Top 5 cost control techniques you can implement today!

Several factors contribute to the management and development of successful businesses, the most important of which are cost control techniques.

Your business could be providing the best product or service globally, but if it doesn't make any revenue, it's not going to work.

So, to run a profitable business, you need to know how to cut costs when necessary and enhance your investment when necessary.

Methods to monitor the evolution of the following 5 costs can help you achieve this balance, maintain your budget, and increase the project's profitability.

What's cost control?

Cost control is managing costs to achieve or maintain the required profitability, efficiency, or competitiveness.

Cost control may include the identification and analysis of costs, the development and implementation of budgets, cost-effective methods and tools, and the development and implementation of effective cost-reduction strategies.

Using cost control techniques improves a company's financial performance while reducing costs.

What's the importance of cost control?

Cost control helps corporate accounting officials maintain a clear budget, which keeps their financial resources stable and promotes increased profits.

In addition, monitoring costs through informed budgeting helps the company stay on track while maintaining high profitability so that revenues are higher than the project's cost, thereby increasing the company's financial resources.

There are a variety of cost control strategies, including:

1. Conduct a review and cost analysis to identify potential areas for cost savings.
2. Determine the most efficient methods of performing tasks or producing products.
3. Use of new technology or processes to increase efficiency and accuracy.
4. Coordination with suppliers and partners to reduce costs and improve quality-quantity relationships.

Cost control factors:

- Employment costs:

It is the sum of the wages paid to its work team, including staff development, training, and creating an appropriate working environment.

- Material costs:

The total cost of all tools and equipment required for the project is the cost of the materials. This includes requested material before, during and once the project is completed.

- Actual cost:

The actual cost is the total expenditure incurred by a project from the start to the end. This includes the cost of labour and expenses related to the project.

- The cost difference:

The cost difference refers to any price difference between the actual cost of the project and the budget identified.

- Return on investment (ROI):

The return on investment (ROI) is the project's profitability, compared to the amount invested.

Top 5 technologies that will help you control costs:

1- Consider budget planning:

It will need to establish a fixed budget at the beginning of the project planning session, including all payments and the costs to be borne during the project's life cycle.

It is also important that the budget be flexible and adjustable in anticipation of changing market prices.

2- Tracking costs:

It is better to prepare budgets, monitor operational costs, and analyse deviations that will help you track the project budget at each stage.

If the project is extended, it is important to track monthly, weekly, or even annual costs.

3- Time management:

Time-effective management is one of the most important methods of cost control. Although this technique applies to different management areas, it is essential for project cost control.

Time management is important in meeting project deadlines, achieving the target, and gaining planned income, as long as the cost set during the project period is not exceeded.

4- Use of change control systems:

Change control systems are vital methods necessary to consider any possible changes during the project journey. Any change in the project implementation period would impact delivery deadlines, affect the implementation plan, and thus cost the project.

5- Keep track of the money you've made.

To determine the value of the work carried out so far, a financial accounting technique known as "acquired value is beneficial."

The value gained is tracked as an effective means of implementing large-scale projects and is flexible enough for emergency changes requiring immediate intervention. However, it is essential to constantly review the budget, ascertain financial and budgetary information, and track costs.

In summary,

coming up with a project budget is not enough at your project planning stage. You and your team will have to monitor the costs to stay close to the exact numbers.

Therefore, you will undoubtedly be guaranteed increased profits and success if you use the above techniques and constantly monitor costs while attending accounting online training courses.

What Are Project Costs?

> Project costs are the funds required to perform a planned business endeavor, and they are a primary subject in project budgeting and cost management. Costs are the entities you estimate when developing a budget. They are the money you actually invest in work and the amounts you track and control until the very end of a project.

Main Types of Project Costs

1. Direct vs. Indirect Costs

One of the most common methods to categorize project costs is by dividing them into direct and indirect expenses.

Direct expenses are entailed by everything you do to produce a particular output. Let's take a hardware development project as an example. In its case, direct costs will include:

- Raw materials for the creation of finished goods (e.g., steel, plastic, etc.),
- Direct labor (i.e., human resources and hours necessary to manufacture the product),

- And production equipment.

