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Building a better working world

Play it safe or double down?

In the face of uncertainty, should you protect and optimize what you already have or seek out new growth opportunities?

The better the question. The better the answer.
The better the world works.

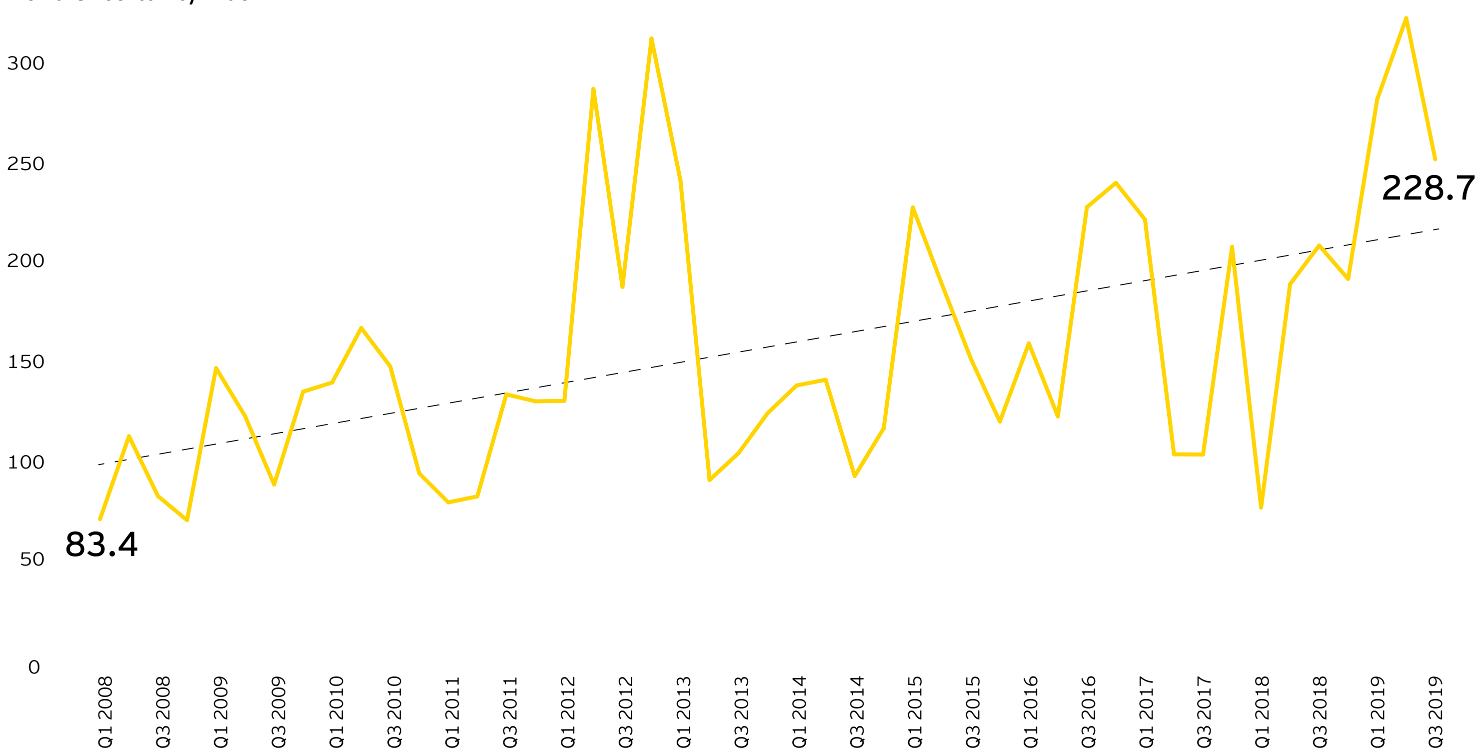
> Uncertainty is preventing the full potential of the economy from being unleashed, limiting growth and investment here in the US.

Joshua Bolten
Business Roundtable President and CEO

We're in a time of great uncertainty.

