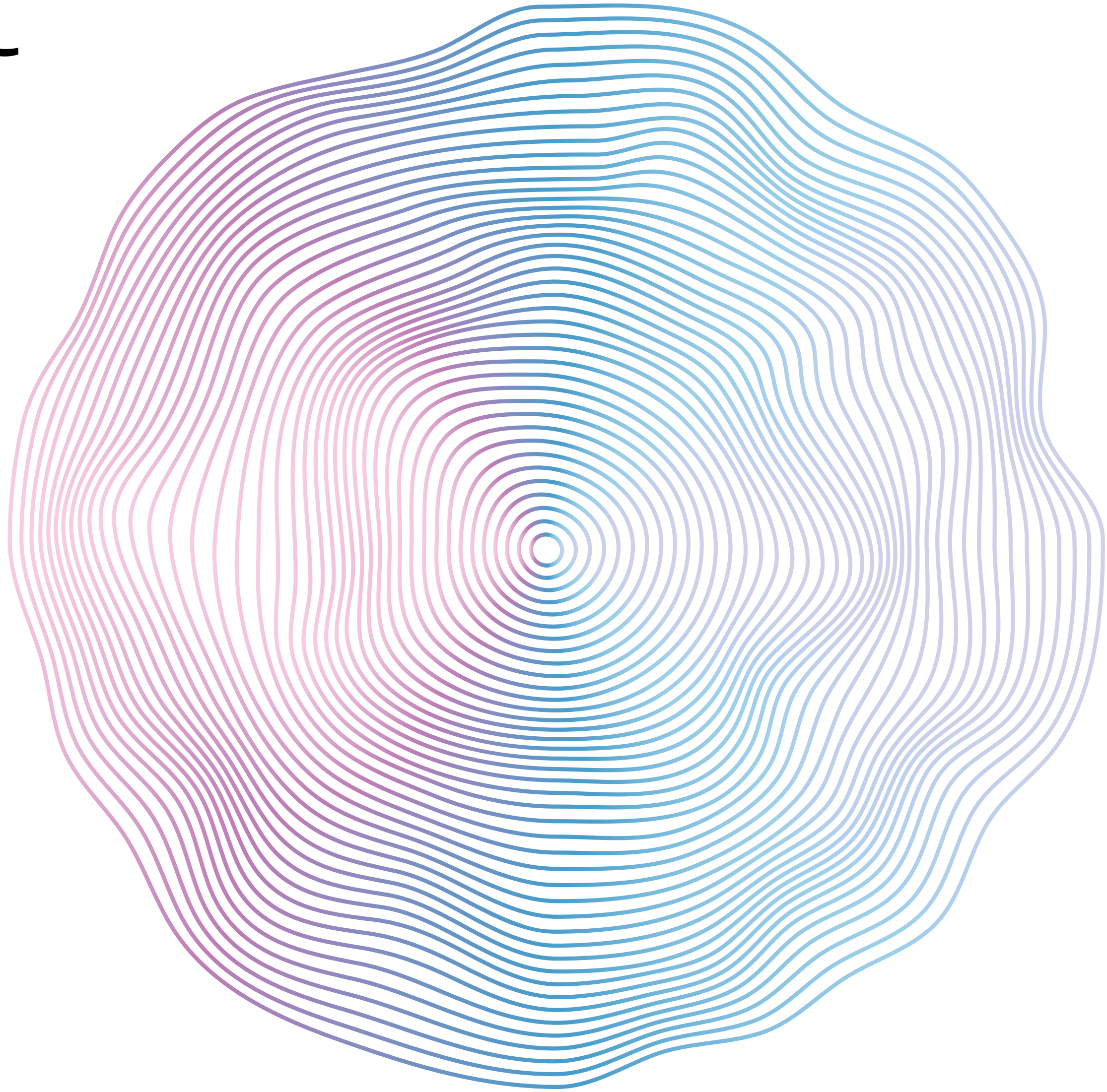
FinSight

Insights for the Financial Services and Real Estate Industries in Ireland

Issue 05 | 2021 | **Ireland**



IRISH 2021 OUTLOOKS
Banking, Insurance, Investment Management and Real Estate sectors

PATH TO CEO IN FINANCIAL SERVICES
In conversation with Francesca McDonagh, CEO, Bank of Ireland

PREPARING FOR TAKEOFF?
Outlook and restructuring options for aviation in 2021

RISKS, REGULATIONS AND RAMIFICATIONS
In conversation with Colm Kincaid, Director, Central Bank of Ireland

Deloitte.

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FOREWORD

DAVID DALTON
PARTNER AND HEAD OF FINANCIAL SERVICES
Deloitte Ireland

Welcome to the fifth edition of FinSight, a collection of the latest articles and perspectives from Deloitte professionals, as well as from experts and senior leaders across the financial services industry.

We publish against a backdrop of ongoing uncertainty. Even while this edition has been in production, the sands have shifted under our feet. Optimism about vaccine breakthroughs has given way to frustration at supply constraints. Hope of a faster reopening of the economy turned to dismay at renewed restrictions continuing well into 2021. Relief at the conclusion of an eleventh-hour Brexit deal has faded into confusion at additional business hurdles and costs.

With all of that said, some trends are enduring. What is striking, in fact, is just how many of the themes we address in this edition were apparent even before COVID-19 struck. In many ways, the pandemic has accelerated developments that had been happening anyway, albeit more slowly. It is the speed and impact of these forces, as much as their very existence, that will shape the financial sector in the months and years ahead.

Whatever stage firms are at in setting the 'reset' button with their strategies, leadership will be an essential component in getting them to their desired future state. So, it is appropriate that in this edition we launch a new spotlight series, 'the path to CEO'. We are grateful to Bank of Ireland's Chief Executive Officer Francesca McDonagh who shared her experiences with us for the article.

Digital first

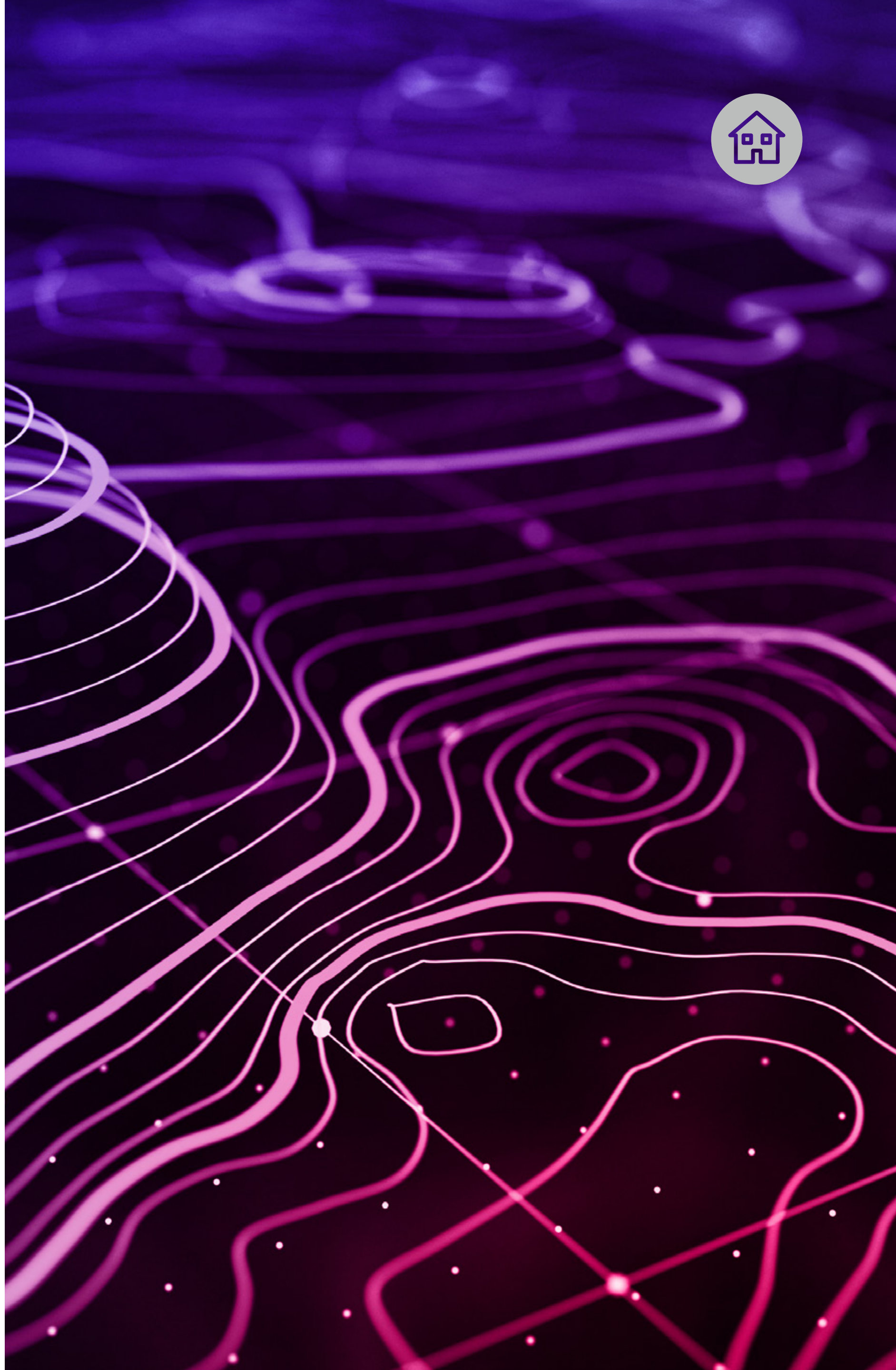
We are seeing some key themes emerge through working with our clients. Not surprisingly, there is a significant focus on digital acceleration. This theme repeats throughout our feature on the Banking, Investment Management, Insurance and Real Estate sectors. This article combines the local insight of Deloitte Ireland's sector leads with the work of our colleagues internationally in producing the 2021 industry outlook reports and surveys. They give a comprehensive view of the market now and offer their opinions on what lies in wait for those key sectors in financial services.

A phrase we are hearing a lot lately is 'digital first', and we are seeing considerable movement in financial services organisations becoming fully digitised, particularly in banking and insurance. This is due in part to the lockdowns that have restricted face-to-face interaction with customers, so online channels have naturally had to take over much of this work.

Cost reduction

The second theme is the pressure on profitability and the bottom line, which banks, insurers, and asset managers in particular are feeling. There is a continued focus on cost reduction, and the sense is that many businesses are looking at obvious ways to take cost out – such as robotic process automation (RPA).

However, RPA effectively automates procedural activities that have well-defined steps. The next wave, I believe, will be intelligent automation that reaches beyond procedure into aspects of the



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business that require more complex decision making. For example, there are opportunities to apply artificial intelligence to improve voice communications such as in contact centres. For example, a technology such as TrueVoice can 'listen' to a conversation and tell if the agent has given the client all the necessary information they need. It also detects sentiment, so it can understand how an interaction might be developing. It is still in the early stages for technologies like this, but they can be part of broader 'digital first' initiatives that underpin providers' broader aims to become more agile and respond to customer demands more quickly.

Role of collaboration

The third theme relates to collaboration. In Ireland, we had a glimpse of where this might be heading after four Irish banks announced plans to collaborate on their own digital payment app in response to competition from emerging 'digital first' companies.

The other aspect of this is that established financial operators may find it advantageous to work with smaller or more nimble players from the fintech ecosystem. There are two immediate benefits to this approach: it gives the legacy firms a capability that they don't have internally, and it allows them to deliver a new product or service to the market more quickly than if they had to build it themselves.

New ways of working

Speaking of business models, we can't talk about the impact of COVID-19 without addressing its effect on ways of working. If we face a future where people are spending more time working from home or remotely, what will the effect of this be on office or branch environments? For financial services firms, looking at this question through the lens of 'digital first' will involve serious consideration of future operating models. Is a centralised model the way forward, with increased automation at the centre? Or if branches are still necessary for serving customers face to face, does it make more sense to decentralise and migrate activity out to those networks?

Another theme the crisis has brought into sharp relief is the question of agility. The financial services industry is struggling with trying to be able to move more quickly in the market, but it has a big constraint in the form of its legacy infrastructure. We see cloud computing helping to address this, because it helps firms achieve the aim of faster speed by cutting ties with their older technology stacks.

Challenges remain around data privacy and security, but these can be overcome. And by addressing their technology constraints, banks, insurers and asset managers can also start to gain a single view of their data, which they need to do in order to leverage it for insights that enable them to target customers and sell to them more effectively.

Brexit – are we there yet

And lastly, another theme that loomed large over much of the past year has been Brexit. From a financial services perspective, a lot of the hard lifting had already been done to prepare for all eventualities, particularly from the global players with European businesses where they needed to have a licenced entity in EU and UK. Now, with a deal agreed, it's a question of how the situation evolves between the EU and the UK from a regulatory perspective.

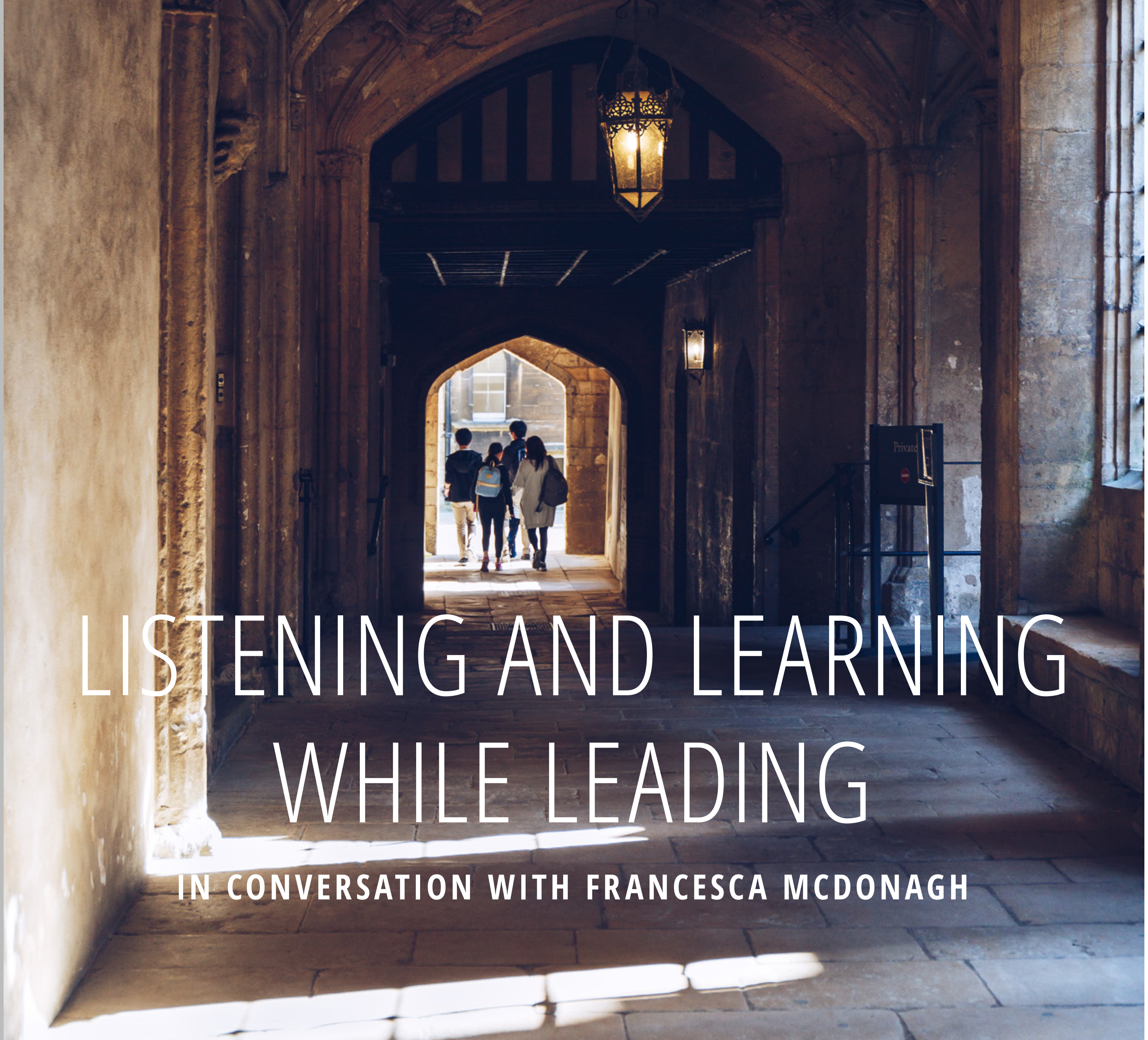
Regulations are another focus for this edition, with further change awaiting the finance sector in the form of the European Banking Authority's final Guidelines on Loan Origination and Monitoring. These regulations are intended to strengthen banks' loan books, avoid the risks that led to the global financial crisis in 2008, and embed greater resilience in financial institutions for the future.

Speaking of complexity, that is a recurring theme of our interview with Colm Kincaid, Director of Securities and Markets Supervision with the Central Bank of Ireland. In a wide-ranging exclusive interview, he explains how the Central Bank has had to deal not just with the challenges of regulating in a remote-first environment, but also dealing with the additional impact of Brexit on the securities and markets sector.

Aviation finance is a sector whose very business model has been so deeply affected by the restrictions needed to stem the spread of COVID-19. Our feature dedicated to that industry looks in depth at the liquidity challenges facing airlines, lessors, and funding partners, along with the options they have for restructuring. As the article makes clear, this is a necessary development but that does not make it a negative one; in fact, it could even have a positive outcome for Ireland, which is becoming a preferred location for complex restructuring processes.

As we hopefully start to envisage an end to the most severe effects of the COVID-19 pandemic, I hope the thought leadership in this latest edition of FinSight are of benefit as we start on the path to recovery.

Kind regards,
David Dalton



LISTENING AND LEARNING WHILE LEADING

IN CONVERSATION WITH FRANCESCA MCDONAGH

FRANCESCA MCDONAGH
CEO
BANK OF IRELAND

In our new ‘path to CEO’ series, Bank of Ireland’s Chief Executive Officer Francesca McDonagh reflects on her career path to date.

CAN YOU SHARE YOUR PROFESSIONAL JOURNEY TO DATE? WHAT HAS ENABLED YOU TO ACHIEVE SUCH AN INCREDIBLE CAREER?

I never thought I would have a career in banking. I knew I wanted to have an international life, or career; I knew I wanted to do something that was intellectually challenging and rewarding, but also something that made a difference, that was bigger than me.

I went to a local state school but managed to get into Oxford University through a lot of hard work and luck as opposed to being naturally gifted. I did a degree in politics, philosophy and economics, and that led me to travel as well. Every summer I found jobs working overseas.

After university, I worked for HSBC for 20 years in the investment bank, and the private bank, but I spent most of my career in the retail and wealth divisions. I worked in the UK for a period but mostly I was overseas in Asia, Latin America and also the Middle East region before going back to the UK.

Then the Bank of Ireland opportunity came up. I got a phone call about the CEO role, and I thought, what an amazing opportunity at this stage of my life, in my career, to be a CEO of such a special institution. It was a bigger role in a smaller organisation but you have the full, enterprise-wide perspective, and full accountability. I was also very aware of Bank of Ireland's special role in Ireland; the bank is unique in terms of the impact it has on the Irish economy, households and businesses. It is an opportunity that was too good to turn down, and this is now my fourth year in the role.

WHAT ARE THE BIGGEST CHALLENGES YOU HAVE FACED ON YOUR PATH TO BECOMING A CEO? HOW DID YOU OVERCOME THEM?

When you come from a relatively modest background and you start having to interact with dons at Oxford University or very senior investment bankers in the City of London, you can sometimes feel quite insecure and think 'is this the place I'm supposed to be?' People will talk about impostor complex; people often talk about diversity in terms of gender or ethnicity, but actually class diversity was probably a bigger factor for me personally: overcoming being from a different class, educational background than a lot of colleagues in an earlier stage of my career. It required a lot of confidence, determination and self-belief.

Second, working internationally, you're a long way from home and dealing with very unfamiliar situations. It's exhilarating but also very personally challenging. For example, I was the head of personal banking in Indonesia when we had the worst floods in recent history and three separate terrorist incidents. Or in Latin America where physical attacks on branches were fairly common.

In environments like that, there is no rulebook, there's no training that you've gone through. You really have to trust your instincts, but also trust your colleagues and seek advice. Know when you're outside your comfort zone and when to ask for help. I think knowing the difference between: do I go with my gut or do I seek advice; those were really accelerated learning experiences for me.

And I would say coming in to Bank of Ireland has also been one of my biggest professional challenges. I appreciate I'm in a position of real privilege but starting in this role as CEO for the first time has been a real learning curve. I was seen as an outsider from the bank when I arrived, despite living here and taking Irish citizenship. It's a fantastic organisation with amazing history and heritage, but it's in a sector that needs to change. Irish banking – and bankers – are untrusted by many stakeholders, particularly the man or the woman in the street, because of banks' role in the financial crisis over a decade ago – but also the more recent tracker mortgages issue which was one of the first issues I had to deal with, literally my first month in the role. Every challenge is also an opportunity, and for me that means transforming Bank of Ireland while restoring trust and pride in the organisation.

Leaders must live and breathe their personal values and integrity, whatever the circumstances, or temptations, or demands of the role.

Communication has become so important during COVID-19, because there's so much uncertainty, ambiguity, and fear amongst colleagues and customers. Being a good communicator in terms of reading, writing, listening and speaking, is very important for leadership.

WHAT CHARACTERISTICS DO YOU BELIEVE EVERY LEADER SHOULD HAVE?

Your own personal values – your integrity – are absolutely non-negotiable. In a world where there is greater transparency and expectation, your personal conduct, as well as your professional behaviour, is really out there for anyone to comment and challenge. Leaders must live and breathe their personal values and integrity, whatever the circumstances, or temptations, or demands of the role.

Secondly, hard work. I've not seen anyone be successful in banking without it. The day to day is about preparation, reading, thinking, listening, taking on feedback. It isn't necessarily glamorous, but it's the reality of a regulated and quite technical sector.

Third is communication. That has become so important during COVID-19, because there's so much uncertainty, ambiguity, and fear amongst colleagues and customers. Being a good communicator in terms of reading, writing, listening and speaking, is very important for leadership. If you look at some of the most inspirational leaders in the world, they're often brilliant communicators. It's something you can enhance and develop. You're not born with it; it is absolutely a learned skill.

The reality, as a CEO, is that the more senior you become, the more edited and refined the information you get is. You sometimes you don't get the nitty-gritty about what's really going on. So one of the things I've been doing, without fail, since arriving at the bank, is to have an 'open door' session once or twice a month. Any colleague can sign up to it, there's no pre-screening by your boss, you don't have to be a top performer: everyone is welcome. It's usually eight to ten colleagues, it's totally off the record. And we have an honest conversation. I answer questions but I ask them as well: what's on your mind? What are the issues your team is discussing? What do you really want me to know?

I get huge insight and understanding at these open door sessions. And sometimes it's really bad feedback. That's really inconvenient but it's honest and true and it tells me where we need to go to fix or address issues.

We do a lot of anonymous surveys for our colleagues where we look at cultural engagement across the organisation. That is, for me, a goldmine of insight and understanding; listening and hearing what people are telling us.

CAN YOU NAME A PERSON WHO HAS HAD A TREMENDOUS IMPACT ON YOU AS A LEADER?

I don't have a role model. The people that have had the most impact on me are the people that I've worked for. This is such a lesson for leaders. Regardless of how senior they are, anyone who is a people manager, they are the most important person in their team members' lives at work.

I have learned so much, good and bad, from my previous managers. I had one leader who was so good at walking the floor, he was able to engage in such an authentic way. I've had other leaders whose technical grasp, understanding and consideration were superb. I've had managers who've been faced with really big moral decisions and no easy answers and seen how they've navigated it.

On the reverse, I've also worked for some people who were pretty bad. And I've learned as much from the less effective leaders about how not to be, as I have from really good leaders about what great looks like.

IN YOUR OWN ROLE AS A LEADER, YOU'VE COMMITTED BANK OF IRELAND TO GENDER EQUALITY IN EXECUTIVE HIRES. HOW DO YOU SEE THE GENDER BALANCE IN THE FINANCIAL SERVICES INDUSTRY?

Gender balance in banking, in Ireland, the UK, and Europe, is poor. Why is that? At the leadership level, you have far less female representation. At the entry points, and in the general population in banking, it's 50/50. Something seems to happen at a certain middle management stage. We've done a lot of work around understanding that and making sure we remove the boundaries or the barriers that are there.

Often, because I'm a woman, people will always ask me about gender, but the broader issue is inclusion and diversity. First of all, the business case for why we want diverse and inclusive work environments is really compelling. If you exclude big chunks of the population from senior management inadvertently, if you exclude people who come from a more diverse background – whether it's ethnic minorities, LGBTQ+, physical ability or gender – you are cutting down your talent pools. So you are just making it more difficult to attract and retain talent.

Also, if you have the same people, from the same background, the same attitudes in a room, they will not make as good a set of decisions as the next room where you have more diversity – particularly diversity that reflects your customer base. So there's a really basic logic to why diversity and inclusion is good.

I think gender is just so visible; women are 50% of the population and 50% of our customer base, why don't we have 50% of our senior management reflecting that? That's obviously a commitment we've made, and we've made great progress and are hopefully on track to achieve that. We are also the only Irish bank to have published our gender pay gap in 2020 and we'll do that again in 2021. We weren't required to that. We wanted to lead the way in Ireland so we did it proactively. Even when our numbers aren't great – because we have more senior men – we wanted to be open, and track it and report against it.

There are other areas too: the LGBTQ+ diversity and inclusion work we've done is really important. Equally, we've just been able to achieve the prestigious disability standard, which is a workplace accreditation to recognise our commitment to disability inclusion.

We've also made the bank's culture less formal. I think COVID-19 has helped that. Everyone has seen the inside of each other's homes and bedrooms, people are more casual. We've probably got a greater sense of each other by working remotely, bizarrely.

MORE WOMEN NOW HOLD C-SUITE LEVEL ROLES IN FINANCIAL SERVICES FIRMS THAN EVER BEFORE, BUT RELATIVELY FEW HAVE BECOME CEO. WHAT ADVICE WOULD YOU GIVE TO WOMEN, OR PEOPLE WITH DIFFERENT BACKGROUNDS OR ABILITIES, ABOUT GOING INTO LEADERSHIP POSITIONS FOR THE FIRST TIME?

