

Governance Challenges 2020

STRENGTHENING THE BOARD'S ROLE IN STRATEGY DEVELOPMENT AND EXECUTION

A Publication of the National Association of Corporate Directors and its Strategic Content Partners

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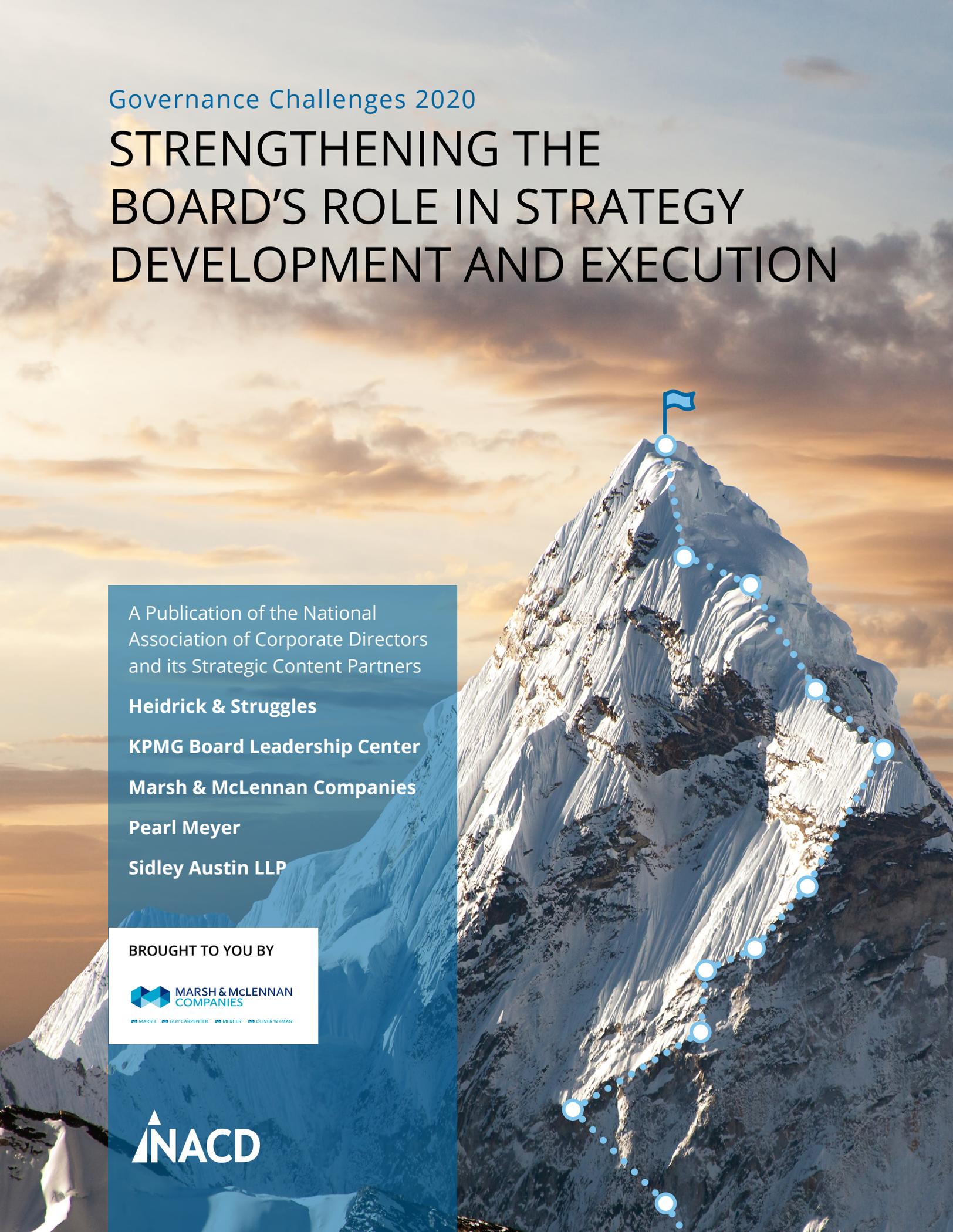
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Facing Uncertainty

25 Strategy and Crisis Questions for Directors

Marsh & McLennan Companies Inc.



