

The COVID implication
Life after lockdown – the “new normal”
A Financial Services Industry overview

July 2020



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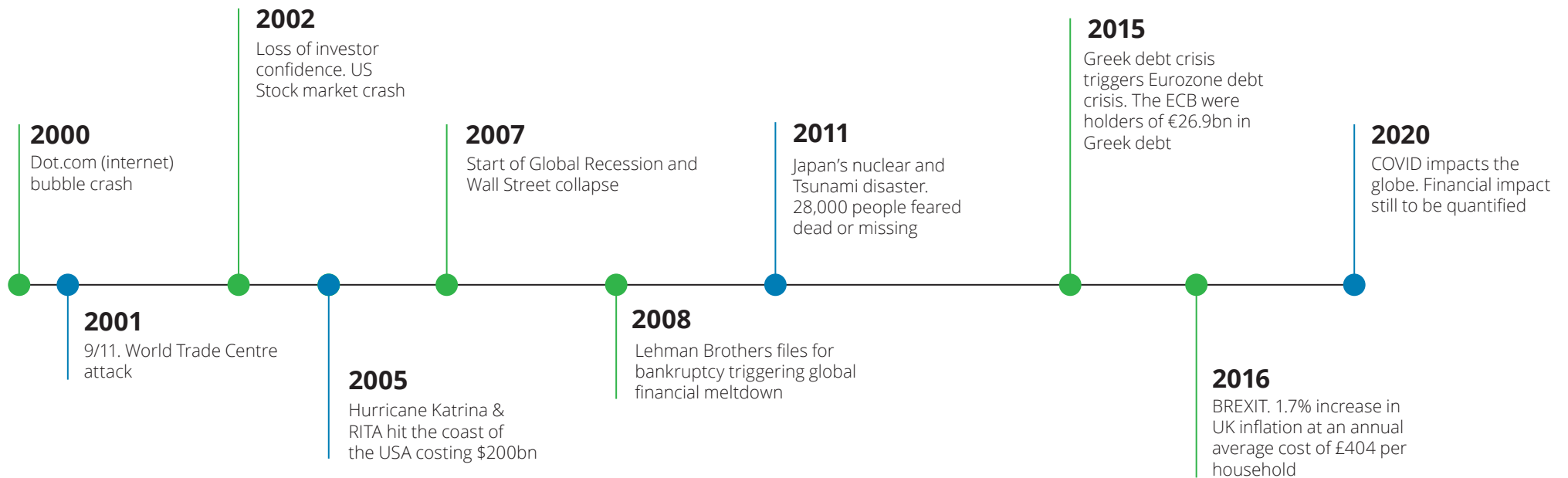
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Global economy



Global events that have shaped financial services

Since the inception of the 21st century several financial and economic events have had a major impact on the global financial services landscape.



The global COVID-19 pandemic will have an indeterminate impact on the South African economy

● Financial market event ● Economic event

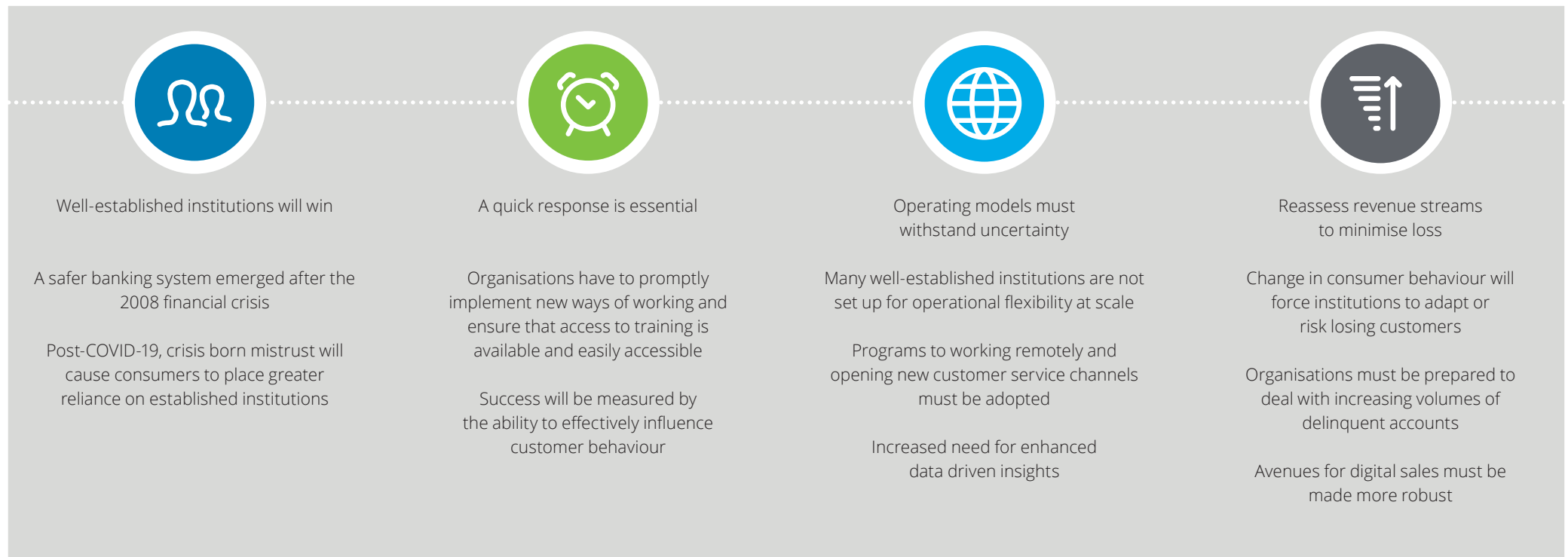
2020: COVID-19 causing a global economic contraction