I do feel, in my role, showing that a female can be CEO of a pillar bank like Bank of Ireland, comes with responsibility. My advice for anyone in financial services: there's a huge amount of change, so a leader or anyone with ambition to really progress in their career needs to be thinking ahead, about what's coming next, and to get prepared.

In a world of change, it's so important to broaden our knowledge base. I would encourage them to be curious about technology in particular. The whole

My advice for anyone in financial services: there's a huge amount of change, so a leader or anyone with ambition to really progress in their career needs to be thinking ahead, about what's coming next, and to get prepared.

digital agenda is already massive for everyone in financial services.

In financial services, the symbols of power have tended to be fairly patriarchal, male and institutionalised, and I'm not sure that has served the stakeholders of banks particularly well. The symbols of power sometimes need to be challenged. And we're seeing that from fintech disruptors, and other new entrants in financial services. I would encourage someone, whether they're working in a startup or working in an organisation like ours, which is 235-plus years old, to be challenging the status quo and looking at different ways of doing things.

Pioneering can be quite a lonely pursuit if you're the only one in the room, so you have to build allies and not give up. My progression in my career hasn't always been in a straight line; I've had ups and downs as well, but I think ultimately I had networks of support that helped me leverage my passions and beliefs.

WHAT ARE YOU DOING TO ENSURE YOU CONTINUE TO GROW AND DEVELOP AS A LEADER?

I speak to my chairman about my own development plans and how I keep on learning as well. Sometimes [it's about] getting out of your own environment and learning. Before COVID-19, when we could travel, I attended an IBM event that was focused on future technology and quantum computing and it opened up my eyes to world of possibility in our industry beyond the here and now.

Sometimes, taking yourself to another sector, or thinking forward, talking to peers who don't necessarily work in your geography or your industry, is really stimulating. So I try and seek out those opportunities. Ironically, lockdown has given us opportunities to go to conferences we would never think of travelling to. I recently took part on a panel at the World Government Summit in the UAE by Zoom; virtually sitting next to Larry Fink as the leader of BlackRock, and other investors, talking about the future.

Plus, I speak to my Irish peers and CEOs, and it's really interesting to understand the challenges they face. Many of them are customers, they give me feedback, and that's also a support network for me. Being a CEO can be quite isolating, and you want to make sure you have a network that supports you and complements your thinking also.

LEADERS ARE FACING HUGE CHALLENGES DURING THE COVID-19 CRISIS, SO HAS THERE BEEN ANY CHANGE IN YOUR OWN LEADERSHIP STYLE THAT YOU'VE MADE?

I really want to make sure we keep some of the changes, that we don't go back: for example, much more flexibility in how we work. More than 70% of our colleagues are working from home all the time. We obviously have many colleagues on the front line, in branches every day as well. But there's a mindset shift, that you don't have to be in the office

to be working. I think we will go back to the office but it will be a hybrid approach.

Number two is the importance of communication. I've probably spoken to more colleagues from my home than I ever did when I was in the office, because you can do a Zoom and invite 10,000 people and have a conversation using technology. People have looked to leaders for empathy, for direction, for motivation, for reassurance; how I speak to colleagues has never been as important as it is now.

We have accelerated decision making, and we have sought to improve empowerment. Now, the challenge is making sure that it sticks: that the more agile, dynamic, delegated way of making decisions remains in place, that we maintain efficiency – in a risk-managed way – and we don't go back to the old way of doing things. During lockdown, we did a big review of our internal governance, to look at ways to have better governance but with fewer meetings or papers at times.

And awareness of our responsible and sustainable banking agenda has increased: our role in society and in community and how we treat our colleagues as well as our impact in the broader sustainability of the environment.

We've also had to make tough decisions. As any business CEO, if your revenue is being reduced – and some of it won't come back – we made some tough decisions in 2020 around costs.

We couldn't stand still. It's not just running crisis management, it's also delivering on the strategy; keeping the discipline between the "here and now" crisis, but also the longer-term strategic focus and deliverables.

This interview took place on 11 February 2021.

Inclusion in progress

Bank of Ireland has four priorities as part of its wider inclusion and diversity [I+D] strategy. These are: increase workforce diversity; foster inclusivity; financial wellbeing, customer and community impact; and strengthen inclusion and diversity governance and accountability.

Milestones to date:

- First Irish bank to set a public target for all management and leadership appointments to represent a 50:50 gender ratio by the end of 2021
- It tracks progress against this target at all stages of the recruitment pipeline, so HR can intervene where there are low levels of female applications and support hiring managers
- Recruitment Charter codifies a commitment to hiring diverse talent
- Board adopted the Hampton Alexander and the Balance for Better Business targets of at least 33% female directors by 2020 and 2023. Medium-term aspiration to have broadly equal gender representation at Board level
- All job specs are checked for gender-neutral language and amended as appropriate
- Working groups in each division drive local, tailored initiatives to improve gender balance
- Gender Balance Network established in 2017, led by colleagues, for colleagues
- Family-friendly rooms across all office buildings as a safe space for colleagues who are breastfeeding or taking fertility injections. The bank also offers menopause consultations, webinars, and supports for colleagues
- Increased maternity pay to 26 weeks full pay, including for adoptive and surrogacy leave, and introduced paid fertility leave. Colleagues of all genders (including non-binary) can apply
- GEC Female Mentoring initiative improves visibility of female talent, supports development and encourages female colleagues to apply for roles
- Quarterly I+D Dashboard circulated to key stakeholders including the Executive Committee Culture Steering and onwards to Board
- Mandatory I+D goal introduced for all senior leaders in 2020 as part of their performance achievement to strengthen accountability
- Bank of Ireland's With Pride network recognised within the LGBTQ+ inclusion awards at the 2020 Diversity in Tech awards
- Bank of Ireland won the best LGBTQ+ employee resource group at the Gala Awards.

ALTERED LANDSCAPE

Assessing the impact of COVID-19 on the Banking, Insurance, Investment Management and Real Estate sectors.

It is no exaggeration to say COVID-19 has remade our surroundings in many fundamental ways. Trends that had been bubbling under for years suddenly burst to the surface. Like an accelerated kind of evolution, the outcome is an environment that looks radically different to that of a year ago.

Just as volcanoes reshape their surroundings with force, they also leave behind changed landscapes that, after a period of adaptation, can bring about new growth.

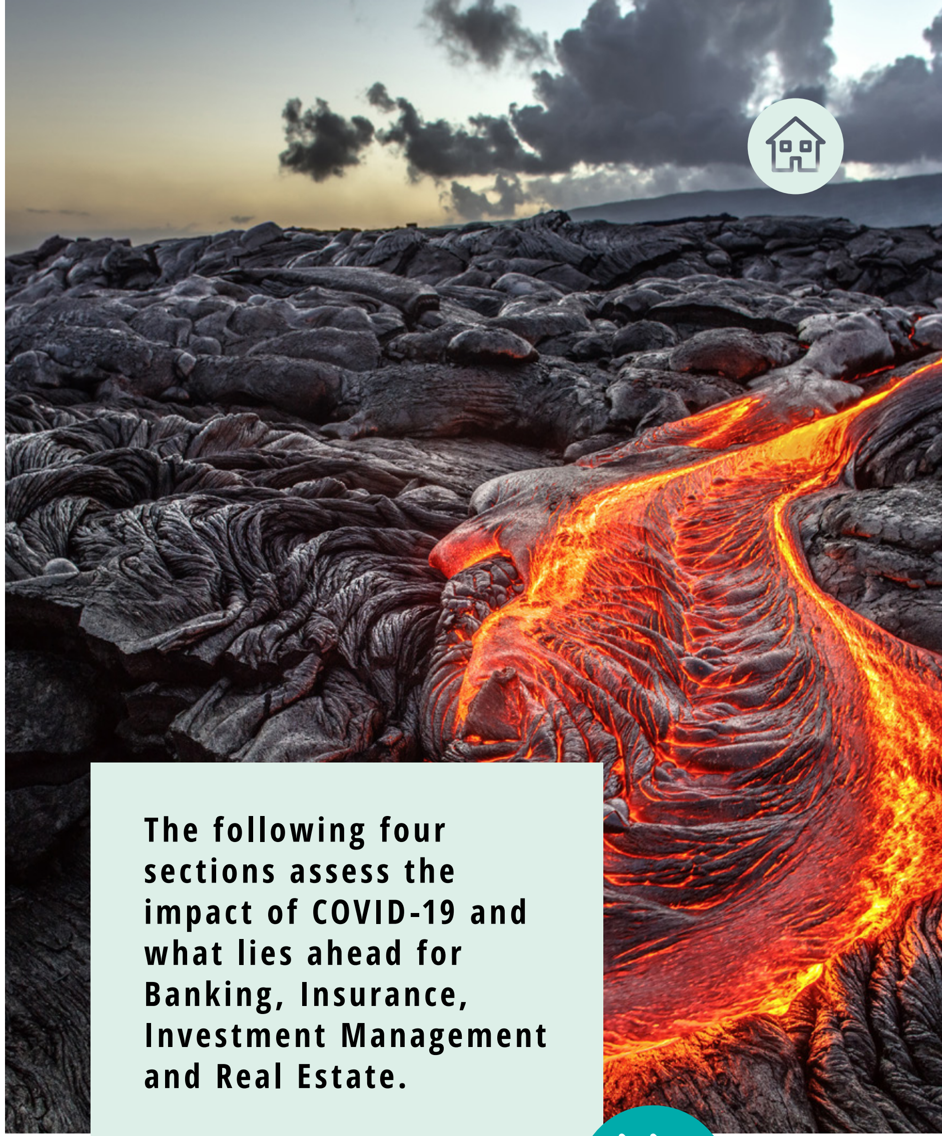
For the financial services sector, a planned gradual evolution towards digital has been overtaken by events. The past year has revolutionised customer behaviour and expectations, while the industry's operating models have also been forced into rapid readjustment.

In this article, Deloitte Ireland experts look in depth at the implications for four sectors within the financial services industry. First, they examine how banking needs to show a greater focus on technology, agility and resilience.

Similarly, the insurance sector must make the right strategic decisions and strike a balance between focusing on cost and protecting their business.

The world of investment management is being reshaped by external forces in the form of regulations, customer expectations and legacy costs. Meanwhile funding for commercial real estate must take stock of a landscape where the dynamics are much changed from a year ago.

Drawing upon in-depth knowledge of the Irish market, together with the insights from Deloitte's global outlook surveys, our experts chart a map for the newly reformed terrain and provide a path for the financial services industry.



The following four sections assess the impact of COVID-19 and what lies ahead for Banking, Insurance, Investment Management and Real Estate.

Learn more by accessing Deloitte.ie

01

IRISH 2021 OUTLOOK FOR

BANKING & CAPITAL MARKETS

- PRESSING THE RESET BUTTON -

SEAN SMITH
PARTNER, BANKING LEADER
Deloitte Ireland

If we wind the clocks back to the beginning of 2020, many banks would have identified pandemic risk on their risk register, but few would have rated its likelihood high on that list. So when COVID-19 struck Europe during the first quarter of last year it meant that banks not only had to navigate a novel and extremely challenging situation, they also had to reassess their business model and the threats to that business. Possibly shaped by their experiences in the financial crisis of 2008, we saw many Irish banks take a cautious and prudent approach whereas we saw many EU banks continue to invest and drive strategic change, particularly where this would give an advantage in the post-pandemic world.

> With digital penetration significantly increasing, more banks are looking at digital in a holistic way to serve their customers – giving the customer the experience they want rather than the process that works best for the bank.

In some ways, COVID-19 has accelerated trends that had been happening in banking anyway. All banks have struggled with profitability during a sustained period of low interest rates. The arrival of new types of competitors also predates the pandemic. But seen from another perspective, the sudden and drastic changes wrought by the crisis are a useful moment for banks to take stock, and even hit the reset button and embark on a different path. Below, we outline some of the key considerations for banks over the coming year.

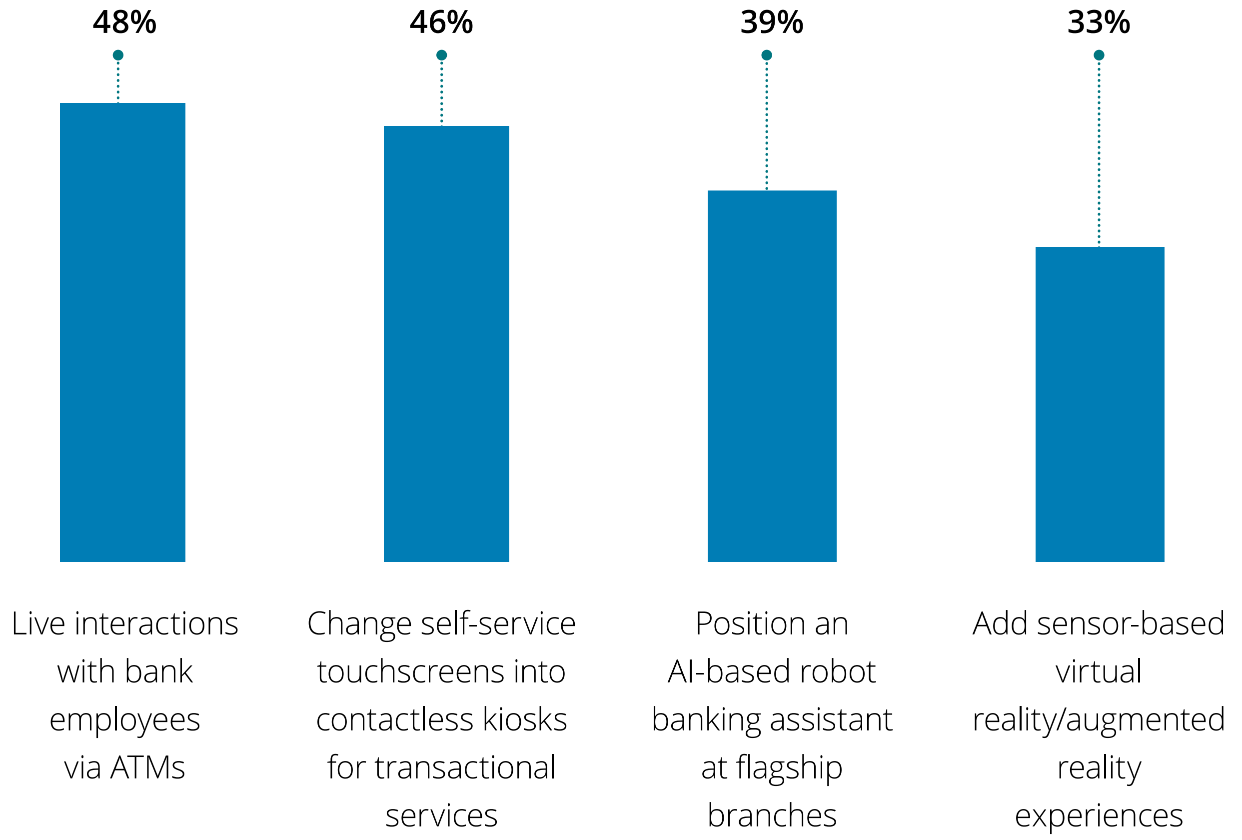
Digital embrace continues at pace

In the past, many banks struggled to achieve widespread penetration of digital channels among their customer base, partly because different segments of society were reluctant to use them. COVID-19 changed all that, because restrictions on movement during lockdowns effectively forced people to go online. The firms that had invested more in digital were able to manage this process more efficiently and were successful in the early days of lockdown.

With digital penetration significantly increasing, more banks are looking at digital in a holistic way to serve their customers – giving the customer the experience they want rather than the process that works best for the bank. Although there will always be a portion of the customer base that want to visit banks in person, I expect to see more of them being repurposed to digital hubs and a lot more customers doing most of their banking online. Hyper-personalisation will be key as will be the technology that can identify suitable and appropriate products for customers and treating vulnerable customers appropriately. As the Deloitte Global Outlook Survey has shown, some banks are considering a number of digital capabilities for their branches over the coming year.

Figure 1. Some banks will add more digital capabilities to branches over the next year.

Digital changes being considered



Source: The Deloitte Center for Financial Services Global Outlook Survey 2020.

Cost efficiency

In an environment where extremely low interest rates challenge profitability, banks must turn to what they can control: cost. This doesn't mean cutting all cost but rather developing a clearer understanding of the bank's return on spend across the business vertically and horizontally. Investment will be crucial for banks to adapt to the coming challenges, further driving the imperative to cut unprofitable businesses, products or processes to allow for future growth. Efficiencies of scale need to be considered also and we expect some significant M&A activity and asset sales/acquisitions over the coming year.

Figure 2. How COVID-19 has affected megatrends globally

Digitisation
Social distancing has already driven further **adoption of contactless technologies and digital experiences.**

Virtualisation of the workforce
Many **organisations have already adjusted to working remotely;** COVID-19 has led to **increased adoption of flexible workplace models.**

Focus on safety and surveillance
More **consumers will likely expect safety and precautionary measures from both brands and governments.**

Corporate responsibility
Taking steps to do the right thing in the COVID-19 context is becoming **table stakes for consumers.** The larger **purpose of banks is changing.**

Emergence of pop-up ecosystems
Value chain disruption will likely result in **more creative partnerships**, innovation, and agility.

Focus on cost reduction
Structural cost reduction could be a critical priority to ensure business continuity based on cash, profits, and revenues.

The sharing economy
Rising health and hygiene concerns and increased virtual work may **reduce demand for shared services.**

Urbanisation
While urbanisation has been growing steadily, **social distancing** and rising fears of contagion **may reduce the likelihood of people living and working in major cities.**

Global movement of people and goods
Based on likely government restrictions, the **movement of people and goods across national borders could decrease.**

Accelerated　　Decelerated

Source: Deloitte analysis.

A greater focus on fee-based products and alternative business models

After the financial crisis, banks had to divest sides of the business that derived fee-based income. Now, some banks will need to diversify their products – for example, bringing pension products to the fore – in order to stay competitive and to offer the end-to-end product set that customers now expect. This mirrors what is happening with fintech startups that are combining traditional banking services with cryptocurrency investment, for example. Other business models such as banking as a service, payments and bancassurance have also come on the agenda for banks looking to grow their offering.

All eyes on customer experience

Another aspect of embracing a digital strategy is how it meets the need to enhance their customer experience in a way that makes it easy and seamless for clients to interact. This is a kind of virtuous circle: the easier it is to do business with a bank via digital channels, the more customers will want to use those channels.

The agility agenda

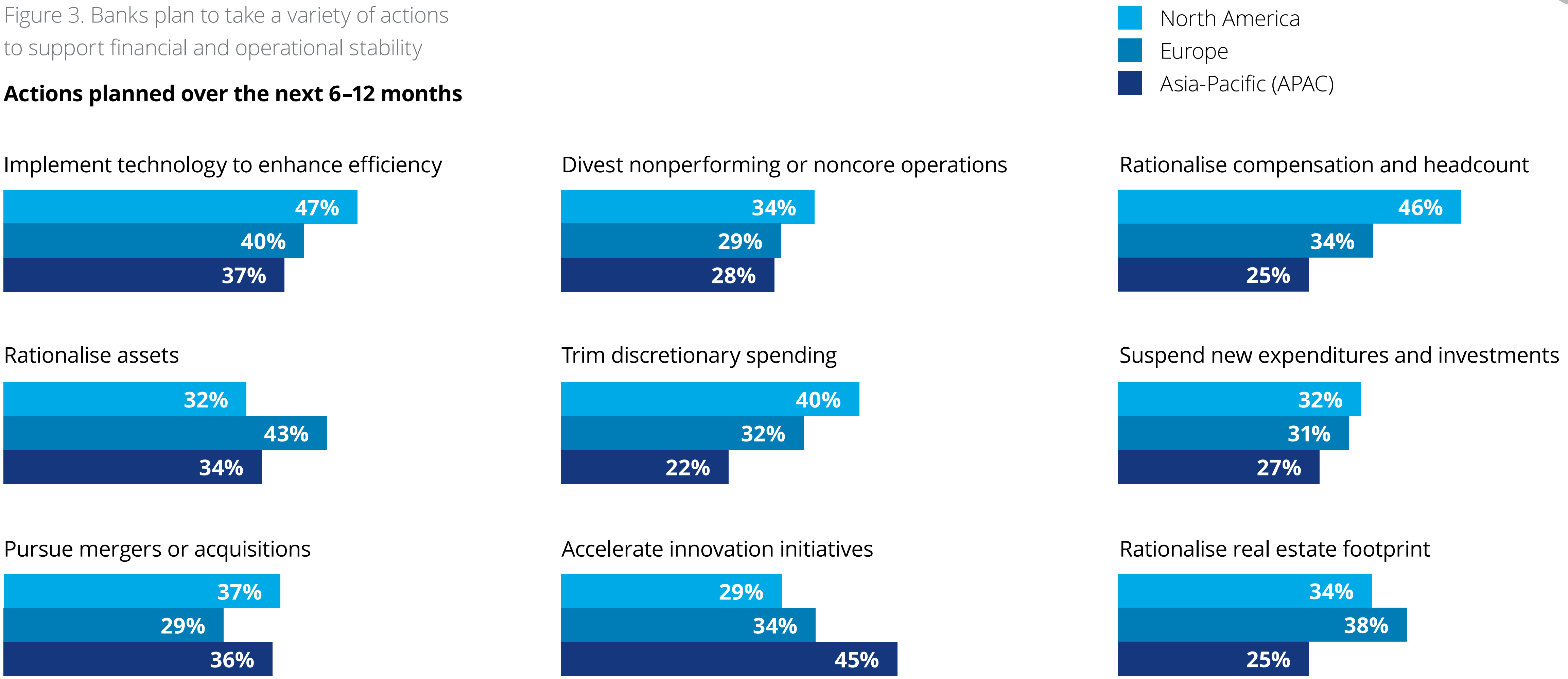
Ultimately, the bigger question for banks' digital strategies is whether to approach it as a layer on top of their existing platforms or carry out a deeper upgrade of their core systems. Banks that approach this question as simply a matter of adding a slick 'front end' are likely to reach a point in the process where their lack of agility could create issues, slowing down their ability to provide new services or manage their costs.

Some clients have chosen to tackle this by effectively building a separate 'digital' bank, running on different infrastructure. This has several advantages: newer technology is better able to meet the goals of resilience and agility, while there are many cost and speed benefits of setting up a greenfield operation.

COVID-19 may also lead to quicker adoption of cloud technology. In our experience, this is usually more successful in delivering agility than achieving cost savings. Financial regulators have historically looked at the cloud with some unease, but the drastic and sudden changes triggered by the COVID-19 crisis has encouraged them to engage more on this issue. We can expect to see a softening of their stance over time as banks demonstrate the reliability and security of cloud and regulators become more comfortable (possibly even regulating the cloud providers). This is likely to be a positive development for banks' digital strategies.

Figure 3. Banks plan to take a variety of actions to support financial and operational stability

Actions planned over the next 6–12 months



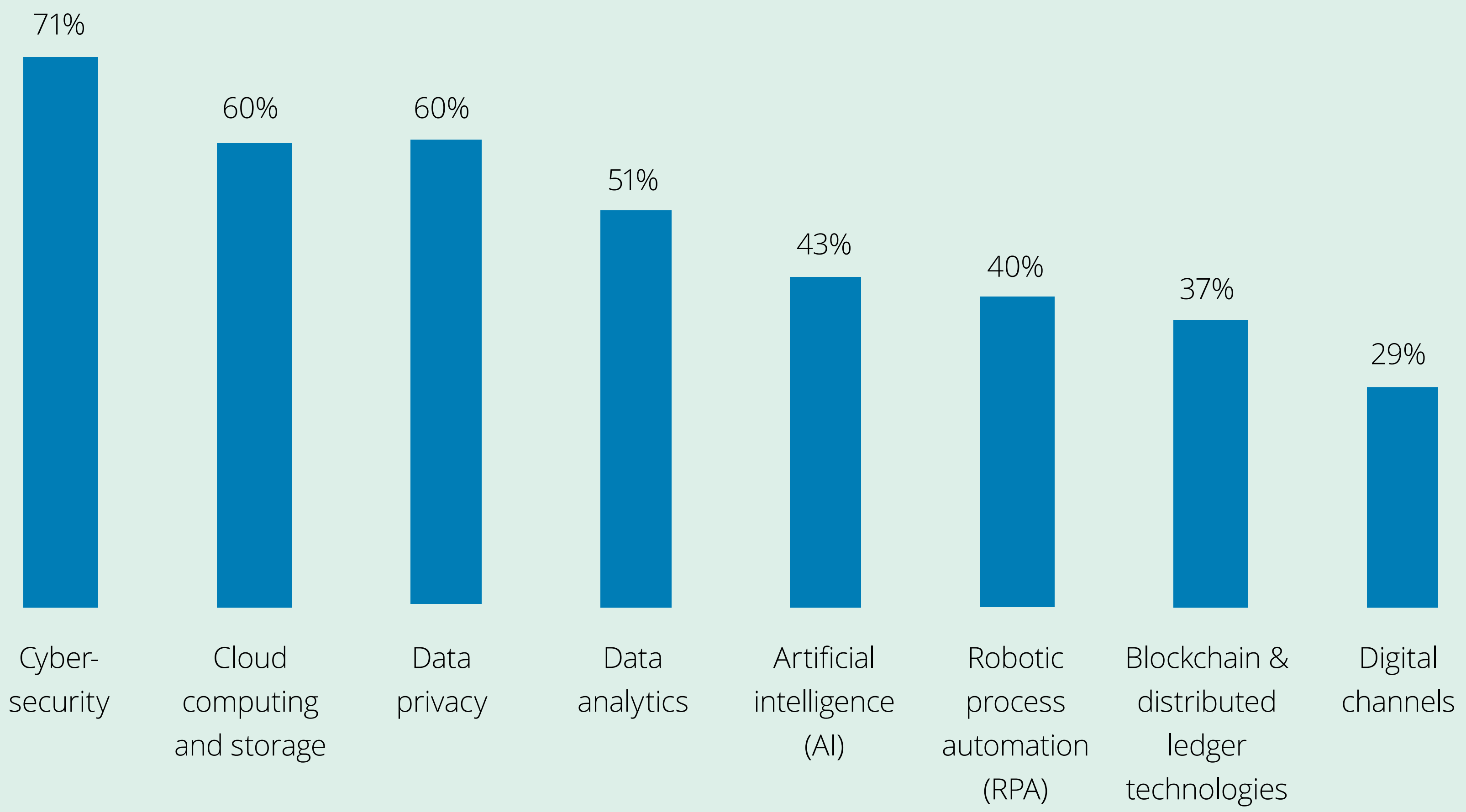
Source: The Deloitte Center for Financial Services Global Outlook Survey 2020.

