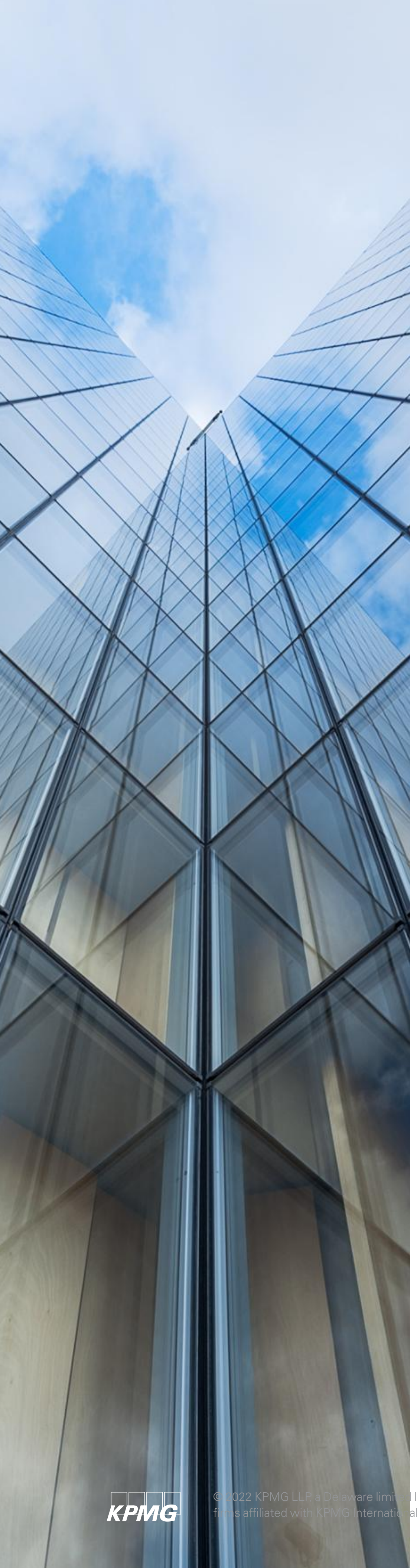
# Riding the wave

Building resilience from top line
to bottom line

**2022 KPMG Inflation Survey**

August 2022

kpmg.com



# How companies are adapting

Companies reeling from the COVID-19 pandemic emerged with only the briefest of respites before being beset with multiple new shocks. The Russia-Ukraine war added geopolitical risk to business considerations for the first time in years, aggravating supply chain disruptions and spreading tremors through energy markets. The prospect of slowing economic growth, and possibly recession, has clouded prospects. And, worse, inflation is at its highest rate in 40 years, with the Federal Reserve poised to raise rates at the fastest pace since the 1990s, increasing the cost of capital for businesses and consumers alike. For deeper perspective on inflation's impact on consumers, see the results of the latest KPMG Consumer Pulse Survey.

But much like COVID-19, this environment requires well-managed companies to creatively re-examine their business models, develop new strategies for accelerating top-line growth, mitigate the impacts to the bottom line, and plan for the kind of exogenous factors that can impact their business.

The extent to which firms change their behaviors and business models is something the Federal Reserve is watching closely, as is it an indicator of how entrenched inflation expectations are becoming. That is something the Fed is attempting to derail.

Executives are clearly responding, with a host of measures designed to weather the impact of rising costs to their businesses and strengthen their resiliency to these new shocks. In May 2022, we surveyed 300 chief financial officers (CFOs) and other financial executives to learn how they're managing the impacts of inflation. We asked about their plans in the weeks and months ahead as well as their inflationary response plan for further down the road. As inflation marches on, how much are they passing on to consumers? How are they managing wages? Are they increasing their technology spend? Rethinking their product suite? And how will they respond to the rising burden of servicing their debt?