The Novel COVID-19 pandemic has caused chaos across the globe with developing economies bearing the greater brunt.



Early lessons learned from global "Black Swan" events

The globe has been shaken by numerous economic events that occur outside of financial services. In order to thrive during this uncertainty, organisations have to innovate, act fast and protect their revenue.



COVID-19 factors causing a further contraction

World trade has slowed down if not halted, supply chains have been disrupted and tourism flows have fallen which has placed significant pressure on South Africa's economic growth. Deloitte has identified 7 wicked problem areas where the Financial Services sector needs to focus to navigate this crisis.

COVID-19 Concerns

Government trade-off between livelihoods & life

While lockdown is intended to ensure that the virus does not spread thus aiming to secure the longevity of an economy; it is also causing economies to slow down.

Shocks hitting both demand & supply...

As global trade slows down due to trade restrictions such as closed ports, the lockdown in most countries around the globe has seen a fall in consumer spending.

Leading to an unusual recession

The cause, size, suddenness and momentum are significantly different from "usual" economic downturns.



The 7 Wicked Problems that the FS Industry must focus on

- 1 Reimagine the customer**
Expand business offerings to meet new customer expectations
- 2 Keeping the organisation safe**
Tighten health, safety and security protocols and strengthen privacy and cybersecurity policies
- 3 Changing ecosystems**
Consider Platform as a Service (PaaS) versus Banking/ Insurance as a service
- 4 Simplify Business**
Automate and streamline processes
- 5 Growth and expansion**
Consider strategic partnerships with other players in the market (e.g. incumbents acquire fintechs)
- 6 Changing ways of working**
Digital and remote working becomes the new normal
- 7 Unlock the data-driven business**
Expand business offerings to meet new customer. Use data driven insights to service customers and find new business streams

SA in the spotlight



Setting the scene for the South African story

South Africa emerged from 2008 financial crisis stronger due to robust economic growth; but this may not be the case for the current pandemic.

2008



Started off with stronger economic growth



More room to spend on economic stimulus due to budget surplus



Relatively less complex financial system and homogeneous customer expectations

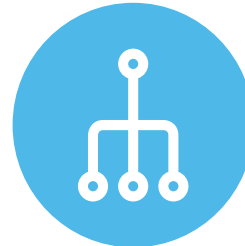
2020



SA already in negative GDP growth



Downgraded to junk status forcing capital to leave the country



Customers' expectations are changing. They choose to engage on their own terms via their preferred channels

The South African Story

Multiple factors are putting the health of SA's economy at risk.

Unlike the rest of the world, SA was already in a technical recession upon entering this lockdown

SA reported **2 consecutive quarters of declining GDP** growth; since the commencement of lockdown, GDP growth has been revised further downward.

The outlook is grim, especially considering SA's biggest exporters (China, Germany and the US) are all under siege. Also mining, which contributes 53% to our export volumes, has slowed production.

Junk status causes further financial woes

As liquidity dries up in the market, governments, corporates and individuals require more debt; however South Africa has been hit by another virus: **sub-investment grade debt**. Forced selling of SA bonds will place further **pressure on the rand and the economy**.

Private sector to the rescue

With the government's hands tied behind their back, **the private sector and financial industry will be required to provide support**; However, with poor country fundamentals it is unlikely that investors will see value in South Africa and may be hesitant to invest in the country.



With limited levers to pull, the Government seeks to provide stimulus to help the economy

The SARB cut interest rates to pump liquidity into the system; but the **slowed system cannot multiply that liquidity**. While the already constrained government has committed to helping certain SMMEs, **SA's debt-to-GDP ratio of 62% pre-COVID and a deep fiscal deficit** leaves the country with minimal budget space to provide the required funding.