Perhaps never before have economic signals and indicators been more confusing. Just as unemployment levels hit historic lows and median household income reach all-time highs, news stories and executive surveys herald an impending recession.[1] Seemingly every day, competing headlines suggest that the economy is on an expansion boom that knows no end or is about to contract alarmingly. The US is enjoying its 11th year of uninterrupted growth, but apprehension and doubt stalk the corner offices of the corporate world. "American businesses now have their foot poised above the brake, and they're tapping the brake periodically," says Joshua Bolten, Business Roundtable President and CEO. "Uncertainty is preventing the full potential of the economy from being unleashed, limiting growth and investment here in the US."[2]

World Uncertainty Index[3]



[1] "Optimism Sinks to a 3-year Low; Recession Expected Before 2020 Election," *Duke CFO Global Business Outlook*, https://www.cfosurvey.org/press-release/optimism-sinks-to-3-year-low-recession-expected-before-2020-election/, accessed 20 October 2019.

[2] "Business Roundtable CEO Economic Outlook Index Decreases in Q3," *Business Roundtable website*, https://www.businessroundtable.org/media/ceo-economic-outlook-index, accessed 20 October 2019.

[3] Hites Ahir, Nicholas Bloom and David Furceri, "World Uncertainty Index," *Stanford mimeo*, 19 November 2018.

An emerging complexity crisis is facing executives

Even without the threat of a potential business downcycle, many executives feel paralyzed in the grip of a **complexity crisis**, where too much is happening too fast. "It is a challenging time to be a leader," notes Kelly Grier, EY US Chair and Managing Partner and Americas Managing Partner, Ernst & Young LLP. "Driving a growth agenda while anticipating potential recessionary conditions is demanding enough. Layer on increasing societal expectations, a more contentious political environment, and a radical transformation agenda powered by digital, and even the most experienced business leader will have his or her skills tested."

Indeed, executives today are facing challenges along a number of different fronts. Geopolitics, sociocultural change and digitalization have all changed fundamentally since the last recession and are creating a complex set of pressures on businesses today.

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EY US Chair and Managing Partner and Americas Managing Partner

Geopolitical risk: rising populism and fragmenting institutions

- "The rise of populism and nationalistic politics are impacting cross border trade," according to Marna Ricker, EY Americas Vice Chair — Tax, "increasing complexity for global companies to an unprecedented level. To thrive in this global landscape, companies must have the ability to continually monitor, model and rapidly adjust to maintain their competitiveness."

- The rules-based, multilateral order that has been a key component of global politics is under significant pressure. Long-standing international alliances, agreements, institutions and norms are all under pressure. This is changing the playing field for global business. Whether they realize it or not, companies are much more exposed to geopolitical risk than ever before.

Changing society: instant accountability and demographic shifts

- The onus on companies to own up to their responsibilities is growing and changing. An ever-expanding set of stakeholders, including investors, boards and employees, now expect businesses to take a stand and get involved in pressing social challenges. At the same time, all companies now operate under greater scrutiny: everything they do is transparent and shareable globally instantly. There is no room, or time, now for a mismatch between what a company avows and what it does: the say-do gap. "The penalties can be rapidly meted out and may be severe," says Sam Johnson, EY Americas Vice Chair – Accounts. "A tweet that takes 30 seconds to write can reach tens of millions of people instantly and cause stock prices to plunge."

- There are now five generations working, and each of them has different work ethics, experiences and expectations. The mix within the workforce, however, is changing. Millennials are now the largest adult generation,[4] and are moving into leadership positions. Behind them, the first "digitally native" generation (Z) is streaming into the workforce. "Gen Z have grown up with the universe in the palm of their hand," says Marcie Merriman, EY Americas Cultural Insights and Customer Strategy Leader. "We can no longer expect employees to do tomorrow's job with yesterday's tools. Companies that realize that Gen Z offers them a preview of the future, of how technologies are transforming expectations — these companies will be tomorrow's winners." By harnessing the insights of Gen Z, companies can bring all generations in the workforce onto the same digital page, not only bridging divides, but orienting the company's strategy toward the future.

> "A tweet that takes 30 seconds to write can reach tens of millions of people instantly and cause stock prices to plunge.
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> Sam Johnson
> EY Americas Vice Chair – Accounts

[4] Richard Fry, "Millennials projected to overtake Baby Boomers as America's largest generation," *Pew Research Center website,* https://www.pewresearch.org/fact-tank/2018/03/01/millennials-overtake-baby-boomers/, accessed 1 September 2019.