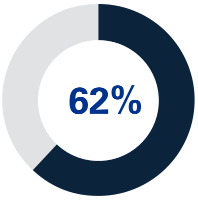
In short, we've learned how inflation is impacting strategic decisions and corporate behavior, with a view to:

1. Protecting the bottom line
2. Growing the top line
3. Planning for unpredictable external factors.

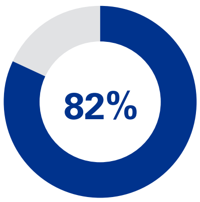
KPMG Economics offers timely insight intended to help companies across virtually every sector and industry make better strategic decisions with confidence. Visit KPMG Economics online for our current thinking.

**Please note that the data in all graphics appearing in this report are from the KPMG Inflation survey.**

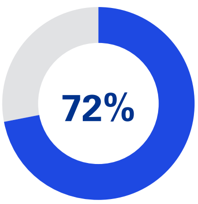
# Key data points



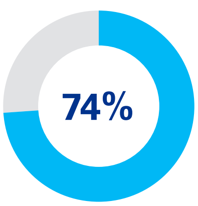

62 percent of respondents cite unforeseen geopolitical risks as the top organizational challenge in managing the impacts of inflation.



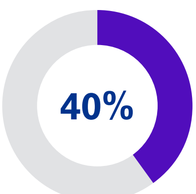

82 percent expect to raise prices at least at the rate of inflation (52 percent), if not more (30 percent), which suggests inflation may still have room to run



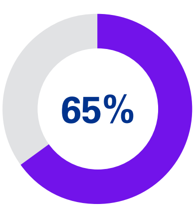

72 percent envision passing on price increases in three to six months, a high and very different figure relative to the data for small businesses overall, which are eating a lot of cost increases in their profit margins




74 percent are looking at right-sizing staff as a means of offsetting the impact of inflation.




Nearly 40 percent plan to allow all employees to work remotely to reduce real estate and related spending.




65 percent anticipate increasing their technology spend between 5 percent and 20 percent to mitigate inflationary impacts.

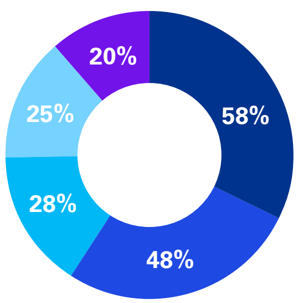
# What are organizations doing to minimize impact to the bottom line?

**Inflationary pressures are causing companies to re-examine business models**

With inflation at a 40-year apex, the Fed expected to raise interest rates at a pace not seen since the 1990s, real estate prices soaring, and businesses scrambling for workers, organizations are looking at strategies to insulate bottom-line income.

Nearly 60 percent of survey respondents reported that they expect to develop new and lower-priced products. Nearly half (48 percent) are considering reductions in force.

**How financial executives might change their business model over the next three to six months in response to inflation**




- Develop new products at new price points
- Reduce our number of employees (reduction in workforce)
- Modify our existing products (e.g., reduce functionality or features, etc.)
- Reduce the number of products (SKUs) available
- Operate in fewer markets

Note: Multiple responses were allowed.

At a time when consumer resilience is critical, the fact that companies might cut employees in the midst of a softening economy is concerning. A pullback in consumer spending, which accounts for two-thirds of economic activity, would dampen output.

**In the face of wage inflation, companies are focused on the right structure, size, and location of their workforce**

The fact that nearly three-quarters of respondents are looking to "right-size" staff is not surprising. A competitive labor market has pushed wages higher at a faster rate than we've seen in decades as companies vie for top, specialized talent. This surge in wage costs is less about people resigning and more about people switching jobs. Churn is costly. A large number of COVID infections in any given month is adding to staffing shortages in ways we never saw before the pandemic. Firms would be wise to look at ways to retain workers to minimize cost of churn.

Relocating large groups of employees is a growing phenomenon and more than half of respondents said moving portions of the workforce to less-expensive regions is a strategy they're looking at to offset wage inflation, not only today but also longer term as well. Companies recognize that they've got to have a presence where their employees want to be. It's a cost-saving measure for companies and helpful for workers because many are looking to move from high-cost urban areas like New York and San Francisco to lower-cost suburbs in the south and southwest.

