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No middle ground: Reimagining G&A at midsize companies

Radically improved G&A functions aren't only for large organizations. Smaller ones can benefit too.

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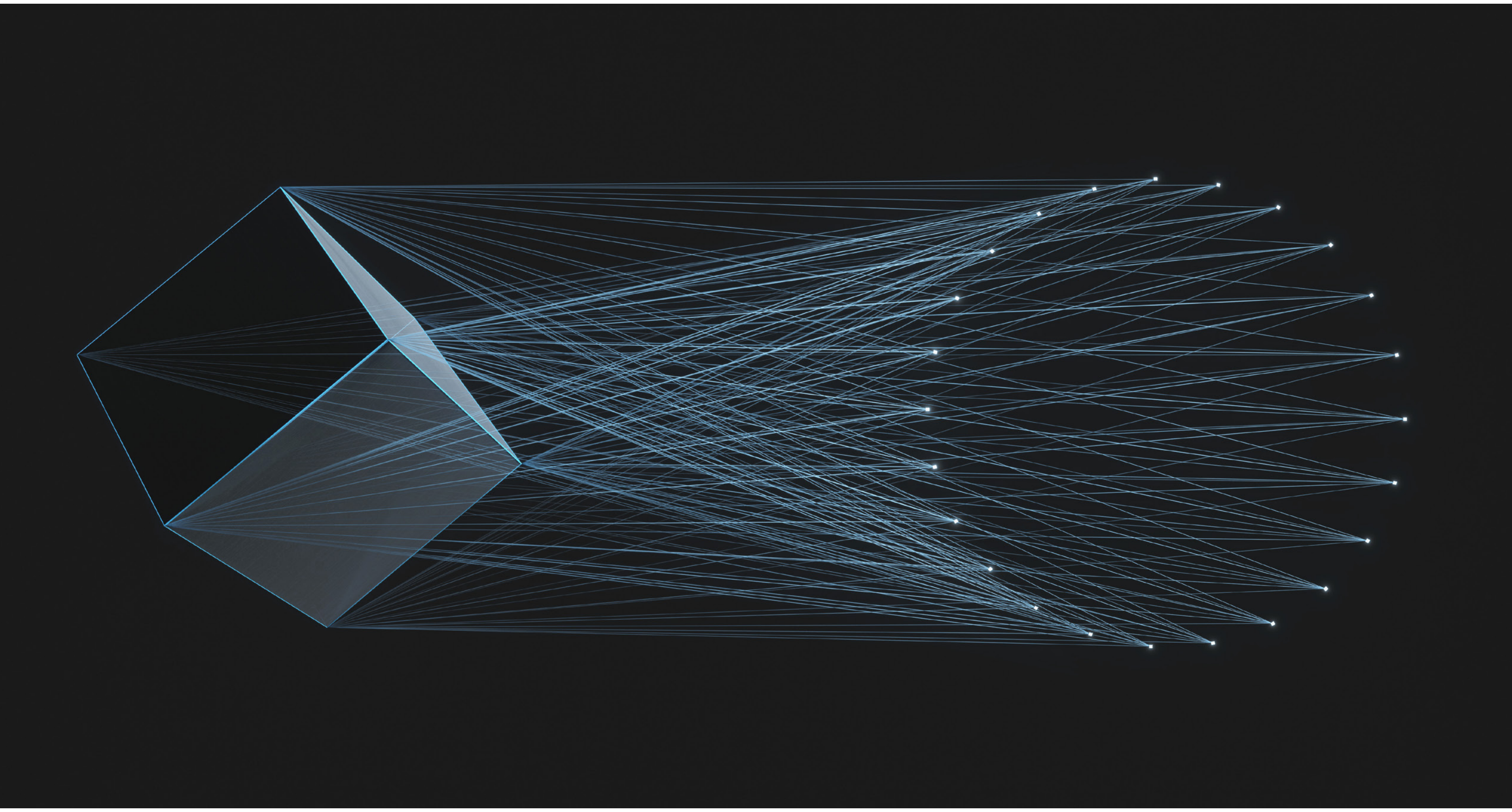

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As the next normal starts to emerge and a wave of change transforms the global economy, most companies have already looked hard at their general and administrative (G&A) structures and expenses,[1] long one of the first levers they pull to boost the bottom line and efficiency. In fact, our research shows that G&A can have a major impact on the performance of a company relative to its peers: across industries, a significant G&A efficiency gap of 4 to 8 percent of revenue, equivalent to 25 percent of market capitalization, separates high from low performers.[2]

Nevertheless, we find that midsize companies[3] hesitate to transform the structure and cost of G&A. Some of their CEOs assume that given the smaller scale of these companies, the payoff from restructuring G&A won't match the effort required. Others think that some obvious improvements, such as digital technologies and shared service centers, are out of reach for all but big corporations.

Yet our new analysis of more than 35 transformations at midsize companies across Europe and the United States shows that these organizations can make their G&A functions much more effective and efficient. In this article, we look at our findings through several lenses: establishing a great foundation, using it to address chronic inefficiencies, and unlocking new value through targeted digital interventions.

All companies need a great corporate center

A well-designed organization is the basis of any successful G&A transformation,[4] especially at midsize companies, where the smaller scale requires a creative approach to improvement. We have conducted research showing not only that organizational design accounts directly for more than half the value of G&A transformations at these companies but also that a solid G&A foundation supports all other aspects of their wider transformation. Our research found that two pillars support effective organizational design in midsize companies:

Strengthen the center. One of our findings was that such organizations should concentrate as much of their deep, high-value expertise as possible in the corporate center rather than individual units or countries. That also seems to be the prevailing view among executives planning for the next normal. Focusing expertise at the center may require companies to consider leaders who can "double hat"—in other words, provide expertise in two or more functional areas. Some companies, for example, combine the tax and treasury functions in a single finance-leadership role. At others, executives double-hat roles in both the corporate center and in regions or localities: a global automotive supplier, for instance, uses the corporate center's leaders of expert HR functions (such as compensation, benefits, and talent management) as business partners for geographic regions as well. That approach promotes not only constant exchanges among different parts of the business but also high levels of efficiency.

