

Operations Practice

Reset and reallocate: SG&A in the next normal

Organizations are facing a set of unique challenges as they make decisions about selling, general, and administrative activities. How are leaders dealing with them?



This article was written collaboratively by the global leaders of the McKinsey Corporate Business Functions Practice, a group that spans different regions and includes Kyle Hawke, Matt Jochim, Raj Luthra, Rowan Mawa, Juliana Pflugfelder, Abhishek Shirali, Yu Ueda and Megan Wells.

In “**The SG&A imperative in times of crisis,**” we looked at how the COVID-19 pandemic has presented organizations with a unique challenge in making wise spending decisions across their sales, general, and administrative (SG&A) functions. The solution to this challenge, we argued, is to use zero-based principles to move SG&A investments where they should be—rather than where they have always been.

We confirm the need for new levels of visibility, and thoughtful discussion to help leaders align on priorities in some of the most consequential decisions they face, in the findings of the 2020 SG&A Executive Pulse Survey. The survey asked more than 190 CXOs and functional leaders across North America and Europe, and representing a wide range of industries and functions, how they are thinking about SG&A in the months ahead (Exhibit 1). Our findings are described below.

Exhibit 1

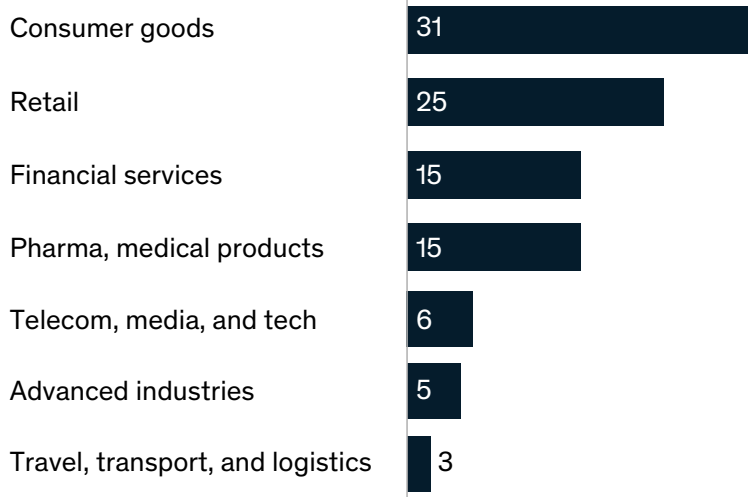
Respondents represented a wide range of industries and sectors.

195 executive respondents as of May 27, 2020



Industry

% of respondents



Function

% of respondents



Cost, cost, cost!