The sudden and drastic changes wrought by the crisis are a useful moment for banks to take stock, and even hit the reset button and embark on a different path.

Figure 4. Banks plan to increase spending on various technologies over the next year

Finance respondents whose organisations plan to increase spending

Source: The Deloitte Center for Financial Services Global Outlook Survey 2020.



Operational resilience

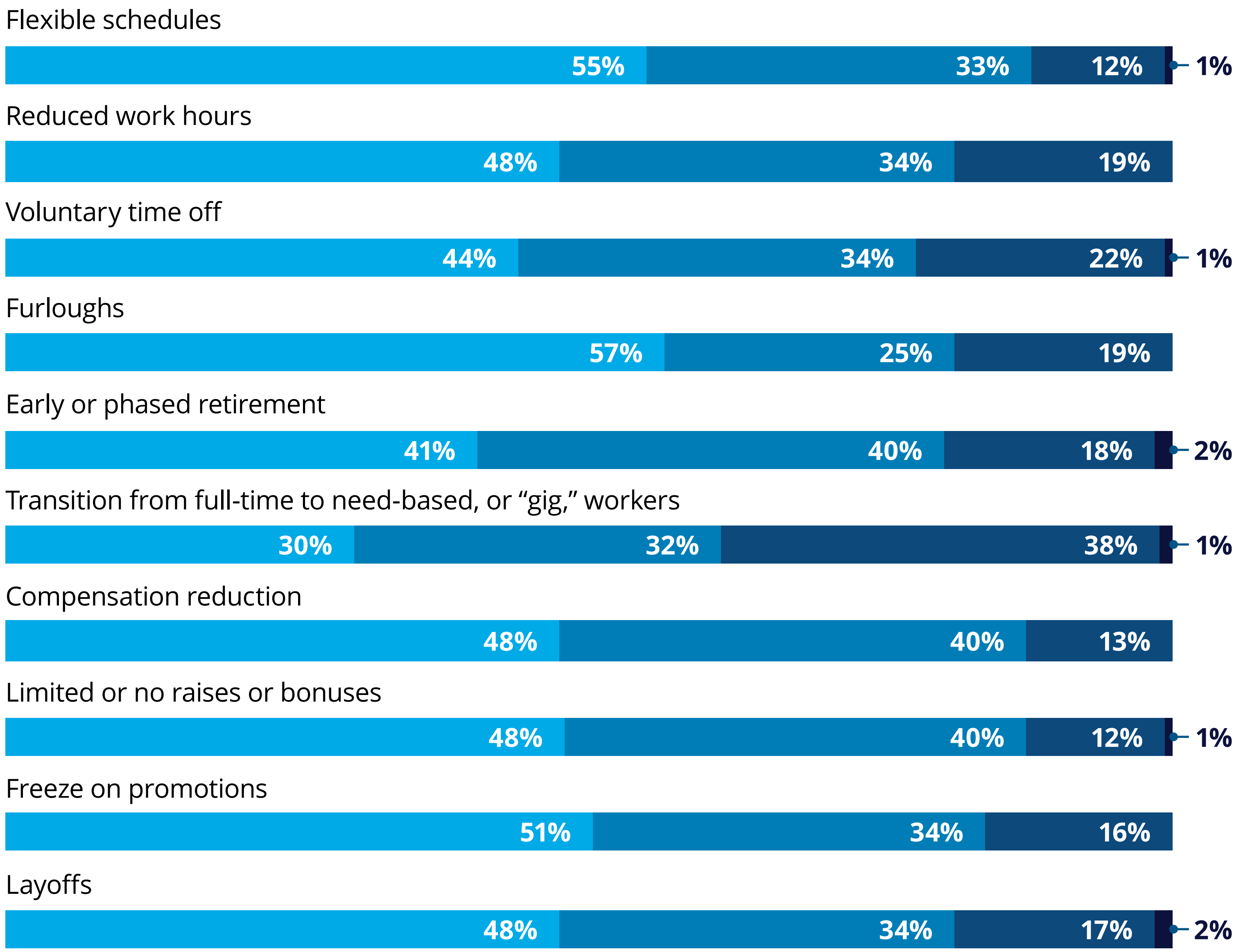
COVID-19 has focused minds on business continuity and the need for greater operational resilience. If a pandemic can happen, then it's not outside the realms of possibility that a system crash, cyber-attack or other event could bring business to a standstill – permanently. Operational resilience focuses not only on your ability to respond to such catastrophic events; it also puts a premium on prevention over cure. For these reasons, it is not surprising that cybersecurity (71%) and cloud (60%) scored highest in Deloitte's global survey of financial firms' planned spending. Both areas directly address the resilience agenda.

The talent question

There have been job losses as banks adapt and try to right size for the new environment, but the deep nature of the move to digital, and the restructuring it requires, will force banks to re-evaluate their talent strategy. In the digital world, the formula for competing with new fintech players and payment providers is likely to involve fewer people and more technology. The roles themselves will change, with banks increasingly needing more software engineers than bank tellers. While many banks are already facing this challenge, we feel it will become more pronounced over the coming years. This means that banks will be competing more regularly for talent with technology companies and social media giants. Are banks an attractive recruitment proposition by comparison? Or can they identify suitable candidates for reskilling for this new world from within their existing teams? Deloitte's Global Outlook survey sheds light on actions that banks have taken to date in adjusting their employment plans.

Figure 5. Banks continue to make talent changes in response to COVID-19

Employment actions taken to date



- Have already implemented
- Planning to implement
- Have not implemented and not planning to
- Don't know

Source: The Deloitte Center for Financial Services Global Outlook Survey 2020.

Conclusion

For the past number of years, banks have been somewhat caught in the middle between low interest rates and limited ability to launch new products that will make a difference to their profitability.

In a way, for all the many challenges brought about by the COVID-19 crisis, it has also created a series of new directions the banks can start to follow. It has allowed digital to make long overdue progress. The enforced moves to remote working have opened up questions about the need for large, centralised offices or extensive branch networks. Questions that were never on the table before are suddenly up for discussion.

From a strategic standpoint, banks can see 2020 as a reset button. It has given them permission to examine some things they couldn't look at before. As we look ahead to 2021 and beyond, the change is not over; it is just beginning. At the time of writing, we are still dealing with a heavy surge of COVID-19, while the ink is still drying on the eleventh-hour Brexit agreement. Now banks must focus on how to navigate the current uncertainty and emerge from it in the hope of remaining attractive to analysts and investors while supporting their customers and meeting regulatory expectations.

Read the global **2021 Banking and Capital Markets Outlook**

02

IRISH 2021 OUTLOOK FOR

INSURANCE

- DRIVING CHANGE -

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Irish insurance carriers, their customers, partners, management and employees faced significant challenges in 2020. The COVID-19 crisis had a material impact on individuals, SMEs and corporates, society and the wider economy which has had a direct impact on the industry's performance and individual insurer action plans and strategies.

However, in Deloitte's point of view, the COVID-19 crisis has accelerated many of the changing dynamics that were already underway, and this is evident both at a global and local Irish level. The Deloitte 2021 Global Insurance Outlook and Future of Home and Motor Insurance reports highlight key macro trends that are very relevant from an Irish context.

General insurance

From a General Insurance perspective, COVID-19 brought the insurance industry into the spotlight and particularly the insurance sector's response to business interruption claims. This affected public confidence in the sector, which will need to rebuild trust through 2021. On a wider perspective, although lower economic activity during the various lockdowns led to some reduction in the volume of insurance premiums, that same reduction in activity also resulted in lower claims frequency.

Although the immediate risk of a shock of a 'no deal Brexit' on the Irish economy has passed, the pandemic and its aftermath are expected to hit many of the GI lines harder than others. Recovery of premium income in 2021 will be very dependent on the vaccination rollout, opening of the economy, improved customer confidence, and a resurgence of the many retail and hospitality businesses that have been severely impacted by multiple lockdowns. As of year end 2020, while insurers were more comfortable with the impact of COVID-19 on their portfolios, there remains a significant amount of uncertainty related to certain lines of business in particular as government supports start to be removed.

Life & pensions

From a Life & Pensions perspective, our sense is that there was a limited impact on new sales of protection business but lower investment volumes in Ireland. However, the high level of cash savings by individuals during the pandemic may mean there are opportunities to attract that cash into savings products when consumers have greater confidence later in 2021 particularly with negative bank interest rates.

Indications are that there were no material increases in lapses in 2020 and that the pandemic had a limited impact on protection and income protection claims to date. The longer-term impact on the morbidity and mortality from the pandemic is unclear. We do expect that growth and profitability in both annuity and non-term life insurance products will continue to be impacted in 2021 beyond by persistently low interest rates. In

Figure 1. Global life insurance premiums written are forecast to recover to pre-pandemic levels in 2021

Markets	Advanced	Emerging	World
2009–2018A	0.6%	6.5%	1.5%
2019	1.3%	5.6%	2.2%
2020E	-8%	0%	-6%
2021F	2%	7%	3%

Note: A denotes average, E denotes estimate, and F denotes forecast.
Source: Swiss Re Institute, *sigma* No. 4/2020.

addition, while it was hoped the pandemic might at least raise consumer awareness about the value of protection products (and the importance of the health agenda), indications are that this is not the case to date. This will be an opportunity for insurers to increase consumer awareness and market penetration.

Health insurance

With regards to the health insurance sector, the impact of the HSE concentrating on supporting the pandemic surge, supported by the agreement with private hospitals which ceased activity during the year to support the HSE, together with the rolling lockdown rules, meant that elective procedures and consultations were greatly curtailed. This in turn meant that there was a reduction in health claims during 2020. This is more than likely a timing issue and expectations are that claims volumes will increase in 2021 as the pandemic starts to lift.

In addition, there may be increasing pressure on health costs in the coming year which will flow through on the health insurance economics.

However, it is worth noting that there is a new agreement with private hospitals and, coupled with the latest lockdown, the expected increase in 2021 may be slower than originally anticipated. We would expect that increasing claims volume would start to materialise as the vaccination programme gains momentum.

A focus on resilience

Irrespective of sector, the COVID-19 crisis tested overall operational resilience in 2020. The manual nature of certain processes and capabilities, as well as legacy IT infrastructure, challenged insurers' ability to respond to the initial stage of the crisis. In addition, workforce, intermediary processes and third-party provider resilience arrangements were tested. We expect that operational resilience will remain a very important area of focus for insurers – and the regulator – in the post COVID-19 era.

Brexit

Although to widespread relief the Brexit agreement between the EU and UK was reached late in 2020, the implications and planning for it had a big impact on several insurers/intermediaries during the year. Brexit's implications will only be fully felt in the years to come.

A focus on regulation

Insurers across all sectors in the coming year(s) will continue to face regulatory and compliance policy and direction. In 2020, there was increased regulatory focus and more scrutiny on a number of COVID-19 related areas including dividend payments, business interruption cover, and solvency concerns.

In addition, non-COVID-19 related regulatory themes will continue to be a focus, including diversity and inclusion, differential pricing, and data privacy. The regulatory agenda will remain a key challenge for insurers – from a cost, business model, operational, customer and channel perspectives. Insurers are also preparing for the IFRS 17 reporting standard and this is taking a significant level of management attention, budget and time.

In addition to the regulatory agenda, government policy and intervention will bring both opportunities and challenges for the industry. The recent programme for government on insurance reform, and related action plan, the Sláintecare programme, and mandatory pensions, will also shape the industry in the coming years. This combination of legislation and regulatory supervision will mean that insurers will have to dedicate significant focus to navigate the immediate and downstream implications.

What customers want

A shift in consumer behaviours and expectations has accelerated and insurers locally and globally are responding to this dynamic. Customers are favouring simplicity – products and services that they can easily understand, buy, and use. In particular, we expect that there will be an increasing demand for features such as parametric/adjustable cover. Our global home and motor survey responses (see figure 2) point to these trends in more detail. At a high level, the key reasons that consumers gave for liking or disliking a particular product or service relate to its ease of use, the ability to compare offerings, adjustability of cover, and data privacy concerns.

The high level of cash savings by individuals during the pandemic may mean there are opportunities to attract that cash into savings products when consumers have greater confidence later in 2021.

Figure 2 part 1. Home and motor insurance customer reasons for liking or disliking products and services

Percentage product #1 choice

Basic	29%	Simple, most familiar Least intrusive, respects privacy Easy to compare	Not personalised or customised May be more expensive Too simple, no features
Self-controlled and adjustable	19%	Freedom to choose, more control Flexible, customisable Cost-effective	Too complicated Inconvenient, too much input Could be underinsured
Freedom to move (motor)	15%	Covers all modes of transport No need for additional cover Flexible	Do not need it Belief that it's already covered
Connected and preventative (home)	14%	Preventative, potential savings Personalised Access to a repair person	Intrusive Concern with privacy/use of personal data
Connected and cost focused (motor)	13%	Can save money, if drive less Seems fair Rewards good driving	Too invasive Lack of trust in insurer Concern with monitoring system

Diagram continued on following page

Figure 2 part 2. Home and motor insurance customer reasons for liking or disliking products and services

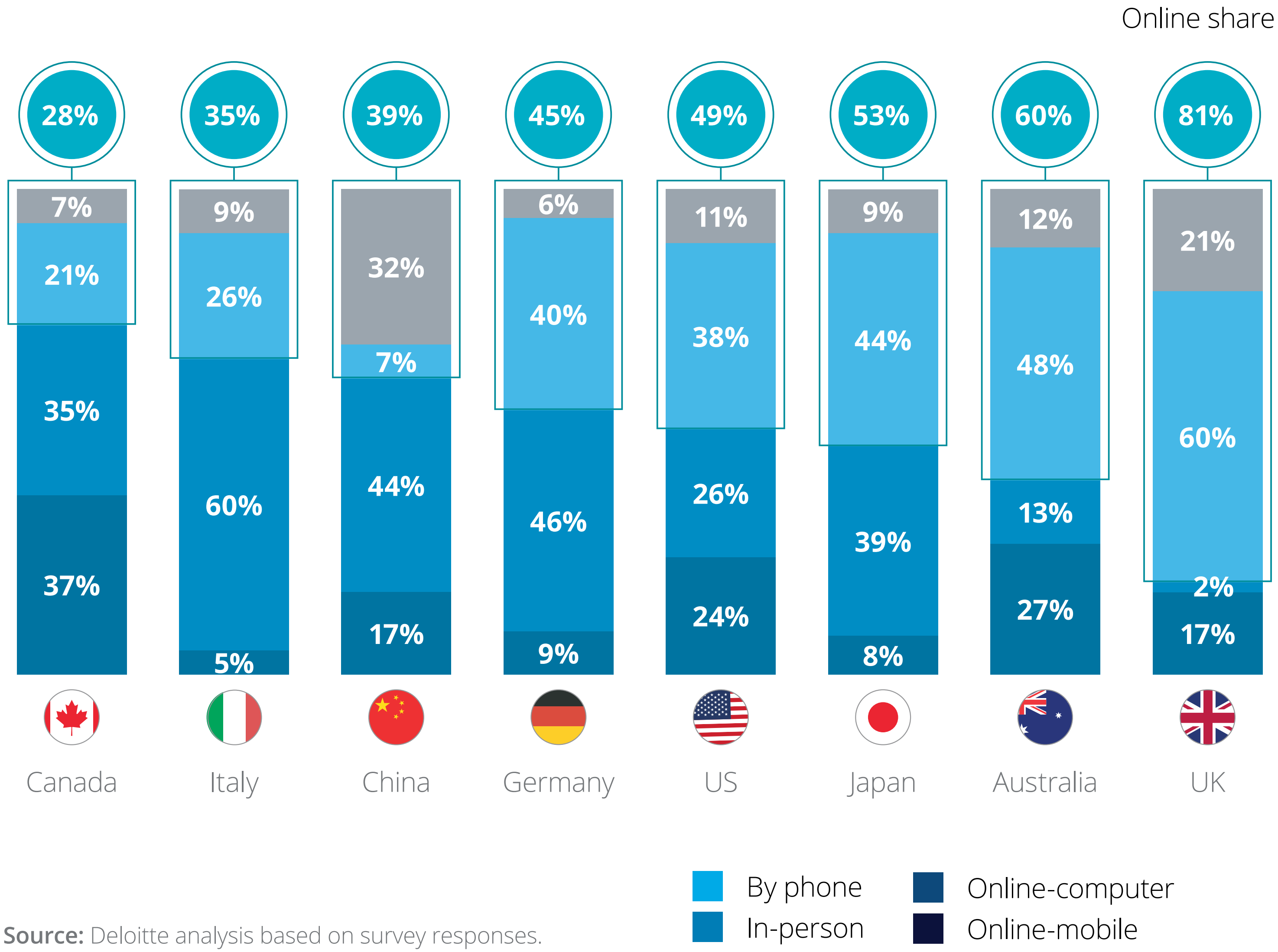
	Like	Dislike
Home concierge (home) 12%	Access to a repair person 24/7 support, peace of mind Simple	Sounds expensive Don’t need a repair person
Invisible 11%	Convenient Less to worry about Repairs by car manufacturer	No control, not transparent Worried about hidden costs Don’t trust bank, estate agent
Connected and broad service (motor) 11%	Tailored Potential savings, rewards safety Remote diagnostics and discounts	Concern cost outweighs benefits Lack of trust in insurer Concern with monitoring system
Connected and cost focused (home) 11%	Personalised Potential cost savings	Invasive Concern with personal data use Do not see need

Source: Deloitte analysis based on survey responses. Percentages do not total 100% because basic, self controlled and adjustable, and invisible products have each been aggregated across home and motor insurance.

While insurers need to shake up the status quo on product development, we expect their retail and distribution strategy and capabilities will be a key focus for them. The need for business agility has never been greater. Insurers will need to have a truly omni-channel capability supported by digital – including clarity on the role of branches, contact centres and social platforms.

Reimagining customer journeys that are truly customer-centric and digital across the business will continue to accelerate, including investment in direct online sales and service, enhanced digital broker/bancassurance supports and the transformation of the claims experience. The survey insights into consumers' preferred channels for buying motor insurance show these trends.

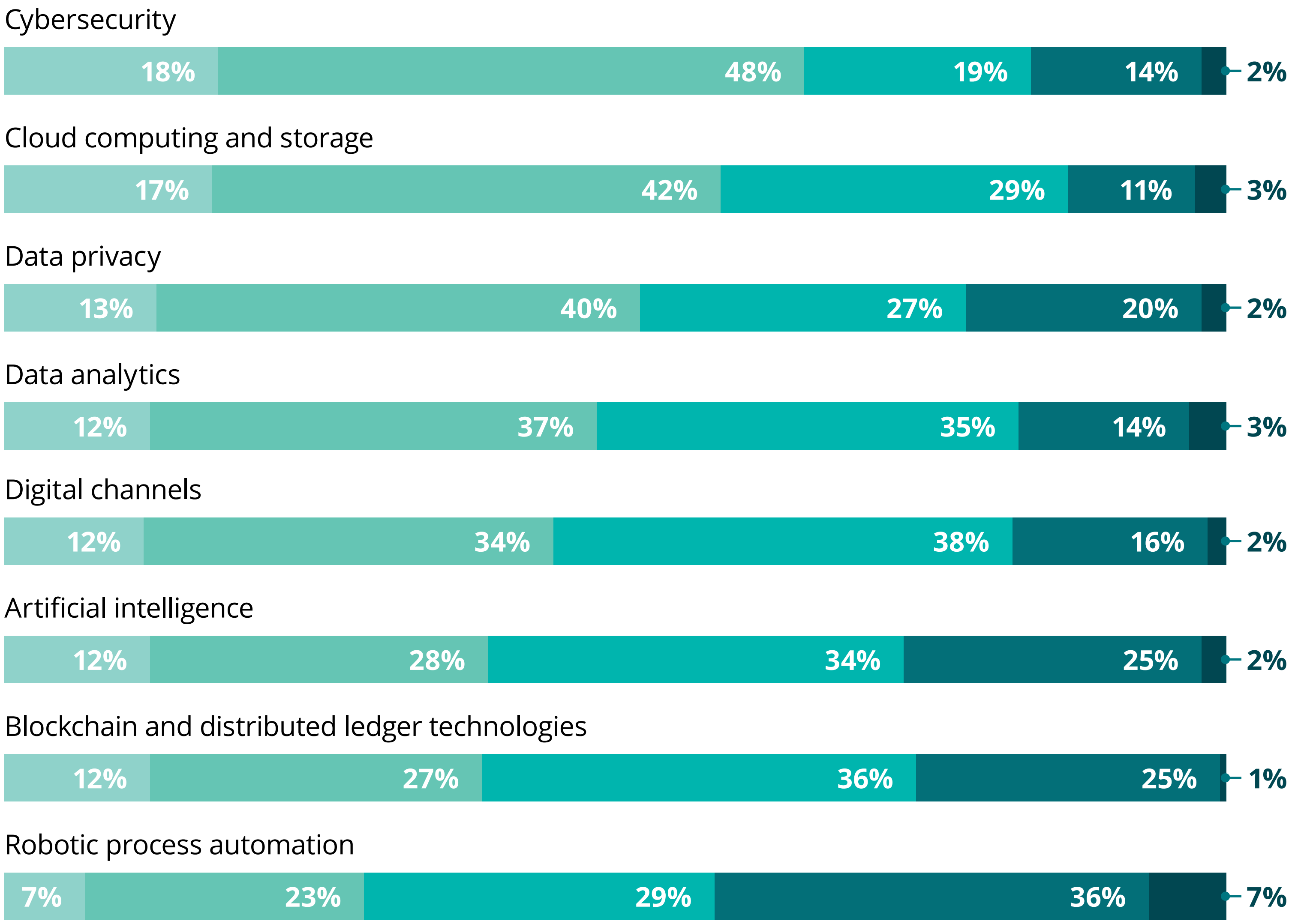
Figure 3. Preferred channel to buy motor insurance



Source: Deloitte analysis based on survey responses.

In our view, what is very important is that insurers have the ability to offer a truly differentiated value proposition for their customers. Key to maximising profitability will be not only looking at opportunities to digitise the end-to-end customer experience but identifying new growth opportunities through enhanced customer-centric value propositions that focus on driving loyalty, increasing cross-product holdings and enhancing customer lifetime value. Insurers should consider exploring new target segments and building tailored propositions to meet their needs, really understanding what drives value for them and how to win in the market.

Figure 4. Cybersecurity, cloud, data privacy, and analytics were identified as tech investment priorities



- Expect a large increase in spend
- Expect a slight increase in spend
- Expect no change
- Expect a slight decrease in spend
- Expect a large decrease in spend

Note: Percentages may add up to more than 100% due to rounding.
Source: The Deloitte Center for Financial Services Global Outlook Survey 2020.

Figure 5. Potential business and technology benefits of cloud

Business benefits	Technology benefits
On-demand self-service: pay-as-you-go, pay-as-you-grow	Rapid elasticity or expansion
Access to on-demand analytical and automation solutions	Broad network access, anytime, anywhere
Reduced burden of entry into new products or markets	IT agility/faster time to market

Source: Deloitte Consulting LLP.

Technology as an enabler

However, in the past, legacy technology infrastructure has hindered insurers' agility to respond and therefore technology will play a critical role in this journey. Insurers will need to have a clear vision of what their future technology architecture and ecosystem required to support the overall strategy – what technologies/capabilities will remain core, what will be outsourced and what partners will they work with (e.g. InsurTechs). Investment in cloud has accelerated innovation in the industry in recent years and we expect, arising from the pandemic, that this will gather further momentum in the year ahead. In tandem, enhancing cybersecurity capabilities will be a 'must' as insurers further develop their technology and digital platforms.

We expect that operational resilience will remain a very important area of focus by insurers – and the regulator – in the post COVID-19 era.

Intelligent automation and data

In addition, although the industry has invested in Robotic Process Automation (RPA) capability in recent years, it has been broadly focused on the efficiency or cost reduction agendas. We see this investment migrating to building a more sophisticated Intelligent Automation capability (leveraging a suite of tools and capabilities such as Artificial Intelligence, RPA, automation tools etc.) to support a more seamless end-to-end customer experience and assist in streamlining operations, enabling real-time decision making and the ability to manage peaks and troughs in demand more effectively. We predict that as insurers develop these capabilities, it will allow them to focus their staff on the moments that matter for their customers and partners, adding value and engaging with them rather than purely on processing tasks and/or data.

In parallel, insurers' ability to capture and harness customer and other external data sources to better target, service and support customers and intermediaries is becoming increasing important while keeping in mind data privacy concerns and ensuring customers are treated fairly. As insurers enhance their data analytical capabilities and continue to strive to maximise the value from data, they will also need to ensure that they have the appropriate governance and controls on the use and security of this data.

Talent/workforce agenda

The pandemic also has forced insurers to re-evaluate their talent/workforce strategies. Many insurers are likely to continue to have a hybrid workforce model even when the pandemic dissipates. This will shape the future workplace, workforce (talent, diversity, flexibility) and employee expectations. Therefore, insurers will need to set out a vision of what the 'future of work' looks like for the organisation and what its organisational archetype and operations model will be going forward.

As the industry is facing the impact on top-line premiums, increasing regulatory costs, changing customer and intermediary engagement models, and changing workforce dynamics insurers are inevitably looking at their overall cost base. This is driven by profitability pressures and the need to fund investments required to transform and digitise the business. It is worth noting that insurers need to strike the right balance between focusing on cost and protecting their business, making sure that they are making the right strategic decisions to drive down their cost base while not negatively impacting their customer experience – how do they use their efficiency gains to turn the dial on new growth opportunities, investing back into the core business through new revenue streams, pricing optimisation, and so on.

On a broader level and looking further ahead, insurers will also need to factor in the potential impacts of climate change on the books of business they write, their operations and funds being invested in. In addition, although there has been limited merger and acquisition activity at an Irish insurance carrier level, there has been increasing M&A activity in the broker sector in the last 18 months. We do not see this changing in the short term and insurers will need to understand the potential implications of this on their channel strategies and business models.