- Climate change is both a more urgent risk that companies need to mitigate and a priority for action. The public increasingly expects companies to act sustainably, to be held accountable for their carbon footprint, and to play a constructive role in helping their communities recover from adverse effects of climate change. In addition to these social pressures, there are substantial economic consequences on the horizon. A new report published by CDP shows that 215 of the world's biggest companies see climate change as a threat likely to affect their business within the next five years, with a cumulative cost of a trillion dollars.[5]

Digital disruption: breaking barriers and redefining operating models

- Artificial intelligence (AI), cloud and blockchain already demand that we see the world in a different way. Startups can launch on short runways, scaling rapidly and inexpensively. Competition is no longer only from sector peers, but from insurgents that can mushroom from nothing to market leaders in a matter of months. Big data and advanced analytics bring the power of research institutions into the hands of any individual with a laptop and an internet connection.

- Products (taxis, hotels, cars, luxury fashion) are being unbundled and recycled as services. The age of personalization is here: get what you want when you want it at the tap of a smartphone. Further, open access to globally connected platforms is blurring the boundaries between consumer and producer: "prosumers" are able to monetize and scale, leveraging assets that are available on the network. The U.S. Department of Energy's Grid Modernization Initiative is responding to moves by consumers to "sell back" solar energy from voltaic tiles to the grid, for example.

$1 trillion

estimated cumulative cost that is likely to affect the world's biggest companies within the next five years due to climate change.

- Companies are no longer singular entities with defined boundaries. They are now networked ecosystems that include suppliers, customers and even competitors in shared enterprises that are more like symbiotic organisms than rigid structures. Company leaders are no longer simply custodians of what value lies within the company walls, but are network orchestrators, controlling the many moving parts of a platform where the value is distributed across multiple players.

As Graeme Wood wrote back in 2009, "change has never happened this fast before, and it will never be this slow again."[6] Given the developments that are detailed above, this is even more true today, and companies are finding it difficult to keep pace.

Recent research conducted by the EY organization reveals that only 22% of leaders feel prepared to operate in a highly digital environment. While the internet is effectively collapsing distance, now the internet of things, AI and blockchain are collapsing time as well. Add to this a possible global economic contraction and what is already a demanding juggling act suddenly becomes a crisis.

In the 2008-09 financial crash, government action (quantitative easing, tax cuts, historically low interest rates) combined with the double-digit growth of China as an emerging super-economy drove us out of recession. But today, the fiscal runway is limited by elevated levels of government debt, low interest rates leave little room for cuts, and there is no equivalent to China's economic rise to provide new demand. It will be left to companies themselves to create the growth opportunities that will fuel the next business cycle.

The question now is, given this shifting landscape, should you play it safe and ride out the storm or double down on growth opportunities?

5 "World's biggest companies face $1 trillion in climate change risks," *CDP website,* https://www.cdp.net/en/articles/media/worlds-biggest-companies-face-1-trillion-in-climate-change-risks, accessed 20 September 2019.

6 Graeme Wood, Social Principal #9, *Geek Media,* http://graewood.blogspot.com/2009/09/ipasocial-principle-9-change-will-never.html, accessed 31 October 2019.

Chapter 1

Playing it safe: tactics to ride out the storm

Build defenses, protect core assets and adopt lean operations

Playing it safe involves using a core set of tactics that help you protect and optimize your business during hard times. Some tried and tested methods of preparing for crises are as relevant now as they ever were.

Protect

Particularly in challenging times, businesses must not compromise on fundamentals that keep their companies safe and secure. For example, crime often increases in recessions. In 2008, the number of online fraud cases increased 33% in the United States.[7] Companies cannot afford to compromise their defenses.

Companies also need to maintain strong governance standards and mitigate against behavioral risks. "Situations where executives stray from company values or ethical behavior can be problematic even in good times," notes John King, EY Americas Vice Chair — Assurance, "but can be doubly challenging in turbulent conditions, as regulators may be even more vigilant."