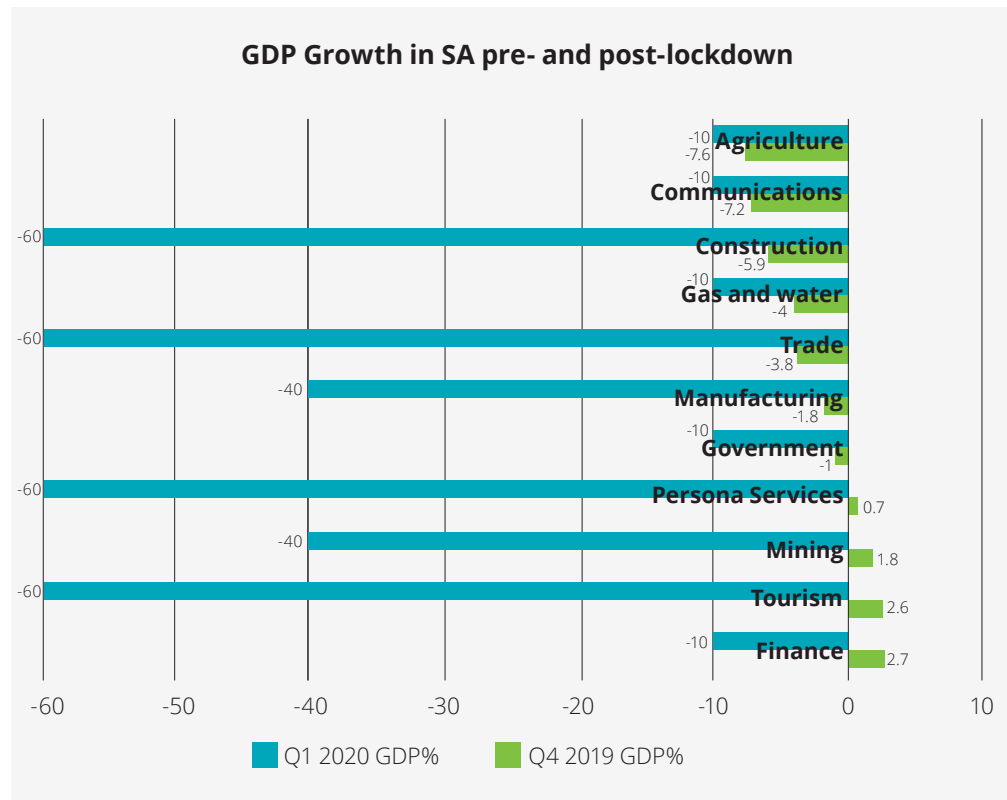
Recession and high unemployment will limit people's ability to spend

An economy already in recession along with **unemployment rates in excess of 30%** will see slowing consumer expenditure and rising unemployment; limiting the intended multiplier effect of excess money in the economy.

General uncertainty and low consumer confidence will also adversely impact consumer spending.

Multiple Industries in South Africa are impacted

The South African economy shrank by 1.4% in the fourth quarter, following a revised 0.8% contraction in the third quarter. With China's global trade being impacted by the Covid-19 pandemic for several months, it has adversely affected South Africa resulting in expediting the further fall in GDP growth for 2020.



Financial: Monetary Policy will be used to manage liquidity in the financial system, while insurers will need to relook life and medical policies to address the pandemic.



Travel and Tourism: Travel ban in place impacting hotels, airlines, luxury and consumer goods.



Mining: Decline in the demand for gold, diamonds, steel and iron ore. Companies producing lithium, cobalt, copper and iron ore have noted decreasing demand.



Manufacturing: Manufacturing and industrial sectors in Africa have been impacted by a decrease in supply from China, resulting in a shortage of construction material, skills and resources and technology.



Trade: Potential drop in sales due to constraints in both the supply of products and consumer demand. Online retailing has increased due to quarantine and lockdown.



Communication: The TMT sector in Africa was expected to attract high-value investments this year. However, the uncertainty around COVID-19 means that expected investment could be delayed as tech investors wait out the uncertainty and recover from the short-term impacts.

South Africa has struggled to emerge from an economic slump, and with the economic downgrade and lockdown, financial services have not been immune.

Source: www.treasury.gov.za



Impact on financial services

The impact on Banking and Capital Markets

The economy will look to the banks to support struggling businesses and individuals, however, the banking sector will be hard hit itself, with the biggest impact being on their balance sheet.



Investment managers managing the aftermath

Investment managers can leverage expertise in risk management to navigate their way through this storm.

What's happened in the market:

- 20 to 30% fall in Global markets
- Fixed Income under stress
- Cash loses its appeal in a low interest rate environment
- Market volatility has spiked given extreme uncertainty
- Faith in equity-backed investments will take time to rebuild

Time for active and alternative managers to shine:

- Passive investors lose favour in a volatile market
- This presents opportunity for active and alternative investment managers to find value and prove their USP
- Protected equity products may be attractive when volatility drops

Business Risk

- **Rethink** the strategy – new flows will be challenged
- Address **remote working** and associated policies
- **Promote** using digital channels to all stakeholders
- Provide **training for new Ways of Work (WoW)**

Cyber/IT Risk

- **Address** cyber security policy and protocols
- **Assess strength** of cyber security across all digital policies and **socialise** revised policies
- **Educate** all stakeholders about potential scams
- **Assess server backups** given the rise in remote working

Reputational Risk

- **Relationship managers** will need to engage with clients and manage expectations more so now than ever
- **Virtually hold-hands** – connect with clients proactively and ensure transparency
- **Educate to relate:** train clients and provide market insights