**Strategies for offsetting the impact of inflation on increased wage costs—today and in a year**

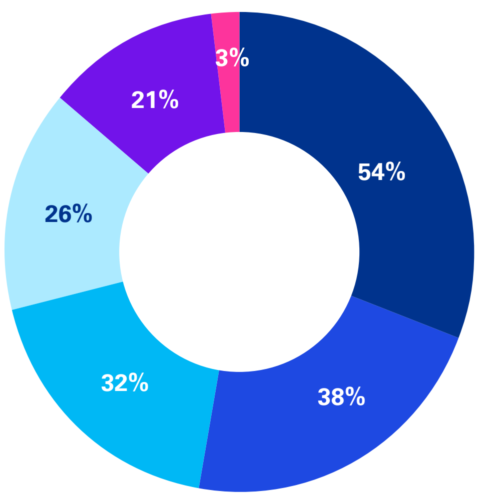
| | Today | In a year |
|---|---|---|
| Right-sizing staff | 74% | 67% |
| Geographic redistribution of work force to lower cost areas | 53% | 50% |
| Reducing nonsalary components of overall compensation | 47% | 37% |
| Outsourcing or offshoring work | 34% | 36% |
| Reduction of new hires | 37% | 13% |
| Other | 0% | 0% |
| Don't know | 0% | 1% |

Note: Multiple responses were allowed.

Companies are also looking to optimize their capital structures. The prospect of the Fed raising rates is inspiring many U.S. companies (54 percent) to explore refinancing or paying down debt earlier. They are reviewing their debt portfolios, and many (38 percent) are issuing shares to raise capital. Companies clearly want to reduce their capital spending to service their debt.

Issuing shares may be a strategy to raise capital while avoiding taking on more debt in a rising interest rate environment. Although issuing shares can be dilutive, it can be a stealth reward to key employees by increasing internal ownership at a time when many of these firms are reducing headcount.

### Amid rising interest rates, financial strategies companies are implementing to mitigate inflationary costs of capital




- Refinancing existing debt
- Raising capital via share issuance
- Paying down debt ahead of schedule
- Increased deployment of cash on hand for operational or strategic spending
- Issuing shorter term of debt
- We are not implementing any financial strategies specifically to mitigate inflat

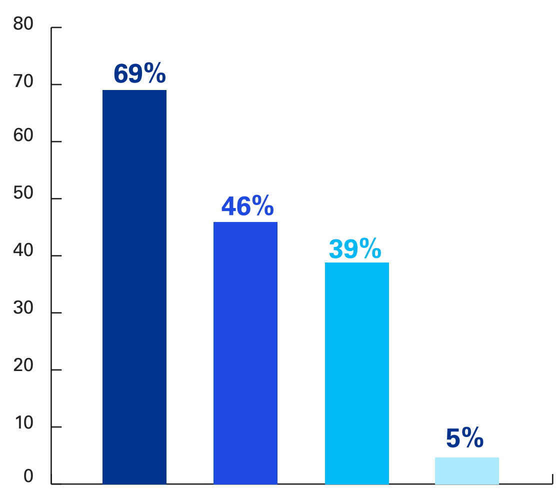
Note: Multiple responses were allowed.

### As real estate costs skyrocket, office space needs, configuration, and location are considerations for both HR and Finance

As markets soften, 69 percent plan to renegotiate current lease deals but stay where they are while 46 percent are considering alternate offices that are cheaper, either in the same area or in another geography altogether. Perhaps this suggests a pattern, considering 53 percent of respondents cited geographic redistribution of their workforce to lower-cost areas as a strategy for offsetting wage inflation. Companies can take even more off of their bottom line if they sell or reduce usage of lease-owned buildings.

Permitting employees to work remotely full-time indefinitely can save companies considerably in terms of overhead and supplies and cut workers' commuting time and save gas expenditures during an episode of heightened fuel costs. The fact that nearly 40 percent of respondents said they will allow a full-time remote structure is significant. It's unclear whether that is directly attributable to the impact of inflation or pressure from employees for more workplace flexibility, but this data point may portend an HR tipping point.