Similarly, it is important for firms to take measures to both protect their brands and look for opportunities to build further loyalty by staying true to their purpose in tough times. A survey undertaken by the EY Beacon Institute reveals that 73% of respondents believe that a well-integrated purpose helps organizations navigate challenging times by building trust and strengthening relationships with stakeholders. In environments where trust erodes, maintaining your status as a trusted brand can pay great dividends. Protecting your core value, the value you deliver to all your stakeholders, means protecting your core values, or what you stand for.

Optimize

In addition to adopting these protective measures, companies also need to optimize their operations as the global economy cools.

Companies that outperformed their peers in the last two recessions had taken steps to both protect and optimize their businesses before recession hit. By doing so, they positioned themselves to take advantage of new opportunities that economic downturns always create. When times got tough, says Bill Casey, EY Americas Vice Chair — Transaction Advisory Services ,"Far-sighted executives strengthened margins, stress-tested business plans, assessed portfolios for vulnerabilities and divested assets that did not align with their growth strategies."

By cleaning up the balance sheet, they were able to take advantage of weaker, stricken players and acquire them, as soon as a downturn hit.

By being clear on the businesses they were in, they were able to divest out of non-core activities, freeing up both cash and mind space to fuel growth.

By moving fixed costs to variable costs, they were not burdened by costly overcapacity and were able to flex as growth opportunities arose.

Honeywell: reducing labor costs without cutting heads

After employing broad-based layoffs during the 2000 dot-com recession and struggling to recover afterward, Honeywell followed a different strategy in 2008. Understanding the corrosive impact that layoffs can have on morale and realizing that cost savings (which can take up to six months to materialize) may be temporary, as companies may need to begin re-hiring during recovery, Honeywell instead chose to furlough employees for one to five weeks with no or reduced pay. This saved an estimated 20,000 jobs and positioned the firm well for when demand picked back up.[8]

By diversifying their product range, they avoided the fate awaiting companies whose narrow focus proved fatal (e.g., Toys"R"Us, Blockbuster, Borders).

[7] "The IC3 Internet Fraud Statistics Report," *Identify Theft Scenarios website*, http://www.identity-theft-scenarios.com/identity-theft-statistics/internet/, accessed 15 September 2019.

[8] David Cote, "Honeywell's CEO on How He Avoided Layoffs," *Harvard Business Review*, June 2013. Walter Frick, "How to Survive a Recession and Thrive Afterward," *Harvard Business Review*, May–June 2019.

The natural tendency of companies facing difficult times is to focus only on defensive measures. Research, however, shows that this is not an effective strategy. Companies need to pair defensive tactics with offensive moves.[9] In other words, winners from the last recessions didn't just play it safe and passively wait for the storms to pass. The real differentiator was that they used the freed-up resources to double down on growth.

Doubling down means having a view of the future, prioritizing investments necessary to protect, optimize and grow the business. This perspective guides the strategic bets companies make to accelerate growth in times of economic uncertainty.

[9] Ranjay Gulati, Nitin Nohria and Franz Wohlgezogen, "Roaring out of Recession," *Harvard Business Review*, March 2010.

Chapter 2

Double down: strategies for growth

Be opportunistic, experiment fast and take bold steps

What do Groupon, Airbnb and Uber all have in common? They were all founded during the 2008–09 financial crash.

Uncertain economic times can bring enormous opportunities as tectonic changes recreate market landscapes. Typically, new entrants grasp these opportunities more effectively, as they are able to move quickly without the baggage that weighs down older incumbents.

A 2009 survey examined responses to the economic downturn of 3,000 country winners and finalists from the EY Entrepreneur Of The Year™ competition compared to C-suite executives in large multinational corporations. While 74% of the multinationals focused on "securing the present," only 30% of the entrepreneur group prioritized the present. By contrast, just 19% of the large company group focused on "pursuing new market opportunities" compared to 67% of entrepreneurs. One winning entrepreneur sums up the attitude: "There's no point in doing anything other than to look for the opportunity in the crisis."[10]

Entrepreneurial companies are focused on building tomorrow's market opportunity, while market leaders, for very obvious reasons, may tend to protect and optimize their current business. In this analysis, we show that pursuing both is the only way to meet the three imperatives of every company leader: protect, optimize and grow.