Operational Risk

- Conduct an **operational risk assessment**
- Reassess **business continuity plans**
- **Update** scenario plans and disaster recovery plans
- **Social distancing** will challenge advice-led face-to-face distribution

Contagion Risk

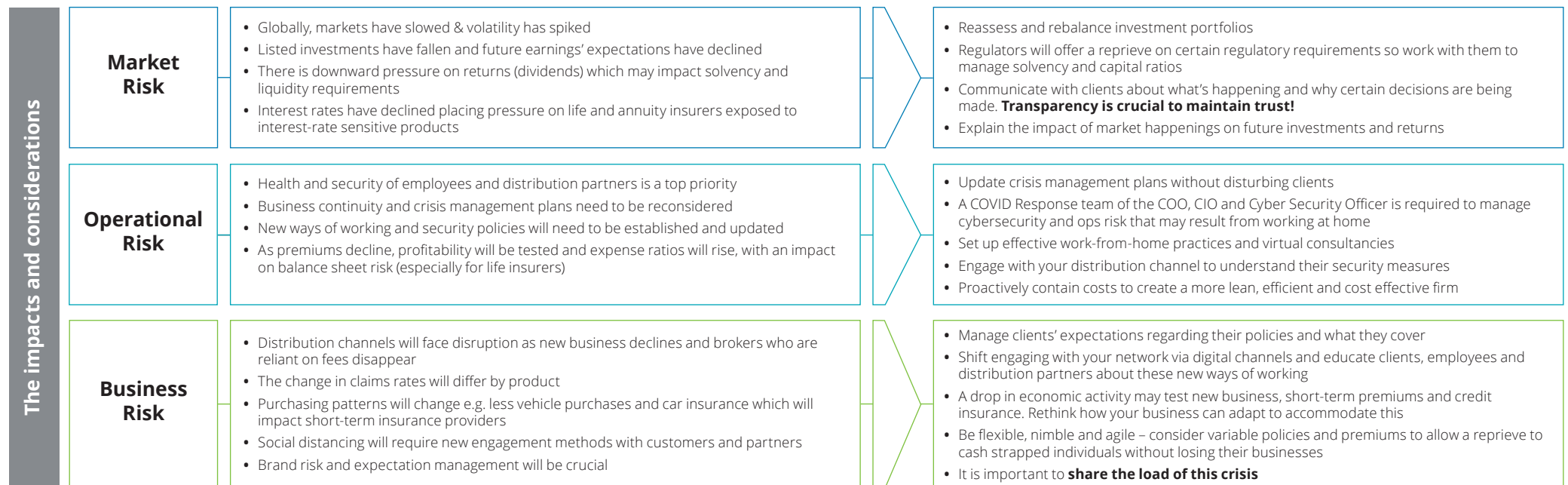
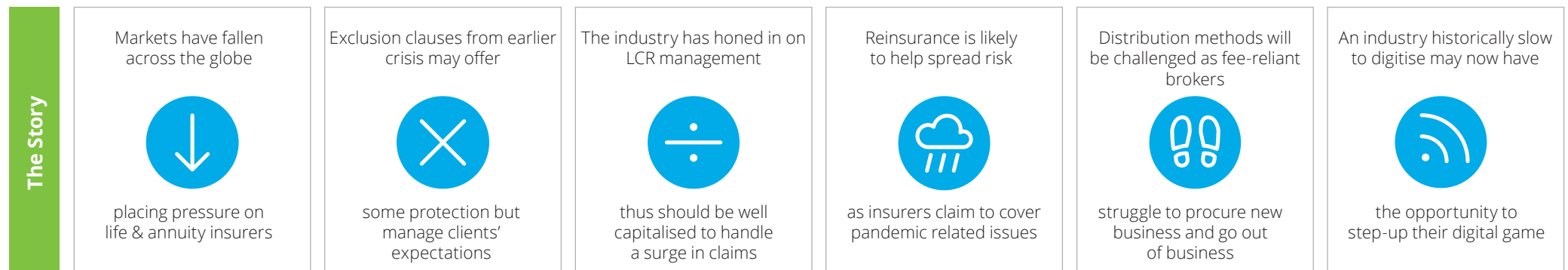
- **Many role players exist within** the vast investment and asset management ecosystem. **Engage with** IFPs, platform providers, administrators, other investment managers and custodians to understand their risk-management policies to avoid adverse knock-on effects

Governance/Regulation

- **Review and update:**
 - Risk factors
 - Liquidity
 - Capital
 - Valuation processes and policies
 - Disclosures

The state of the insurance industry

Insurers will continue to operate as the stabilisers and shock absorbers of the economy; but must prepare for shocks of their own.



The 7 wicked problems impacting financial services

FS institutions are in the midst of dramatic structural change and an unprecedented transformation journey which has given rise to what Deloitte has termed, “The 7 Wicked Problems”.