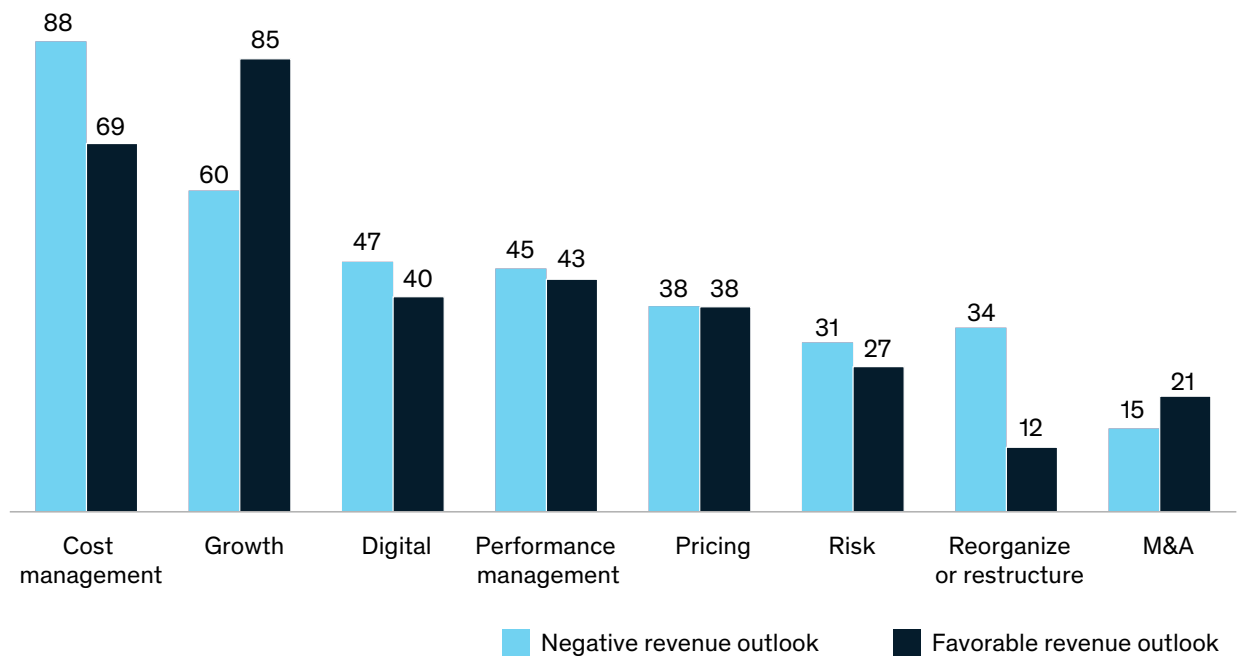
A majority of executives selected cost management among their top three priorities for the next 12 months, together with growth and digital transformation. This was true across industries, regardless of a company's revenue outlook (Exhibit 2).

Exhibit 2

Cost management is a top priority.

Top priorities for next 12 months

% of respondents including answer among top 3 priorities



The train is leaving the station, but lacks direction

Seven in ten organizations are already tackling SG&A efficiency and effectiveness. Another two in ten expect to launch initiatives within six months.

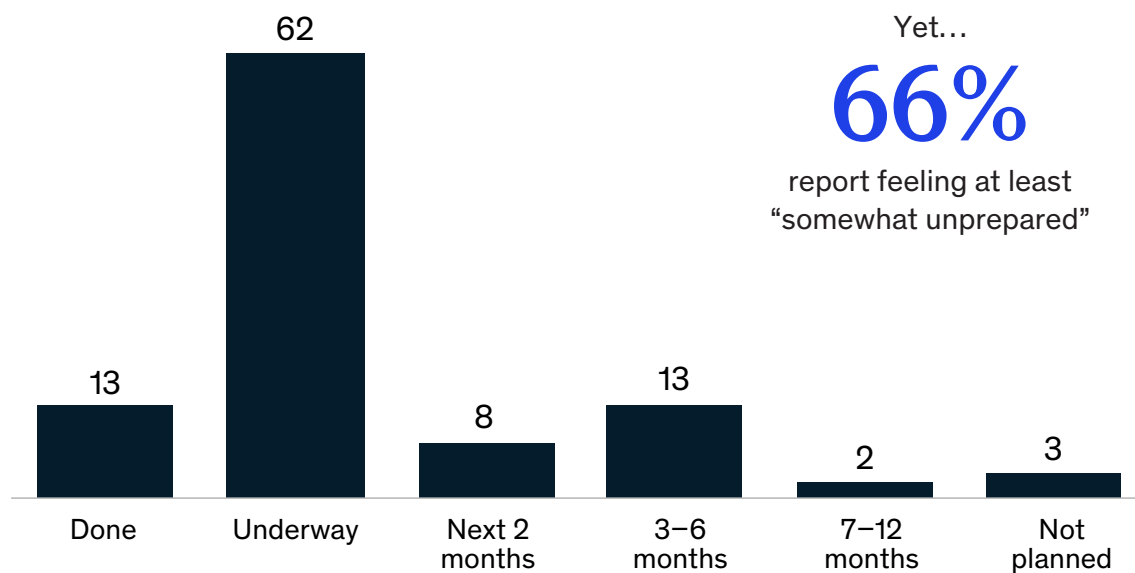
While actions have been set in motion, there is uncertainty around whether such programs can achieve success. More than 60 percent of executives reported feeling at least “somewhat unprepared” to meet SG&A improvement targets this financial year (Exhibit 3).