Read the Global
2021 Insurance Outlook

An analysis of the **'Future of Home and Motor Insurance'** survey.

03

IRISH 2021 OUTLOOK FOR

INVESTMENT MANAGEMENT

- A DRIVE TOWARDS DIGITAL -

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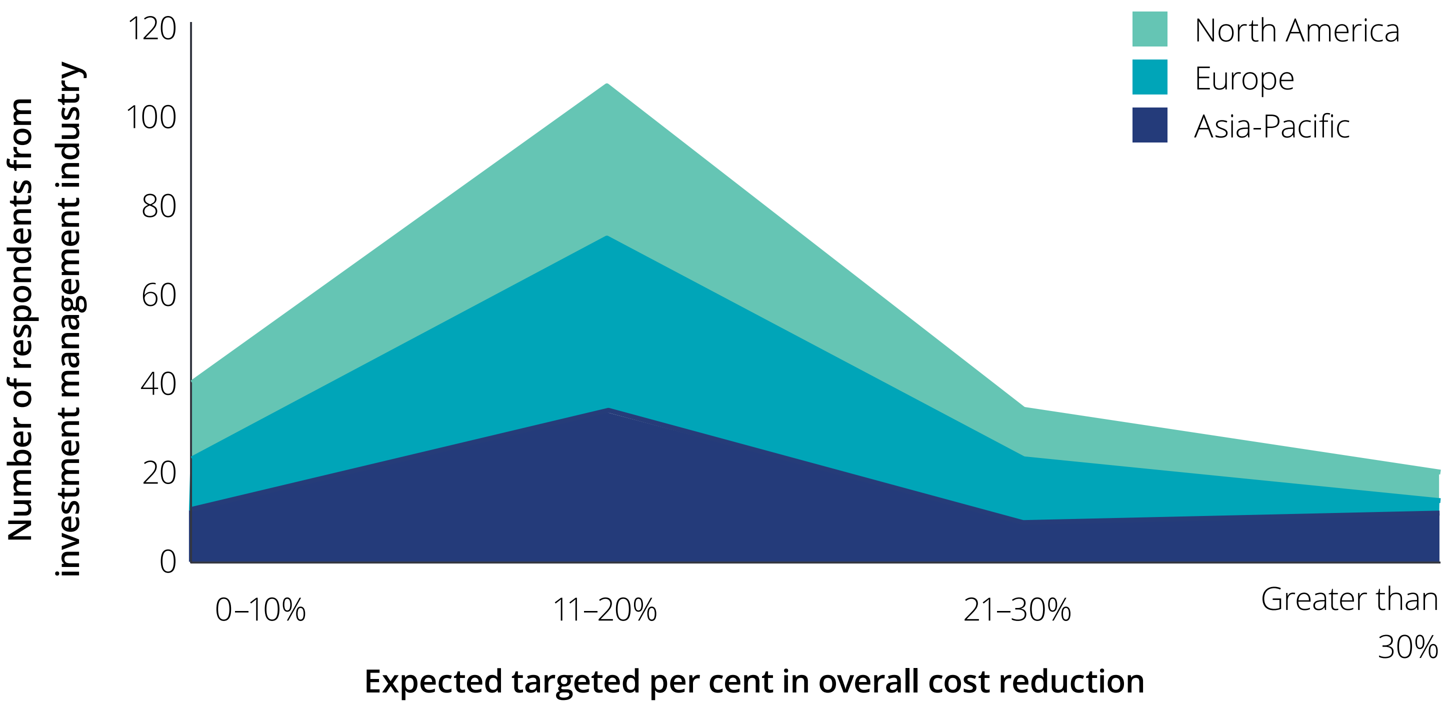
INVESTMENT MANAGEMENT LEADER
Deloitte Ireland

Even if we remove COVID-19 from the equation, the investment management market was always ripe for change. In many cases, the crisis triggered by the pandemic accelerated trends that were already emerging. Chief among these is cost pressure: increased competition was driving down the management fees that investment managers charge. As assets under management fell at the height of the crisis, the reduction was very significant and, in many cases, has not recovered. We have also seen a significant move from active management to passive management, where the fees are not as high.

On the cost side, investment management had become quite a personnel-heavy business over the years. Over time, and often in response to regulatory pressure, infrastructure costs have grown with enhancements to risk management and oversight areas in the business. Many organisations both on the asset management and asset servicing side had been looking at this area before COVID-19 struck.

Figure 1. Given the actions planned, what is the expected targeted per cent in overall cost reduction over the next year or more?



Source: The Deloitte Center for Financial Services Global Outlook Survey 2020.

Over time, and often in response to regulatory pressure, infrastructure costs have grown with enhancements to risk management and oversight areas in the business. Many asset management and asset servicing organisations had been looking at this before COVID-19 struck.

Tightening margins

Combine increasing demands on the infrastructure, together with pressure on fees, and ultimately it adds up to squeezed margins. Since the market dictates what firms can charge for the funds they manage, they need to shift their focus onto their internal costs in order to save margins.

This is one of the forces driving a renewed focus on digital technology. This is a multifaceted area: it covers both operational efficiency (using technology to automate where possible and drive down costs), and customer service (where digital technology serves to deliver a richer customer experience).

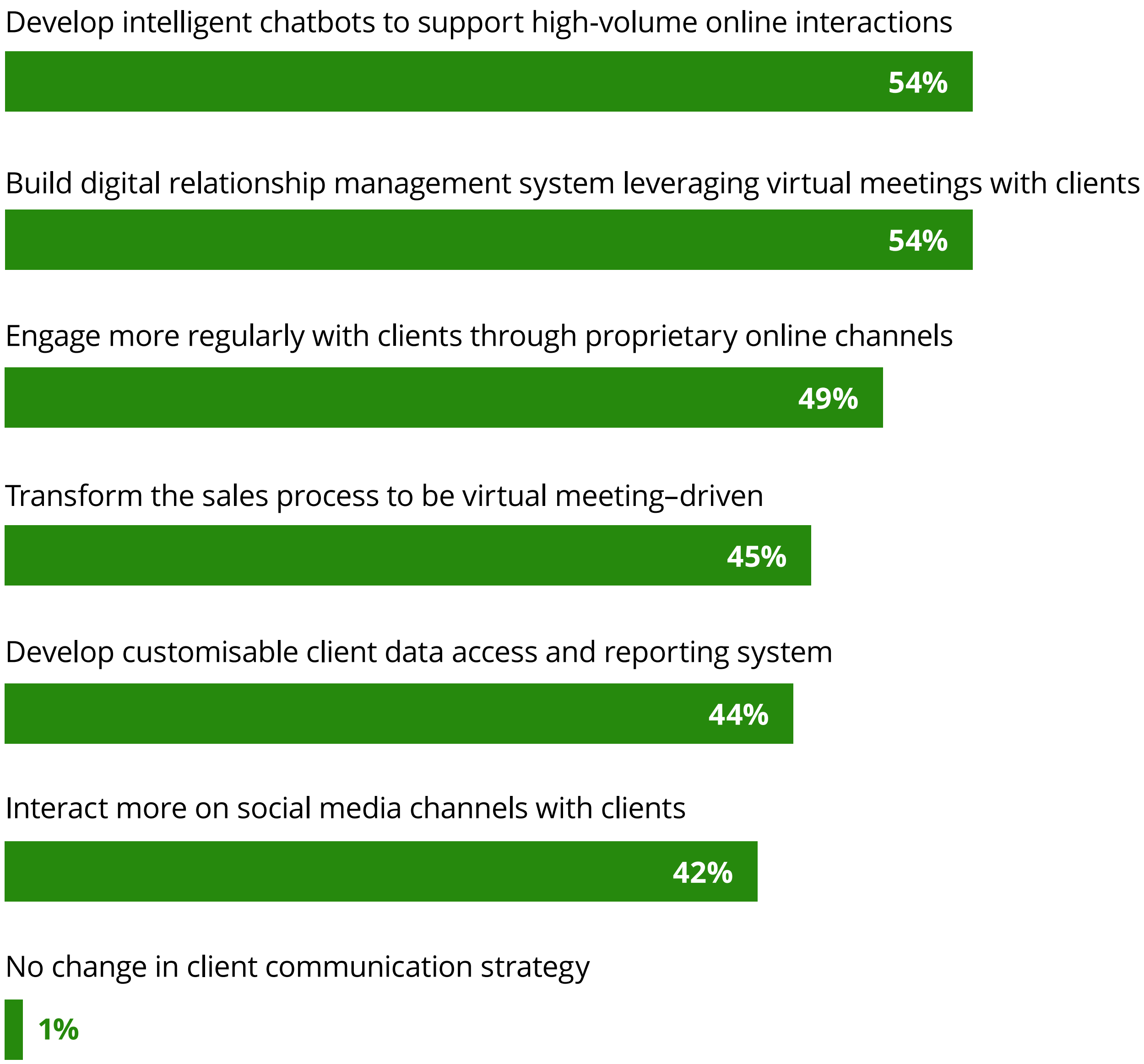
As consumers, we expect our interactions to be on a par with what we see on our smartphones and tablets. COVID-19 has only increased those expectations by speeding up the embrace of digital technology. As much of the world was forced to take shelter, mainly indoors, during the restrictions, use of digital channels grew as people sought access to information online. This is the changed world that firms must now confront.

Digital customer experience

Traditionally, investment managers have been quite slow to embrace app technology – and clearly there are security concerns around delivering data this way – but it is also true that firms don't want to have unnecessary manual aspects in their processes if there is an opportunity to remove them and deliver a more streamlined, positive digital experience to their customers. The Deloitte Global Outlook survey has highlighted areas where firms are most likely to change how they communicate and engage with clients, and digital technology figures strongly.

Figure 2. How will you change your client communication and engagement strategy based on the COVID-19 experience?

Percentage of respondents from investment management industry

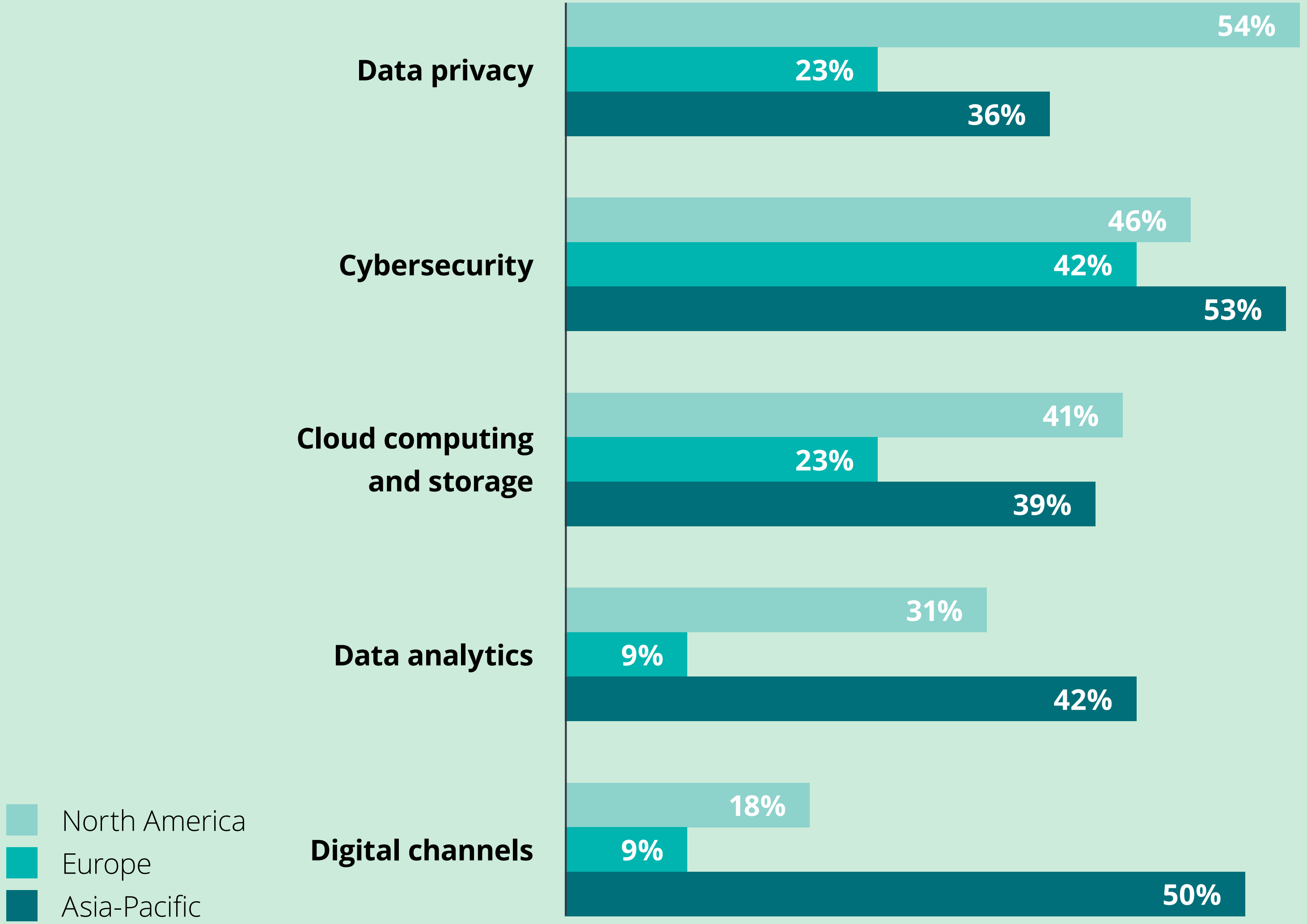


Source: The Deloitte Center for Financial Services Global Outlook Survey 2020.

Optimising operating models

Digital technology is key for firms looking at ways to reduce manual input in their processes and optimise their operating models. This has become more imperative since regulators require that certain activities must take place in Ireland, and place limits on how much activity can be outsourced or offshored. These factors are driving an increased focus on technologies such as digital channels, cybersecurity, robotic process automation, and cloud computing and storage, as the Deloitte Center for Financial Services Global Outlook Survey data shows.

Figure 3 part 1. For each of the following technologies below, how do you expect spending to change in your functional area over the next one year?



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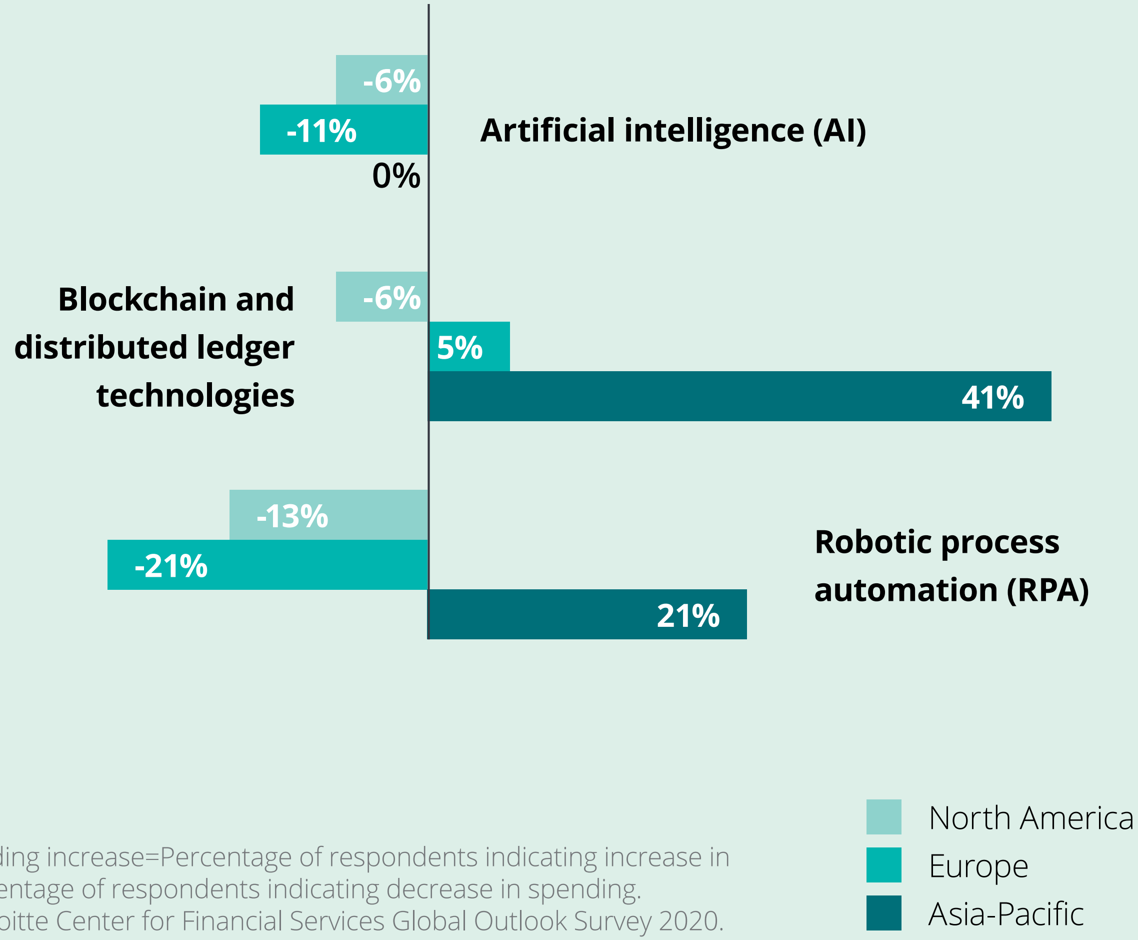
As consumers, we expect our interactions to be on a par with what we see on our smartphones and tablets. COVID-19 has only increased those expectations by speeding up the embrace of digital technology.

Figure 3 part 2. For each of the following technologies below, how do you expect spending to change in your functional area over the next one year?



Note: Net spending increase=Percentage of respondents indicating increase in spending – percentage of respondents indicating decrease in spending.
Source: The Deloitte Center for Financial Services Global Outlook Survey 2020.

A leaner industry?

It is clear that if 2020 was a year of COVID-19, 2021 is a year of measuring how firms respond. In an Irish context, firms were able to pivot quite quickly to a situation of widespread working from home. Over the longer term, this could prompt questions relating to real estate, and whether administrators need to bear the costs of large offices if they can manage the transition to a remote or hybrid workforce. This may lead to a leaner industry than we have had before.

Deloitte's survey of investment managers has identified several employment actions that companies have taken to reduce workforce-related expenses.

Figure 4 part 1. What employment actions, if any, has your company taken to reduce workforce-related expenses?

Percentage of respondents from investment management industry

- Have already done
- Planning to do
- Have not done and not planning to do
- Don't know

Note: Percentages may not add up to 100% due to rounding.
Source: The Deloitte Center for Financial Services Global Outlook Survey 2020.

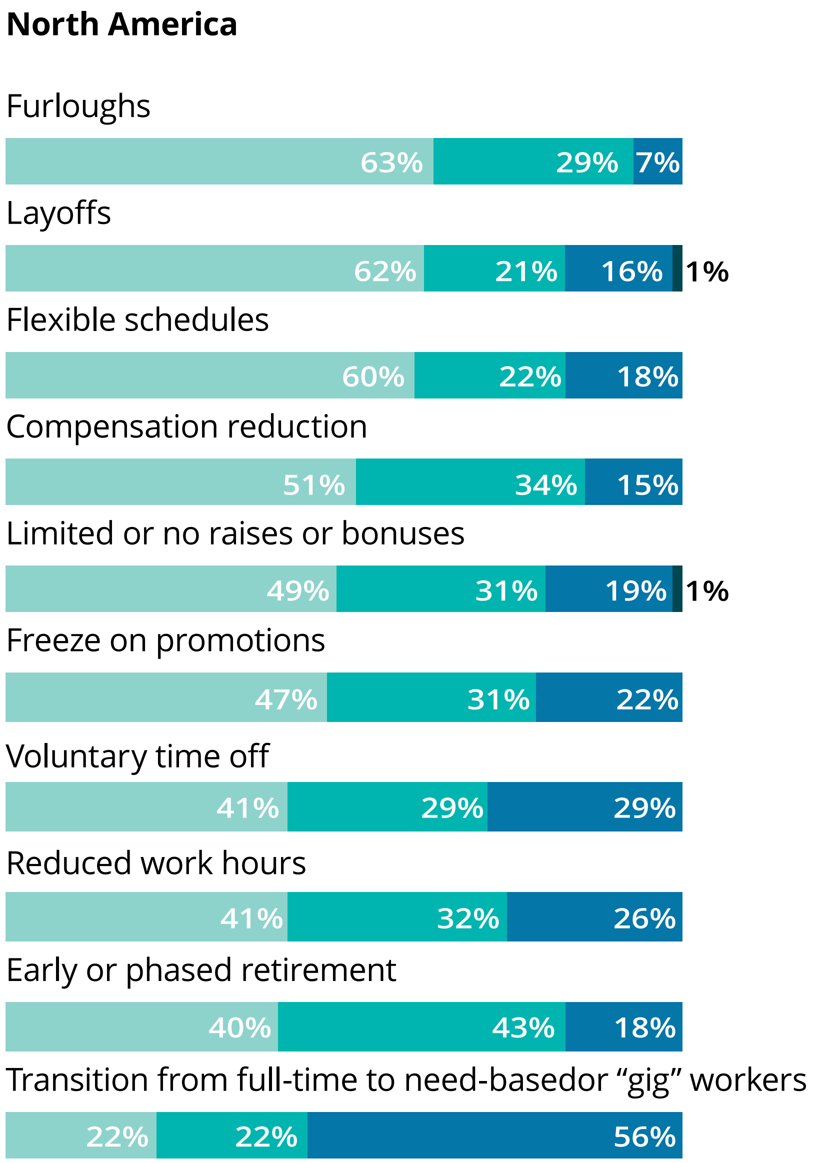


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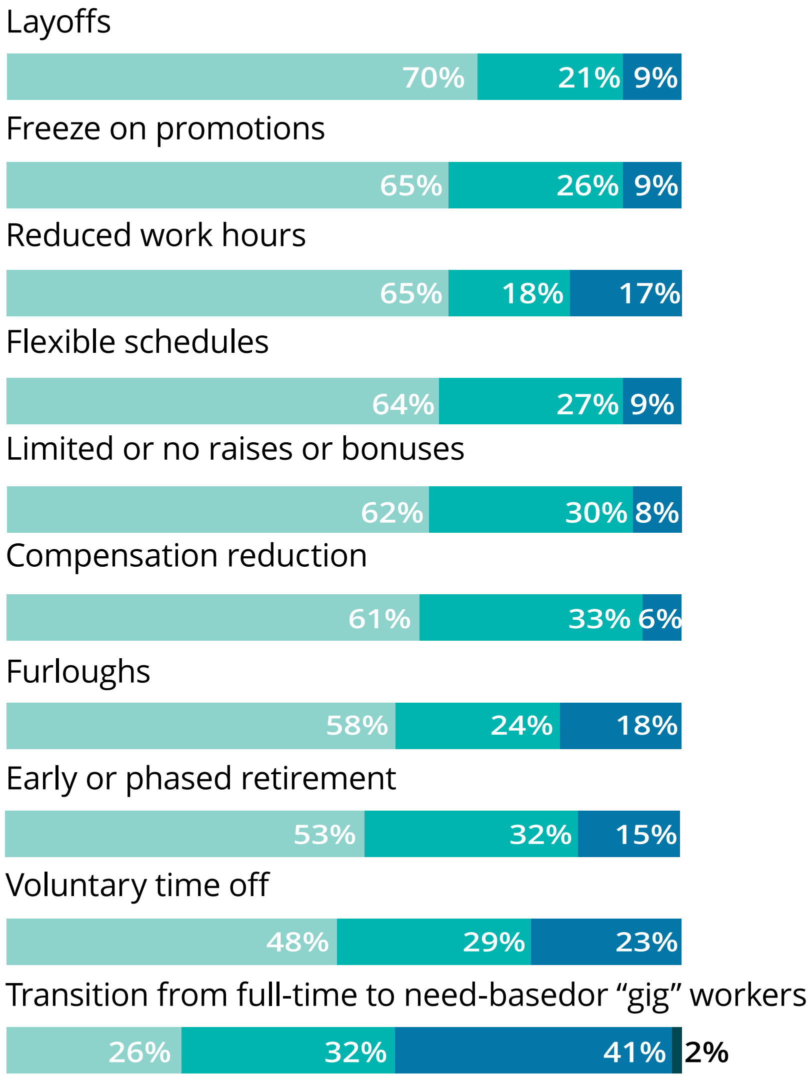
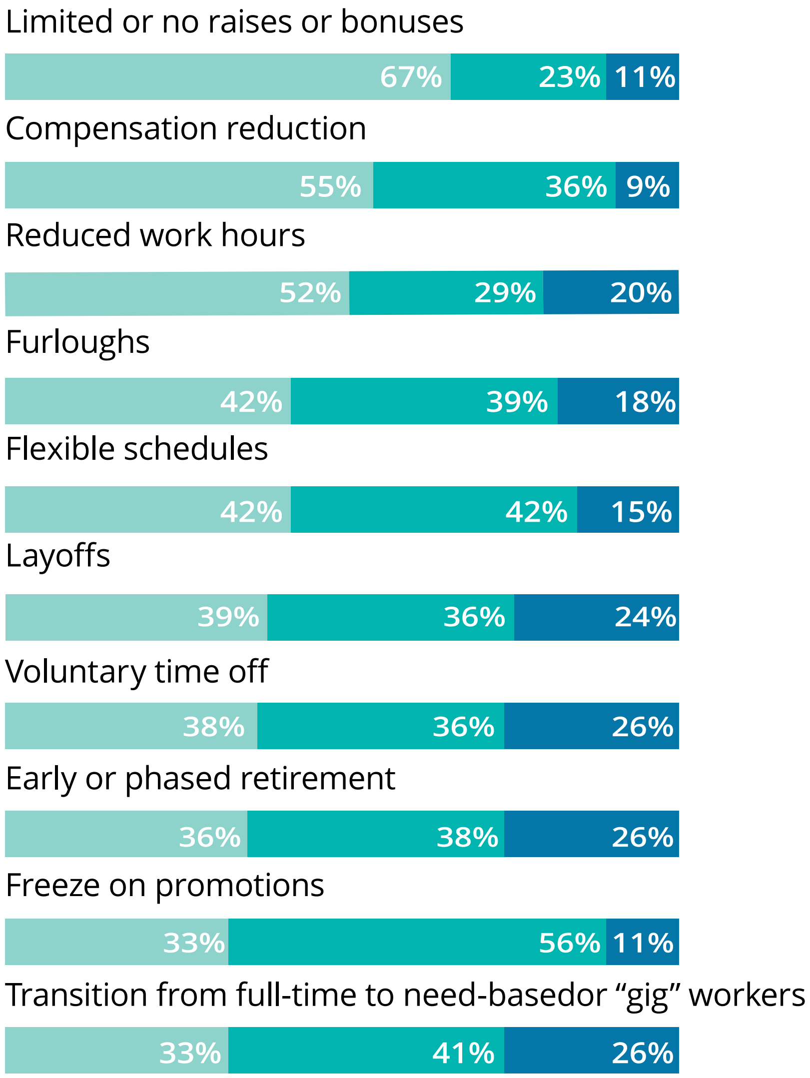
Figure 4 part 2. What employment actions, if any, has your company taken to reduce workforce-related expenses?

