INSIGHTS
SERIES

SAVANNAH MARKET INSIGHTS

Leadership for the 'Next Normal'

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MARKET INSIGHTS

Leadership for the 'Next Normal'

Over the past six weeks we've held hundreds of conversations with board members and senior executives across a range of sectors and industries during phase one and the early part of phase two of the coronavirus crisis. This document summarises key themes, concerns and forward plans from those conversations.

The three phases we've seen so far:

1. REACTING:

- Re-evaluating cashflow and liquidity – trimming budgets
- Understanding impact on sales and operations
- Examining supply chain
- Moving to remote working and furloughing staff
- Internal and external comms

2. STABILISING:

- Adjusting commercial focus and operations
- Further cash saving measures introduced
- Understanding regional impact
- A focus on employee engagement and wellbeing support
- Financial modelling/scenario planning
- Evaluating post lockdown emergence

3. PLANNING:

- Now that we are leaner, how do we avoid becoming bloated again?
- How can we emerge stronger?
- How do we capitalise on what we're learning now to be better than our competitors?
- How do we re-start operations and get back to pre-pandemic levels of output/ sales?

LEADERSHIP CHALLENGES

LEADERSHIP

- There is "no leadership manual for this" according to a CEO in the Hospitality, Travel & Leisure sector, "so good and bad leaders are being exposed in equal measure and everyone is learning on the job". This has never been truer than in today's increasingly volatile, uncertain, complex, and ambiguous (VUCA) business environment.
- One Chairman described his CEO recently as a "process-monkey" but not a strong leader.

We expect there will be other Chairmen and Shareholders out there who share similar thoughts about their CEOs and also numerous CEOs who have been underwhelmed by the performance of some of their direct reports through the crisis.

- The consequence of this will be significant levels of executive change in late 2020 and early 2021 as businesses emerge from the economic effect of the crisis and transition to the 'next normal.'

The three critical leadership dimensions that the crisis has brought strongly into focus – and which we believe will increasingly be required in future – are as follows:

1. Breadth of experience

When there are no precedents for the challenges faced, the best-equipped leaders are those with a diverse set of skills and a breadth of knowledge gained through wide and varied career experience – different companies, sectors, functions and geographies all add to the mix. This allows them to draw on multiple reference points to develop new strategies and actions when there is no existing playbook. Conversely, those who have climbed narrow career ladders – no matter how rapidly – now find themselves lacking that breadth of experience to draw on.

2. Agility and adaptability

Rapidly changing business environments and unprecedented challenges require agile leaders, able to quickly adapt to changing situations, and to switch back and forth between setting strategic direction and overseeing operational implementation. A 2015 Harvard Business Review study found that only 8% of executives are highly effective at both developing and executing strategy. Those 8% are worth their weight in gold right now.

3. Empathy and engagement

The most effective executives today have a natural and authentic leadership style that includes the humility that Jim Collins associates with 'Level 5 Leaders', together with a high degree of empathy and strong moral compass that ensures that they remain true to their values, even in adversity. These enable more effective leadership through influence and persuasion, rather than the 'old school' command and control approach that is increasingly at odds with the challenges of uniting disparate groups of stakeholders in uncertain times.

Ultimately, exceptional leadership is an art, not a science, and we cannot entirely codify it any more than we can bottle and sell it. Nevertheless, recent experience has shown that the leadership traits outlined above correlate strongly with the most effective executives – not only now in times of crisis, but for the 'next normal' that will follow.

HIRING

- The slow-down in full time executive hires has been somewhat balanced by an increase in hiring executive interims to help with crisis management or bring in new skill sets.
- Existing assignments have become more difficult to deliver due to candidates dropping out – not wanting to leave their company in the lurch at a difficult time. It's been interesting to see the moral responsibility many have felt to their business and their colleagues at this time, even though they were previously considering leaving.
- Most businesses have been happy to switch to video interviewing through the process, but there is still a desire for final stage interviews to be completed face to face. The UK seems to have a particular issue with this. Businesses in the rest of Europe have been happier to hire for executive positions entirely remotely.

RETENTION

- Several PE houses mentioned needing to re-calculate compensation schemes for senior management within their portfolio businesses in a bid to keep them engaged. Unless they do this, and even if they do, many CEOs and their teams might decide they don't have the appetite to work another 3-5 years on a deal that may now have a smaller prize.
- Boards and HRDs are concerned about furloughed staff potentially losing their connection with the business and with it their loyalty to the company. There will likely be high movement as people either aren't asked to come back or have used their time off to reflect and decide that they want to take their career in another direction or try and move into an industry that is seen as more stable.