### Actions companies may take to reduce real estate and related spending over the next year




- Renegotiate existing leases
- Identify lower cost office space or geographies (e.g., energy efficient spaces)
- Allow all employees to work remotely full-time
- We are not taking any actions to reduce real estate spending

Note: Multiple responses were allowed.

# What are organizations doing to accelerate top-line growth?

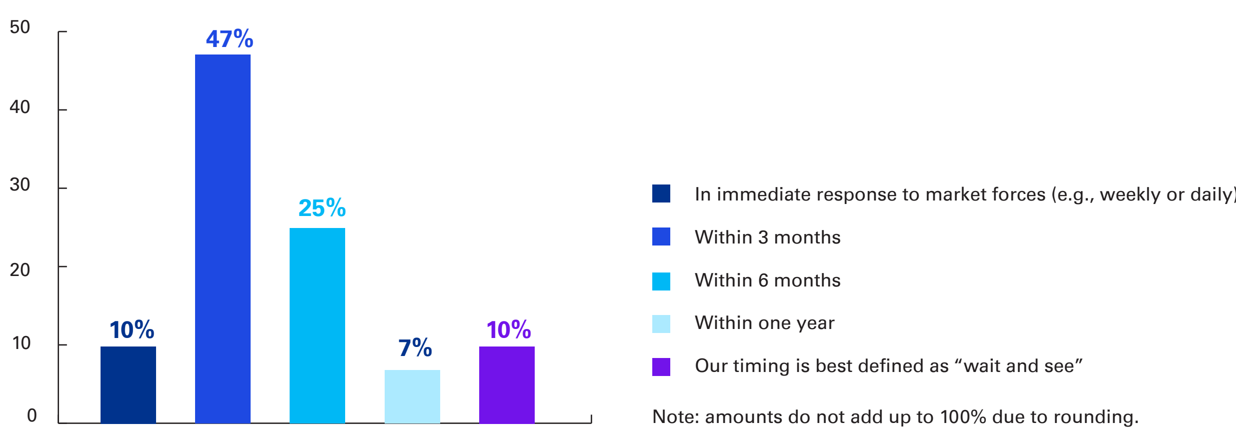
**If they haven't already done so, most companies envision instituting price hikes within three to six months**

Disruption is as rampant as it's ever been. U.S. consumer sentiment is falling across the marketplace. This is often the result of perception as opposed to data-based economic realities, but in today's market it's real and ultimately will impact behavior and spending.

How will this situation affect corporate behavior going forward? While 10 percent of respondents said they expected to pass on inflation-related cost increases to customers immediately, nearly three-quarters (72 percent) said they expect to do so within three to six months. This data reinforces the view that inflation may still have room to run. These trends may keep inflation from cooling as rapidly as the market would like.

Price elasticity—how demand for a product is affected by changes in its price—and the urgency with which it becomes apparent will be a harbinger of how well companies navigate these inflationary waters. Demand for an elastic product is particularly sensitive to fluctuations in price. As inflation ebbs, how much of the price decreases, if any, will be passed on to consumers? Nearly 60 percent of respondents may look to develop new products at lower price points in response to inflationary pressure in an effort to maintain or increase customer wallet share.

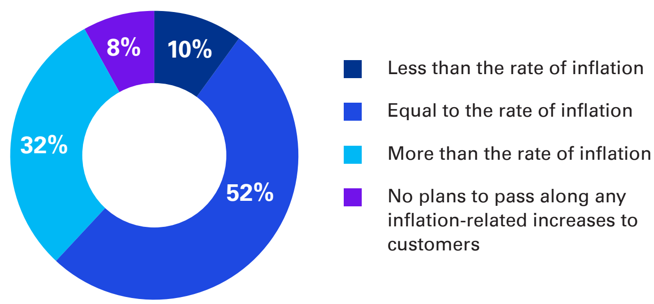
**The pace at which companies intend to pass on price increases to customers**




Note: amounts do not add up to 100% due to rounding.