Percentage of respondents from investment management industry

Europe



Asia-Pacific



- Have already done
- Planning to do
- Have not done and not planning to do
- Don’t know

Note: Percentages may not add up to 100% due to rounding.
Source: The Deloitte Center for Financial Services Global Outlook Survey 2020.

2021 will also be the year that we stop talking about what sort of Brexit we might get, and we get on with implementing the agreement that was reached, however as regards financial services there remain a number of areas of uncertainty. The Irish market has seen a significant influx of asset management firms setting up a presence in Ireland to ensure continuity of access to the EU. The presence of these firms, together with the existing asset managers on the ground in Ireland, will only enhance the overall investment management offering in Ireland, complimenting the existing asset servicing business.

The lasting legacy of COVID-19 and 2020 is a lot of learning and changes to the way we do business which will have some benefits into the future. And while forecasting is a risky endeavour after the turmoil of last year, I do anticipate that the areas of sustainability and ESG investing will come to the fore this year. This is borne out by global trends identified in Deloitte's Outlook report. It would be helpful if the long-discussed Taxonomy was agreed and perhaps 2021 will be the year to see this happen.

Read the Global **2021 Investment Management Outlook**

04

IRISH 2021 OUTLOOK FOR

REAL ESTATE

- ROOM TO IMPROVE -

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Like many industry sectors, the real estate market has felt the effects of the Coronavirus crisis, but its impact has varied across the different segments, hitting some more deeply than others. This has meant the appetite for investing or debt funding from banks, direct lenders and equity investors varies greatly across the various segments. The appetite to put capital at risk is linked to the risk profile and return potential of particular asset classes within the sector.

Hospitality

The real estate sector that has felt the most impact, unsurprisingly, is hospitality. As lockdowns came into effect, hotel occupancy and restaurant bookings plummeted, causing severe pressure on these businesses from a cash flow perspective. Banks took the view that they will continue to support their existing clients in the hospitality sector by offering forbearance, but they have limited appetite to take new exposure.

Direct lenders have become a bigger feature of the Irish real estate funding market in recent years. The Coronavirus crisis was probably the first real test that the direct lending market has had in Ireland because the Irish economy had performed very strongly since 2012. So, a key question for clients as we raise capital for them is this: how do direct lenders behave in a downward cycle?

As far as the hospitality sector is concerned, direct lenders have taken a similar approach to the traditional banks, tending to grant forbearance while showing limited appetite for taking new exposure.

We are also starting to see some funders seeking shareholders to share in the cost of supporting the business during this period, when cash reserves are no longer adequate to support the business through this period until trading beings to normalise.

Overall, most funders are taking the view that the impact on hospitality will be temporary but severe. The emergence of vaccines is a positive development. Regional hotels are likely to recover sooner than city hotels due to strong domestic demand. Cities such as Dublin will be dependent on the return of international and business visitors and events such as concerts and sports. This recovery is expected mostly in 2022/23, with some first signs of recovery towards the end of 2021.

The appetite to put capital at risk is linked to the risk profile and return potential of particular asset classes within the real estate sector.

Retail

Another sub-sector of real estate severely impacted by COVID-19 is bricks and mortar retail. With all but essential shops forced to close during the heaviest restrictions, consumer spending moved online. Some segments of retail were more adversely impacted than others.

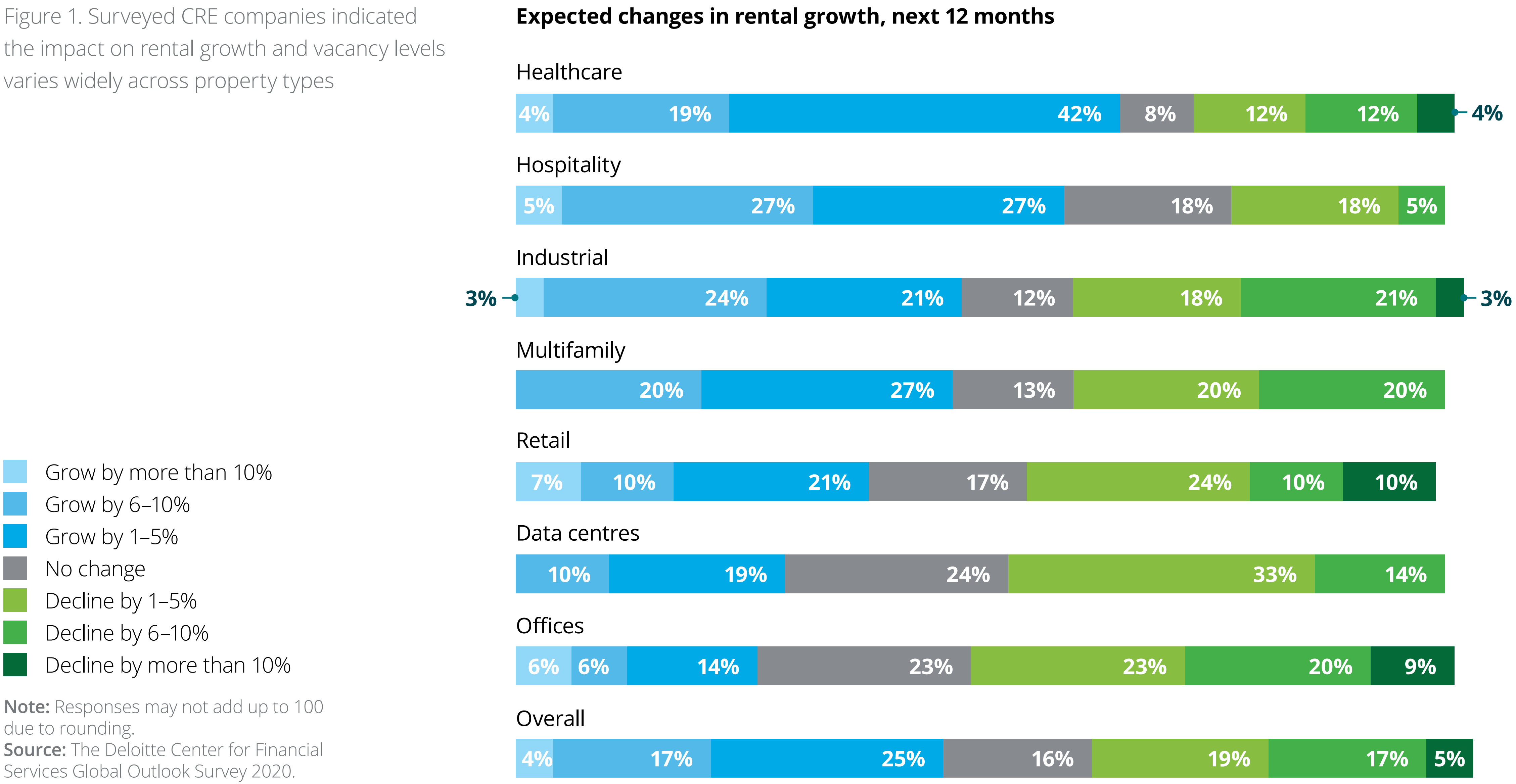
This trend was already under way on the high street, but the effect is a fundamental shift in the landscape, resulting in weaker retail covenants and unfavourable lease terms for the landlord. We expect to see a repositioning of many retail assets, but assets potentially suitable for a more wholescale repurposing will need careful assessment due to the level of capital expenditure required. This landscape will continue to evolve.

Consequently, banks and direct lenders have a limited appetite for funding bricks and mortar retail whilst equity investors are seeking value in strong locations where there have been significant drops in value, but the asset has the potential to recover in time and with new investment to repurpose it.

The converse of the high street is that we are seeing a lot of capital now looking towards logistics and industrial units. One key driver has been the move to e-commerce and a requirement for additional storage, including cold storage for online grocery shopping. Strong demand for modern industrial buildings has reduced vacancy rates to below 2%. This trend has been further reflected in a significant tightening of prime industrial yields from 5.00% in 2019 to 4.75% during 2020. Yields are expected to compress further over the course of 2021, potentially by as much as 50 basis points to 4.25%.

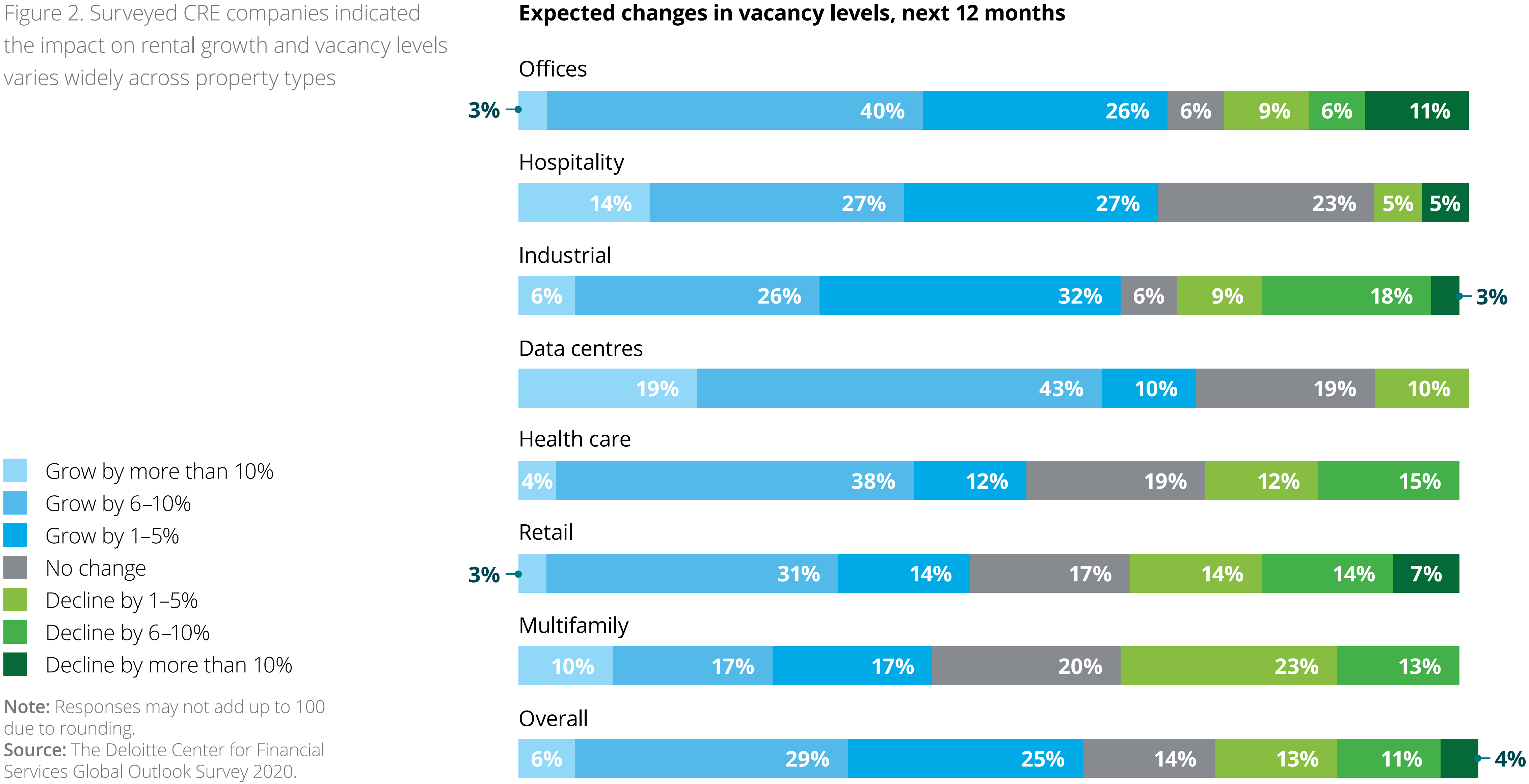
This asset class is becoming increasingly attractive for banks, direct lenders and equity to provide funding into. We are also seeing an increased appetite amongst funders to advance development funding for this asset class on a speculative basis.

Figure 1. Surveyed CRE companies indicated the impact on rental growth and vacancy levels varies widely across property types



Note: Responses may not add up to 100 due to rounding.
Source: The Deloitte Center for Financial Services Global Outlook Survey 2020.

Figure 2. Surveyed CRE companies indicated the impact on rental growth and vacancy levels varies widely across property types



Note: Responses may not add up to 100 due to rounding.
Source: The Deloitte Center for Financial Services Global Outlook Survey 2020.

Residential property

In the residential sector, the Coronavirus crisis has impacted the delivery of units, as the enforced shutdown of building sites in early 2020 slowed progress on construction and will do again now in 2021. The number of new units delivered is likely to fall well short of those needed.

Although sales and values are holding up well in the build-to-sell residential sector, there is increased sales risk given the impact of the Coronavirus crisis on people's employment prospects and future earnings. This affects how banks and direct lenders are looking at funding residential schemes. Conservative phasing of large schemes is likely to continue for 2021.

We are continuing to see a lot of activity in the private rented sector (PRS), for build to rent schemes where the dynamic is different than with build to sell. Here, much of the sales risk is removed for the developer and funder through forward commits with a large institutional off take.

The same dynamic exists in social housing; if a development is pre-sold or pre-let to a local authority or affordable housing body, the sales risk is significantly reduced. For funders, the risk is then limited to construction and development. Therefore, the strength and experience of the developer is a key focus. This has meant that more capital is going to a smaller number of large developers that are selling into PRS and social and affordable housing. This mirrors trends we see in other European markets.

Debt funding for land without planning remains limited due to the additional risk involved. Direct lenders tend to have a higher risk appetite than banks, and they are prepared to consider funding land without planning that is serviced and zoned, but they will want to ensure that such land can be 'shovel ready' within 12-18 months.

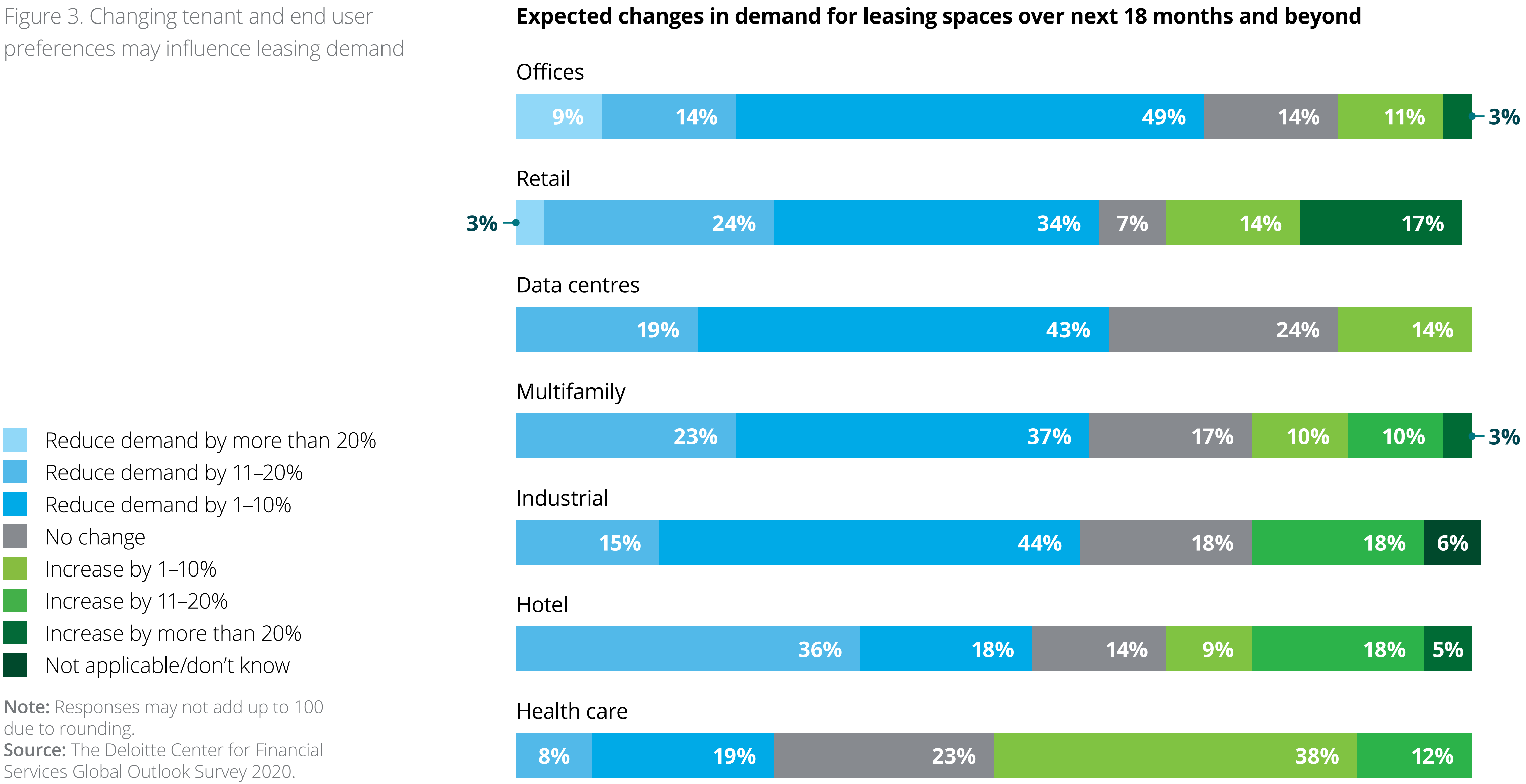
Banks remain the main providers of working capital facilities but where there is planning and/or a higher level of sales risk in a project, their appetite for funding is limited. The direct lenders are playing a bigger role, particularly in the early stages, in residential development.

Commercial property

We are still seeing a lot of activity in commercial real estate, due to the strong level of foreign direct investment over the last couple of years. Companies like Salesforce, Facebook, and Amazon have taken up large leases and we are seeing a lot of capital on the equity side and debt side following these covenants into the commercial space.

Scale continues to attract capital. Large-scale, strongly let commercial developments are seeing a lot of interest from investment capital including debt, Irish and international banks, and insurance funds entering as investors or as lenders. Strong commercial office space still provides yields of around 4.0% for investors, whereas corporate or sovereign bonds in some cases are negative yielding.

Figure 3. Changing tenant and end user preferences may influence leasing demand



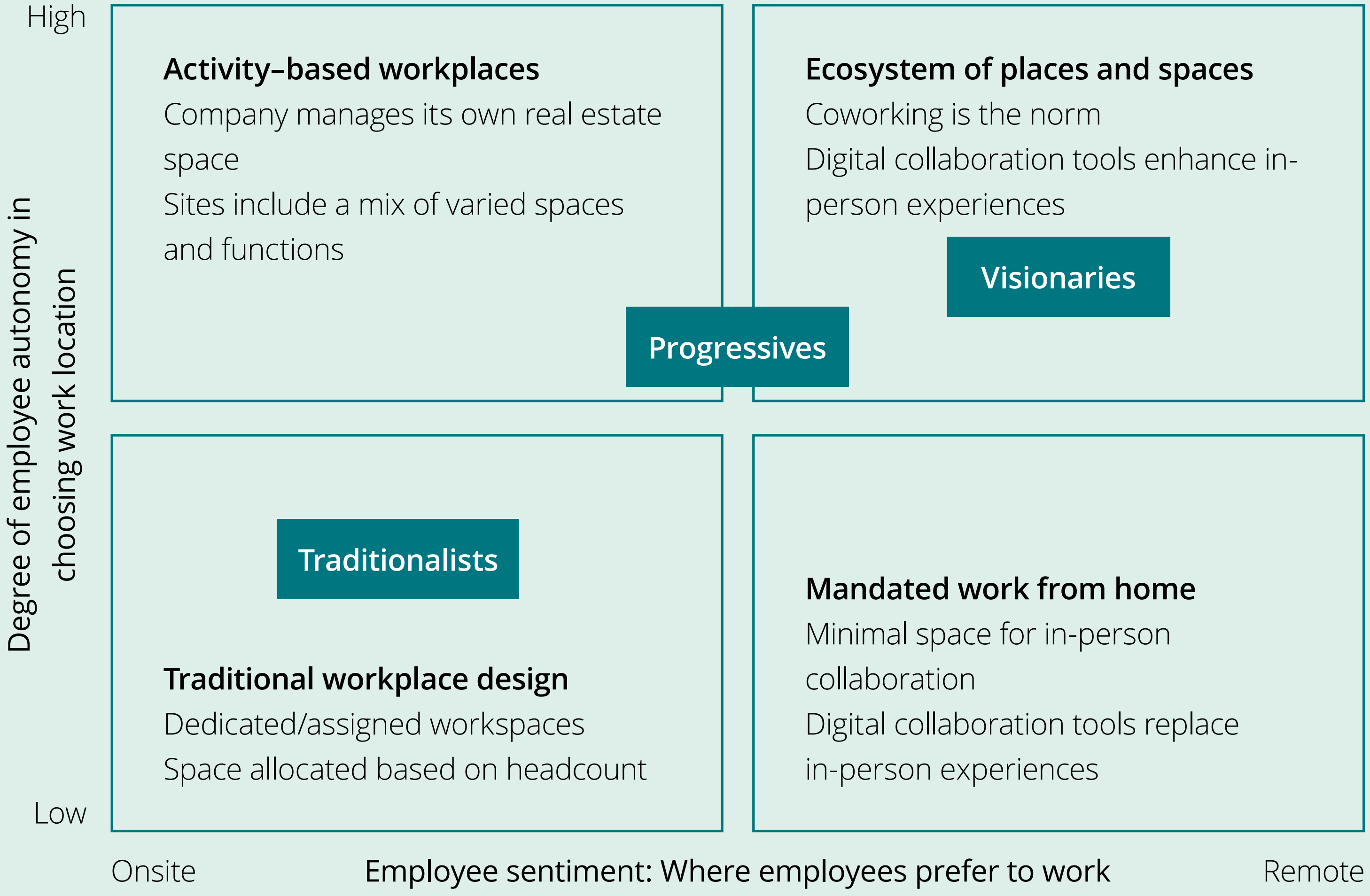
Note: Responses may not add up to 100 due to rounding.
Source: The Deloitte Center for Financial Services Global Outlook Survey 2020.

The impact of COVID-19 has led to much commentary about trends like increased remote working, and whether this could affect the longer-term viability of office space. Work practices were becoming more flexible; the Coronavirus crisis has accelerated that trend. However, physical workplaces remain essential both for attracting the right calibre of people and training them, as well as fostering team dynamics and instilling loyalty. Businesses will continue to require office space. What may change is the configuration of floor space that companies will require. Deloitte's analysis indicates most companies will fall into one of three types – traditionalists, progressives, and visionaries – and this will determine the type of workplace they occupy.

Figure 4. Determining where people work will likely depend on business needs and employee preferences

Source: Deloitte analysis.

Workplace choice and sentiment, by company profile



Nevertheless, capital continues to be attracted into commercial space with long remaining lease terms of 10-15 years to investment-grade companies. This type of commercial property is still giving a positive yield and the risk profile is still acceptable. Even if FDI projects are not as plentiful in the year ahead, the ongoing Brexit situation is making Ireland an attractive place for relocation.

There is no doubt that speculative office development is much riskier post-COVID-19. Banks will not fund office property unless a large proportion of it is pre-let or is multi-tenanted. Direct lenders are more likely to fund these projects, provided they are in the right location and there is a high degree of confidence around the ability to lease.

Overall, the market dynamics in the various sub-sectors discussed above, coupled with the availability of capital (both debt and equity), will ensure that 2021 is a busy year for real estate developers and investors in Ireland.

While both traditional banks and direct lenders are showing forbearance to borrowers, we are starting to see some funders seeking shareholders to share in the cost of supporting the business during this period.

Read the Global **2021 Commercial Real Estate Outlook**

PREPARING FOR TAKEOFF?

What is the outlook for the aviation sector as it bids to recover from the impact of the COVID-19 crisis?