Exhibit 3

SG&A improvement programs have started, but respondents feel ‘unprepared.’

Timeline to launch SG&A improvement program as of May 2020

% of respondents



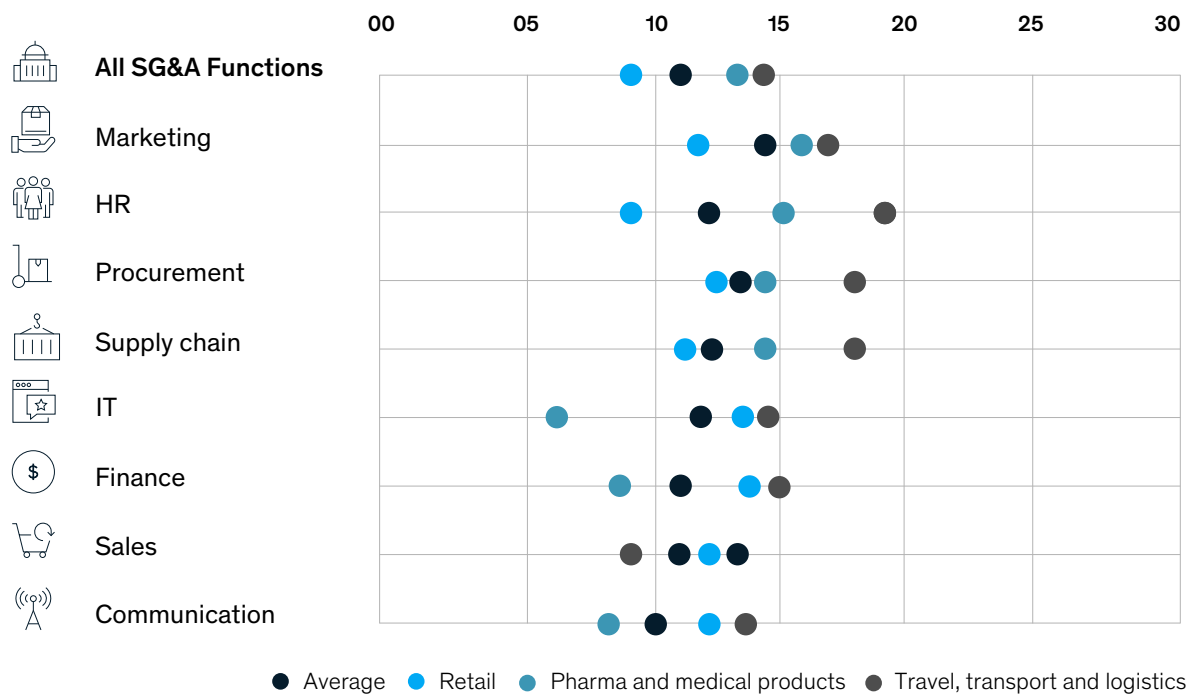
‘One size fits all’ targets are back—unfortunately

Most executives suggested all SG&A functions needed to deliver a 10-20 percent reduction across the board. This alludes to a mindset of “we need to control costs so everyone needs to chip in,” rather than a more surgical and thoughtful approach to managing spend (Exhibit 4).

Exhibit 4

Cost targets show high uniformity across functions.