	Banking & Capital Markets	Insurance	Investment Management
1 Reimagine the customer	<ul style="list-style-type: none"> Customer expectations are rising and customers wish to engage on their own terms, through their preferred channels, as unique individuals 	<ul style="list-style-type: none"> Customers are digitally-savvy, informed, sceptical with heightened expectations One size will not fit all – personalisation is required New ways of engaging from a distance are required 	<ul style="list-style-type: none"> Utilise investor DNA to drive portfolio selection, compliance and engagement. Meet with clients once or twice a year Regular communication is required to continue defining the investor DNA as life events happen in order to retain trust
2 Keep the organisation safe	<ul style="list-style-type: none"> Data protection and customer conduct is crucial Cyber security laws need to be enhanced Risks within intermediated business model must be enhanced 	<ul style="list-style-type: none"> Tighten health, safety and security protocols Strengthen privacy and cybersecurity policies Increase monitoring of capital and liquidity Manage customer expectations and brand risk 	<ul style="list-style-type: none"> Heighten health, safety and security protocols at the office Stricter control over asset information and data, access controls and cyber controls Ensure long-term sustainability and business resilience
3 Changing ecosystems	<ul style="list-style-type: none"> Banks as providers of integrated solutions Platforms as a Service versus banking as a service Open banking is a priority and banks must invest in APIs to support this 	<ul style="list-style-type: none"> Know when to build capability, partner, acquire or exit “Non-traditional” players become insurers Distribution models will change The “shared” economy will test business – P2P, C2C 	<ul style="list-style-type: none"> “Non-traditional” players become investment managers Technological megatrends and big data FinTechs will continue to disrupt
4 Simplify business	<ul style="list-style-type: none"> Connect producers & clients to transform value propositions to rationalise your product set. Products versus services Fintechs as collaboration partners 	<ul style="list-style-type: none"> As new business and revenue struggles arise, automate and streamline processes to reduce costs Robotics, digitisation and blockchain can help Simplify offerings and outsource where possible 	<ul style="list-style-type: none"> Monetise data analytics Globally diversified portfolio based on risk tolerance Invest in processes for the long-term returns Implement automated processes to enhance operations
5 Growth and expansion	<ul style="list-style-type: none"> Use data for cross-selling opportunities Develop new lines of business to cater for current needs 	<ul style="list-style-type: none"> The “Smart” world will challenge existing risk pools Be open to new business models and ideas Economic conditions will lead to consolidations as smaller InsureTechs seek partnership opportunities 	<ul style="list-style-type: none"> Digital disruption bringing structural changes in business models Grow importance of cyber security and financial risk management Develop an innovative product strategy
6 Changing Ways of Working	<ul style="list-style-type: none"> A new way of doing banking is organised around customers, enabled by service delivery and operating models supported by many interconnected technologies 	<ul style="list-style-type: none"> Social distancing and virtual working is here to stay Automate to manage costs and boost efficiencies Train employees, distribution partners and clients on how to work and engage in this new world 	<ul style="list-style-type: none"> Increase awareness and response to environment change Blending human intelligence with technology Partner with new players
7 Unlocking the data driven businesses	<ul style="list-style-type: none"> Harness data to drive decision-making for clients Clients will expect banks to leverage data to provide tailored solutions 	<ul style="list-style-type: none"> Consolidate data for effective data driven decisions RPA, IoT, AI and ML are the way forward. Embrace digital disruption and enable digital transformation Predictive analytics can help address clients’ needs 	<ul style="list-style-type: none"> Use data analytics to segment clients and serve their needs Monetise data analytics Social channels can be highly effective in sharing/obtaining investment insights to attract investors

Operating model impact



Protect your operating model against future "Black Swans"

Amidst this uncertainty, what remains certain is that organisations will need to reassess their operating model in order to embrace the pending challenges of the "new world" and plan accordingly.



Innovate

Existing strategies and trends for digital innovation must be accelerated.

- Invest in automated solution that have long-run benefits
- Invest in workforce transformation that will continue post crisis
- Help your clients service their own clients



Act Fast

Financial Services institutions need to act fast while considering both the short and long-term.

- Implement relief programmes for clients
- Enable remote work
- Form a "plan-ahead" team
- Test for multiple scenarios