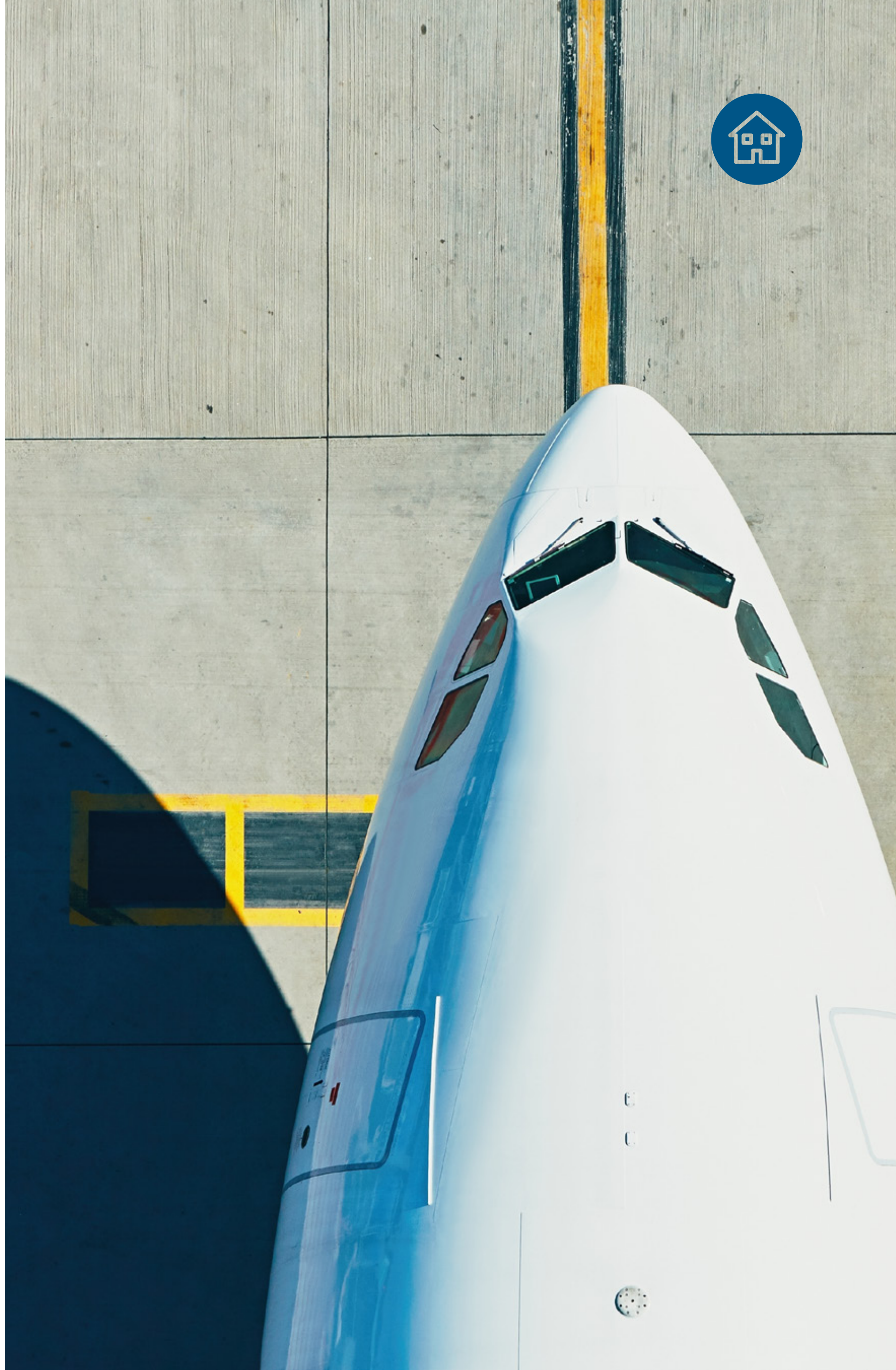
MARK DEGNAN
PARTNER
RESTRUCTURING & FINANCIAL ADVISORY SERVICES
Deloitte Ireland

COVID-19 has struck the aviation industry especially hard, with travel restrictions to combat the spread of the virus effectively grounding planes for much of 2020. The latest estimates from IATA show that last year, European passenger traffic fell by 73% in the Middle East, 72% in Africa, and 70% in Europe, when measured by revenue per kilometre. Total estimated losses according to IATA in 2020 amount to $118 billion dollars when compared to 2019.

The situation is still changing rapidly even at the time of writing. The emergence of variants of the virus in late 2020 led to travel bans being reinstated between some countries and as we look ahead into 2021, the arrival of vaccines is unquestionably a positive development, even if they won't provide an instant cure for the sector. However, we anticipate a time lag between vaccines rolling out on a mass scale, and consumer confidence returning.

Overall, it is likely the industry will see a stepped phase recovery with industry estimates suggesting regional air travel should start to return towards the end of 2021, but long haul flights are not expected to come back in significant numbers until 2022-2023. Less optimistic forecasts suggest widebody and long-haul aircraft could remain grounded for considerably longer. The more hopeful forecasts are, obviously, predicated on the vaccines being a success as we all hope. In addition, government supports are still quite active in the industry and we expect they will continue to be a critical lifeline for the industry for another 12 months at least.

In this article, we look ahead to what the next 12 months could bring, for airlines, lessors and lenders within the sector. We will outline the various restructuring options available to all stakeholders within the sector, using some recent cases and our market experience.



01. Financial concerns

The key challenges for the sector are the long-term financial impacts the pandemic will have on company balance sheets; these include increased debt burdens and significant working capital requirements to restart operations across all segments.

Recent estimates of $160 billion have been made with respect to the level of additional debt raised in the sector to assist companies through the initial phases of COVID-19 and with limited liquidity or free cash flow available from operations, liquidity challenges will come sharply into focus in 2021.

In order to raise such debt facilities and with airlines not anticipating the length and depth of the crisis, airlines have drawn down on available credit facilities and secured further funding by providing unencumbered aircraft as security to lenders. This has resulted in debt-laden balance sheets and a narrowing ability to raise further debt on the back of a smaller asset pool. To prevent events of default and insolvency in the sector, airlines and lessors have relied upon significant creditor and state support ultimately to survive the crisis.

Payment holidays, deferrals and 'power by the hour' agreements have become normal course; however, the scale of the underlying issues has resulted in some creditors initially receiving requests for three months, with such requests now being extended to twelve months and beyond.

While airlines are seeking such deferrals on their individual fleets, the lessors have received multiple such requests. This has placed significant pressure on the leasing sector and their funding partners in addition to potential significant impairment of fleet values due to the current crisis, which will further impact on the underlying financial stability of many companies.

The industry now finds itself in a waiting game reliant on governments opening borders before any improvement can occur. While the sector remains in stasis, it is burning considerable cash in the maintenance and preservation of aircraft. After that, airlines will face significant working capital requirements in order to start back up again.

02. Creating stress

This situation is putting leasing companies under considerable stress. We are already seeing a lot of 'power by the hour' deals being negotiated in the market, where lessors only get paid when and if the plane flies, reducing income for them.

Last year, Nordic Aviation Capital was the first large aircraft lessor to engage in a corporate restructuring in Ireland under Part 9 of the Companies Act due to the pandemic. Given the extent of COVID-19's effect, we expect processes under the Irish Companies act, such as examinership and Part 9 schemes of arrangement, to form an essential part of the industry's recovery after COVID-19.

Restructuring can sometimes be mistaken with an insolvency process where a company can no longer continue as a going concern, however the aforementioned processes allow companies

Restructuring processes allow companies preserve their underlying value and restructure their balance sheets to allow them continue to trade into the future.

preserve their underlying value and restructure their balance sheets to allow them continue to trade into the future. We believe this is a positive and necessary development in order for them to remain viable. The reason there have not been as many schemes to date is because there wasn't sufficient clarity about the market in 2020 which would have determined the next steps. Now that a recovery is hopefully within sight, there is more certainty for stakeholders and will allow them consider their restructuring requirements in a more robust manner for long term survival.

In addition to restructuring across the sector, we also anticipate an element of consolidation in the market with some leasing companies seeking merger opportunities. There may also be fewer operators, or smaller airlines than before. We are also seeing positive signs of new investment into the market as investors seek to enter the market at a time of lower cost for assets, and we anticipate that where there are sales, it will be to preserve value rather than because an operator has failed outright.

COVID-19 is not just affecting airlines, but the entire aviation supply chain: airports, catering, engineering, and retail. The financial challenges are equal for both large international hubs and regional and private airports, with high levels of cash burn to preserve facilities and significant amounts of debt. While airports have the ability to divert capital project funds in order to maintain facilities and meet operating costs, they also face significant working capital challenges in restarting full operations in due course, and they themselves may have to consider an element of restructuring.

03. Key stakeholders

The principal stakeholders within the sector which will be engaged in the restructure processes will be airlines, lessors and secured creditors, with original equipment manufacturers playing a key role in helping both participants arrest capital expenditure commitments in the near term. The airlines have been front and centre of the immediate impact on trade and will continue to be affected by the inability to generate revenue for a considerable period of time.

Beyond the airlines, the aircraft lessors are also facing significant pressures, across multiple portfolios, to engage in short-term restructures, which in turn creates issues for the secured and unsecured lenders that have provided funding for aircraft.

The current level of commercial aircraft subject to lease is estimated to be about 40%, with Ireland holding a 60% share of the global leasing market. The relationship between airlines and lessors is a typical debtor-creditor relationship. In the current crisis, airlines' ability to generate revenue has been decimated with lease defaults and/or deferrals, as referred to above, becoming a more regular feature of the market.

Some aircraft lessors have cash reserves to enable them to ride out the current crisis for some time. Many investment-grade aircraft lessors were fortunate to access the capital markets up to the end of the first quarter of 2020 in private placement, bond issuance or asset-backed securitisations.

The secured lenders in this sector previously would have held comfort in loan-to-value metrics where they would lend to a maximum of 80% of an asset value and created a buffer against their debt. However, given the collapse in the sector, asset values will have diminished, at least in the near term, and created a higher level of risk for the secured lenders.

The aforementioned liquidity challenge will in itself create other challenges for airlines and lessors with regards to underlying financial and performance covenants, which regularly form part of finance and leasing transactions.

Clarity on risks:

Risk of non-payment – risk of default

Based on Iata's impact assessment (January 2021) a transition from cash burn to cash positive is in sight, but the sector still faces a challenging six to nine months with positive cash generation not estimated until Q4 of 2021 at the earliest, and as with many other sectors such forecasts are changing regularly as the impact of the pandemic moves by geography and phase of recovery.

Based on such figures, the risk of non-payment or default in the sector remains significantly high and when considering the additional debt burden taken by many in the sector in 2020, an increase in defaults and a requirement to extend, defer or amend underlying financial covenants is not unexpected.

Given the ongoing uncertainty in the sector, airlines will find it difficult to raise debt or equity, and if either is available, it will be at a higher price than that was previously achievable within the markets.

Financial covenants – risk of default

Financial covenants are a key term in any finance and leasing agreement on which the lender can rely. Such covenants and their underlying tests, in normal circumstances, can give a lender early warning signs that a customer is not performing as planned.

The principal test which lessors may rely on, and which may now be under the most scrutiny, is the loan-to-value test to ensure the lender's security covers the remaining debt of the customer. Given the current distress in the market, the potential number of insolvencies, and subsequent impact on asset values, this will heighten the risk of covenant breaches for lessors.

Maintenance/holding covenants – risk of default

Given the number of fleets that have been grounded, airlines also must be cognisant of the non-financial covenants of their underlying agreements and specifically the maintenance covenants for aircraft not in use.

Many leasing agreements have specific covenants that a lessee must undertake to maintain and preserve the underlying secured assets. As multiple fleets have been grounded, the underlying cost of meeting such covenants is high for lessees and engagement with the lessors is crucial to ensure a technical default does not occur.

Early engagement with specialised advisers is extremely important to allow all stakeholders determine the optimum strategy to protect value in the business and its underlying asset base.

Addressing the underlying concerns – what are my options?

Early engagement with specialised advisers is extremely important to allow all stakeholders determine the optimum strategy to protect value in the business and its underlying asset base. Given the levels of distress in the aviation sector, engaging early and therefore having a suite of options should be the preferred choice versus a lender being 'forced' to take a position because of an event of default.

Traditional options available to secured lenders in an event of default may also now be limited, in that repossession of aircraft from a practical, logistical and value perspective may not be a preferred route to recover funds. Lenders and lessors will have to review each of their portfolios on a risk-appropriate basis and take action where there is a lack of engagement or an appropriate strategy to meet current market issues.

Restructuring options

There are a number of restructuring options available to companies across various jurisdictions where a court process may be used to negotiate formally a preferred outcome. We will focus on Part 9 Scheme of Arrangement (Ireland), examinership (Ireland) and Chapter 11 (US), in addition to reviewing briefly some direct stakeholder approaches which can also be considered.

01 Part 9 Scheme of Arrangement – Ireland

Ireland is fast becoming a preferred base for complex restructuring processes and this has been seen most recently in the case of Nordic Aviation Capital (NAC) DAC, which successfully applied to the Irish courts for a restructure of its positions under a Scheme of Arrangement, after negotiations with its principal stakeholders.

Ireland is fast becoming a preferred base for complex restructuring processes and this has been seen most recently in the case of Nordic Aviation Capital (NAC) DAC.

While NAC is the first such restructure in the aviation sector, the Part 9 Scheme of Arrangement process has been successfully used by other large multijurisdictional entities such as Ballantyne RE plc, an Irish reinsurance special purpose vehicle, to restructure its reinsurance obligations and $1.65 billion of senior New York law-governed debt.

The Nordic scheme effectively provided the company with a 12-month standstill from its creditors for certain payments of interest and principal on its borrowings. In addition, and critically, the scheme also waives a number of covenants, such as those mentioned previously, which likely would otherwise have been breached as a result of the current market distress.

The scheme was implemented across 89 different facilities governed by a mixture of English, New York and German law and reflecting a variety of different financing structures.

Commenting on the process, NAC stated in a press release on 9 July: "Whilst NAC entered the current global crisis in a strong liquidity position, the fall out in the aviation sector as a result of the COVID-19 outbreak resulted in the company receiving requests from the majority of lessees seeking to defer some or all elements of their lease payments. To mitigate this, the company has been liaising with its lenders and their advisors since April to agree a standstill on and deferral of its debt obligations. This agreement will ensure NAC's stability as the aviation market gradually recovers."

From an Irish perspective, this was a noteworthy development. The Nordic arrangement was implemented via a solvent Irish scheme of arrangement, and Ireland could well play a key role as a preferred location for future restructuring deals. There are two reasons for this. Firstly, Ireland is base for many of the world's largest leasing companies; secondly, there remains a question over whether UK restructuring processes will be recognised within the EU after leaving on January 1st, whereas a restructuring in the Irish courts system would be recognised throughout the EU member states, thus allowing applicants apply a restructure over a number of geographies and reduce costs.

Irish courts and practitioners have already shown flexibility in delivering effective restructuring solutions across a number of sectors to include aviation, which helps Ireland's case as a restructuring jurisdiction. Ireland is open for business, and with highly skilled restructuring professionals offers a very cost-effective option compared to U.S. Chapter 11 or the UK Super Schemes.

Given the positive feedback in general from the Irish courts about such schemes, and the speed at which the process can be implemented, we believe Irish-led schemes will become more prevalent given the concentration of lessors based in Ireland and the relative flexibility of the process.

What is a Part 9 scheme of Arrangement?

The process is an Irish Companies Act procedure, which can be proposed by any company subject to the jurisdiction of the courts of the Republic of Ireland. This can be achieved through centre of main interest (COMI) or by virtue of the parties governing law being in Ireland.

The process is very flexible and allows a company to compromise with its members or creditors (or any class of them), subject to it being deemed fair for all classes subject to the restructure. If the scheme is approved by the requisite majority and then sanctioned by the court, it will bind all parties within the relevant class, whether or not they voted in favour of what was proposed.

A key point for this process is that it is not a formal insolvency process. A company does not have to be insolvent, or facing imminent insolvency, before it can propose a scheme. No insolvency practitioner is appointed, and the company directors retain control throughout the process.

However, compared with Irish examinership legislation, there is no statutory moratorium available with regards ongoing payments during the process, and therefore a company should always be aware of its underlying liquidity position throughout such a process.

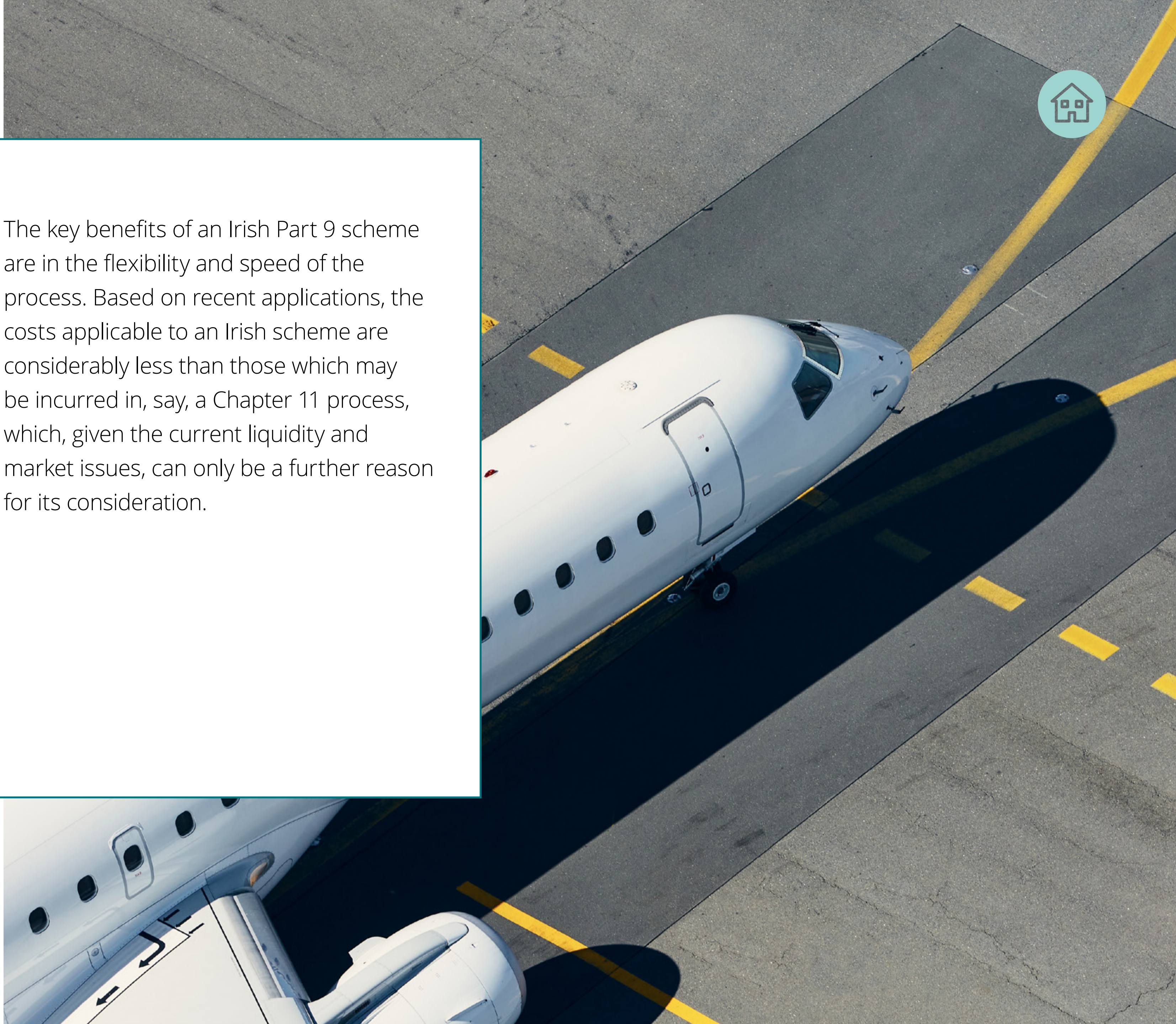
The process
Before the launch of the formal scheme, negotiations and commercial terms will be discussed and agreed and a 'lock up' formalised to ensure the scheme meets the requisite approvals.

This period of negotiation is fluid and will be dependent on a number of factors to include experience of advisers, engagement of all creditors and complexity of the company's funding structures which may be subject to the scheme.

In the case of NAC, the process commenced in April and concluded in July, with the court process taking about 28 days from application. Therefore, the lock-up period in this case was approximately three months, which when considering the broad range of creditor classes, quantum of debt and company structure, demonstrates the ability to restructure quickly with adequate engagement from all stakeholders.

At the court application stage, the company will seek to have the matter admitted to the Commercial Court and seek directions in regards the convening of the creditors' meeting. Every notice summoning a meeting of creditors must be accompanied by a scheme circular explaining the effect of the scheme and stating any material interests of the directors of the company and how the directors would be affected by the scheme in so far as it differs from the like interests of other persons. Where the scheme affects the rights of debenture holders, a similar explanation in relation to debenture trustees must be given.

Once sanctioned by the courts, a copy court order must be delivered to the Companies Registration Office (CRO) within 21 days of the order being made by the Commercial Court and the scheme takes effect immediately on delivery of copy order to the CRO.



Voting and sanction

Another key point that is relevant to an Irish-based scheme is in seeking recognition under Chapter 15 of the US Bankruptcy Code for foreign-based restructures, and to date such schemes have been approved under the said code.

Given the recent exit of the UK from the European Union (EU) and with no current agreement in place between the UK and EU on recognition of insolvency processes across member states, the recognition of Irish schemes across the EU is of considerable importance when considering the availability of restructuring tools across the sector.

The key benefits of an Irish Part 9 scheme are in the flexibility and speed of the process. Based on recent applications, the costs applicable to an Irish scheme are considerably less than those which may be incurred in, say, a Chapter 11 process, which, given the current liquidity and market issues, can only be a further reason for its consideration.

02 Examinership process – (Ireland)

While Part 9 schemes in Ireland are a consensual process led through the courts, there is an alternative court process in Ireland, which can also be used to restructure a business.

Examinership is an Irish Companies Act procedure, which can be proposed by any company where it can establish COMI in Ireland. It permits a company to compromise with its creditors and propose a viable scheme of arrangement to the court. The appointment of an examiner provides the applicant company with an automatic moratorium from all its creditors, for balances due and owing up to the date of the application.

Any amounts falling due during the protection period, including borrowings or leasing obligations, must be met and an applicant would have to demonstrate they had adequate cash flow for the protection period to meet such costs.

The scheme is only required to be approved by one class of impaired creditors, subject to no creditor being unfairly prejudiced by the scheme and it is a process that can be applied for by companies which are insolvent or likely to become insolvent.

The scheme must demonstrate that all creditors would achieve the same or a better return from such a process versus a liquidation of the company. Such a scheme of arrangement must be prepared and approved by the Courts within 150 days of an application for Court protection being made. (This was previously 100 days, but the Irish government passed temporary legislation in August to extend this period to 150 days, given the current global economic issues. This extension will apply to applications made prior to 31 December.

Initially, the appointment of an examiner, which is normally a recognised insolvency practitioner, is on an interim basis, on foot of an application by the company, and would be by way of an ex parte application with no advance notification required to creditors. A full hearing would be set down for about one week post-petition. Parties would be put on notice of the hearing and an objection could be made to the appointment at this time.

In order for a company to apply for court protection, an independent experts report (IER) is generally required as part of any petition, the contents of which are detailed under s.511 of the Companies Act 2014.

In summary, such a report would provide an overview of the business and reasons for its financial difficulties, and the independent expert must opine on the viability of the business to continue as a going concern and what conditions would allow for this.

Where the petitioner is a creditor (such as a secured lender), it should be possible to file and obtain protection without an IER, on the basis that an IER would be filed within a period of 10 days during which period the directors would be required to assist in its preparation.

The key benefits of Examinership, versus those of a Part 9 scheme, are that an examiner's scheme can be negotiated throughout the protection period, and up until its presentation at the various meetings of creditors versus a lock up most likely having to be negotiated in advance of a Part 9 process to ensure its success.

In addition, the company automatically is protected from its creditors for all balances due and owing prior to the appointment of the examiner, whereas in a Part 9 scheme, no such moratorium exists, and a creditor could move against a company where a default position arises.

From a lender perspective, an examiner (who when appointed is an Officer of the Court and independent of the company) would be in a position to ensure no assets/limited assets moved during the protection period, to include cash balances which may be subject to a secured position and protect against cash burn, where a company seeks to meet payments in a stressed scenario.

Examinership facilitates cross-border restructuring because it is a specified insolvency process under Regulation (EU) 2015/848 on insolvency proceedings and subject to limited exceptions, the appointment of an examiner and any proposals under a scheme of arrangement for the company which have been confirmed by the Irish Court are automatically recognised and binding throughout the EU, apart from Denmark. Examinership is generally a recognised process in the United States under the US Chapter 15 recognition process and is a more cost-effective process than Chapter 11.

The flexibility of examinership and its recognition across the EU and also under Chapter 15 in the US was a key reason for Norwegian Air entering into examinership in November 2020. In addition to its operating airline a number of related Companies, primarily involved in aircraft leasing also entered the process.

The leasing entities were Irish registered companies and were the main applicants for the appointment of an examiner, however, the company was also able to prove sufficient connection to Ireland for Norwegian Air Shuttle (Norwegian Air), a Norwegian based company, to enter the process and the appointed examiner is now seeking to negotiate a viable scheme of arrangement for the business to continue as a going concern. Such a scheme will consider the size of the operating fleet, lease agreements in place with lessors and the overall debt position on the company's balance sheet.

It is anticipated that a scheme will be presented to company creditors and the High Court in Ireland during Q1 2021, and the outcome of the process could further strengthen Ireland's position as a destination of choice for international restructuring processes.

While there are a number of benefits to an examinership process, it is not without certain drawbacks, where complex companies with cross -jurisdictional positions may not meet the COMI requirement. There may also be a significant funding requirement during the examinership process to maintain the company as a going concern, which could require external financing from existing lenders. Additionally, if a scheme is not agreed within the period, the courts may order the winding up of the company, if deemed just and equitable.

03 Chapter 11 – (US)

Chapter 11 is a form of bankruptcy that involves a reorganisation of a debtor's business affairs, debts and assets, and for that reason is known as "reorganisation" bankruptcy.

Companies generally file Chapter 11 if they require time to restructure their debts. This version of bankruptcy gives the debtor a fresh start. However, the terms are subject to the debtor's fulfillment of its obligations under the plan of reorganisation.

Chapter 11 as a process has been used heavily within the aviation sector for many years with recent filings under Chapter 11 for LATAM, the Chilean-based airline, Avianca and Aeromexico, and it is envisaged that a number of other such applications will be forthcoming in the future.

The business is not able to make some decisions without the permission of the courts: these include the sale of assets, other than inventory, starting or terminating a rental agreement and stopping or expanding business operations.

The court also has control over decisions related to retaining and paying attorneys and advisers and entering contracts with vendors and unions. Finally, the debtor cannot arrange a loan that will commence after the bankruptcy is complete.

Chapter 11 bankruptcy is the most complex of all bankruptcy cases. It is also usually the most expensive form of a bankruptcy proceeding. For these reasons, a company must consider Chapter 11 reorganisation only after careful analysis and exploration of all other possible alternatives.

04 Non-formal processes – consensual negotiations

Consensual negotiations should be the default starting position for companies in distress and we have seen a number of such positions in the market, with airlines, for example Azul (Brazil), seeking direct deferrals or payment holidays from their lending and leasing creditors.

While such negotiations can yield quick results, in most circumstances they will not produce a long-term viable restructuring plan, which given the depth of distress in the market will be required.

In addition to the lack of long-term restructuring outcomes, where each creditor is approached individually, some creditors may hold out on agreeing any terms while they await the outcome of negotiations with other creditors and may hold out for what they believe is a better return for them, thus making the process difficult to achieve optimum results.