Thinking further about how companies will respond to rising costs, 82 percent expect to raise prices at least at the rate of inflation, if not more (52 percent at the rate of inflation, 30 percent more than the rate of inflation).

**More than 80 percent of respondents expect to increase prices at or greater than the rate of inflation**



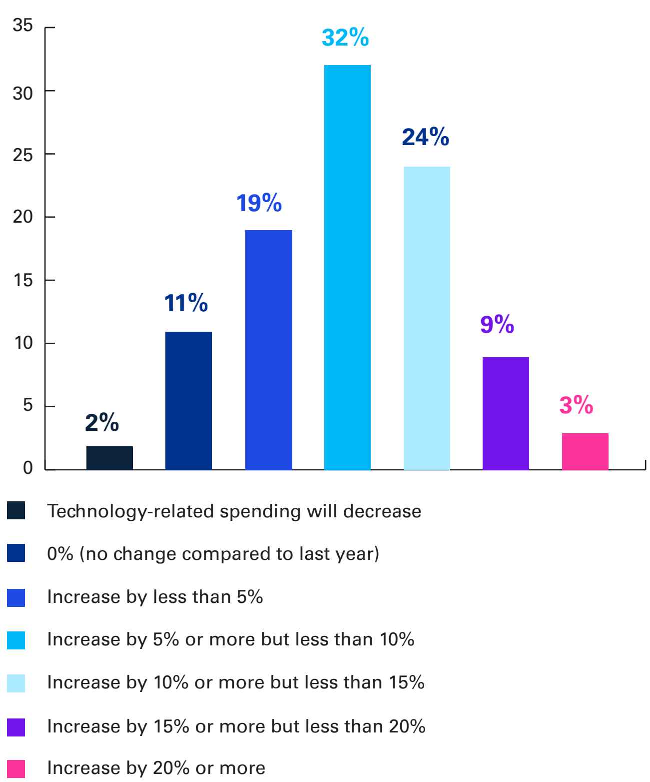

The question to which the marketplace is waiting for an answer is: How long can companies pass on the inflated costs of products and services before customers start to look for alternatives?

### With headcount reductions and right-sizing programs looming, companies expect to counter the potential hit to productivity with more technology

The vast majority of respondents (84 percent) expect to increase their technology spending by up to 20 percent. Similarly, 63 percent say they are gauging changes in customer reaction to inflationary increases through online/digital measurement of brand sentiment. This correlates with respondents' revelations about reducing head count (48 percent) and right-sizing staff (74 percent), which might suggest a focus on increasing efficiency by automating processes.

Indeed, emerging technologies such as artificial intelligence, machine learning, blockchain, and cloud computing will be vital inflation-fighting tools—worthy of increased investment—for automating back-office functions, providing seamless customer experiences and enabling organizations to build agile, data-driven operating models.

### Technology spending is expected to increase as companies look to mitigate the impact of inflation

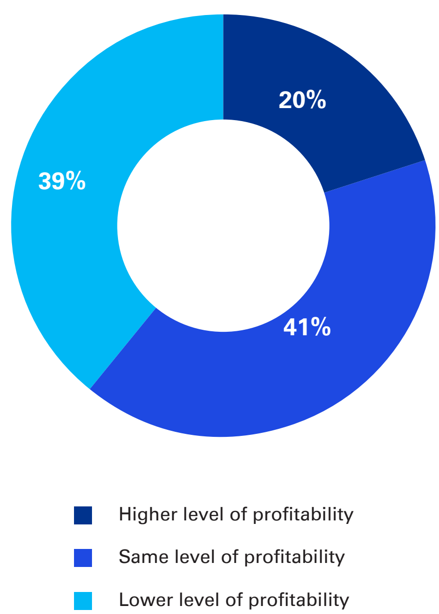



### Companies expect to remain profitable—good news for shareholders, perhaps less so for consumers

As consumer prices go up, so too go corporate profit margins. Not surprisingly, most respondents (61 percent) believe their companies will at least maintain the same level of profitability, if not higher levels, in the face of ongoing inflation. This was to be expected considering 2021 was the most profitable year for U.S. firms since 1950.[1]

These responses seem plausible considering the number of respondents that expect to reduce headcount (48 percent) while raising prices at or more than the rate of inflation (82 percent).

