How do you reshape today to reinvent your tomorrow?

As the window to take action narrows, the need to adapt and reshape results fast is critical.
Content

1. The paradigm shifts 03
2. Reshaping results in an era of volatility 10
How can EY help? 18
We are no longer in the usual economic cycle. Social, political, economic and technological changes are converging to produce a business environment whose only constants are volatility and uncertainty. This is a new paradigm; the disruption goes far beyond the extent and pace of change that we have become used to.

To operate successfully in this marketplace, businesses can no longer rely on traditional performance improvement models to achieve growth. Instead, they need a mindset of adaptive performance and a new framework to respond to volatility and grasp the opportunities that are now emerging. An adaptive performance mindset embraces leadership that is agile, iterative and adapts continually, regardless of where the business may be along the performance curve.

Source: https://www.policyuncertainty.com/
Why is it important to act now? Because we are standing on a burning platform — and because competitors are already seizing the initiative. “There is no reason to wait to make your company more resilient, adaptable and agile, and more ready for what’s to come,” says Falco Weidemeyer, EY EMEIA Head of Reshaping Results and a Member of the Global Restructuring Leadership team. “If you wait too long, you will no longer be master of your own destiny.”

The rules-based, multilateral order that has long defined global geopolitics is under pressure. Longstanding international alliances, agreements, institutions and norms are all feeling the strain. The trade dispute between China and the US has seen international trade stagnate,¹ and social unrest — from the demonstrations in Hong Kong to the rise of populism in Europe, which is now at its highest level since 1980² — is unsettling markets.

In a business as well as an existential sense, the climate emergency is pressing. The world’s biggest companies now believe climate change threatens to cost their businesses US$1 trillion over the next five years.³ There are short-term pressures, too. The prolonged economic upswing appears to be running out of steam. According to the Bank of England, the proportion of the global economy growing above trend has already fallen from four-fifths to one-third.⁴ Meanwhile, the International Monetary Fund says that growth is falling to its lowest level since the financial crisis.⁵ And global debt has almost doubled since the crisis,⁶ which points to challenges ahead.

If you wait too long, you will no longer be master of your own destiny.

Falco Weidemeyer
EMEIA Head of Reshaping Results and a Member of the Global Restructuring Leadership team

---

At the same time, companies have to catch up with digitalization and technological disruption sooner rather than later in order to stay competitive. A wave of transformation has swept across industries, including financial services, retail, media and consumer goods, leaving a trail of corporate failures in its wake. In 1964, the average S&P 500 company spent 33 years in the index, but this is expected to fall to just 12 years by 2027.7

Some sectors are more exposed than others to this kind of disruption. “We are seeing more situations in which companies’ business models are threatened,” says Weidemeyer. “A new downturn would probably not be a general one where volume and utilization fall off a cliff, but one where whole sectors diminish.”

"Take brick-and-mortar retailers," he says. "They are exposed to a business model threat due to changing consumer behavior on the basis of digitization and channel shifts."

Get ahead of the risks

This perfect storm has prompted a deep sense of unease in the boardroom. EY Global Capital Confidence Barometer – October 2019 reveals that only 55% of businesses are confident about their earnings prospects, down from 80% in 2018, and that just 59% are positive about short-term market stability, down from 68% in 2018.8

The upside is that pessimism is translating into action. Nearly two-thirds of C-suite leaders in the Confidence Barometer say they are actively planning to respond to ongoing geopolitical, trade and tariff concerns.

What might their responses look like? “The most important thing that corporates need to do today is be decisive — full stop,” says Mona Bitar, EY UK & Ireland Reshaping Results Leader. “Time is gold.”

The window of opportunity is often small and is continually narrowing. Post-global financial crisis (GFC), companies that suffer a “crisis” (defined as a major share price fall) are less likely to recover and more likely to go out of business than they were pre-GFC. EY analysis from Capital IQ data of major indices between 2000–19, showed a sharp contrast observed between the "crisis" (2007–11) and "post-crisis" (2012 onward) periods. Accordingly, following a 50% observed fall in the share price, in 45% of the cases, the company recovered during the crisis period. During the post-crisis period, only 28% of the companies were able to recover following the same 50% share fall.9

So, time is of the essence — and even more so today than in the past. On average, a business moves from its third profit warning to its first restructuring event in just 91 days — down from 156 days prior in 2016.10

The most important thing that corporates need to do today is be decisive — full stop.