[10] *Seizing opportunities: a once in a lifetime chance*, EYGM Limited, 2009.

Percentage of entrepreneurs who would pursue new market opportunities during economic downturn:

67%

> “There’s no point in doing anything other than to look for the opportunity in the crisis.
>
> Entrepreneur Of The Year® Award winner

Not all the previous recession’s winners were startups. Some big companies made the brave steps it takes to emerge stronger out of crisis. They doubled down on long-term growth strategies, which positioned them to emerge as leaders into the next business cycle.

They invested in new technologies in support of goals such as improving operational efficiencies, creating more intimate customer connections, gaining a better understanding of their business and customer through data analytics, or moving into the cloud for more agile computing.

Starbucks: strengthening connections with its customers through digital and social channels
After Howard Schultz returned to lead Starbucks in early 2008, the company took steps to shore up its operations while also investing to reinvigorate customer connections. Starbucks closed almost a thousand underperforming stores in 2008-09 and focused on its core commitment to the customer experience. Schultz made his objective very clear: “reigniting the emotional attachment with customers.” The company used social media to allow customers to share ideas and, importantly, listened to the suggestions and implemented over 100 of these ideas. Starbucks was also early to embrace mobile apps to facilitate personalization. One feature, MyStarbucksSignature, allowed customers to design their own signature drinks.[11]

They continued to invest in R&D to bring innovation to market in time for the upsurge after the recession.

Microsoft: doubling down on R&D
During the 2008–09 recession, Microsoft significantly increased its R&D budget, growing spend around 15% in 2008 and 10% in 2009. One key target of the research program targeted cloud computing. Development of the firm’s Azure platform was announced in fall 2008 and was launched in early 2010. By the end of FY10, approximately 70% of Microsoft’s engineers were working on cloud-related products and services. A decade later (April 2019), Microsoft’s cloud revenues hit a run rate of $38.46b.[12]

They took advantage of weaker competitors to gain market share, to acquire key talent and to undertake strategic acquisitions.

InBev: a competitive strike
In the depth of the financial crash in 2008, just as Lehman Brothers filed for bankruptcy, European beer-maker InBev swooped to acquire the 100-year-old, family-controlled Anheuser-Busch, whose brands included the all-American Budweiser. Anheuser shareholders had seen profits flatline and despite opposition from the controlling Busch family, the US firm was sold for about $52b.[13]

[11] Shezray Husain, Feroz Khan and Waqas Mirza, “Brewing innovation,” *Business Today,* 28 September 2014. Alexis Fournier, “My Starbucks Idea: an Open Innovation Case-Study,” *Braineet website,* https://www.braineet.com/blog/my-starbucks-idea-case-study/, accessed 15 September 2019. Maureen Morrison, “Starbucks Forges ‘Moments of Connection‘ by Offering Experience,” *AdAge,* 7 November 2011.

[12] Steven A. Balmer, “Shareholder Letter,” *Annual Report 2010: Microsoft Corporation,* 3 September 2010. Steven A. Balmer, “Shareholder Letter,” *Annual Report 2009: Microsoft Corporation,* 1 September 2009. Shanhong Liu, “Microsoft’s expenditure on research and development 2002–2019,” Statistia, 9 August 2019.

[13] Michael J. de la Merced, “Anheuser-Busch Agrees to Be Sold to InBev,” *New York Times,* 14 July 2008.

They invested heavily in their delivery system while also adopting open and transparent communication styles with their customers, gaining trust, even when it involved owning up to harsh truths.

Domino's: doubling down on brand trust
Domino's Pizza was in trouble in the past recession, with its stock reaching an all-time low in 2008 and its pizza tied for last in a national taste test in 2009. The new CEO instituted several changes to turn things around. One area of strength that he set to improve was the company's delivery system, primarily by bolstering online, mobile and social media channels. More fundamentally, the company completely overhauled the recipe and ingredients used for its pizzas. While rolling out the new recipe, Domino's undertook a major advertising campaign, noted for its "legendary boldness." The company chose to address former shortcomings of its product head on. According to then-CEO Patrick Doyle, "the old days of trying to spin things simply doesn't work anymore ... great brands going forward are going to have a level of honesty and transparency that hasn't been seen before." Domino's "radical authenticity" and the reinvention of its core product helped it reinvigorate its brand and boost sales.[14]

This Transformative Age is already creating enormous growth potential for companies able to adopt a new mindset. "Executives need to be value navigators," says Hank Prybylski, EY Americas Vice Chair — Advisory Services. "We need to understand the real value of being connected, of managing our networks to chart uncertain territories."