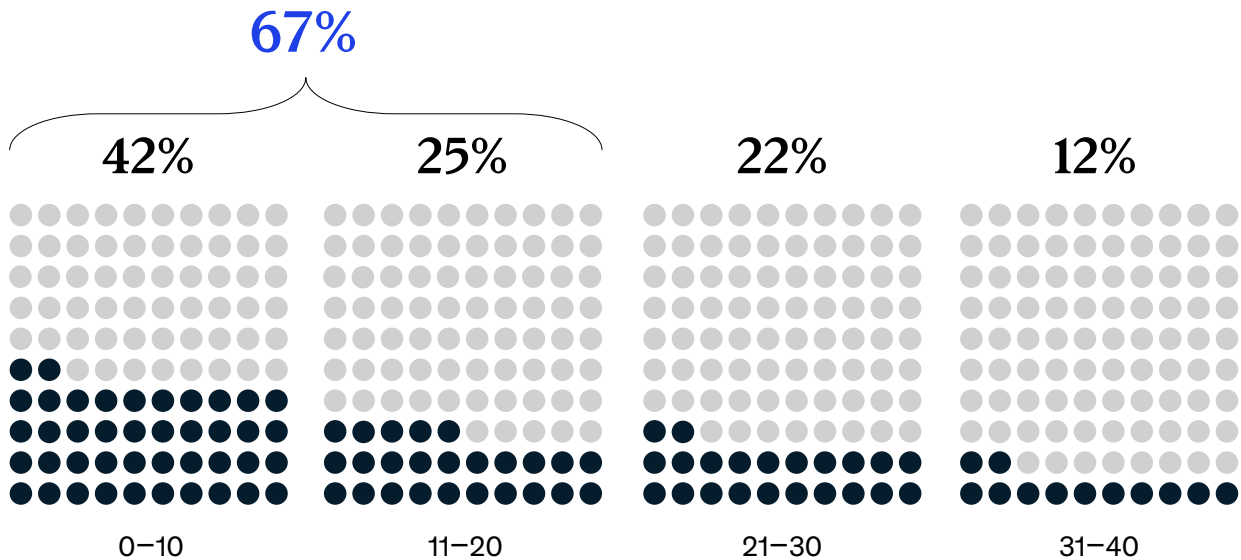
Target reduction in SG&A spend in FY20, % average among respondents



An analysis of individual responses shows 67 percent of executives had less than 20 percent dispersion—the difference between maximum and minimum assigned targets—across functions (Exhibit 5). In our experience, this uniformity tends to raise a dual challenge: leaving money on the table in some areas that could be compressed further, while implementing unsustainable reductions in others.

Exhibit 5
Across functions, executives report only narrow differences between highest and lowest cost targets.

Maximum dispersion of responses for individual functions, %
% of respondents



¹Difference between maximum and minimum assigned target across functions.

Reallocate, but how?

Our colleagues have previously shown that those organizations that regularly reevaluate where their resources are channeled create more value and deliver higher returns to shareholders.

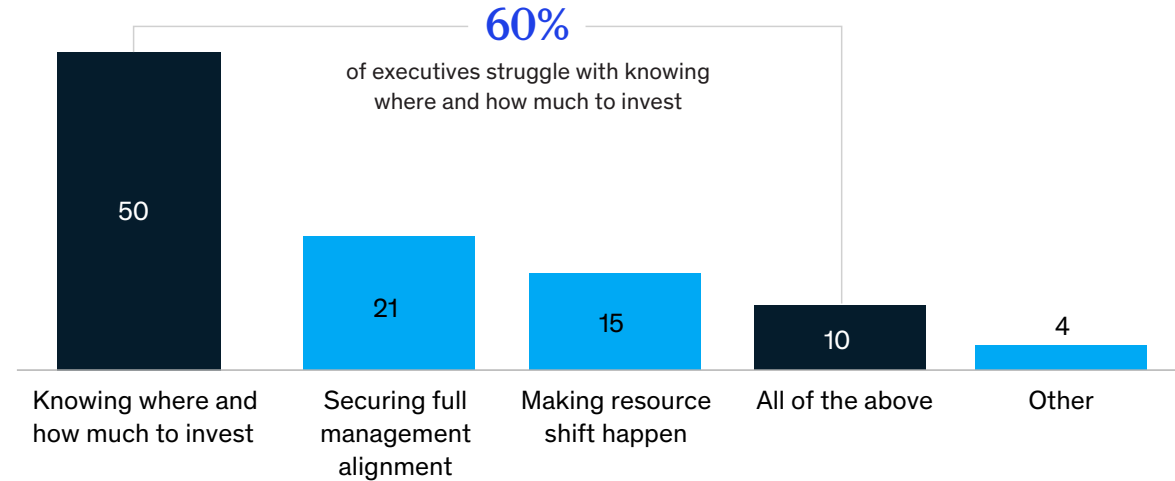
According to our survey, 70 percent of executives said they are good at reallocating resources—yet on the flipside, 60 percent find it difficult to identify where they can get the best returns (Exhibit 6).

