies should integrate new category-expenditure-tracking KPIs into the perfor-

mance management process; this will enable companies to test whether their policies and savings initiatives are being implemented and how well they are working. Companies should adopt a carrot-and-stick approach to achieving budget targets, promising managers incentives for reaching their targets and negative consequences if they fall short.

Some companies reward managers who meet or exceed their targets by permitting them keep to the resulting savings to reinvest in growth projects under their purview. An even stronger incentive would be to link cost category targets to managers' bonuses. Intrinsic motivation can be effective, too: at some companies, managers view the role of cost category owner as prestigious. As a way of increasing the visibility of an individual or a team to company leaders, it can be a powerful performance management lever.

**Put the right talent in place.** Our experience tells us that change programs, regardless of their specific features, require stalwart, dedicated people to carry them out. ZBB is no different. As one CEO we work with said, "Put your strongest people in it, and you'll create a snowball effect." Enlist team players who support the program and its goals and who are comfortable challenging colleagues and being challenged themselves. It's important to present critical ZBB roles—the program leader, methodology champions, and workshop participants—in the appropriate light, touting the opportunities that these roles provide, such as exposure to senior management.

Every ZBB program requires a critical mass of participants drawn from throughout the organization to help mobilize the effort and build capabilities. We advocate training ZBB champions through a "learn, do, teach" approach. These champions can then participate in workshops to learn about ZBB, disseminate the practice in other locations through workshops and playbooks, and teach others the tenets and practices of ZBB across the farthest reaches of the company.

**T**HE ATTITUDES AND habits surrounding traditional budgeting and spending are deeply ingrained. Because companies that understand ZBB know that it is, above all, a philosophy, they recognize that changing hearts and minds is as critical to ZBB success as implementing the requisite processes, systems, and tools.

By fostering a culture of cost consciousness, ZBB allows companies to direct their resources to achieve maximum impact, reinvesting toward growth and toward accom-

plishing their strategic goals. When leaders design and establish a ZBB program properly—not as a cost-cutting effort in disguise, but as a fundamental transformation that aims to optimize resources for the greater good—they help set the stage for significant, sustainable results.

In adversity lies opportunity, and there may be no better time than today to adopt ZBB. The COVID-19 crisis has already demonstrated that positive change is not only timely, but welcome.

### About the Authors

**Karin von Funck** is a managing director and senior partner in the Munich office of Boston Consulting Group. She is the European lead for the zero-based budgeting topic. You may contact her by email at [vonfunck.karin@bcg.com](mailto:vonfunck.karin@bcg.com).

**Mark Austin** is a managing director and senior partner in the firm's London office. He is the global topic leader for the cost and zero-based budgeting topics. You may contact him by email at [austin.mark@bcg.com](mailto:austin.mark@bcg.com).

**Donat Wunderlich** is an associate director in BCG's Hamburg office. He specializes in cost transformation and reorganization projects. You may contact him by email at [wunderlich.donat@bcg.com](mailto:wunderlich.donat@bcg.com).

**Christina Schenk** is an associate director in the firm's Zurich office. She works with clients on large-scale transformations and is an expert on zero-based budgeting. You may contact her by email at [schenk.christina@bcg.com](mailto:schenk.christina@bcg.com).

Boston Consulting Group partners with leaders in business and society to tackle their most important challenges and capture their greatest opportunities. BCG was the pioneer in business strategy when it was founded in 1963. Today, we help clients with total transformation—inspiring complex change, enabling organizations to grow, building competitive advantage, and driving bottom-line impact.

To succeed, organizations must blend digital and human capabilities. Our diverse, global teams bring deep industry and functional expertise and a range of perspectives to spark change. BCG delivers solutions through leading-edge management consulting along with technology and design, corporate and digital ventures—and business purpose. We work in a uniquely collaborative model across the firm and throughout all levels of the client organization, generating results that allow our clients to thrive.

© Boston Consulting Group 2021. All rights reserved. 3/21

For information or permission to reprint, please contact BCG at [permissions@bcg.com](mailto:permissions@bcg.com). To find the latest BCG content and register to receive e-alerts on this topic or others, please visit [bcg.com](http://bcg.com). Follow Boston Consulting Group on Facebook and Twitter.