Embrace shared services—yes, even at this middling scale. The economic benefit can be more obvious for larger companies than for smaller ones, which may therefore consider shared services beyond reach. Yet our analysis suggests that this belief may not always be true: it showed that several companies with fewer than 200 full-time-equivalent (FTE) employees succeeded in making a viable business case for this approach and went on to improve both the cost and the quality of their services significantly. Companies that choose to create a shared service center can generate true value from investments in tech-enabled processes and tools. To strengthen the business case, use

[1] Steven Eklund, Heiko Heimes, Matt Jochim, Rowan Mawa, Carey Mignerey, Jung Paik, Rob Pepper, Abhishek Shirali, Megan Wells, and Ed Woodcock, "Reimagine: Preparing for SG&A in the next normal," November 5, 2020, McKinsey.com.
[2] Analysis of Capital IQ and S&P 1200 data.
[3] We define midsize companies as organizations with turnover of about €2 billion.
[4] Torsten Bernauer, Nathalie Bouvier-Tersiguel, Heiko Heimes, and Abhishek Shirali, "The corporate center: Driving the next normal," January 11, 2021, McKinsey.com.

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existing locations so far as possible and avoid adding new ones. When a European chemical company established its shared service operation for a large part of the accounting function, for instance, it built on an existing team in one of its Eastern European country units.

The current COVID-19 pandemic has underscored the ability of shared service centers to add significant value for midsize companies: vast employee populations across nearly all functions maintained or exceeded productivity expectations while working from home. A shared service center where employees work remotely can help enhance productivity not only in the center itself but also in the wider business.

Inefficiency in the organization: Midcaps are not immune

The core of any transformation of G&A has always been improving its processes and streamlining its capacity. Our analysis underscores the importance of these moves for midsize companies, where they account for more than 20 percent of a G&A transformation's value. For the CEOs of such companies, the message from this analysis is clear: if you sense inefficiency in the structure of G&A, trust your instincts.

Midsize companies, like large ones, find significant efficiency gains by first looking at what they do and then at how they do it. Two areas are especially important:

Begin with a service catalog. Our analysis shows that many midsize companies transform G&A by creating a service catalog listing the activities and services each function does and doesn't provide and then considering its scope of work. A US media company's IT department, for example, scaled back or eliminated low-value services by launching a service catalog and using it to hold effective demand and supply conversations with the business. Redesigning a service-catalog system also provides a critical look at current processes, identifies the overall capacity of resources, and helps prioritize critical applications and services. Reducing the level of resources and reengineering service levels can cut costs by up to 15 percent.

Similarly, leaders should ask whether service levels reflect the requirements of specific business areas. One organization's financial-planning-and-analysis department, for example, eliminated 20 percent of its ad hoc work and off-cycle forecasts by explicitly defining service levels and establishing a tiered support model that embodied its priorities. Users then had an incentive to request only essential services, and if they anticipated a need for ad hoc requests, they would preemptively shift to a more expensive support model. Some organizations have cut the costs directly associated with the processes that underlie services by up to 50 percent.

Optimize for now … and for the future. Midsize companies that successfully optimize their G&A functions go beyond obvious moves, such as eliminating waste and reducing variability. After clarifying the work that the G&A functions perform, successful companies have also used digital technology and agile work models to improve them.

Even targeted digital interventions can help

Just about all CEOs agree that "going digital" is important for the long-term success of their companies. Nonetheless, the leaders of many midsize ones may think that digital solutions are not appropriate for them. What's more, many organizations, large and small alike, have not yet implemented a number of important digital productivity enhancements in their back-office functions—despite their rapid digitization during the pandemic.

Our pre-COVID-19 research shows that digital G&A levers are a problem for midsize companies, where they contribute only some 7 percent of the value of a typical G&A transformation. Yet the digital contribution can be larger at some companies, which tend to progress along three horizons:

Take advantage of what you already have. Many midsize companies underutilize their legacy enterprise-resource-planning (ERP) systems. To leverage them better, such companies could enforce basic ERP hygiene (for example, a very limited number of applications) and create a consistent data hierarchy and structure. A mining company, for instance, liberated up to 12 percent of its overall HR effort by using its ERP system to automate time collection in the field.

Replace manual interfaces. Many midsize companies can realize substantial value by digitizing basic processes—for example, using macros, optical character recognition for accounts payable, and automated reconciliations. One company with less than 3,000 employees linked timekeeping systems with payroll and immediately cut the cost of managing it by 20 percent. (The savings included lower software-licensing costs thanks to a more homogenous IT environment.) This company also increased the accuracy of its reporting, lowered the risk of error, improved transparency and oversight, and made payroll cycles more predictable.

Adopt self-service. Midsize companies can improve their services and the bottom line by investing incrementally and focusing on the needs of the business, not on technology. Off-the-shelf solutions could be essential in these circumstances: productivity may rise significantly when companies use self-service tools, internally and for customers; advanced process-digitization systems, such as zero-touch accounts payable; and advanced analytics as a service for both the G&A functions and the wider business.

Our research shows that tried-and-true approaches to optimizing G&A can help midsize organizations realize many of the same benefits larger ones do. What's more, they can help the CEO of a midsize company improve its bottom line—and its pivot to the next normal—considerably sooner than it could without them.

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