TOOL OBJECTIVE

Directors can use this tool to improve the board's agility during a crisis and use that agility to adapt the long-term company strategy.

Boards and management teams face two critical challenges at the time of a crisis:

1. How can we keep the strategy and mission resilient in the face of threats that have the potential to make existing business models obsolete, change industry structure or operating conditions, or derail growth?
2. How can we provide a transformative opportunity for the long-term strategy of the organization?

One such example is the current COVID-19 crisis. A fundamental difference between this COVID-19–driven crisis and previous crises is the lightning-fast impact and the significant scientific uncertainty about its duration.¹ The US economy went from a booming economy and full employment into an economic coma with skyrocketing unemployment in a matter of weeks. No one knows when the world will return to normal, or what the “new normal” will look like.

The forces at play are unforgiving, and boards have a careful balancing act ahead of them: companies cannot afford to either underreact to the crisis (thereby risking financial ruin) or overreact to it (thereby diminishing relative competitive positioning or losing investor confidence). And while survival is a first-order existential priority, to thrive is the aspirational opportunity, and thus this is also a time for strategy.

For example, a leading auto insurance company in the United States recently announced that it would refund premiums as part of a “shelter-in-place payback” to customers to offset a massive decline in driving. While this was motivated in part by a desire to preempt regulatory intervention, competitors now must decide if they will follow suit—and take a financial hit themselves—or risk customers switching to a seemingly more customer-centric insurer. Several CEOs have pledged not to lay off employees during the pandemic. Competitors that do not make similar pledges may risk losing the war for talent post crisis. What M&A opportunities have been unearthed as company valuations have plummeted? Can we identify new domestic suppliers that are less prone to disruption before competitors lock up sourcing contracts?

These are just a few examples of decisions management needs to stare down. There are numerous, high-magnitude, high-velocity forces in motion—from trillion-dollar government bailouts to provide short-term relief and grants to eliminate global supply-chain dependencies over the longer term, to new multibillion-dollar investments in industries like biotech and 3D printing, to taking

¹ *Responding to COVID-19: Almanac*, Oliver Wyman, June, 2020.

positions on questions of financial, operational, strategic and moral importance. It should also be noted that how a company acts in this global crisis could sear reputations for a long time to come.

Such crises thrust the board into a new role: working with management to help the business stay afloat and survive a real-time, critical, and uncertain event. Boards are usually engaged in robust and incisive strategy discussions that focus on opportunities, risks, and the firm's overall direction for the next three to seven years. These strategy discussions create a venue for management and the board to pressure test assumptions underlying strategy and to hone a clearer vision for the organization.

Boards are not designed to react to fast-moving events. Nor do boards have the facts and inputs that management does. Boards typically meet four to six times a year, whereas in crisis conditions management may be making major decisions hourly. Also, directors are not always fully immersed in a given industry. They are frequently involved late in key, often material, decisions and have strong pressures exerted on them to quickly approve significant changes urged by management.

When faced with fast-moving crises, such as those we are experiencing now, directors have another role to play in the short-term: to stress test management's plans and decisions made in the heat of battle. When lost in the fog of uncertainty, how best to stress test with incomplete facts? How best to oversee and test data collection? How best to question decisions that might lead to unintended consequences?

After verifying the fundamentals and establishing situational awareness, the board must lean in and engage differently than they have before—on two dimensions: the first relates to how the board engages with management, and the second is to ensure broad thinking (stress drives myopia!) to help define or confirm what is most critical for management to focus on.

In this context, existing management routines and processes will not be kept up, and waiting for the data will be like driving looking through the rearview mirror. Instead, it is now important to respond rapidly to the emerging challenges of today, while preserving optionality for the future. The combination requires that a number of elements be in place, from a shared vision and vector, to trust and support between management and the board, to frequent (daily, weekly) updates to the board, as well as modified roles for the key executives due to the crisis.

JUMP-STARTING BOARD AGILITY IN A CRISIS

The board has a unique opportunity to support the management team and organization in becoming more adaptive and agile—not only to help with the current challenge but also to help prepare for future risks. Agility means different things to different people, and different things in different situations. And agility is rarely applied to the workings of a board, although it is increasingly an aspiration for boards.