Furthermore, this process can be expensive and time-consuming for management of the company seeking the consensual agreements of its creditors, with individual engagement and negotiation taking place with each party on a standalone basis and each agreement having to be documented and formalised on an individual basis also.

Given the heightened liquidity risk in the sector already, incurring significant costs in a non-binding process could further add to a company's insolvency risk and create an event of default prior to all agreements being put in place. With this in mind, it would be preferable for some level of creditor group negotiation in this scenario to ensure the company has the best chance for survival.

Consensual negotiations should be the default starting position for companies in distress and we have seen a number of such positions in the market, with airlines, for example Azul (Brazil), seeking direct deferrals or payment holidays from their lending and leasing creditors.

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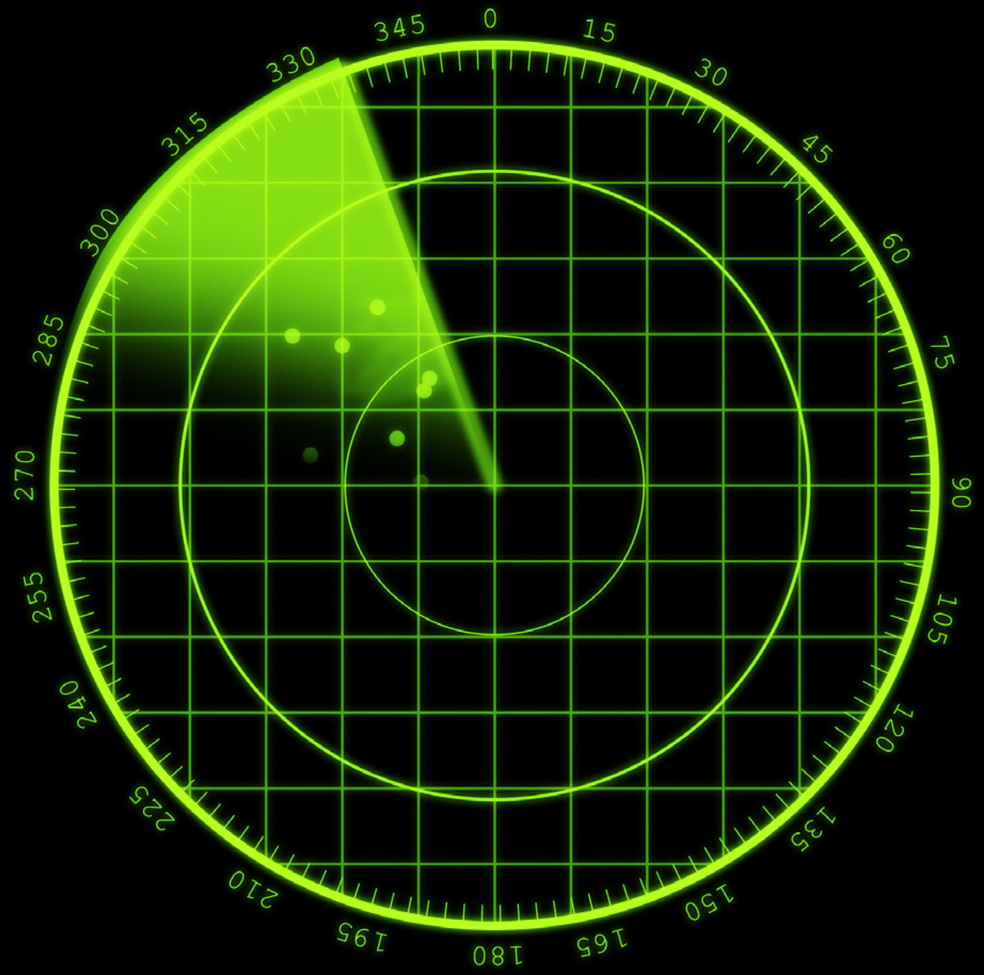
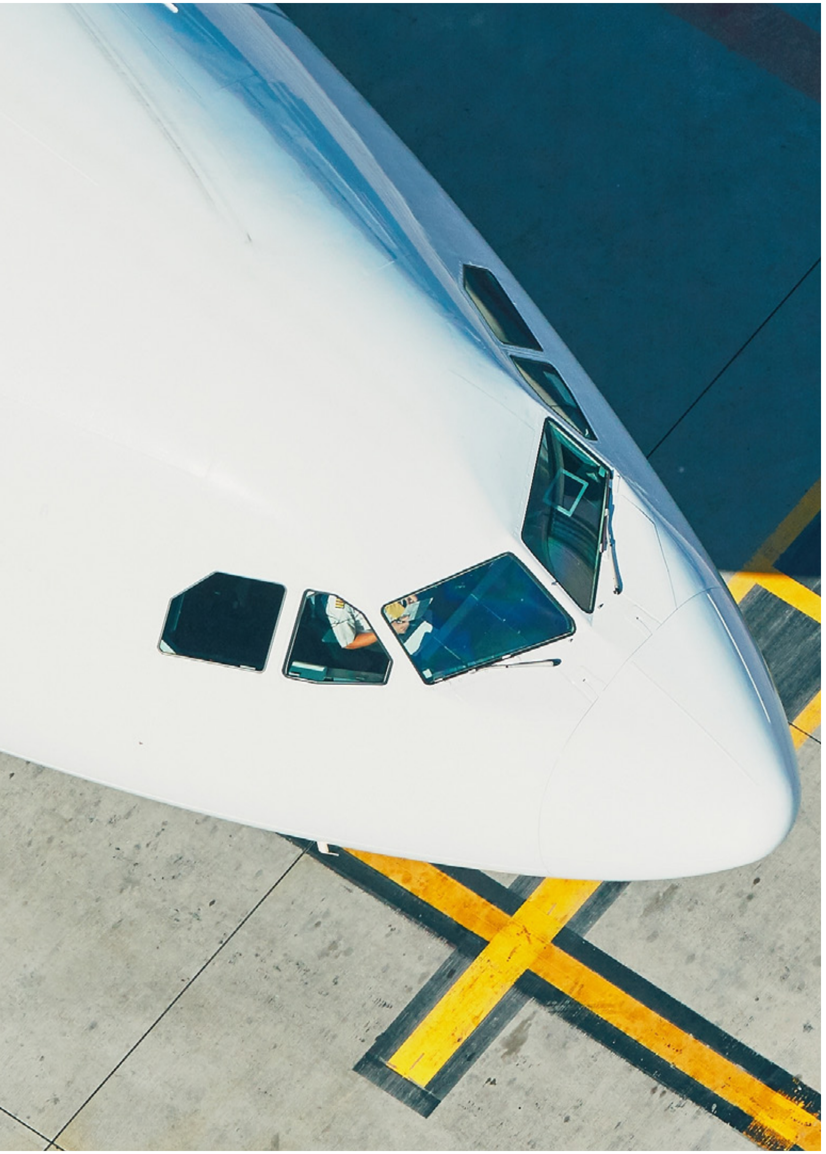




05 Ad-hoc groups

The formation of an ad-hoc group of creditors, motivated as a group to achieve a long-term restructuring of a business, is an alternative approach to individualised engagements, and has been used successfully in many cases.The intention of such a group is to negotiate a viable restructuring plan for the business, which can then be brought to a wider body of creditors for approval. This in itself is difficult in normal circumstances, and given the structure of the airline sector, where different groups of creditors will have differing levels of security and positions, achieving consensus for all creditor groups through one ad-hoc group would be challenging.

While providing a benefit of streamlining processes, the informality of the group and narrowness of the focus on one class of creditor is not the most effective route to achieve a long-term and viable restructure. However, it may act as a catalyst for a company to move toward a process of formal restructuring and act as a sounding board prior to seeking an overall lock up of creditor positions.

06 INSOL Statement of Principles for a Global Approach to Multi-Creditor Workouts (2000) - Coordination committees

Given the complexities highlighted above in the structure of the aviation sector, its key stakeholders, cross-jurisdictional requirements and complex funding positions, a coordinated approach to restructuring should yield the best results for all parties. Under the above statement of principles, coordinating committees form a key part of multi-creditor workouts in cross-jurisdictional processes and should be adopted globally.

The use of such committees has been proven to enhance a restructuring process for all parties in multiple sectors. To assist with the coordinated approach, it is usual for the relevant creditors to appoint one or more representative committees to progress dialogue with the debtor and to help manage the evaluation process and the standstill arrangements. Through the committee, the company can engage in in-depth discussions about its financial position and share information relevant to the restructuring.

Coordinating committees form a key part of multi-creditor workouts in cross-jurisdictional processes and should be adopted globally.

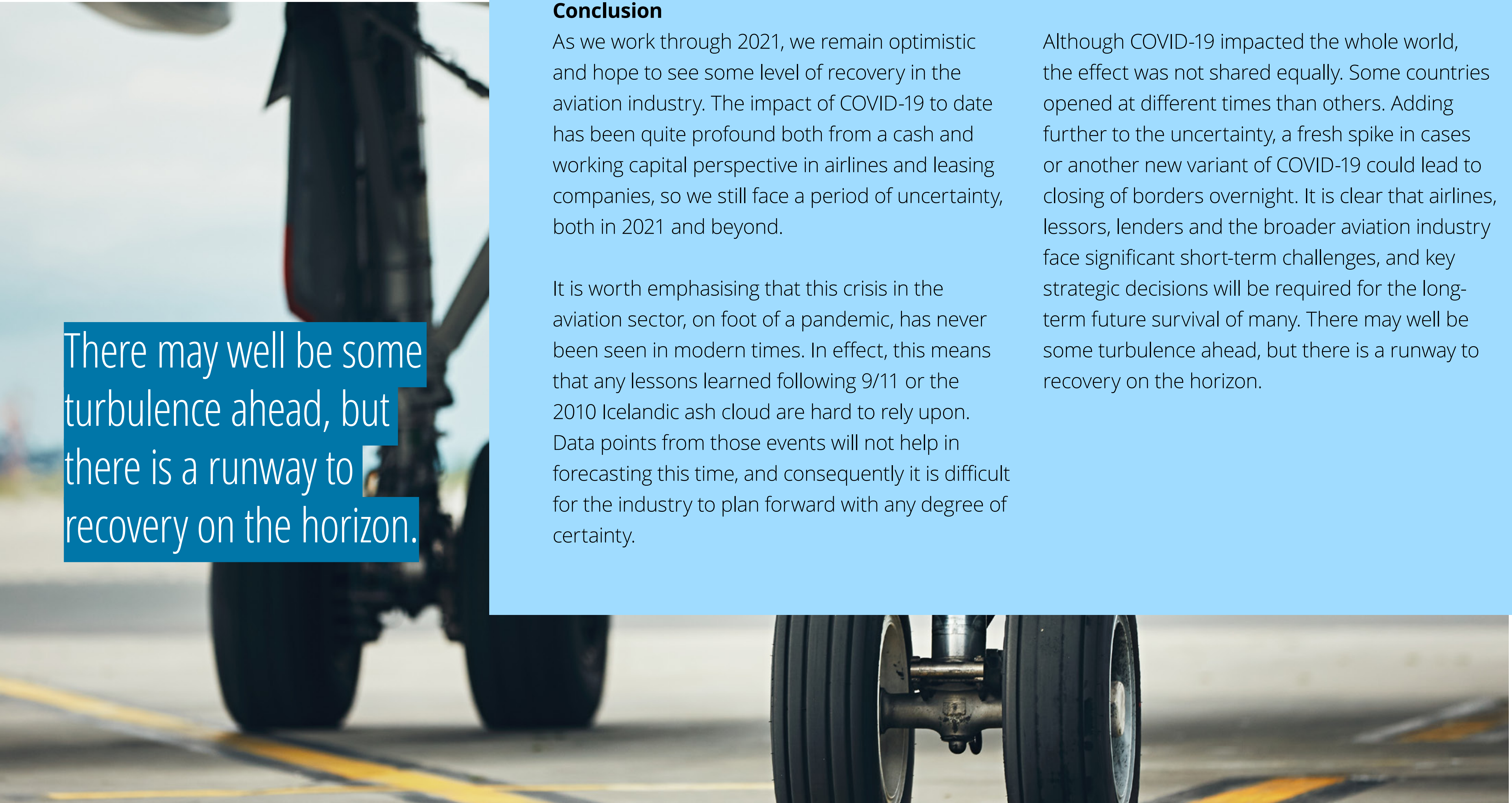
While the ultimate commercial decision on whether to accept a proposed restructuring remains with each individual creditor, the intention of such a committee is that reaching an agreement with them, having the members consisting of some or all of the most significant creditors of the company, should indicate that the proposal stands a good chance of being acceptable to creditors as a whole.

Coordinators are best described as facilitators of the negotiation process and coordinators of the provision of information to the relevant creditors (with appropriate professional advice). The appointment of coordinators should, in any case, be for the convenience of the parties and the efficiency of the process.

As part of the process of forming a committee, specialist advisers, both financial and legal, would be retained by the committee, and while not acting directly on behalf of each creditor, they will provide assistance in streamlining the provision of advice generally and remove an element of duplication where each creditor would normally appoint their own individual adviser (the formation of a committee does not preclude a creditor from still seeking further independent advice).

The company seeking the restructure will pay the professional fees associated with the committee advisers, but may not be willing to pay individual creditor costs. One of the principal advantages of using coordinators is that it helps to ensure that all the relevant creditors receive the same information and advice during the restructure process. For the company, the benefit of a committee is that it offers a more efficient and reliable process for pursuing restructuring negotiations with its creditors. Costs should also be reduced by needing to fund only one set of adviser's fees.

Given the current scale of distress in the aviation sector and with multiple stakeholders involved in each potential restructure (airlines, lessors and lenders), the use and formation of such committees can only benefit all parties and are well suited to the structure of such processes.



There may well be some turbulence ahead, but there is a runway to recovery on the horizon.

Conclusion

As we work through 2021, we remain optimistic and hope to see some level of recovery in the aviation industry. The impact of COVID-19 to date has been quite profound both from a cash and working capital perspective in airlines and leasing companies, so we still face a period of uncertainty, both in 2021 and beyond.

It is worth emphasising that this crisis in the aviation sector, on foot of a pandemic, has never been seen in modern times. In effect, this means that any lessons learned following 9/11 or the 2010 Icelandic ash cloud are hard to rely upon. Data points from those events will not help in forecasting this time, and consequently it is difficult for the industry to plan forward with any degree of certainty.

Although COVID-19 impacted the whole world, the effect was not shared equally. Some countries opened at different times than others. Adding further to the uncertainty, a fresh spike in cases or another new variant of COVID-19 could lead to closing of borders overnight. It is clear that airlines, lessors, lenders and the broader aviation industry face significant short-term challenges, and key strategic decisions will be required for the long-term future survival of many. There may well be some turbulence ahead, but there is a runway to recovery on the horizon.

Act early
This will allow each business and its management team make the most appropriate decision for their continued success.

Maximise options
By acting early, businesses increase the number of options available to them, whether through direct stakeholder negotiation or creditor-supported formal restructuring processes.

Develop appropriate options analysis
Given underlying debt and liquidity challenges in the sector, by developing an appropriate options analysis and engaging with creditors, a business can successfully navigate this period of volatility and recover.

Deloitte's restructuring advisory team in Ireland, supported by our wider aviation finance services (including tax, risk and accounting advisory teams), is best placed to advise clients in navigating the current trading environment. In addition to our local expertise, Deloitte's wider global team allows us to consider all available processes across relevant jurisdictions through the preparation of a robust options analysis and cross-border supports. We have already advised a number of companies in seeking available options and have led a number of coordinating committees in cross-jurisdictional restructures for secured lenders.

EQUAL OPPORTUNITY?

Prioritising gender diversity and inclusion in leadership development.

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Financial services leaders, like those at most companies, are grappling with unprecedented challenges brought on by the COVID-19 outbreak – taking care of clients, employees, and intermediaries while maintaining business continuity. At the same time, many may still be addressing organisational challenges that arose well before the outbreak. One such issue is how to create greater gender diversity and inclusion throughout their companies and among leadership, including the consideration of candidates for the C-suite.

This report, the third in our Within Reach series on women in financial services, examines the path to chief executive officer (CEO) at the 107 biggest public US financial services companies (by asset size), as well as where women are currently situated in leadership.

Among our main findings are the following:

01 The current CEOs at these companies are almost all male and predominantly drawn from three talent pools – lines of business, operations, and finance – where women are generally underrepresented.

02 Of those talent pools, the path to CEO for women appears to be the most promising in finance, where 40% of current CEOs held positions in one of their prior two roles. What's more, women account for 21% of all finance leadership roles compared with just 11% in operations and only 9% leading lines of business.

03 Women tend to be much more highly represented in leadership roles not historically considered for CEO candidates, such as talent (66%) and marketing/business development (48%).

04 One way to achieve greater opportunity for women at the highest level may be for boards and leadership teams at financial companies to establish programmes that would encourage and enable more women to assume roles historically considered as potential CEO candidates, as well as track their progress.

05 At the same time, boards and leadership teams could widen their lens on succession planning to consider those in leadership roles not currently prevalent in CEO searches. This would involve reassessing the background criteria, skill sets, and capabilities required for CEOs to reflect the transformation underway in most aspects of their business.

More women hold C-level roles in FSI firms than ever before, but relatively few have risen to become CEO. Our research shows the biggest barrier may have to do with the paths to get there.

The business case for D&I initiatives is clear to a growing number of board members and leadership teams at financial services companies, the business case demonstrating how diversity and inclusion (D&I) programmes can improve results, provide different perspectives, and better connect with a more diverse customer base and workforce has been made. More and more companies are realising that diversity can drive innovation[1] and increase productivity companywide.[2] Gender diversity at the leadership level may also boost profitability.[3]

Many US banks, insurers, investment management firms, and commercial real estate companies are examining how to increase gender D&I in their C-suite and senior leadership ranks. Yet, as of 2019, among the 107 largest public financial institutions in the United States, only six had female CEOs.[4] Financial services firms seeking more diversity in their candidate pool will likely need to recruit and develop more women in the areas in which CEOs have historically come from – lines of business, finance, and operations. This can be part of a company's comprehensive effort to achieve greater gender diversity in leadership and throughout the organisation to better reflect their workforce, customer base, and society as a whole. It will likely require some significant changes in culture, talent development, and succession planning.

1. Rocio Lorenzo and Martin Reeves, "How and where diversity drives financial performance," Harvard Business Review, January 30, 2018.
2. Stephen Turban, Dan Wu, and Letian (LT) Zhang, "Research: When gender diversity makes firms more productive," Harvard Business Review, February 11, 2019.
3. Yoni Blumberg, "Companies with more female executives make more money – here's why," CNBC, March 2, 2018.
4. Proprietary analysis and custom segmentation by the Deloitte Center for Financial Services of 107 large, public US financial services institutions' data from BoardEx. The analysis of such data referred to throughout this report includes banking, investment management, insurance, commercial real estate, and select payments provider firms.

At the same time, companies could also reconsider what it takes to become a CEO, and how a more diverse pool of candidates – not just by gender but also background and capabilities – might benefit their competitiveness and profitability over the long term.

In addition, recruiting more women in high profile C-suite positions traditionally leading to CEO consideration might, in and of itself, help enhance diversity down the line. Our research for this series revealed a powerful multiplier effect: Each woman added to the C-suite of financial services firms resulted in a three-fold increase of women in senior leadership positions at these companies.[5]

In this report, we dive deeper into the types of responsibilities and roles that historically have led to CEO appointments and document the statistical underrepresentation of women in those areas. We also spotlight the leadership[6] roles that women tend to hold. While these are all worthy and important roles, they do not appear to align with the traditional path if one's ultimate goal is to be considered for the CEO job.

The path to CEO is narrow

All but six of 111 CEOs at the 107 largest US public financial institutions (including four with co-CEOs) are men. In analysing the career paths of the 92 CEOs who were not founders of their companies, we found three significant patterns:

- The vast majority of current CEOs had occupied three types of leadership roles in one of their prior two jobs (figure 1) – leading lines of business, finance, or operations.
- Among these three leadership pools where CEOs are typically groomed and recruited, women are underrepresented.
- Women tend to have a far higher representation in leadership roles that, historically, have not led to promotion to CEO.

While 62% of current CEOs had been line of business (LOB) leaders in at least one of their two prior roles, only 9% of LOB leaders at these firms are women. This is particularly significant because half of all leadership positions at these companies are LOB-related.

5. Alison Rogish et al., Within reach? Achieving gender equity in financial services leadership, Deloitte Insights, November 5, 2019.
6. For the purposes of our analysis and as used throughout this report, the term "leadership roles or positions" includes C-suite roles and senior leadership roles, defined as 1–3 levels below the C-suite.

Figure 1. Most women leaders in financial services firms have responsibilities that fall outside the traditional realm of becoming CEO

Leadership responsibilities	Distribution of leadership roles across categories	Share of women leaders in these areas	Per centage of CEOs who held roles in these areas in one of prior two roles
Line of business	50%	9%	62%
Finance	8%	21%	40%
Operations	3%	11%	38%
Portfolio management	2%	10%	12%
Regional business unit	13%	14%	8%
Strategy	2%	17%	7%
Marketing and bus dev	3%	48%	5%
Legal	5%	33%	4%
Technology	5%	22%	2%
Risk/compliance	5%	27%	1%
Talent	3%	66%	1%
Administration	2%	39%	1%

Source: The Deloitte Center for Financial Services analysis of BoardEx LLC data.

Women tend to have far higher representation in leadership roles that, historically, have not led to promotion to CEO.

On the other hand, operations may have only accounted for 3% of leadership positions at the 107 companies studied, but it was a major source of CEO candidates. One out of four current CEOs had been chief operating officers (COOs) in their most recent prior position, making COO the most prevalent former title. And an even larger share – 38% of current CEOs – had leadership posts in operations in at least one of their two prior roles. Yet women only make up 11% of the current operations leadership pool.

The numbers are a bit more promising in finance positions, which accounted for 40% of current CEO backgrounds, and where women make up 21% of the leadership pool. But that's still below the overall per centages of women in the C-suite at these companies – 27% of traditional C-suite titles and 32.5% of more recently added titles (such as chief information security officer, chief privacy officer, chief sustainability officer, chief innovation officer, and chief diversity officer).[7]

Meanwhile, women account for 66% of leadership positions in talent, 48% in marketing and business development, 39% in administration, and 33% in legal – none of which are commonly included on the path to CEO.

Widening the path to CEO

Reflecting on this evidence, it appears more needs to be done to enhance gender equity in the leadership ranks throughout the biggest financial firms.

One way to look at this is through a traditional lens. If financial services firms want to continue to draw future CEOs chiefly from LOB, finance, and operations pools, boards and leadership teams may need to reconcile these criteria with gender-based diversity and inclusion goals. They could focus on recruiting and enabling more women to join these traditional paths, preparing them for leadership roles with the necessary LOB, finance, or operational responsibilities.

7. Alison Rogish, Stacy Sandler, and Neda Shemluck, Women in the C-suite: Growth in emerging leadership roles creates new opportunities in financial services, Deloitte Insights, March 4, 2020.

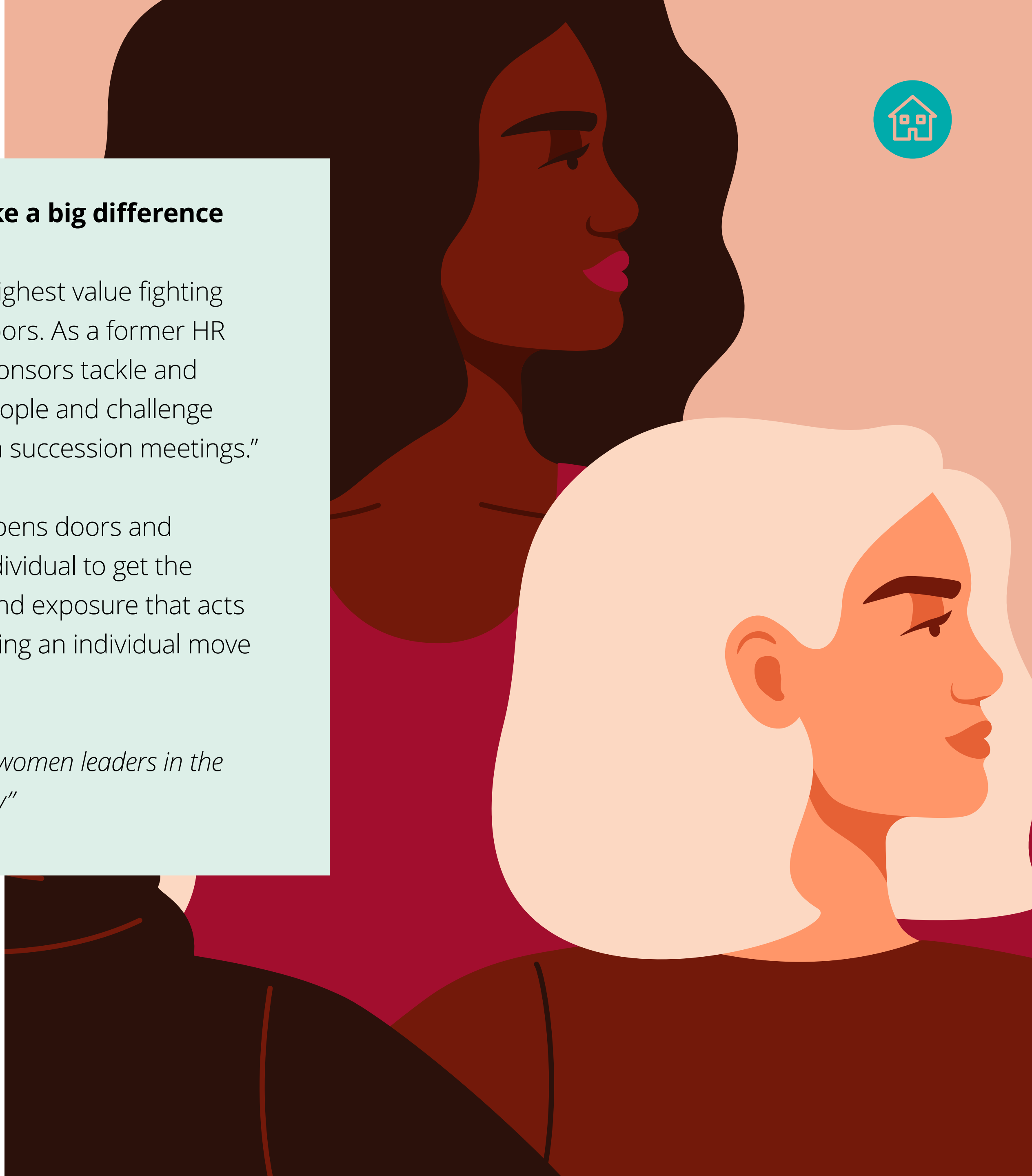
Our research found that sponsorship can significantly help women move into leadership roles at financial services firms. Encouraging both women and men already in those key roles to sponsor others looking to follow in their footsteps could help increase diversity on the path to CEO. Indeed, in a virtual panel of women leaders across the industry discussing gender diversity and inclusion, several participants cited sponsorship as a key element in their own career growth.[8]

Sponsorship can make a big difference

"Sponsors garner the highest value fighting for us behind closed doors. As a former HR executive, I watched sponsors tackle and move mountains for people and challenge stereotypical thinking in succession meetings."