Mona Bitar
EY UK & Ireland Reshaping Results Leader

---

9. EY analysis of 5,000 companies based on Capital IQ data.
The timetables to which private equity firms work may be a useful reference point here. When they take on a new business, they form a clear strategy for their first 100 days of ownership, and often plan to restructure or reshape it within six months. That requires decisiveness and an agile plan of execution. That kind of rapid decision-making and action is paying off: investors expect private equity returns to continue to outpace those of public markets. 11

A framework for response

With a mindset of adaptive performance, business leaders are better positioned to pursue a proactive and fast-paced approach to business transformation. Digital technologies also provide a means to move forward with confidence. However, the key for business leaders lies in understanding how the specific characteristics of their organization can be mapped onto the volatility that surrounds them – and how their business realities are shaped by the difficult operating environment they face.

First, companies have to get better at analyzing where they currently stand, in order to identify where and how they need to act. In practice, different parts of a single business may sit at different points. And, in this era of volatility, even businesses that are in a strong position today, can slip back at surprising speeds.

“As organizations look to manage volatility and build resilience in their operating models, they will need to look at each component of their value chain and assess the extent to which they are optimized to deal with the markets’ future requirements,” says Peter Manchester, EY EMEIA Advisory Leader for Managing Volatility. “The development of new and disruptive technology, analytics and artificial intelligence provide significant opportunities to more rapidly enhance and transform organizations’ capabilities and skillsets.”

91 days

On average, a business moves from its third profit warning to its first restructuring event in just 91 days – down from 156 days prior in 2016.

EY value framework provides businesses with a model for carrying out this process of self-assessment. It rests on four value pillars that reflect a performance curve:

1. **Value transformation**
   Visionary organizations driven by purpose with healthy balance sheets, excess cash flows and clear market opportunities must now prepare for the transformation requirements of the future.

2. **Value creation**
   Proactive businesses with solid revenue and profitability, and which are ready for change, may still need to optimize their strategies and must consider how to stay relevant and create value in the years ahead.

3. **Value preservation**
   Resilient and preservative businesses that are losing market share, facing structural operating flaws or adjusting to new levels of demand, must work out how to turn things around while preserving value.

4. **Value recovery**
   Reactive and defensive businesses that are facing liquidity issues are dealing with unfavorable financing structures or are at risk of insolvency and must focus on recovering from crisis.
Importantly, self-assessment is not a one-off exercise. The value framework provides a basis for the continuous reflection that is implicit in an adaptive performance mindset. Business leaders who know, at any given moment, where they stand on the performance curve – and how that might change in the light of disruption such as a new competitor, transaction or technology – are in a position to take positive action.
Part 2
Reshaping results in an era of volatility

22% of leaders feel prepared to operate in a highly digital environment.
Value transformation: be visionary and capture emerging sources of value

However successful the business, standing still is not an option. As we experience accelerated change, businesses that are currently performing at their peak may quickly see their competitiveness slipping if they take that position for granted.

Nevertheless, transforming from a position of strength is better than being forced to change direction by a period of decline or circumstances beyond the leadership’s control. A healthy balance sheet and strong cash flow provide the foundations for transformation, which will give these businesses the space to identify and pursue new market opportunities.

Agile leaders recognize this. They see, for example, how the viral effect of social media can undermine a business in an instant: a celebrity tweet might cost them millions in a matter of hours. They also know that new technologies could transform their organizations: for instance, we are on target to see an increase from 10 billion internet-connected devices in 2015 to 34 billion in 2020.

---


But responding to threats and opportunities is difficult. A recent EY poll found that 47% of business leaders worry that they are too passive – or reactive – in their response to disruptors. Other EY research finds that only 22% of leaders feel prepared to operate in a highly digital environment.

“The status quo is very sticky in organizations,” says Andrew Wollaston, EY Global Reshaping Results, Restructuring and TAS Private Equity Leader. “Many business leaders think they just need to keep the ship going in the right direction.”

**Implications for decision-makers**

The key lies in constant stress-testing and horizon-scanning – identifying the business’s greatest strengths and working out how to capitalize on them in a rapidly changing marketplace.

New technologies, or even just new ways of working, could improve efficiency and productivity. And unorthodox alliances and collaborations could open up new opportunities for growth. Digital levers will unlock change.

A wholesale culture change might be necessary to overcome the status quo. “Don’t be complacent,” urges Suwin Lee, Head of EY Global Restructuring Tax team, “this is a real chance to stay ahead of the competition and to have a very strong vision for your business. Does it make sense to enter a new market and establish a business there? Do you need substantial investment? How can you use technology better in your business? Now may be the time to make bold decisions and get stakeholders on board.”

M&A is one way to seize the initiative. In turbulent times, the temptation may be to hold back from deal-making, and the data supports this: while global M&A looks healthy enough, foreign direct investment into Europe now appears to be falling. But retreating from deal-making could be a mistake; with the right deal, organizations can gain in one move the assets, skills, experience and impetus they need for transformation.