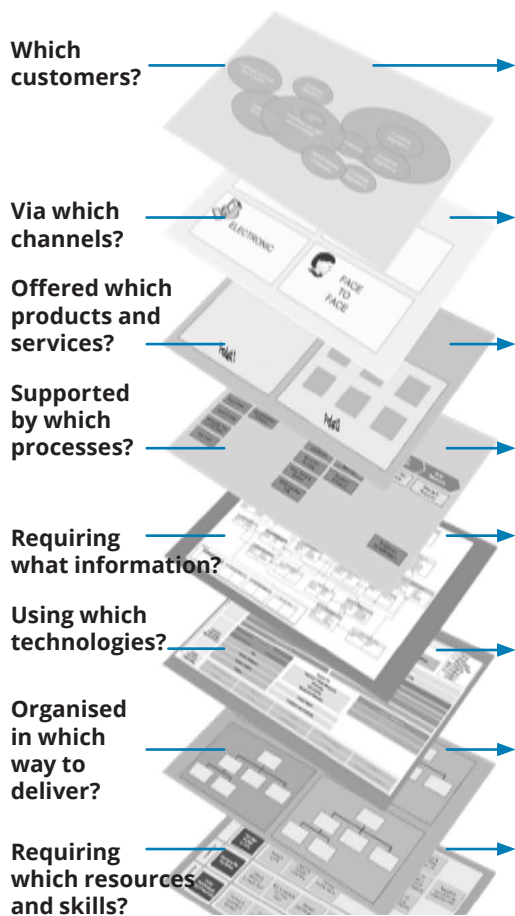
Protect Revenue

Short-term profit considerations need to take a back seat and organisations should focus on protecting long-term revenue.

- Use enhanced analytics to support cross-selling post the crisis
- Design interventions that have long-term value
- Improve focus on advisory services and digital sales

Operating model Impact

To protect operating models against future Black Swan events, financial services organisations will need to consider the implications of these events on multiple layers of their operating models.



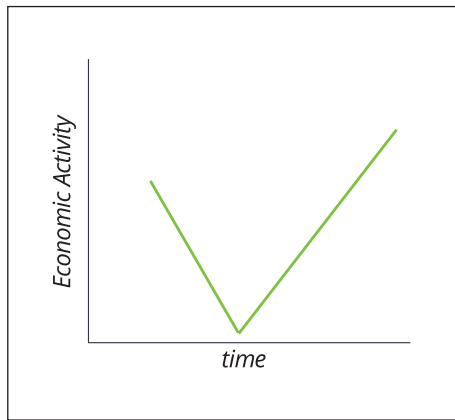
Operating Model Layers	Key considerations to address Black Swan impact	ABC Response Checklist
Customer segments	<ul style="list-style-type: none"> Online communication will become the norm Robust contact centre Customer training on new interaction methods More transparency in products/services offered to clients 	<ul style="list-style-type: none"> Customers and Clients Improve health and safety measures
Channels	<ul style="list-style-type: none"> E-signature and digital ID tools must be made available Assess capabilities to move certain transactions onto conversational platforms like WhatsApp Develop appropriate and tailored communication for various stakeholders Distribution systems will change – brokers, admin, platforms, etc. 	<ul style="list-style-type: none"> Go Digital Enhance Tech and Training
Products	<ul style="list-style-type: none"> Accelerate digital sales and services Reassess product suitability in the "new world" e.g. variable premiums, payment terms, loans, investment products Identify cross-selling opportunities 	<ul style="list-style-type: none"> Be Agile Move quickly
Processes	<ul style="list-style-type: none"> Digital first approach to servicing clients – consultancies, risk assessments, claims processes Assess remote working capabilities Processes that require in person interaction must move online Update your business continuity and crisis management plans 	<ul style="list-style-type: none"> Rethink your operating model Plan for the future Stress test
Data	<ul style="list-style-type: none"> Data driven insights to manage business lines e.g. credit extensions, opening of new accounts, conducting risk assessments Enhanced analytics to develop personalised communication strategies 	<ul style="list-style-type: none"> Enhance Tech and Training Build a virtual business
Technology	<ul style="list-style-type: none"> Cloud capabilities – if remote working/WFH becomes the new norm, will need to access systems and applications in the cloud Ensure best-breed data security as workers operate remotely 	<ul style="list-style-type: none"> Enhance Tech and Training Assess Processes & PPP
Organisation	<ul style="list-style-type: none"> Enhanced controls around AML/KYC/Cyber related risks Maintaining open lines of communication with regulators Ensuring health, safety and security practices are updated (sanitisers, masks, etc) 	<ul style="list-style-type: none"> Rethink Operating Model Manage your (e)xposure
Talent	<ul style="list-style-type: none"> Focus on Training – tech savvy, digital, Agile and flexible work Reassess MSAs and SLAs based on changes faced (e.g. working from home, hours, flexibility, bonus and reward) Reassess and align KPIs in order to ensure productivity Re-establish organisational culture post lockdown 	<ul style="list-style-type: none"> Protect Employees Improve Health & Safety measures

A digital globe composed of a grid of blue and white points, with a network of glowing blue lines connecting various nodes across its surface and extending into the background. The globe is positioned on the left side of the frame, and the network lines radiate outwards, creating a sense of global connectivity and data flow. The background is a dark blue gradient with faint, out-of-focus network patterns.

Considering the recovery scenarios

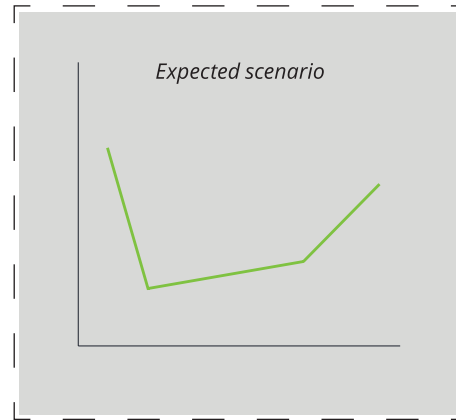
Potential Recovery Scenarios

It is highly likely that the economy will continue to suffer for a longer period before we see an uptick. Businesses may experience a recovery at different time horizons and business leaders must ensure that they are prepared for this.