THE MENTAL HEALTH AGENDA

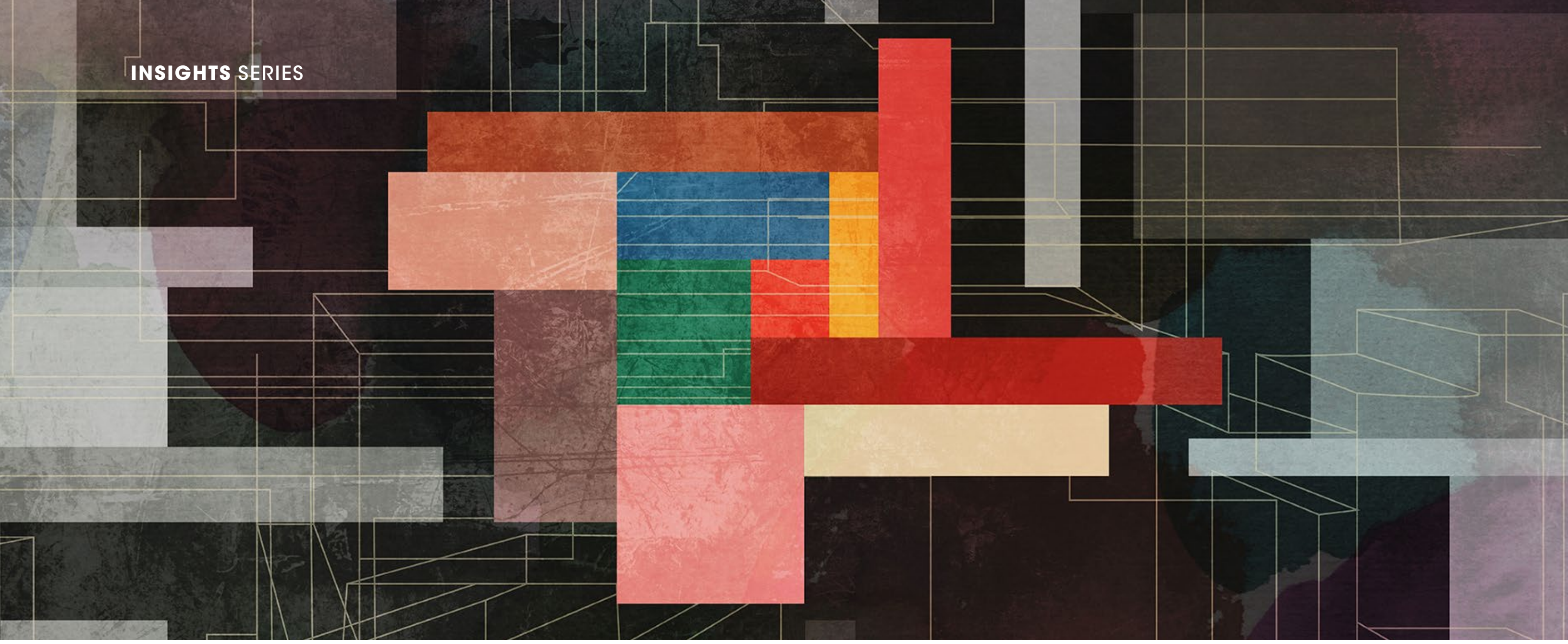
- Mental health comes up regularly – there are serious concerns among executives about the mental health of both furloughed and active employees and their individual worries about family and financial security resulting from the uncertain outlook.
- HR leaders are discussing subjects including remote psychological safety and tracking and surveying what is happening to people whilst managing the variances in workforces across life stages and settings. Many are looking at what digital platforms are available to assist in this. Some are seeing mental ill-health peaks in new populations such as older employees struggling with issues around isolation and loneliness, middle-aged men, working parents and leadership teams.
- There is a new focus on Learning & Development, both work related for those still in the business and non-work related for those on furlough, to try and keep everyone engaged - using the time to look at one or two aspects of personal development.

MACROECONOMIC ENVIRONMENT

NEW WAYS OF WORKING

- According to an Industrial sector CEO, "following VUCA and the new normal, we're now moving into the 'next normal' – a blend of the virtual and physical worlds."
- For the digital natives or organisations who have invested in digital systems their transition was very smooth. They experienced a drop in productivity over the first few weeks as people struggled juggling children and families but that soon picked up.
- For people still working, with no commute and less to do in the evenings the workday has got longer. One study showed that on average Americans are working 3 hours longer per day and the British, French, Canadian and Spanish are working 2 hours longer per day on average.
- A FTSE 100 chairman commented that many people are missing the social element of the workplace and everyone working from home all of the time is not viable. Equally neither will being in the office 5 days per week. Following significant investment from businesses in collaboration technology (Zoom, Teams, Hangouts, etc.), expect an acceleration within the VR/AR space to allow fully immersive virtual meetings.