Exhibit 6
Organizations face challenges in reallocating resources.

How would you characterize your organization’s ability to reallocate across functions?
% of respondents



What part of the resource reallocation process is most problematic?
% of respondents



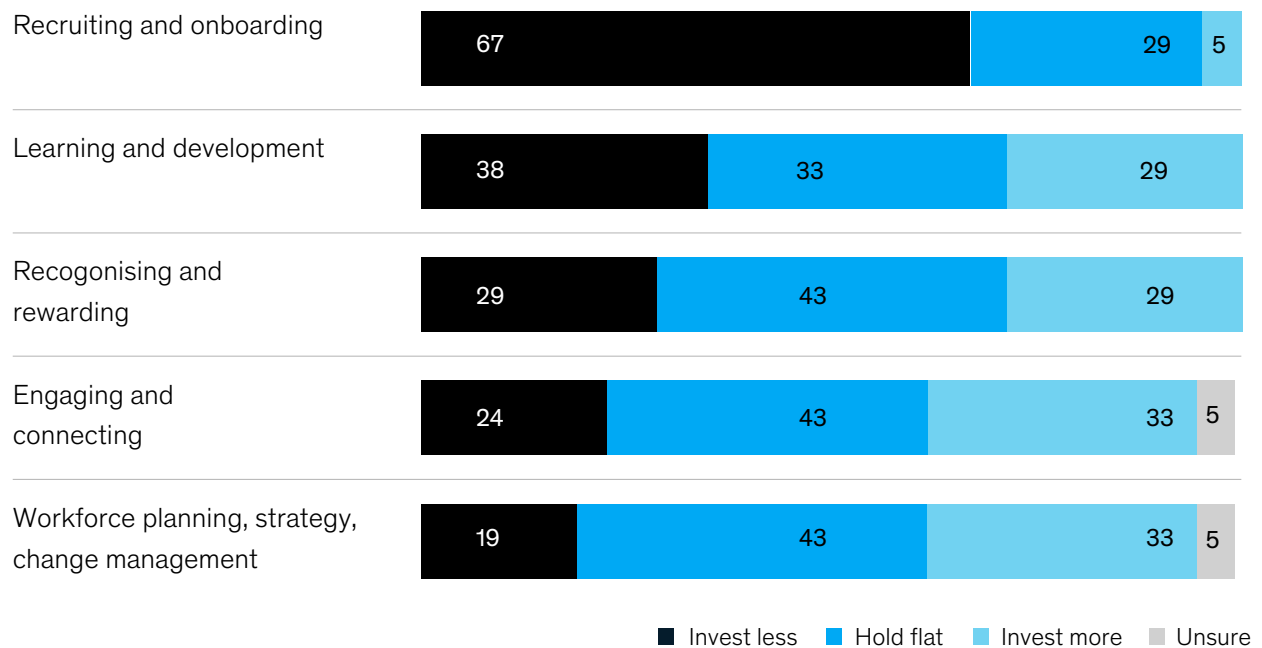
Not all activities are created equal

The survey revealed that 61 percent of SG&A activities are viewed as needing to have their investment levels adjusted. For example, in HR, organizations are reducing investment in recruiting and onboarding activities (Exhibit 7). At the same time, there is appetite for more investment in workforce planning, as well as in activities for engaging and connecting—perhaps explained by increased levels of remote working.