Value creation: set the stage for strategy optimization

Even when revenue and profitability are healthy, vigilant business leaders will be on the lookout for warning signs of decline. For example, growth may be slowing, costs may be rising, returns on investment may begin to look less impressive or business may begin to feel like it’s coasting.

With an adaptive performance mindset, the C-suite will pick up on these signals at an early stage and identify where the business is going wrong or missing out on opportunities. And, unless a business has a clear process and timetable for strategic review, it might not spot its missteps until it is too late — and will miss vital opportunities to create value.

“Value improvement programs help businesses to unleash the potential that is within their assets,” says Falco Weidemeyer. “Sometimes, the potential is within the asset itself; sometimes it’s acquired through buying and building, or consolidating and synergizing; and sometimes through a mix of those.”
Implications for decision-makers

Value creation is about understanding how the organization can once again function at peak level of performance. It may be that the operating model now needs to change, or customer and product portfolios need to be rationalized. The business may no longer be the ideal size to achieve maximum value, or costs might be rising too quickly. It may need new skills or a different type of intellectual property. It may need to focus on where emerging technologies can help create new value.

Agile leaders will quickly identify what it is that threatens to hold the business back. “Value creators are looking to build the capabilities to transform their business to meet the future model,” says Peter Manchester. “That could be through transformative M&A, it could be through making greater investments in the technology and data that put them in a leading position within each of their segments and markets.”

Many businesses are adept at portfolio review and performance management, but struggle to assess their position in the broader ecosystem in which they operate. They might not have analyzed their stakeholder groups, for example, or mapped the strength or weakness of their relationships with customers and suppliers. Or perhaps they have not considered their regulator’s position and how it might change in the near term. More than half of all US consumers say they now consider the values of a company before purchasing from it – this rises to almost 70% of millennials.18

This work is crucial in a hyperconnected marketplace where relationships have never been more important – or more fragile.

70% of millennials

More than half of all US consumers say they now consider the values of a company before purchasing from it – this rises to almost 70% of millennials.

Value preservation: adapt the business when earnings are challenged

Businesses that are not focused on how to transform and create value will struggle. Market share may slip, earnings growth may diminish and structural flaws may become more apparent. In some cases, the decline is gradual and will not be noticed unless the business is paying attention. In other cases, problems will suddenly mount up – particularly in the sectors or markets that are facing the most disruption and new competition.

The value preservation challenge underlines the need in the C-suite for resilience, determination and transformational zeal. “If your business model is stable, being a manager is enough but, in disruptive times, you have to be a leader,” says Falco Weidemeyer.

Without an adaptive performance mindset, companies slip into reactive mode. They take incremental steps to address issues as they emerge, rather than taking more proactive, decisive action. That can lead to a downward spiral that becomes much more difficult to resolve.

Implications for decision-makers

Businesses that have thought about value preservation before they get to this point on the curve have a clear advantage, says Mona Bitar. “You need to act really fast, but crisis takes people by surprise,” she says. “Companies need to have a plan much earlier on for what they’re going to do if they get here.”

Preventing a chain reaction then becomes the focus. Senior leaders must agree to act radically, decisively and quickly, with the board ready to take decisions that have far-reaching consequences. Cost reduction is a crucial part of the mix. Leaders need to give themselves headroom for restructuring and to pivot to new opportunities, which means being bold. Be radical with contract renegotiations, process improvements and product rationalization; more modest adjustments may simply delay the effects of the problem and lead to lengthy rounds of cost-cutting. Technology solutions may unlock more dramatic change.

It may be time to say goodbye to some parts of the business that are no longer central to the company’s purpose and long-term value. However, while timely divestment will secure greater value and give more time for reinvestment, it is a practice that many companies struggle with. In the most recent EY Global Corporate Divestment Study, 61% of businesses in the UK said they had held onto a non-core business for too long. 19

Identifying problems early is a crucial element of adaptive performance. This includes, helping leaders to implement their plans for value preservation and business turnaround before it is too late. “The most critical thing is not being blind,” says Mona Bitar. “Metrics are ignored for too long.”

Value recovery: turn the business around when crisis hits

For businesses experiencing significant difficulties, the challenge is existential: how do they remain viable and maintain liquidity? Day-to-day trading may be seriously compromised, financing structures will be put under strain and insolvency may loom.

Business leaders stuck in reactive and defensive mode are putting their companies in serious jeopardy. “In this context, adaptive performance means taking a restructuring approach to business problems,” says Andrew Wollaston. “Get on top of them quickly, and then be rapid and deliberate in the steps taken to right-size the business for the new technology or the new market or the disruption that it faces.”