### Most companies expect to maintain the same or a higher level of profitability as they manage through inflation



# How are organizations preparing for and managing unpredictable external factors?

### New business models must be agile and adaptive to current and future challenges

At the beginning of 2022, we certainly would have anticipated supply chain woes and labor costs to be on a list of perceived inflation-driven corporate challenges—but we would not have expected geopolitics to be a major factor, let alone at the top.

However, in the wake of the Russian government's decision to invade Ukraine, 62 percent of our survey respondents cited "unforeseen geopolitical risks" as their top challenge. Clearly, companies are baking geopolitics into their risk and inflation scenario planning.

These results correlate with the Economic Policy Uncertainty Index, which remains extremely elevated.[2] The uncertainty that geopolitical risk has introduced dovetails with firms' ESG targets, which also affects their ability to retain and attract workers. The rapid investor exodus from Russia following its invasion of Ukraine was a rude awakening confirming how acute geopolitical risks have become.

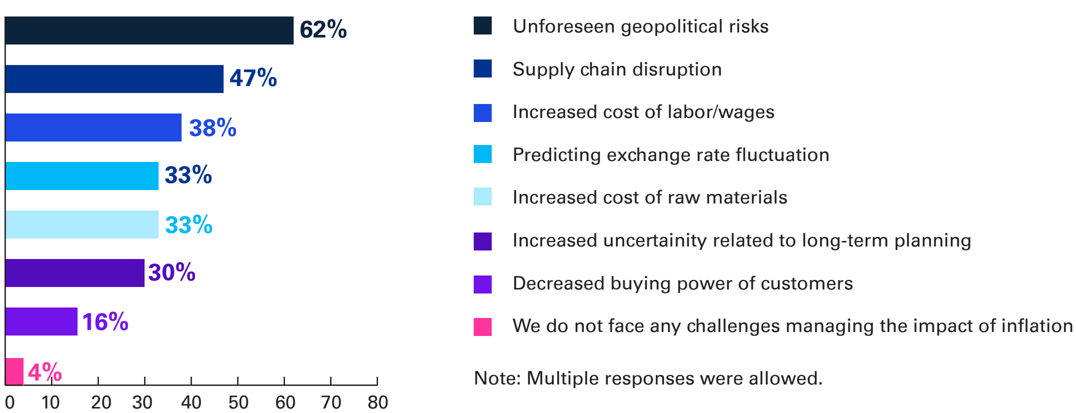
Supply chain disruption has been a clear and present challenge since the early days of the pandemic. For these survey respondents it remains top of mind, as nearly half (47 percent) say it is one of their greatest concerns in regard to managing through inflation. Russia's February 2022 invasion of Ukraine not only further complicated COVID-19-driven global supply chain issues but also exacerbated shortages of goods and natural resources at least through 2022 and possibly beyond, which in turn has amplified inflationary pressures.

As a result, U.S. businesses may want to consider on-shoring or near-shoring functions such as production, logistics management, and call centers, among others, to increase resilience to their supply chain network.

We believe the aforementioned new business models that many companies are pursuing must be both agile and adaptive to future developments. Beyond the fact that a decided majority of companies are devoting a significant portion of their thinking to latent risks—to the proverbial black swans—another interesting data point is the 33 percent that cited managing currency fluctuation risk as a top challenge. In that regard, spiking inflation in developed economies would tend to increase the volatility of global exchange rates, pushing down the value of currencies in countries with the highest inflation.

That one-third of respondents are concerned about exchange rate movements suggests that companies, particularly multinationals, are as concerned about the level of inflation outside the U.S. as inside and are unclear on how their domestic businesses will fare relative to their international subsidiaries.

### The biggest obstacles organizations face in managing the impacts of inflation




Note: Multiple responses were allowed.