Exhibit 7

Within functions, companies are reallocating investments.

Expected change in spending over the next 12 months, % of respondents

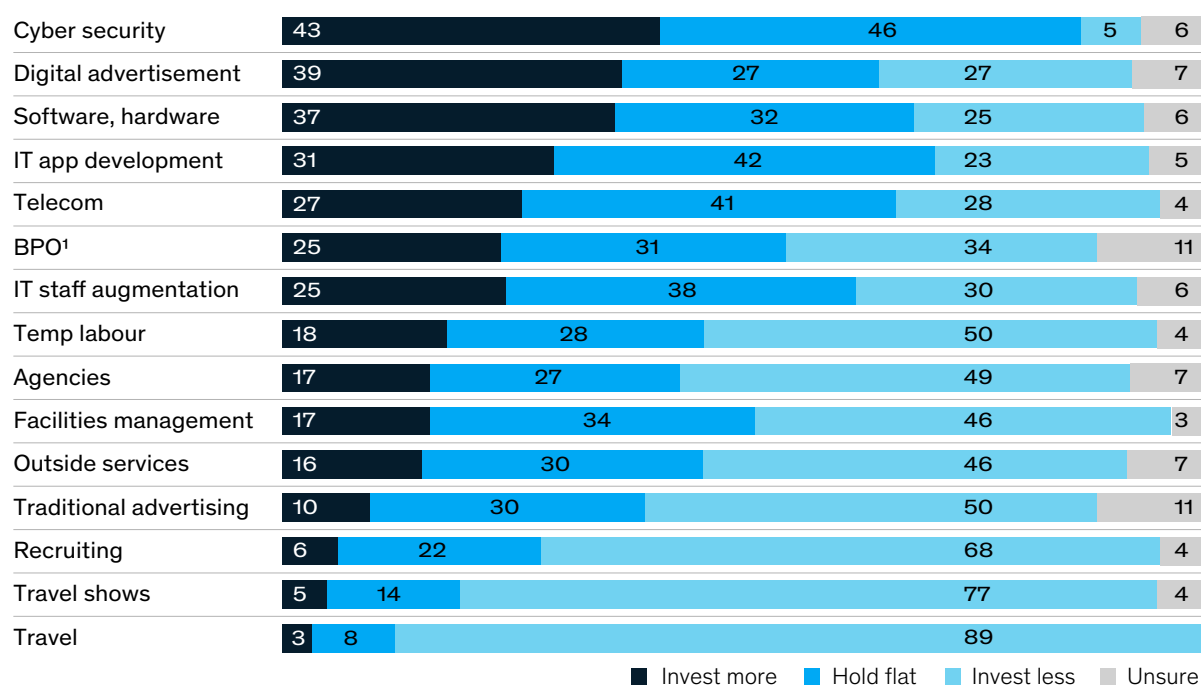


Similarly for indirect spend categories, there has been a dramatic reduction in discretionary spending such as travel, tradeshow, and outside services—some of which can be attributed to government policies and recommendations—while there is a push for more investments in areas such as digital advertising and cybersecurity (Exhibit 8).

Exhibit 8

Investments are moving across indirect spend categories.