Overall, any cost that directly influences your output volume belongs to the category of direct expenses. Any change in the magnitude of production will lead to either an increase or decrease in the number of specific things needed to meet the set output goal. These things will be your direct expenses.

In contrast, **indirect expenses** comprise the cost of everything that isn't directly linked to primary project operations but is required to support them.

Let's consider the above example again. To create hardware, you need to:

- Rent a facility,
- Pay wages to administrative employees,
- Use technology for communication between business units,
- And travel to different cities to sign contracts with suppliers.

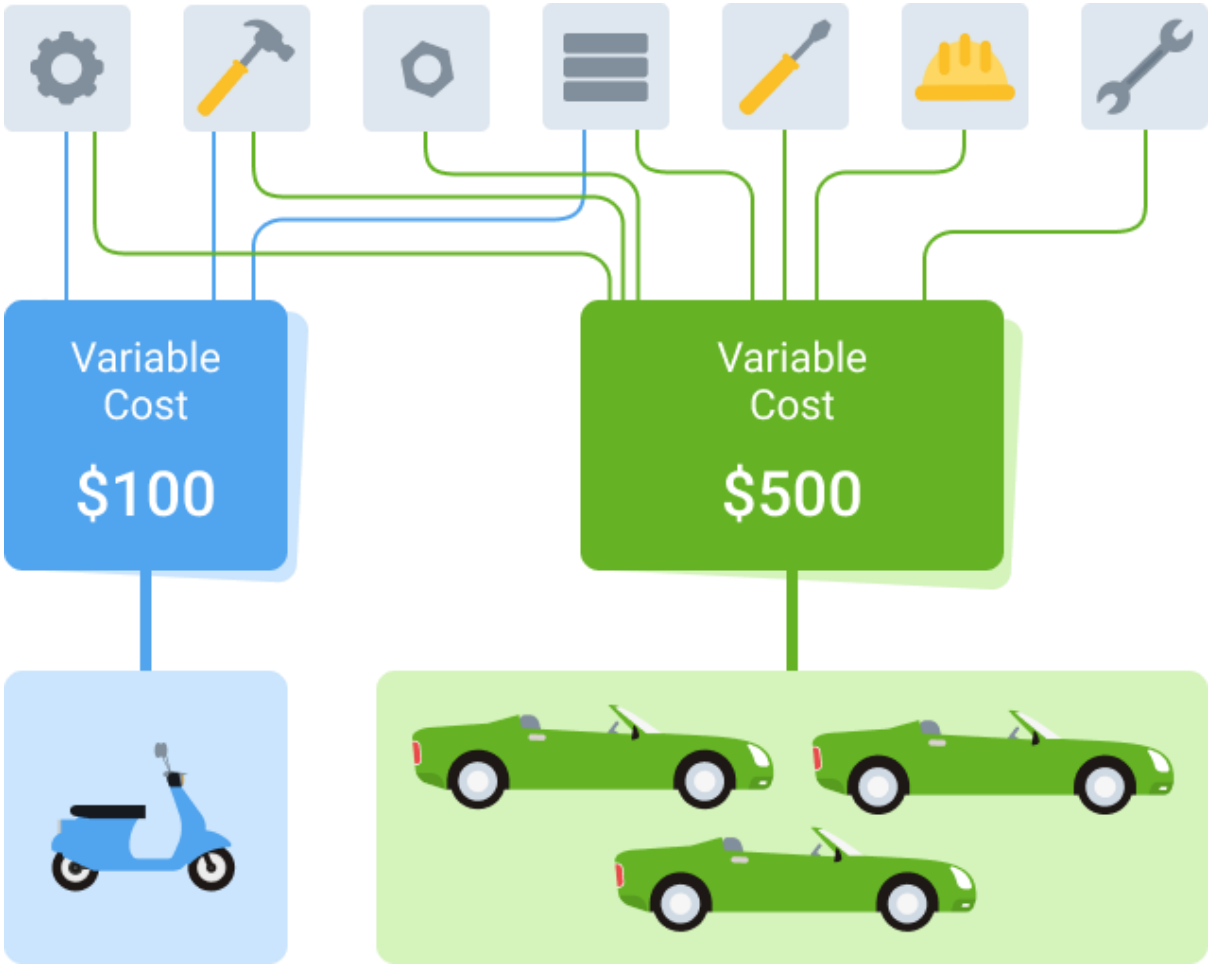
All these activities fall under the category of indirect costs. They are essential for the sustainability of the business as a whole but are not associated with the production process itself.