# What's your next move?

**New business models must be agile and adaptive to current and future challenges**

As a historic geopolitical shock continues to roil the global economy, with the effects of a historic public health crisis still in play, corporate leaders must plan now for an uncertain future. Rather than wait and see, companies are encouraged to consider a range of possible scenarios to shape their own future. However uncomfortable, thinking well ahead of events still unfolding will ultimately be the less risky path than reacting—and potentially overreacting—too late.

Amid this uncertainty, there is a broad array of powerful strategies firms can employ to organize their thinking, align responses, and swiftly initiate appropriate actions.

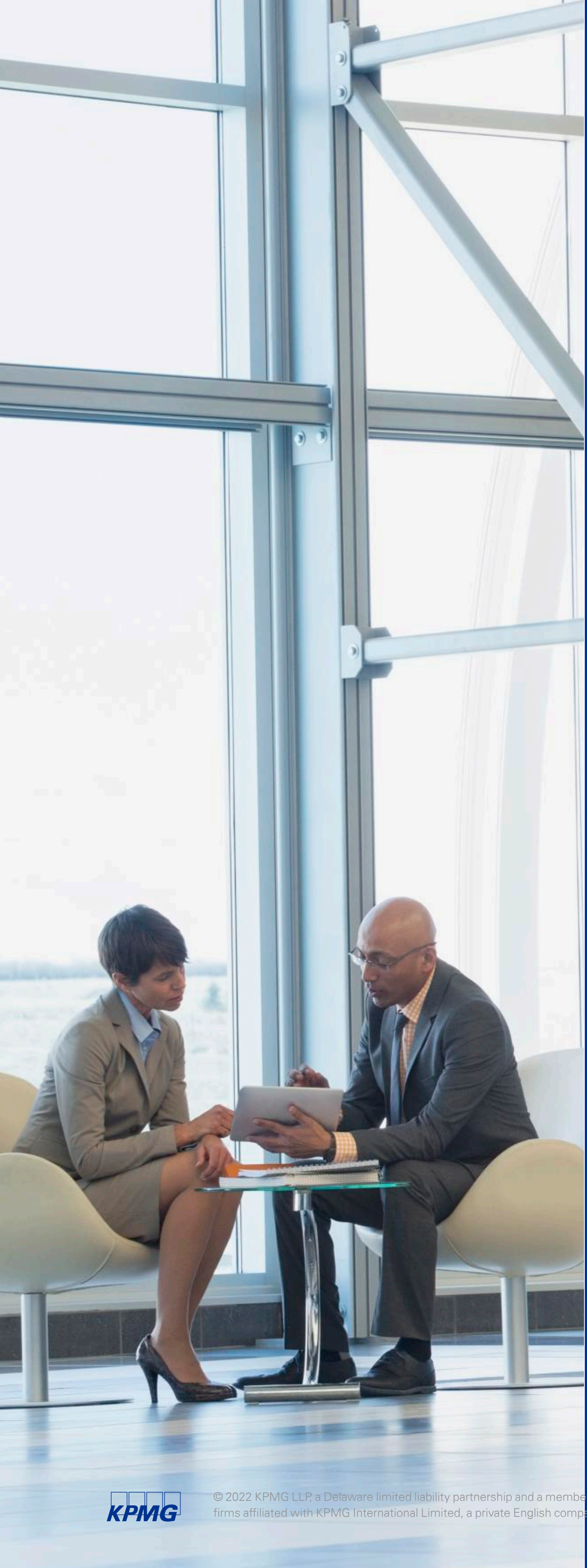
**Action steps for building operational resilience in today's inflationary environment**

- Enable a connected enterprise that is flexible and agile to adapt to both demand- and supply-side changes.
- Leverage digital capabilities to institutionalize decision-making based on data-driven insights across the enterprise.
- Establish a digital-first mindset to engage with employees and ecosystem partners to enhance retention and institutionalize business process knowledge.
- Explore strategies for improving on the transparency and integrity of data.
- Seek to optimize the workforce and enhance talent across the organization; acquire new talent where necessary and upskill/reskill where feasible.

---

[1] Bloomberg, Profits Soar as U.S. Corporations Have Best Year Since 1950, March 30, 2022.