- Almost every chairman and board member we have spoken to say their boards are working effectively with video technology but predict some quick changes to company law to allow fully virtual AGMs.



LIFTING RESTRICTIONS

- Even though lockdown restrictions are starting to be relaxed, most leaders still can't see how they can be practically managed. An executive at a Management Consultancy noted that because they occupy an entire high-rise office building it would take eight hours just to get staff up the elevators to their desks if social distancing is adhered to.
- Many executives are concerned about their furloughed staff and, in particular, how to bring people back from furlough, make them feel like an essential part of the team going forward whilst trying to rapidly scale the business back to pre-crisis revenue levels and not running out of cash.
- As many board members (chairmen in particular) tend to be in their senior years, there is considerable personal concern about continued confinement.

MACROECONOMICS AND GLOBAL BUSINESS CHALLENGES

- A new global dynamic, an emerging cold war with China and a collapse of free-market capitalism are all themes of many high level conversations.
- One repeated concern is the real impact of the medium/long-term reduction in consumption caused by lower incomes, higher unemployment and business failures. A drawn out process of lifting restrictions and prolonged social distancing rules will add to the recessionary pressures. Structural changes already underway in some sectors (e.g. automotive) are exacerbated. Commodity sectors will suffer.
- It's still yet to be fully understood what the knock-on effects will be in the value chain. Suppliers to the Industrial and Leisure sectors are concerned. It's become clear how interconnected our economy is, and significant falls in demand in one industry for a sustained period are sending ripples through all the suppliers of products and services to that industry and in turn, to all the suppliers of those suppliers and so on.
- It's still unclear what the full implications of prolonged lower profit/lower dividend from the big corporates will be, in particular oil companies, and the geopolitical re-alignment.
- Some regions are doing better than others. The Far East is doing well, and we've had several CFOs say they can see growth in Scandinavia. "Asia is booming but the UK is dead" said one.

CASHFLOW, MARKETING & COMMERCIAL

BRANDS BECOMING MORE HUMAN

- What will a brand be remembered for after the pandemic? Direct communications are now coming from the CEOs of businesses and COVID-19 has turned Maslow's hierarchy of needs on its head. Brands are shifting their messaging onto the lower layers of the pyramid. For the foreseeable future messaging that appeals to physiological needs (such as food, water, clothing, wellness), safety and security (health, employment, property, family) and love and belonging (friendship, family, intimacy, sense of connection) – rather than lofty aspirational messages – will be prioritised.
- How do your customers perceive your business performance? With some companies under pressure and experiencing big delays, will long term customer confidence will be hurt?

SALES RECOVERY

- It's clear that doing the same thing that we were before isn't going to work. Some PE houses are telling us they have instructed portfolio businesses to forecast no new sales for 6 months and assess liquidity needs to keep trading. They are asking what investments are needed in marketing and technology to get back to pre-pandemic levels of sales.

> "It's clear that doing the same thing that we were before isn't going to work."