In the context of a crisis, one element of board agility is understanding the need to balance the discussion on both the short and long term. Management is more likely to be preoccupied with the short term—whether to take out loans, whether to lay off or furlough employees, and whether to shut down certain operations fully or move all operations to a more bare-bones approach. The board is part of that discussion—testing to make sure decisions are well thought through—but must also be keeping an eye on long-term repercussions.

Balancing real-time responses with longer-term, strategic thinking is exceptionally difficult to do absent hard data and in the heat of the pandemic. But boards are uniquely positioned to help management engage in revolutionary thinking in the midst of a crisis. Independent directors are removed from the day-to-day operations of an organization, so they can think broadly and holistically about the future—taking a crow’s nest perspective on what threats or opportunities might be emerging—without being weighed down by the details of the current business strategy.

Finally, perhaps the most important role the board can play in strategy discussions with management is in asking questions about the future of the business, its operating environment, and assumptions about the future. In a prolonged crisis scenario, these are critical questions. What is the “new normal” today, and what will it look like post crisis? An effective dialogue allows the board and management to rethink or reconfirm existing strategies and underlying assumptions and prepare for unanticipated future scenarios.

Directors can raise a series of “have we considered . . . ?” questions that may unlock a paradigm shift in mindset, operating model, and industry. Board members also often have specific areas of expertise and extensive networks that might become relevant in this new context; connecting management to individuals outside their core competencies can help shed light on otherwise-difficult-to-untangle Gordian knots in this pandemic.

At some point, we will emerge from the pandemic. If boards of directors keep their eyes on the horizon and bring broader and longer-term perspectives to management, with luck and skill organizations will navigate the rocks through the hurricane, keep the ship and crew intact, and ultimately reach safe harbor—maybe even finding new trade routes and lands in the process.

25 QUESTIONS FOR AGILE AND ADAPTIVE DIRECTORS

Pivot to Stress Testing Crisis Oversight

1. Is management’s response and approach adequate to meet the crisis?
2. Are all stakeholders (shareholders, regulators, employees, customers, and suppliers) being considered and informed about the company’s plan?
3. What are the credit and liquidity risks in a crisis, and is there a risk of loan defaults and/or covenant breaches?
4. In order to enable solid decision making, what other data do we need and what data needs to be more robust?
5. What unintended consequences and potential future risks do today’s actions invite?
6. Do we need to add a new standing committee or a special committee to protect against immediate risks, such as a hostile takeover?

Align Today’s Short-Term Decisions With the Long-Term Mission and Strategy

7. Will today’s “new normal” remain static over time, ultimately reverting to the “old normal,” or will it evolve into a “future normal”?
8. What contingencies/mitigants should we put in place?
9. Is there an up-to-date crisis management plan and team, and how should they evolve over time?

10. What changes in strategy should we consider for the near/mid/long term?
11. What opportunities do we see in M&A, talent acquisition, company acquisition, new products, or programs?

Monitor the Evolving and Emerging Risk Profile

12. What are the new/emerging risks? In different geographies? In different arenas, like cyber risk?
13. Relative to our business, are the profound changes seen in the COVID-19 situation a megatrend or a one-time event?
14. What issues normally discussed in committee should now be raised from the risk, audit, and compensation committees to the full board?
15. Are any competitors providing a solid road map for action?
16. How is our ecosystem evolving, and what or who is entering or exiting our ecosystem?
17. How might our social license to operate be constrained or expanded in an evolving business context?

Build Resilience for Future Crises

18. What lessons have we learned to incorporate into future responses? How will views toward companies/sectors evolve as a result of action during the crisis and due to changed norms after the crisis?
19. Is there a strong cross-functional management team in place, and are there successors prepared to take the key positions?
20. How will employees and consumers/customers behave differently when the crisis is past?
21. What are the key assumptions underlying our strategy and business model, and what plausible business-environment scenarios might disrupt our vision and planning assumptions?

Strategy Requirements

22. How can we best (re)organize our assets and business model to drive future revenues?
23. Is the organization agile enough to respond to new opportunities and a changing risk environment, and where do we need to focus to improve our agility?
24. Which capabilities do we need to acquire and retain to achieve our strategy, including talent, production, technical, partners, and risk capabilities?
25. Can we model three scenarios (worst case, most-likely case, and best case) for outcomes to the crisis and develop strategies to match each?

About the Contributors

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