[2] The Economic Policy Uncertainty Index measures policy-related economic uncertainty based on three underlying components: The first quantifies newspaper coverage of policy-related economic uncertainty; the second draws on Congressional Budget Office reports that compile lists of temporary federal tax code provision; and the third draws on the Federal Reserve Bank of Philadelphia's Survey of Professional Forecasters.



# How KPMG can help

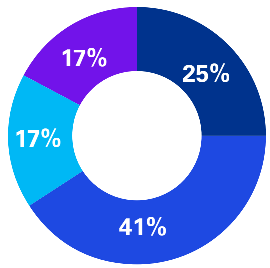
In a rapidly changing marketplace, the finance function has a key role to play in delivering efficiency, insight, and value to the business. The introduction of new technologies, increased volumes of data, regulatory changes, and the need to deliver more for less add to the pressure on CFOs and finance directors. Finance functions must pivot from transaction processing and reporting towards strategic business support to drive profitable growth, reduce costs, and assume a broader set of strategic responsibilities within the enterprise.

The Finance Transformation practice at KPMG supports the full agenda of the CFO. We help strengthen the performance of the finance function by focusing on the questions that global finance leaders tell us are their priority, including:

- Evolving the finance operating model to meet future needs of the business
- Increasing focus on value creation
- Assessing the skills and capabilities that are required for the future, and how to best access them
- Turning data into actionable insights for performance management and capital allocation
- Improving on the transparency and integrity of data/information
- Using digital solutions and analytics to enable profitable growth
- Creating a more cost-effective and resilient finance function
- Establishing and meeting ESG targets considering the potential impact on priorities such as hiring, pricing, margins and climate change

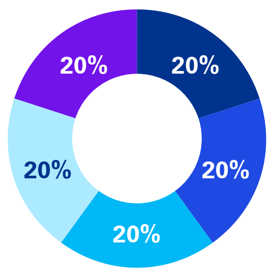
# Survey demographics

**Respondent roles**



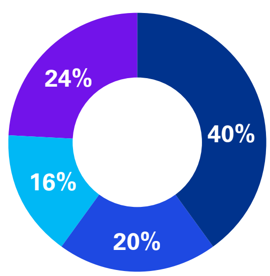

- Chief Financial Officer (CFO) or designee
- SVP/VP/Director/Department Head of Finance/Accounting
- Comptroller
- Treasurer or designee

**Industries represented**



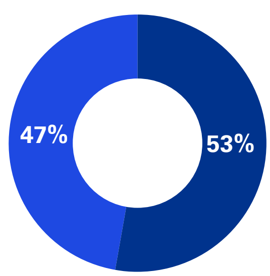

- Industrial Manufacturing
- Consumer and Retail
- Banking
- Insurance
- Energy, Natual Resources, and Chemicals

**Firm annual gross operating revenue (current fiscal year)**



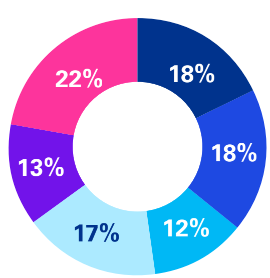

- $500 million to $999 million
- $1 billion to $2.49 billion
- $2.5 billion to $4.99 billion
- More than $5 billion

**Firm revenue U.S. versus non-U.S.**




- U.S.
- Non-U.S.

**Firm assets under management**




- Less than $10 billion
- $10 billion to $49 billion
- $50 billion to $99 billion
- $100 billion to $249 billion
- $250 billion to $499 billion
- $500 billion or more

# Meet the authors

**Prashanth Brindavan**
**Principal, Advisory**
**Finance Transformation**
**T:** 949-885-5437
**E:** pbrindavan@kpmg.com

**Yash Acharya**
**Managing Director, Advisory**
**Finance Transformation**
**T:** 212-954-2125
**E:** yacharya@kpmg.com

Some or all of the services described herein may not be permissible for KPMG audit clients and their affiliates or related entities.

**kpmg.com/socialmedia**