2. Fixed vs. Variable Costs

When categorizing expenses based on the production capacity, business practitioners divide them into fixed and variable costs.

Fixed costs are those expenses that never vary in their amount regardless of possible changes in output volumes. One of the best examples of a fixed cost is rent payment. For instance, the abovementioned hardware development company may have to pay $15,000 for a production facility monthly. This price remains the same, invariably of how many items the business has manufactured during the rent period – 15 or 500.

Conversely, **variable costs** constantly change as the company increases or decreases its production outputs. If the same hardware development company decides to manufacture 300 USB flash drives for the cost of $15 (i.e., the sum of all relevant direct expenses), the total variable cost for that project will be $4,500. At the same time, if this company will choose to produce 800 USB drives instead, the variable cost will go up to $12,000.



3. Period vs. Product Costs

There is yet another way to classify expenses based on their relation to the production process – by dividing them into product and period costs.

Product expenses refer to EVERYTHING involved in the production process:

- Direct costs,
- Expenses your business incurs when running its daily operations,
- Equipment maintenance,
- Salaries of production managers, etc.

Overall, this group of expenses includes a variety of objects and activities that are both directly or indirectly linked to the central process of production (or service provision) itself.

As for **period expenses**, they are incurred not by the purchase or production of goods or services but by time. To clarify this, let's see how companies write off product and period costs in their balance sheets. The former group of expenses is usually reported either as inventory or as the cost of goods sold. In contrast, period costs are normally expensed in the period incurred as selling costs or general and administrative expenses that result from daily business operations. For instance, since product promotion activities, wages of administrative employees and corporate office rental are typically bound in time and aren't in direct relation to the primary production process, they should be regarded as period costs.

4. Pre-operating vs. Operating Costs

Costs can be grouped depending on their connection to different stages of the project's life cycle. In this way, pre-operating and operating expenses are discerned.

Pre-operating costs are incurred prior to the actual start of the project and all relevant operations. Before engaging in project realization, you may need to conduct an environmental analysis, develop a strategic plan, and train new staff members. All these preliminary activities fall under the category of pre-operating costs. Since they serve to guarantee successful completion of the project, pre-operating expenses are an essential part of the initial investment. For this reason, they must be expensed as intangible assets in the accounting documents.

Operating costs are incurred after the official start of project operations. This group of expenses comprises everything required to keep the business going, including inventory, employee wages, technology, intellectual property, rent, and funds allocated to such vital activities as marketing, sale and production. It means that both direct and indirect project expenses are considered operating costs as long as they take part in the daily maintenance and management of the project. After figuring out this type of expense as per your project's needs, you may also use the numbers to calculate its operating income – the sum of earnings realized from project activities, after deducting all operating costs. This practice will allow you to see whether your endeavor is profitable or not.

5. Retrospective vs. Prospective Costs

Another way to look at costs is by considering their time orientation and the potential for recovery. Thereby, project expenses can be either retrospective or prospective.

Retrospective costs, also known as sunk costs, are expenses that have been incurred in the past and cannot be recovered. Since retrospective costs have already taken place, they usually are not taken into account during financial decision making. In contrast, as future expenses that haven't yet taken place or past expenses that could be recovered, **prospective costs** influence decision making to a substantial degree.

Assume a publishing business that plans to issue a novel. When choosing the pricing strategy for the new book, the management thinks over the costs of materials and labor required to print a single item. Depending on the quality and price of paper and ink utilized for production, the charge for the final product will vary. At the same time, such things as a $9,000 printing equipment or a $500,000 facility that the company purchased a long time ago won't affect the pricing decision in this situation.