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Mastering the complexity of our age involves more than understanding the capabilities of new technologies: it means developing an acute skill at continuously re-imagining the business we are in.

Amazon: from bookseller to tech platform and hardware developer
When Amazon launched its Kindle electronic book reader, many thought it was a crazy cannibalization of its business: customers would abandon physical books in favor of cheaper, electronic versions. The company had already acquired Audible.com in 2008, entering the audiobook market. By Q3 2009, Amazon Founder and CEO Jeff Bezos was able to announce, "Kindle has become the No. 1 best-selling item by both unit sales and dollars — not just in our electronic store, but across all product categories on Amazon.com." Besides offering customers a cheaper option for purchasing books at a time when many were tightening their belts, the Kindle served a longer-term strategy by introducing a platform that would be expanded to offer customers additional digital products and services, not least paving the way for the Kindle Fire and Amazon's entry into the tablet market. Amazon was farsighted enough to recognize that it was in the business of selling books in multiple formats.[15]

These are object lessons from successful cases that combine tactics to play it safe and strategies to double down. But, as we think about how to apply these to the next business cycle, what's really different in this Transformative Age? How does the complexity crisis change the game?

[14] Bill Taylor, "How Domino's Pizza Reinvented Itself," *Harvard Business Review*, 28 November 2016. Jim Edwards, "Dominos Admits Pizza Was 'the Worst'; Bets the Company on Ads Vowing Change," *CBS News,* 14 January 2010. Abbey Klaassen, "Domino's Talks Radical Authenticity," *AdAge,* 28 October 2010. Sam Oches, "The Many Acts of Domino's Pizza," *QSR Magazine,* August 2010.

[15] Bobbie Johnson, "Amazon busts through recession with profit surge," *The Guardian,* 22 October 2009. Zoë Henry, "Amazon Has Acquired or Invested in More Companies Than You Think — at Least 128 of Them," *Inc.* Adam Clark Estes, "Amazon's Recession-Friendly Tablet Strategy: Cheap Now, Pay Later," *The Atlantic,* 28 September 2011.

Chapter 3

Play it safe, double down or change it up?

The Transformative Age requires transformative skills

"Business shouldn't be slowing down because of uncertainty," says Carmine Di Sibio, EY Global Chairman and CEO. "It should be speeding up because of transformation."

At its simplest state, a business must set out to do three things every day: it must protect itself, optimize everything it can and ultimately grow. These are business imperatives that remain constant in face of societal, technological and geopolitical change. However, what is really different now is the pace of change.

The current business environment demands that a company employ a new skill set to help it continually see the world differently and to move with agility as opportunities for growth emerge. Key transformative skills are the ability to harness and embed new technologies to effect transformative change at speed, an adaptive mindset (that will allow you to respond to unforeseen changes to thrive, not just survive) and a new level of decision mastery to drive an ever-more-complex connected ecosystem.

Winners will be those who can master the "what" of digital capabilities and the "how" of leading that change. To protect, optimize and grow, businesses have to embed digital into every aspect of their strategy and operations; they have to develop an adaptive mindset and they have to master decision-making in spite of uncertainty.

"Be prepared and begin to act," advises Michael Inserra, EY Americas Senior Vice Chair and Deputy Managing Partner, Ernst & Young LLP. "It's the companies who are going to be out on their front foot, willing to make mistakes and iterate on strategy that will emerge as clear winners."

Learn more:

How to reshape your business with agility and build resilience

Why managed services can be the C-suite's greatest weapon

How to drive the future of compliance, with integrity in the spotlight

How to chart the right course for your transformation

Doesn't incremental innovation need to keep pace with exponential opportunities?

> “Business shouldn’t be slowing down because of uncertainty. It should be speeding up because of transformation.

Carmine Di Sibio
EY Global Chairman and CEO

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