

Introduction

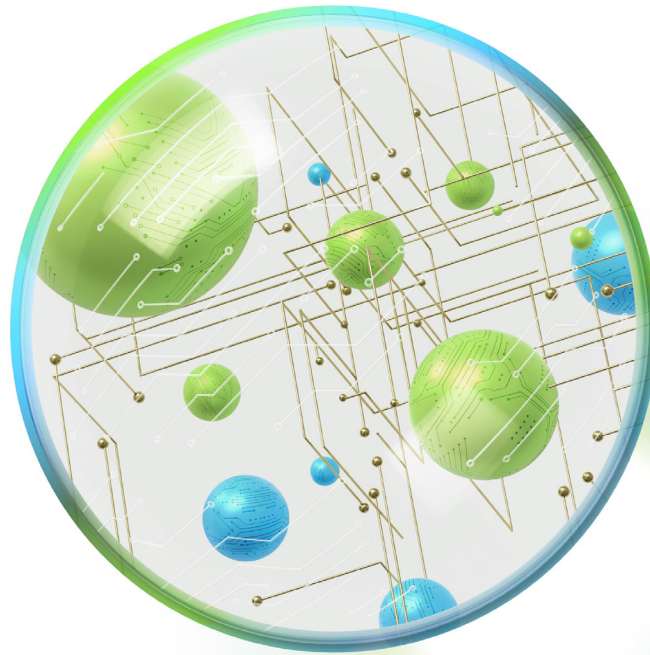
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The lingering impacts of COVID-19: lessons for Boards on sustaining business resilience

The lingering impacts of the COVID-19 pandemic are a stark reminder for Boards of the need to pivot quickly and manage unexpected risks through ongoing scenario planning.

It's close to 20 years since SARS and the question of how a pandemic should be managed from a health, political and economic perspective was front and centre.¹ Since that time the topic of pandemic preparedness has been on the agenda of many Risk Management Conferences attended by many of today's Board directors² and risk executives and was included on many risk registers.

It is fair to say however that few were prepared for COVID-19 and understandably so as it was very different to anything we'd experienced in recent memory and both human and corporate nature does tend to focus on upside opportunity rather than preparing for downside challenge.

Although the virus and its resultant impacts seem to be normalising after two years of our drastic responses to keep everyone safe;³ industries continue to have their business resilience tested. What can be learned from our COVID-19 experiences as we move into a wider set of uncertainties including rising inflation and interest rates, global supply chain disruptions, labour shortages and fundamental changes to the ways many employees work?

¹ <https://www.ncbi.nlm.nih.gov/pmc/articles/PMC3329048/>

² <https://www.ncbi.nlm.nih.gov/pmc/articles/PMC7147509/>

³ <https://www.abc.net.au/news/2022-03-18/china-to-stick-with-zero-covid-strategy-president-xi-says/100919774>

Key challenges and uncertainties

The impact of the COVID-19 pandemic

In addition to the tragic health impacts, business impacts were felt in a range of ways including restrictions on the ability to work, workforce availability and resulting supply chain issues, and now the impacts of large amounts of economic stimulus.

Alan Joyce, CEO of Qantas implored the government to allow airline workers to return to work as the airline had 18% of parts of its workforce unavailable, having contracted COVID-19 over the Easter 2022 holiday rush to travel. The airline had to continue operating with office staff working as ground crew.⁴

Brad Banducci, CEO of the Woolworths Group explains that the shortages of stock experienced by the supermarkets in early 2022 were due to “COVID-driven absences of 20%+ in our distribution centres and 10%+ in our stores.”⁵

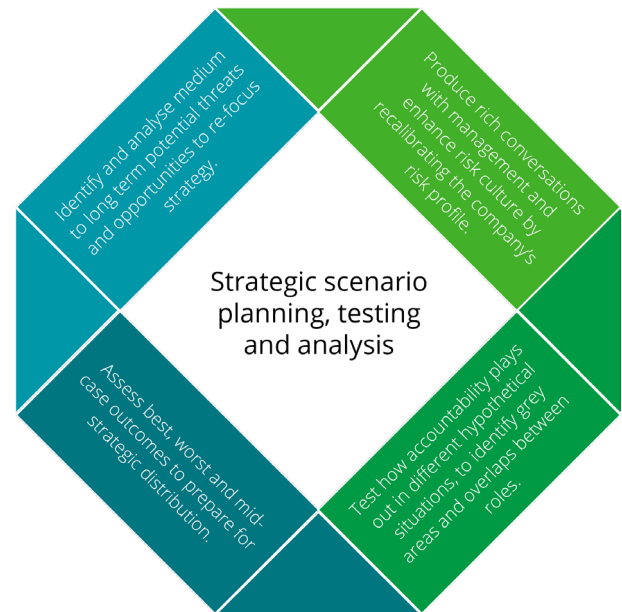
Jakob Stausholm, CEO of the Rio Tinto Group said operating conditions “remained challenging” due to prolonged COVID-19 disruptions, impacting iron ore output in 2022.⁶

Adapting to the changing terrain

The experience of the global pandemic represents a crisis for Boards today in supporting management to refocus the company's strategy. Lingering challenges of disrupted and strained supply chains, energy cost increases, talent and labour shortages, absent employees, financial strains, and operating challenges generally in a period of ever-increasing inflation and interest rate rises make it a difficult terrain to navigate. Boards are also required to respond to constant changes in the economic environment due to the implementation of monetary policy measures by the Reserve Bank of Australia (RBA), such as a reduction in the cash rate and the interest rate paid on Exchange Settlement (ES) balances.