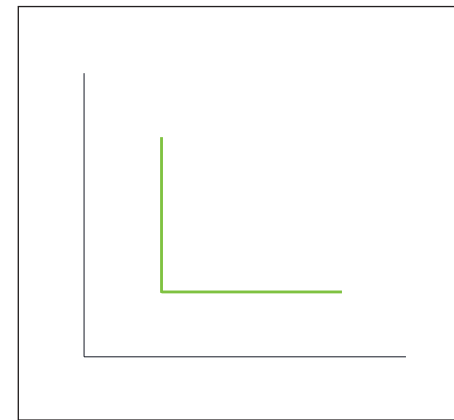
V-Shape

- Sharp shutdown to contain economic catastrophe and rapid recovery as controls are removed



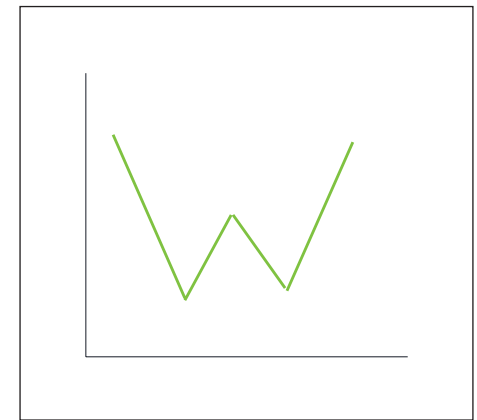
U-Shape*

- Sharp shutdown continues for a prolonged duration as economic impact is managed, before a gradual recovery



L-Shape

- Total shutdown as all businesses are impacted and permanent loss of output as firms go bankrupt and losses are not recovered



W-Shape

- Sharp shutdown followed by mini recoveries as multiple waves of the catastrophe hit and are managed accordingly

Economic impact

Business impact

- Immediate impact to revenue, cash reserves and working capital
- Less loan capability and lower spending over the short term
- Large risk for capital intensive businesses e.g. Banks

- Rapid product innovation required to capture share of wallet during economic downturn
- Adequate capital requirements for banks and insurers are critical to ensure business continuity until economic recovery

- Current way of operating unlikely to return to normal
- Businesses to pivot in order to remain in existence
- Industry consolidation is likely and the strongest will survive
- Reassessment of credit policies to assist businesses to recover

- As companies seek to return to business as usual, they may experience this double bounce in the short to medium term
- Financial forecasts to be revised to ensure adequate capital is available to recover from dual economic impact

* Anticipated economic response based on Deloitte Research

In conclusion



Managing the Bounce back

Leaders will need to think through financial, stakeholder and operational implications when managing the bounce-back across the various recovery scenarios.

Balance sheet

Key Stakeholders

Demand, Supply & Operations

Understand and monitor liquidity impact

- Identify liquidity risks early
- Monitor and control liquidity regularly
- Conduct scheduled stress tests
- Create a contingency plan

Proactively manage key stakeholders

- Key stakeholders: Regulators, central banks, providers of liquidity and funding, customers, suppliers, investors, lenders and trade financiers
- Clear communication and transparency to ensure trust

Assess impact on sales

- Calculate Return on Investment (RoI)
- Calculate conversion rate of sales
- Purchase funnel and customer leads
- Customer Lifetime Value

Manage working capital and profitability

- Meet debt obligations and examine interest payments
- Manage inventory
- Use up-to-date financial information for quick calculations
- Ensure expense ratios remained within acceptable

Test need/opportunity for more radical restructuring

- Digital platforms to enhance user experience
- Innovation and new product development
- Streamline value chain

End-to-end supply chain management*

- End-to-end supply chain assessment
- Assess inventory levels and financing
- Cost to expedite deliveries (transportation)
- Return of Goods

Seek additional funding early if required

- International Monetary Fund (IMF)
- Fiscal Policy
- Central Banks

Take advantage of relevant government policies and support

- Tax relief to assist impacted sectors
- Deferred payments
- Rental reductions/deferrals
- Decreased interest rates