CASH & LIQUIDITY

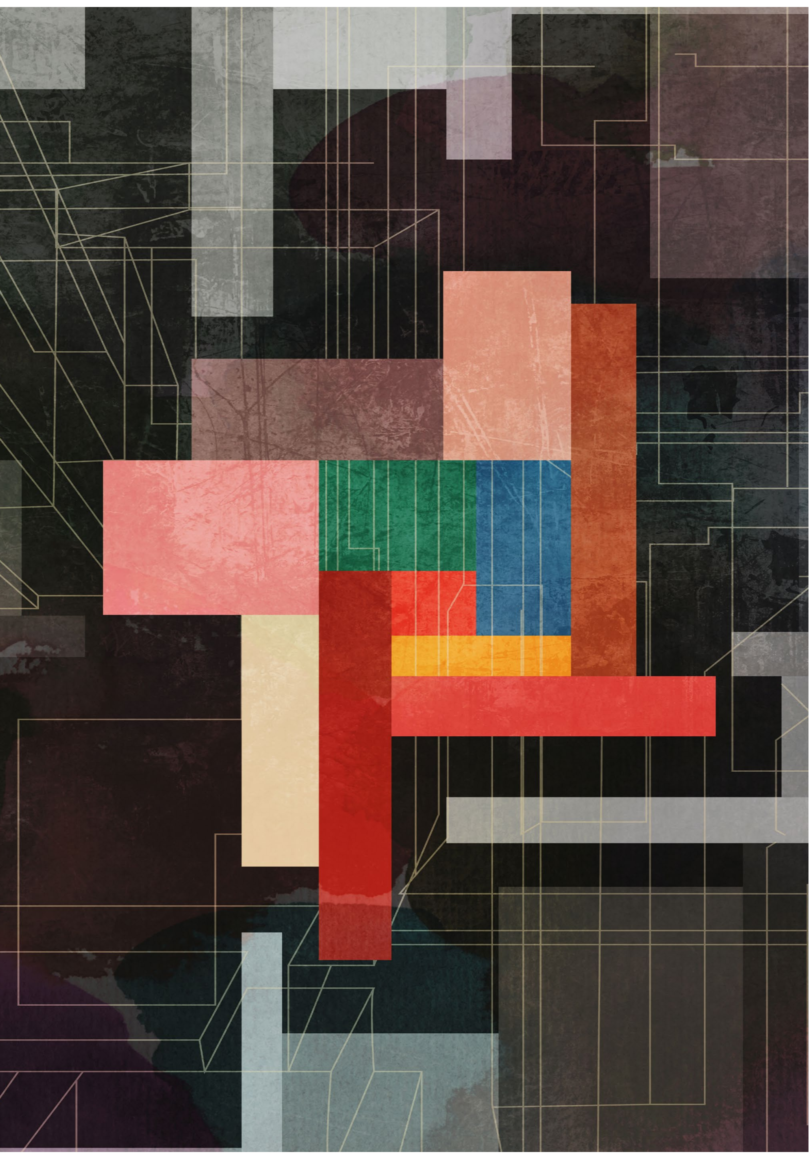
- The expected call for cash and liquidity specialists within PE portfolio companies is lower than expected, largely due to the effectiveness of the Government furlough scheme and deferrals on some tax payments. Many see this issue across their portfolios as a time bomb with the true cash hit to the businesses expected in Q3, Q4 and end of Q1 2021.
- Many executives in multi-site hospitality organisations (pubs, restaurants, gyms, etc.) think this is the calm before the storm. Being mothballed, they can conserve cash, but as soon as they open, everyone will expect to be paid i.e. staff, landlords, suppliers, HMRC, etc. Given the impact of prolonged social distancing, it'll be challenging to get enough people through their doors while remaining profitable.
- High Street landlords are already worried about non-payment of rent in Q2 and Q3 as a result of retailers (hairdressers, independent shops, restaurants, etc) not wanting to open at less than full capacity.
- Many CFOs are using the current climate to clamp down on expenses and are trying to engineer a change in culture around work spending. Some also think this will be reflected in people's personal spending and discretionary expenditure will be constrained with the consequential flow-on effects.

MERGERS & ACQUISITIONS

- Consolidation and privatisations in some sectors (e.g. oil& gas) are on the cards. More broadly, there is a focus on opportunities to acquire businesses impacted by the pandemic at lower cost. Revaluations are a big topic in the M&A world. M&A activity is expected to accelerate but with a new base point for valuations.
- Among deal side PE firms, there is a view that any organisations that has undertaken big M&A deals recently or are highly leveraged will struggle, particularly if they are in the most heavily impacted sectors such as hospitality.

> "There is a focus on opportunities to acquire businesses impacted by the pandemic at lower cost."

PEOPLE, OPERATIONS & INFRASTRUCTURE



TECHNOLOGY, SECURITY & INFRASTRUCTURE

- CIOs and CISOs are reporting an explosion in phishing emails linked to the furlough scheme, business loans, etc. and the opportunity for data loss has increased exponentially with many organisations reliant on employees using personal laptops and gateways that are constantly probed leaving organisations open to attack.
- There is an opportunity to reduce the fixed costs of offices as there is less of a need for every person in the business to have a desk, but organisations will need to invest in their technology, moving to the cloud, moving from desktops to laptops, using cloud-based apps for finance, call centres to improve accessibility and improving the basic technology infrastructure.
- CIOs are saying that the move to working from home went very well. Outside of the function the feedback isn't always so positive. Clients are looking at the performance of their technology function and in some cases it has really been found wanting throughout the crisis so far. They can't afford for it not to serve them in the right way if we have a second wave of lockdowns.

HR & RESTRUCTURING

- Beyond the furlough process and IT support for working from home en masse, the expected need for intensive HR surgery hasn't yet hit. Restructuring firms predict that this will kick in one month before the furlough scheme is signalled to close. Although that has now been extended until October there will be a tapering from August, and we therefore expect to see an increase in redundancy programmes from the end of July, if not sooner.

SUPPLY CHAINS

- Supply chains are being fundamentally reassessed as the pandemic exposes weaknesses, and a new level of resilience will be demanded going forward. Many feel that a local capability will be more resilient and reliable.
- On shoring has been a topic in multiple conversations with some organisations frustrated at their inability to kick start their supply chain due to availability of parts/components or indeed the whole stock. Some firms are predicting a surge of UK manufactured products and a great emphasis of the robustness and continuity of the supply chain.

> "Supply chains are being fundamentally reassessed as the pandemic exposes weaknesses."

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