In the face of uncertainty, there is significant value in Boards performing more strategic scenario analysis. This type of analysis is used extensively to address major operating environment shifts and disruptions. The lingering pandemic after effects have heightened the need for all Boards, across all sectors, to reframe their risk profiles and appetites and analyse and plan in new ways.⁷ This is critical for risk management, strategic decision making and corporate reporting through detailed assessment of going concerns and impairments, if appropriate.

New and unfamiliar scenarios unapologetically expose gaps if Boards are not adequately demonstrating oversight of their company's response to these challenges in sustaining resilience.



Opportunities

Scenario analysis

Crisis resets the competitive landscape, providing new opportunities for Boards to adjust their corporate strategy, get ahead of trends and increase distance from competitors. The time to act is now. Scenario analysis helps Boards identify and analyse medium to longer term potential threats and opportunities, market-wide and those that threaten their ongoing viability. Consider the alcohol manufacturers pivoting to making hand sanitisers.⁸

By assessing the best, worst, and mid-case outcomes, Boards can better prepare for strategic disruption. Decision-makers may better anticipate the future and design future-proof, yet flexible strategies, with Boards working with management on re-focusing their strategy. Testing can also produce rich conversations with management and enhance the company's risk culture by recalibrating the company's risk profile.

Experiences in the market

In the superannuation sector, regular and comprehensive scenario or 'stress' testing is used to develop a robust approach to the formulation and implementation of investment strategies, as required by the Australian Prudential Regulation Authority (APRA).⁹ This is accepted methodology for managing risks both foreseen and unforeseen, by assessing the entity's resilience to severe but plausible downturns.

⁴ <https://www.afr.com/work-and-careers/workplace/easter-travel-threatened-as-airports-reel-under-staff-shortages-20220408-p5abxt> & <https://www.bloomberg.com/news/articles/2022-06-08/qantas-so-depleted-it-needs-office-staff-to-work-as-ground-crew>

⁵ Latest Woolworths CEO Updates | Woolworths Online

⁶ <https://www.smb.com.au/business/companies/rio-tinto-s-iron-ore-exports-fell-in-2021-amid-labour-crunch-20220117-p59o2h.html>

⁷ <https://www.imd.org/research-knowledge/reports/scenario-planning-for-a-post-covid-19-world/>

⁸ <https://www.forbes.com/sites/chrisfurnari/2020/03/25/with-sanitizer-in-short-supply-alcohol-producers-pivot-to-battle-coronavirus-pandemic/?sh=5ccea29971f2>

⁹ See APRA Prudential Standard SPS 530 - Investment Governance

In the current disrupted operating environment, severe but plausible is the new norm, and strategic scenario analysis has never been more of an imperative. In APRA's review of the implementation of the Banking Executive Accountability Regime (BEAR), APRA stressed the importance of regular scenario testing to facilitate a deeper understanding of accountabilities for entities. APRA noted that this allows for an examination of where handoffs, decision rights, joint accountabilities or gaps exist.¹⁰

These examples although based in a regulated financial services environment (where regulatory focus in this instance is on stability and resilience) can provide a roadmap for all businesses. Scenario testing and planning allows entities to see how accountability plays out in different hypothetical situations, and flag grey areas and overlaps between roles. In adverse situations, these clearly defined accountabilities are critical. Relevant scenario planning ensures Boards and management are better equipped when inevitably faced with the unexpected.

What are the questions directors should be asking?

In a climate where the unexpected is to be expected, sustaining strategic and operational business resilience demands of Boards, together with management, greater agility and preparedness than ever before. Boards are expected not to cope, but thrive through the complex and unique scenarios presented to them.

Although we hope the most disruptive challenges are behind us, daily events are a merciless reminder that nothing can be taken for granted. Boards have tools, such as the use of strategic scenario analysis, to allow them to take a proactive approach to deliver sustained resilience. Taking full advantage of new opportunities by adopting these tools will benefit companies in terms of preparedness, stability and consistency, allowing decision-makers to gain against their competition.

Key questions for Boards navigating governance during critical market-wide period

- 1 Is the range of scenarios the organisation considered suitably broad to cover plausible future events and is the plan to respond robust?
- 2 Have you recalibrated your organisation's Risk Appetite Statement and Stress Recovery Plan, and ensured they are appropriately adapted to the uncertain and ever-changing challenges and resultant impacts by engaging your Risk Committee?¹¹
- 3 Have you ensured your Corporate Strategy is aligned to the risk return profile defined by its Risk Appetite, to enable functionality and stability even in times of uncertainty?¹²
- 4 Is your Executive and Board planning aligned for emergency succession?
- 5 Are your reporting systems supporting prioritised information from management to the Board and committees in close to real time, to enable the executive and Board to forward-plan, with timely and tactful decisions to achieve strategic outcomes even during periods of uncertainty?
- 6 What are the lessons you have learned from previous critical market-wide periods that can be used to inform future conduct, and identify potential opportunities?
- 7 Are the core scenarios contemplated being consistently used across the business including in financial reporting?
- 8 Are the executives and Board aligned on best, mid-case and worst-case scenarios and their associated responses?
- 9 Is the business regularly testing how they would respond to unexpected events so the business is 'stress ready'?
- 10 Are the executives and Board aligned on workforce contingency planning and the implications on talent and workforce shortages during uncertain periods?

¹⁰ BEAR information paper (apra.gov.au)

¹¹ See APRA Prudential Standard CPS 510 – Governance (paragraph 106)

¹² See APRA Prudential Standard CPS 510 – Governance (paragraph 106)

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