Printing materials in this instance belong to the category of prospective costs since their amount could be changed as a result of the management's ultimate decision. Contrariwise, the purchased equipment and building are sunk costs – they were committed in the past and, thus, are irrelevant to the current pricing decision.

6. Opportunity Cost vs. Cost of Risk

The last category in the list – costs of opportunity and risk – is defined based on the potential outcomes of incurred expenses and their ability to produce financial benefits or loss.

Since risks frequently cause damage to the financial health of businesses, the **cost of risk** primarily refers to the loss of money due to the failure to foresee various environmental hazards. Nevertheless, expenses incurred when managing risks are often regarded as the cost of risk as well. Thus, besides direct financial damages induced by external influences, the total cost of risk (TCOR) comprises such activities as risk analysis, risk mitigation, risk control and all relevant administrative expenses. Therefore, by evaluating different costs of risk, you can not only predict the extent of a possible loss due to changes in the market environment but also see how effective and efficient your risk management strategy is.

As for **opportunity cost**, it refers to financial benefits that a business may miss because of selecting one investment alternative over another. Imagine that you have two investment options to choose from, and each of them could lead to disparate financial outcomes. To calculate an opportunity cost in this case, you would need to:

- Predict the expected return on investment per each opportunity,
- And identify the difference between their assumed returns.

This difference would be your opportunity cost. As you can tell from the provided example, this type of expense is a purely analytical concept. Nonetheless, it bears an immense value for managers because it supports the making of more informed decisions.

How to Manage Project Costs

Project cost management is the process of planning for expenses and controlling the costs of a project. It includes identifying, estimating and budgeting for all the costs associated with a project and its primary goal is to ensure that your project is completed without any major budget overruns.

There are four main steps in the project cost management process:

- Estimate costs
- Create a budget
- Track and control costs
- Close out the project and account for all final costs

Let’s look at them one by one.

1. Estimating Costs

Estimation is the process of predicting the future cost of a project. You may choose one of many different cost estimation methods to get this task done, but the most important thing is to ensure that all potential project expenses are taken into account. This includes the costs for materials, labor, overhead, etc.

There are also a number of various factors to consider when carrying out cost estimation:

- Scope of the project. You need to think of things like how many people will be working on the project, how long it will take to complete it and what kind of resources will be required.
- Nature of the project. This includes things like whether it is a new product or service or an existing one that is being modified.
- Size of the project. Determine the number of products or services that must be produced or the number of people that will be using the product or service.

The more accurate cost estimates you make, the better it is for your overall project outcomes. Accurate estimates are the key to good project planning: if you’re off by even a small amount, it can throw your whole project schedule off course. Thus, it’s better to take project estimation as seriously as possible.

2. Creating a Budget

Once the costs have been estimated, it's time to proceed to project budgeting, i.e., to allocate funds to different aspects of a project.

To create a perfect budget, it's essential to know not only how many expenses your project will incur but also how much money you will have at your disposal throughout the course of work. Thus, you need to analyze your income and expenses using some high-quality data. This will give you a good idea of where your project money will go and how much you will spend at different work stages.

It's also vital to be realistic when creating your budget. Make sure to factor in the unexpected costs and leave room for some contingencies. If your budget is too tight, you'll likely end up going over it.

3. Tracking and Controlling Costs

Once the actual work begins, costs should be closely monitored to ensure you stay within the approved budget. If expenses begin to exceed the initial estimates, you will have to undertake some steps to take them under better control. This may involve cutting back on some aspects of the project, rethinking some objectives or renegotiating contracts with suppliers or contractors. And to prevent any serious alterations to your original plans, you need to identify the risk of cost overruns early on. Hence, accurate cost tracking is critical.

So, what is the best way to track project costs?

A simple work breakdown structure template can do an excellent job for smaller and simpler projects, while the larger ones will require you to apply advanced software. But whatever method works best for you, be sure to keep track of every single expense, no matter how big or small.

With actiTIME, for example, you can easily keep a detailed record of your direct staff-related expenses. It is a perfect tool for tracking both billable and non-billable hours worked by employees. Plus, it features a few handy cost and profit reports that are helpful not only for better control over your current projects but also for estimating future ones.