Expected change in spending over the next 12 months, % of respondents



¹Business process outsourcing

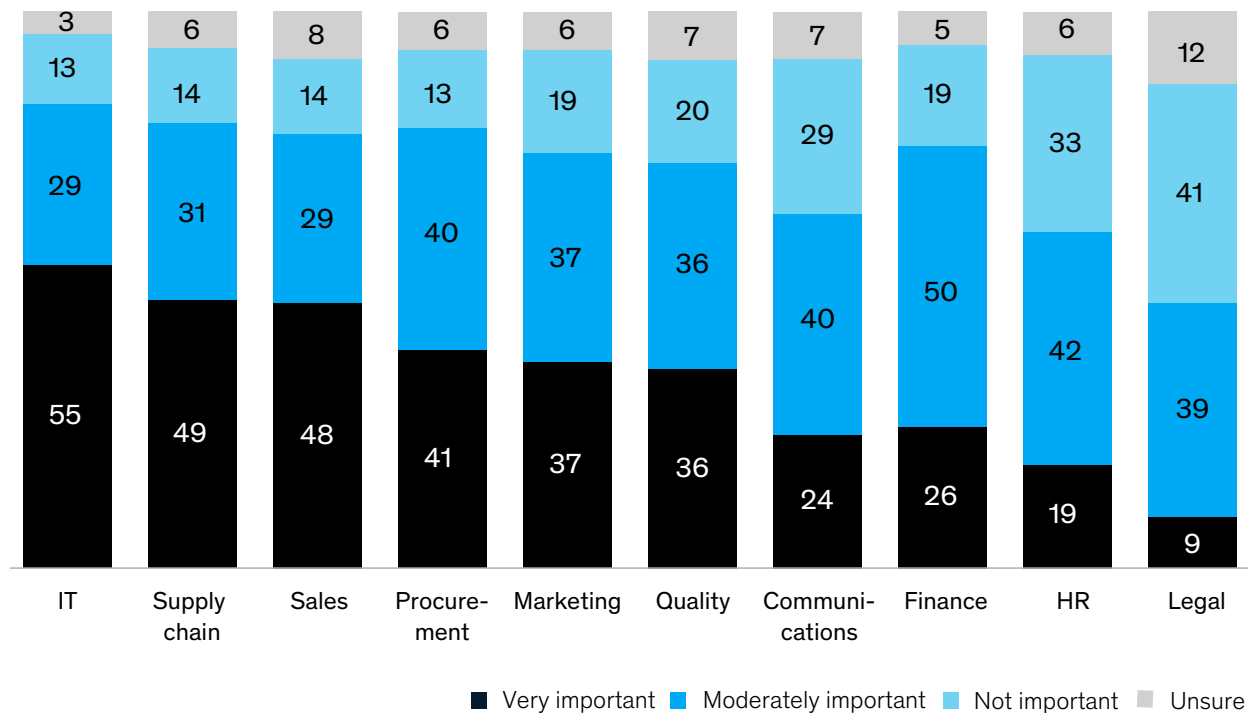
Skill them up!

Organizations must act fast to build up critical workforce capabilities to function in the post-COVID-19 environment. 72 percent of our respondents indicate reskilling as being moderate to very important for all functions—and particularly for IT, sales, and supply chain (Exhibit 9).

Exhibit 9

Importance of reskilling varies by function.

How important will reskilling employees be in this function?, % of respondents



From the survey results, it seems that organizations may be adopting a one-size-fits-all approach to improving the performance of SG&A functions. This can have a negative impact on productivity in the long run, resulting in resources that are spread too thinly across the business. Instead, saving and then thoughtfully reinvesting resources—such as by identifying and funding one or two breakout moves—can enable businesses to shift their SG&A spend from cost to investment, and focus for the greatest effect.

On the positive side, executives are rallying to address the challenges early and head-on, launching initiatives to optimize SG&A in the wake of the crisis. Also, a majority of SG&A activities are seen in a new light as needing their investment levels adjusted.

In the coming months, SG&A leaders will have to make tough spending choices that should be informed by where they are getting the most return for their resources. And finally, adapting employees' skills and roles to the post-pandemic ways of working will be crucial to building operating-model resilience.

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