Businesses in value recovery mode will often be under new leadership. EY analysis suggests that, within a year of the third profit warning, half of CEOs will have departed.20 Even so, new and existing leaders must take a cold, hard look at the business to identify what is salvageable and then take immediate action.


---

Half of CEOs

will have departed within a year of the third profit warning.
“This is an exercise in options analysis,” says Suwin Lee. “Those options may include an insolvency process leading to a change of ownership or a search for new investment that gives enough breathing space to turn around the viable parts of the business. It may be critical in saving assets and jobs.”

Businesses that have embraced the adaptive performance mindset will be ready for such an exercise. They will have stress-tested their businesses under a range of market scenarios, including the most difficult, and examined capital allocations with great care. They will also have built strong relationships with stakeholders through regular communication, and will be able to have open conversations with shareholders, suppliers and employees.

Implications for decision-makers

Value recovery requires accelerated diagnosis of the problem and plans for confronting it, and then rapid execution. The priority must be to secure solvency, conserve cash, deleverage the asset base and restructure finance. Having taken the most critical steps to avert disaster, leaders can then rebuild for the future.

Clearly, no business wants to find itself in value recovery mode. Those that do, often reflect that they did not act early enough.

“Get on top of the business problems quickly, and then be rapid and deliberate in the steps taken to right-size the business for the new technology or the new market or the disruption that it faces.”

Andrew Wollaston
EY Global Reshaping Results, Restructuring and TAS Private Equity Leader
How can EY help?

The reality is that today’s challenges will not be solved in isolation by a "one-size-fits-all" approach. They require an agile, integrated and bespoke response in a broad range of disciplines, from capital allocation and business strategy to operational expertise and performance improvement – while simultaneously monitoring tax and legal implications, and applying digital levers wherever possible.

EY value framework provides a new model for assessing where companies need to focus in order to thrive in the “new normal” of volatility and radical disruption. It brings together skills and expertise from across the entire organization to help clients realize their full value potential.

Through its four performance pillars, this framework represents an innovative way for business leaders to think about their next move. For businesses with an adaptive performance mindset, the framework provides a means by which to plan ahead – not just react.

The objective is to transform leaders into agile agents of change, constantly looking for new ways to move their organizations forward. They:
Assess
They establish planning processes, allow for regular or trigger-event based reassessments to identify areas requiring action, and integrate that work into key performance indicators.

Adapt
They use approaches and tools according to whether their businesses require value transformation, value creation, value preservation or value recovery, tailored to deliver their desired outcomes.

Anchor
They embed a drive for performance in the organization by adapting processes and key performance indicators. Performance becomes an attitude and is no longer just a program.

Each of these steps is crucial but, in this era of accelerated disruption – the paradigm shift to volatility – the challenge is to take them more quickly, more iteratively and with greater agility. Rather than passing through these steps in a linear sequence, business leaders with the right mindset will move to a journey of continual adaptation in order to operate successfully in the new normal.

EY multi-disciplinary, international team offers guidance for your business. We have significant breadth and depth, with 1,000 restructuring professionals and 3,000 reshaping professionals. By leveraging all those competencies, our teams build bespoke services for clients, developing and deploying at speed.
About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. Information about how EY collects and uses personal data and a description of the rights individuals have under data protection legislation are available via ey.com/privacy. For more information about our organization, please visit ey.com.

© 2020 EYGM Limited.
All Rights Reserved.

EYG no. 000056-20Gbl

BMC Agency
GA 1014078

ED None

In line with EY’s commitment to minimize its impact on the environment, this document has been printed on paper with a high recycled content.

This material has been prepared for general informational purposes only and is not intended to be relied upon as accounting, tax or other professional advice. Please refer to your advisors for specific advice.

ey.com

EY contacts

Falco Weidemeyer
EY EMEIA Head of Reshaping Results and a Member of the Global Restructuring Leadership team
+49 6196 996 18335
falco.weidemeyer@de.ey.com

Peter Manchester
EY EMEIA Advisory Leader for Managing Volatility
+44 20 7951 1728
pmanchester@uk.ey.com

Andrew Wollaston
EY Global Reshaping Results, Restructuring and TAS Private Equity Leader
+44 20 7951 9944
awollaston@uk.ey.com

Mona Bitar
EY UK & Ireland Reshaping Results Leader
+44 20 7951 4437
mbitar@uk.ey.com

Suwin Lee
Head of EY Global Restructuring Tax team
+44 20 7951 7952
slee1@uk.ey.com