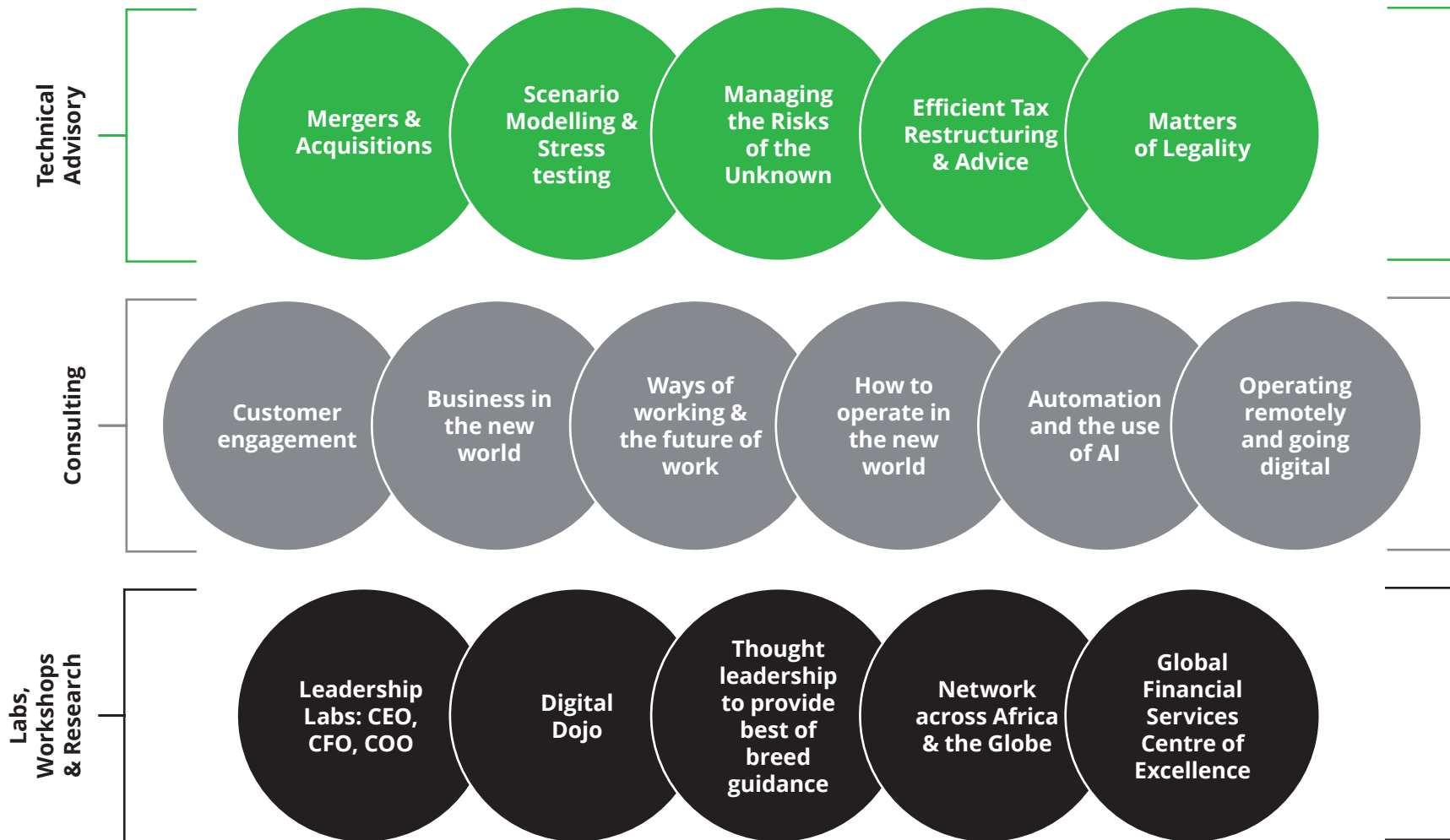
Assess impact on sales

- How many operating locations are still active?
- If not, when might they resume service?
- What is the capacity impact and timing of recovery?

*Not a priority concern to Financial Services organisations

What Deloitte can do with you

You are not alone - Our multidisciplinary organisation with an array of versatile professionals across both Africa and the Globe can partner with you to address the challenges that you may face in the "new world".



The ABC Response Checklist

Do you know your ABCs to effectively respond to this pandemic and navigate the "new world"?

- A** Be **Agile**
- B** Strengthen your **Balance Sheet**
- C** Put **Customers and Clients** first
- D** Go **Digital**
- E** Protect **Employees**
- F** Plan for the **Future**
- G** Engage **Globally**
- H** Improve **Health & Safety** measures
- I** Strengthen your **Income statement**
- J** **Join forces** and work together
- K** **Keep** calm and plan
- L** Manage **Liquidity**
- M** Enhance **Marketing Strategies**
- N** Thrive in the **New World**
- O** Rethink your **Operating Model**
- P** Assess **Processes & PPP**
- Q** Move **Quickly**
- R** Manage your **Risk & Response**
- S** **Stress Test**
- T** Enhance **Tech & Training**
- U** **Unite**
- V** Build a **virtual business**
- W** Implement new **Ways of Working**
- X** Manage your **(e)xposure**
- Y** **wh(Y)** the need for a new strategy?
- Z** **"Zoom" in** – consider new forms of communication

Contacts

Dirk Kotze

Director
dikotze@deloitte.co.za

Andrew Warren

Director
anwarren@deloitte.co.za

Bhavin Lala

Associate Director
blala@deloitte.co.za

Phuluso Kwindi

Senior Consultant
pkwindi@deloitte.co.za

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