"Sponsorship is what opens doors and opportunities for an individual to get the hands-on experience and exposure that acts as a critical step in helping an individual move forward in their career."

Panellists, "The future of women leaders in the financial services industry"



8. The future of women leaders in the financial services industry, crowdsource exercise by Currnt for the Deloitte Center for Financial Services, July 2019.

It's understandable why most companies generally pick from just three pools for their CEO candidates. LOB leaders often run mini-versions of the larger company, with multiple direct reports handling a wide range of functions, along with profit and loss responsibility. Those in finance have visibility into the balance sheet, strategic investments, and merger and acquisition activity. And chief operating officers are already often considered second in the chain of command at many companies, overseeing day-to-day internal business operations.

The likelihood of being considered for the CEO role drops precipitously after the top three roles/responsibilities cited in figure 1. However, that does not necessarily mean future CEOs could not, or should not, be drawn from alternative leadership pools. A cross-industry study by *The Wall Street Journal*, echoing our financial services findings, cited the importance of rethinking a one-size-fits-all path to CEO.[9] It also pointed out the importance of taking a concerted, systematic approach to achieving gender D&I, which would include incorporating a broader set of metrics (such as consensus-building skills) and remapping leadership pathways accordingly.[10]

Therefore, more companies may want to consider widening their lens by reassessing the criteria traditionally applied to CEO successions. This may be especially valuable at a time when major changes are being made in products, technology infrastructure, distribution platforms, talent requirements, and customer experience. Perhaps it is also time to make progressive changes to senior leadership composition, recruitment models, and succession strategies, including the path to CEO.

These changes would likely involve altering the standard assumptions about requirements in terms of background, skill sets, and leadership abilities to take over as CEO. They would also need to factor in the growth in C-suite positions created to tackle emerging business and market challenges. Financial companies could start considering those with additional leadership skill sets, such as strategy, technology, business development, customer experience, communications, and talent management. These are the capabilities likely to help financial institutions keep up with the rapid changes in an increasingly digital, consumer-centric economy.

In addition, to further diversify the pool of women candidates, financial firms may want to consider widening their search to recruit outside their companies. Of the 92 CEOs studied, only 22% were external hires. Firms could even consider looking beyond their own financial services sector for potential CEO candidates, which doesn't happen often now.

9. Vanessa Fuhrmans, "Where are all the women CEOs?," The Wall Street Journal, February 6, 2020.
10. Ibid.

This will likely require getting all employees, especially men, more actively involved in the gender D&I effort, by serving as mentors, sponsors, and allies.

Bolstering gender diversity among CEO candidates

To diversify the overall leadership pool and prepare more women to be potential CEO candidates, many financial services companies may have to:

- **Reassess the presence of women in leadership roles across the company.** Boards and leadership teams should continue to track and measure the progress being made to enhance gender D&I, particularly during leadership searches and CEO succession planning. Tracking should include discussions about widening the lens and considering additional qualifications and roles.
- **Launch and sustain initiatives to accelerate gender D&I and measure results.** This effort should be led by an individual with the resources and high-level access to effect the necessary changes in process and culture, such as a chief diversity officer (CDO). While 62.5% of US financial services firms had a CDO as of 2018,[11] it is uncertain how many have direct access to the CEO and the board, along with the budget, staff, and authority to drive significant change.
- **Foster a more inclusive culture, from recruitment to on boarding, training, and performance management assessments.** This will likely require getting all employees, especially men, more actively involved in the gender D&I effort, by serving as mentors, sponsors, and allies.
- **Build a feeder pipeline of women in leadership roles with P&L, finance, and operational responsibilities.** This might include a rotational programme to encourage professionals of all genders and backgrounds to be exposed to a wider variety of leadership roles and/or develop additional skill sets. Financial firms could also establish or expand re-entry programmes for professionals who paused their careers for any number of reasons but later decided to return.

11. NewVantage Partners, "Data and innovation: How big data and AI are driving business innovation," 2018.

Visibility can make a big difference

"I am motivated to be a role model for other women. ... I believe you cannot be what you cannot see."

"Bring other women along ... [Create] an environment with more women ... Have a bench of other women you are grooming or helping to come up as well."

Panellists, "The future of women leaders in the financial services industry"

- **Capitalise on the multiplier effect.** As noted earlier, our research found a threefold increase in the number of women in senior leadership for each woman added to the C-suite.[12] Therefore, efforts to enhance gender equity in the top ranks would likely have a ripple effect throughout an organisation, and could result in more women being considered for leadership appointments, all the way up to CEO. Indeed, one study found that having multiple women in a pool of finalist candidates can make a huge difference in leadership hiring decisions.[13] And at a recent symposium on "Women and diversity: Expanding opportunity in insurance," several speakers urged women who reach senior leadership and C-suite positions to think about "how do I lift others as I climb myself?" via mentoring, coaching, and sponsoring.[14]

12. Rogish, Sandler, and Shemluck, Women in the C-suite.
13. Stefanie K. Johnson, David R. Hekman, and Elsa T. Chan, "If there's only one woman in your candidate pool, there's statistically no chance she'll be hired," Harvard Business Review, April 26, 2016.
14. "Women & diversity: Expanding opportunity in insurance," symposium sponsored by the American Property Casualty Insurers Association, American Council of Life Insurance, and the Life Insurance Council of New York, New York City, on February 28, 2020.

The long and short game on succession

Progress has already been made toward enhancing gender diversity in the C-suites of big, public US financial services companies. Our two earlier reports revealed, however, that to establish even greater equity of opportunity, especially when considering who might occupy the CEO's proverbial corner office, more work needs to be done.

Diversifying leadership, up to and including the CEO spot, will likely take time. Succession planning is generally considered a "long-term discipline in a short-term world," which "by its very nature … takes years to bear fruit."[15] Still, financial firms that are prioritising D&I goals should explore strategies to accelerate the process to position more women in leadership and as CEO candidates. They have several options to help make that happen.

15. Jeff Rosenthal et al., The holy grail of effective leadership succession planning: How to overcome the succession planning paradox, Deloitte Insights, September 27, 2018.

Methodology

The quantitative analyses reported are based on the Deloitte Centre for Financial Services' proprietary analysis and custom segmentation of 107 US public financial services institutions' data from BoardEx LLC through 2019. The 107 institutions represent the top 25 each in banking, investment management, insurance, and commercial real estate firms by asset size, in addition to select payments provider firms included in the banking segment. These 107 institutions had 111 CEOs in all, as four of the institutions had two CEOs. In addition, our statistical analysis focused on the 92 CEOs who were not founders of their companies. A cross-sectional association analysis was conducted at the organisational level to determine the multiplier effect, which found a threefold increase in the number of women in senior leadership for each woman added to the C-suite. Where used throughout the report, 'financial services' denotes the previously listed industry segments.

Additional qualitative material was taken from a crowdsourced virtual panel exercise conducted by Currnt on behalf of the Deloitte Centre for Financial Services. That project, fielded over four days during July 2019, involved 20 senior leadership-level women representing banking, insurance, investment management, and commercial real estate firms.

RISKS, REGULATIONS AND RAMIFICATIONS

IN CONVERSATION WITH COLM KINCAID

COLM KINCAID
DIRECTOR OF SECURITIES AND MARKETS SUPERVISION, CENTRAL BANK OF IRELAND

How can financial firms adapt to a changing environment as they face an array of challenges, from COVID-19 and increasing regulatory complexity, to conduct risk, Brexit and more.

2020 WAS A DIFFICULT YEAR FOR US ALL. HOW HAS THE CENTRAL BANK RESPONDED TO THESE CHALLENGES IN TERMS OF ITS SUPERVISORY MANDATE?

It was a very challenging year, and I think we will see many of those same challenges persist over the course of 2021. Indeed, some of the COVID-related challenges may even become more acute as natural fatigue sets in and medium- and longer-term implications start to emerge. So, we need to remain vigilant to these risks.

For the Central Bank of Ireland, as for other organisations, 2020 required us to react quickly to emerging events and target our interventions appropriately to the evolving situation. This is nothing new in principle for us of course, as our approach to supervision is always to be risk-sensitive and, in my own field of securities markets supervision, events move at an especially and increasingly swift pace in any event. What was new was the particular logistical challenge of managing the situation in a remote working environment. This included supervising firms remotely in a manner that ensured we remained assertive and challenged firms on how they were dealing with the situation.

One thing I did observe was the extent to which the issues that emerged over the course of 2020 mapped to the priority areas of concern that we had previously highlighted. This is not to claim any special prescience on our part about the events of 2020. Rather, I think the impact of COVID-19 and Brexit threw the issues and vulnerabilities we had been highlighting for some time into especially sharp relief. Many of these are about the basics of good governance, systems and controls and proper resourcing within Irish-regulated entities. To take a sector where there was a particular COVID and Brexit focus – the funds sector – we had already planned specific supervisory reviews of liquidity risk management and compliance with our framework for fund management companies' governance, management and effectiveness. These topics became absolutely central to the discussions we had with firms as they weathered the challenges of 2020.

BASED ON WHAT WORKED WELL, CAN FIRMS EXPECT A DIFFERENT FORMAT OF SUPERVISION INTO THE FUTURE, MORE VIRTUAL AND LESS ONSITE?

While we are still in the middle of this pandemic it is too early to speculate on potential longer-term modifications. But there are lessons to be learned and efficiencies to be gained. For instance, I think the remote environment placed a particular premium on quantitative data and documented evidence of operational procedures and controls. These are two areas firms can expect the Central Bank to continue to place a special focus on, and in particular that systems and controls are fully documented and operational. It is also essential that data is reliable. The remote working experience and fast-moving market events really brought home the importance of this and the limitations of manual work-arounds or *ad hoc* approaches.

I also see lessons from this period for how we conduct virtual engagements more effectively, bearing in mind that even pre-COVID we had calls and so on, so the principle of 'virtual engagement' is not new. Overall, however, while we might use these tools to be more targeted, I expect onsite inspections to remain a regular and important part of our suite of engagements into the future. I would also counsel against any expectation that there would be less onsite engagement by the Central Bank in the future, even if the proportion of onsite to virtual were to change, since our overall engagement with the securities market sector will continue to be robust and, if anything, can be expected to increase.

> The impact of COVID-19 and Brexit threw the issues and vulnerabilities we had been highlighting for some time into especially sharp relief. Many of these are about the basics of good governance, systems and controls and proper resourcing within Irish-regulated entities.

BREXIT HAS IMPACTED THE SECURITIES AND MARKETS SECTOR MORE THAN MOST. GIVEN RECENT EQUIVALENCE DECISIONS, HIGH PROFILE RELOCATIONS AND CHALLENGES AROUND BUSINESS MODELS, HOW DO YOU SEE THE IRISH AND EU SECURITIES AND MARKETS ECOSYSTEM EVOLVING OVER THE COMING YEARS?

Firms did a lot to prepare for Brexit, including a hard Brexit, and it has been a supervisory focus of the Central Bank for some time. So we come into the post-Brexit period well prepared.

However, the decision by the UK to leave the EU has changed the structure, composition and operations of securities markets in both jurisdictions. It will take time to see how the issues and risks we identified in the run into Brexit manifest themselves in a post-Brexit environment. So for example, we have seen the migration of firms and trading activity from the UK to EU member states and venues, including Ireland. This results in new or existing EU firms taking on assets, activities and risks which are new to these firms and require the appropriate controls to ensure that conduct risk is managed prudently.

Brexit also changes the manner in which EU and now UK rules apply to dealing on securities markets and we need to be vigilant to the novel risks and trends that could emerge as a result. I would say that the effort firms put into preparing for Brexit needs to be replicated now as they experience the realities of operating in the new environment and that firms put concrete plans in place to identify, mitigate and manage the specific risks arising for their firm and the markets in which they are active.

In terms of how the securities and markets ecosystem might evolve over time, I expect this will be influenced as much by wider developments in technology and wider priorities such as CMU and the imperative of combatting climate change. Our focus, of course, will continue to be on ensuring that however the markets evolve, the best interests of investors and market participants using those markets are protected and the firms we authorise and supervise apply the highest standards.

WE ARE STARTING TO SEE MORE M&A ACTIVITY IN THE SECTOR. FOR FIRMS CONSIDERING A POTENTIAL ACQUISITION, WHAT ARE KEY THINGS THEY SHOULD BE CONSIDERING, TO ENSURE THEY ARE SUCCESSFUL WITH THEIR APPLICATION?

First, firms considering an acquisition should familiarise themselves with the regulatory requirements which are available on the Central Bank website – centralbank.ie. In May 2017, the Joint Committee of the European Supervisory Authorities issued guidelines entitled 'Joint Guidelines on the prudential assessment of acquisitions and increases of qualifying holdings in the banking, insurance and securities sectors'. A proposed acquirer should take note of these Guidelines when preparing the Acquiring Transaction Notification Form for submission to the Central Bank.

> One of the most powerful forces affecting trust in financial markets and their participants is, quite simply, how regulated financial service providers conduct themselves. With the increasing scale and complexity of the securities market we supervise, we have had to become more systematic in our approach to the sector.

Secondly, they should ensure the notification form is completed in full and all required documentation is provided to avoid undue delays in the notification and assessment process.

Finally, firms should be able to articulate how the acquisition will benefit the firm and its clients, the risks arising and how those risks will be mitigated and managed.

WE HAVE SEEN QUITE A BIT OF ACTIVITY FROM YOUR TEAM OVER THE LAST YEAR IN THE FORM OF DEAR CEO LETTERS AND RMPS. WHAT SHOULD WE READ INTO THIS, IF ANYTHING?

One of the most powerful forces affecting trust in financial markets and their participants is, quite simply, how regulated financial service providers conduct themselves. With the increasing scale and complexity of the securities market we supervise, we have had to become more systematic in our approach to the sector, including in our communication with the sector where we see things that need to change. This includes publishing 'Dear CEO' letters so that the industry as a whole has the benefit of those findings and issuing detailed RMPs to individual firms. We will be looking to see firms take concrete and substantive actions to implement the findings in these letters, and to be diligent and comprehensive in their implementation of the RMPs they receive. Where appropriate, we will make use of stronger tools.

FROM A SECURITIES MARKETS PERSPECTIVE, WHAT HAVE BEEN THE KEY WHOLESALE CONDUCT RISK CONCERNS THIS YEAR?

As I referred to earlier, COVID-19 and Brexit were dominant themes in 2020, along with trade tensions and events such as the US election. However, a key overarching theme has been the increasing scale and complexity of the securities markets we supervise. In 2020, we saw continued growth in the investment fund sector, continued volumes of applications for approvals of prospectuses for securities issuances and further new firms establish themselves in Ireland in anticipation of Brexit, some of which brought business models that were new to us as supervisors. We also see an increase in trading volumes, making it ever more important that firms are proactive in discharging their obligations to monitor and report suspicious trading activity.

With this complexity comes an increasingly complex regulatory framework also. In 2020, we saw the implementation of a range of new legislative measures, including new reporting obligations under the Money Market Fund Regulation and SFTR. Together with existing legislative regimes such as MiFID and EMIR, this increases again the scale of the data regulators require to discharge their statutory functions, and the importance of that data being of good quality. We also saw the implementation of the revised Prospectus Regulation, raising the standards required of approved prospectuses and the extent of competent authority scrutiny of those prospectuses before such approval can be granted.

So a key concern for us is ensuring that regulated firms, market operators and market participants are on top of this complexity and that they have the resources, frameworks and controls in place to identify, mitigate and manage conduct risk. This includes ensuring that these elements themselves evolve in tandem with the firm or venue's own growth and adaptations; for example, increased reliance on technology. This can require compliance and risk functions within firms to have new skills and to develop new tools to monitor and manage risk. You will see this focus come through in our industry letters on wholesale conduct risk, governance in funds, and in the focus of our current thematic review on market abuse, the results of which we aim to publish later this year. Fundamentally, if firms do not have the resources, frameworks and controls in place to identify conduct risk within their firm, then they cannot mitigate those risks.

Faced with this complexity of market and regulatory framework, I would also encourage firms to take a step away from a legalistic or minimalist approach to their obligations towards a more prudent risk-based approach, including on resourcing.

WHAT ARE YOUR FOCUS AREAS FOR 2021?

In many respects, 2021 will see a continuation and follow through on our work of 2020. This means continued work on fund liquidity management and of course the implementation of the findings of our review of the framework for Fund Management Companies' Governance, Management and Effectiveness. Also, in 2020, we commenced a supervisory review of compliance with MAR requirements for issuers and those that act on their behalf, on the main Irish regulated market. The review focuses on the extent to which participants comply with requirements to recognise, manage and in the case of issuers, publicly disclose inside information in accordance with applicable legislation. At the same time, we commenced a supervisory review on the practice and governance of detecting and reporting suspected market abuse. In 2021, one of our supervisory priorities will be to complete these reviews and take appropriate action on foot of our findings (which we aim to publish later this year).

We have been strong supporters of an increasingly effective approach to supervisory convergence at EU level. This is especially important in view of the pan-EU and indeed international nature of the securities markets activities and services provided in and from Ireland. Key areas of focus here will include of course the ESMA Common Supervisory Action on the supervision of costs and fees of UCITS and our continuing work to enhance data quality across the EU market.

In our 'gatekeeper' functions, we will continue our implementation and embedding of a more risk-based approach to the assessment of applications for fund authorisation and prospectus approval consistent with our wider supervisory risk outlook and approach.

And of course, 2021 will see further implementation of new aspects of the regulatory framework, not least the requirements of SFDR which come into force on 10 March 2021. The evolving climate crisis and the universal need to mitigate its effects requires that financial products and services become more environmentally sustainable. By financing initiatives and trends aimed at stemming the climate crisis, sustainable finance can play a key role in ensuring that securities markets aid the transition to greener economic activities.

Indeed, I would highlight the transition to a greener securities market as one of the key overarching themes for the period ahead and firms can expect us to challenge them to be vigilant to avoid the risk of greenwashing, be that intentional or through a failure of proper diligence. This includes that where the sustainability aspect of the product or service is unclear or dependent on future developments, this is explained clearly in the product documentation. Where investments or financial products are described as green or sustainable, firms should ensure that this is meaningful and accurate and based on reliable parameters that are consistently applied both within jurisdictions and across Europe.

The SFDR requires financial market participants and financial advisers, which includes UCITS management companies and Alternative

A key concern for us is ensuring that regulated firms, market operators and market participants are on top of this complexity and that they have the resources, frameworks and controls in place to identify, mitigate and manage conduct risk.

Investment Fund Managers (AIFMs), to make pre-contractual and ongoing disclosures to end investors with regard to the integration of sustainability risks, the consideration of adverse sustainability impacts, the promotion of environmental or social characteristics, and sustainable investment. To facilitate orderly implementation of the SFDR, the Central Bank has established a fast-track filing process for pre-contractual document updates based on the SFDR Level 1 text, under which both UCITS management companies and AIFMs will be able to certify their compliance with the SFDR. Both will need to determine the fund's appropriate product classification and ensure pre-contractual disclosures are appropriate to their particular funds.

Finally, and to go back to where we started, there are lessons from 2020 for the regulatory framework. Given the nature and scale of our securities markets industry, including funds, the Central Bank is an active participant in this work at EU and international level. Our supervisory insights from 2020 inform our approach in these discussions.

MANY OF OUR CLIENTS ASK US HOW THEY CAN IMPROVE THEIR REGULATORY RELATIONS, GIVEN THERE IS SO MUCH ON THIS YEAR. WHAT ADVICE WOULD YOU GIVE THEM?

In the context of our supervision of securities markets specifically, we work to achieve a market that satisfies five principles: it provides a high level of protection for investors and market participants; it is transparent as to the features of products and their market price; it is well governed and comprises firms that are well governed; it is trusted, by both those using the market to raise funds and those seeking to invest; and it is resilient enough to continue to operate its core functions in stressed conditions and to innovate appropriately as markets evolve.

These are the principles that guide our supervisory judgments. So, it would be good advice to a firm to keep these principles in mind when framing their engagements with us. We also look to see that firms have done substantive and thoughtful work to meet their regulatory obligations, including to implement our 'Dear CEO' letters and guidance. Here in particular, we are looking to see a prudent, risk-based approach to achieving outcomes that advance the five principles outlined above, and not a minimalist or legalistic approach.

Finally, as with any regulator, we expect firms to be well prepared and open in their engagements with us and to remember that the Central Bank's supervisory teams have a public service to perform on all our behalf.

This interview took place on 14 January 2021.

Read the **Securities Markets Risk Outlook Report from Central Bank of Ireland**

DEEP IMPACT

New European guidelines on loan origination aim to improve financial institutions' practices throughout the loan cycle while also preparing them for future challenges.

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The final Guidelines form part of the response to the European Union's Action Plan regarding high levels of non-performing exposures witnessed throughout the global financial crisis (GFC), with non-performing loan (NPL) ratios remaining at pre-GFC levels in some countries at present.

The objective of the Guidelines, which differ significantly in some aspects to the previously published draft Guidelines issued 19 June 2019, is to:

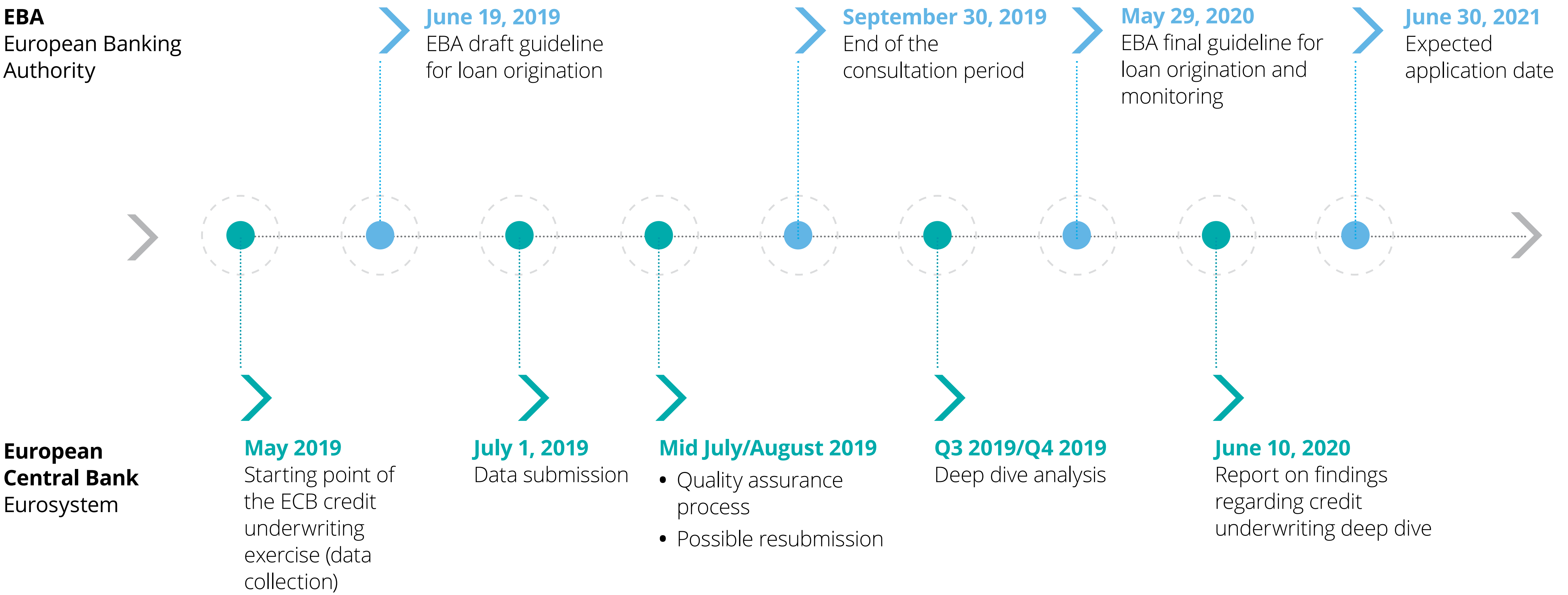
- Further improve institutions' practices and governance to ensure effective management and monitoring throughout the loan cycle;
- Prepare the banking sector for upcoming challenges within the EU banking sector (for example, sustainability, fintech etc.); and
- Improve profitability by ensuring that newly originated loans are of high credit quality, while respecting and protecting the interests of consumers.

The COVID-19 pandemic has heightened the necessity of maintaining good credit risk management standards to support lending to the economy. This also ensures the adequate identification and proactive management of situations where obligors may face financial difficulty. In May 2020, it was estimated that COVID-19 is set to drive €4bn in loan losses for the Irish banks[1].

It is worth noting that the European Central Bank (ECB) is also strengthening its approach in this regard with a focus on credit underwriting being a supervisory priority for a second year in a row. The ECB's report from June 2020 outlines findings on the topic with further detailed analysis anticipated this year across areas of perceived heightened risk via onsite inspections and follow up actions.

1. *The Irish Times* May 27, 2020.

Figure 1. Framework of the EU Council's Action Plan



Key areas of impact

The Guidelines were published much later than anticipated which reflects the depth of requirements and the volume of consultation comments provided by industry.

Given the changes, even banks that have already adjusted their loan origination and monitoring process to meet the draft Guidelines will have some distance to travel to meet the updates outlined in the final Guidelines.

The Guidelines were published much later than anticipated which reflects the depth of requirements and the volume of consultation comments provided by industry.

Even if banks have commenced work in recent months in light of the draft Guidelines, it is worth noting that the final Guidelines:

- Add a number of additional requirements to ensure the effective incorporation of ESG factors and associated risks into credit risk appetite, valuations and credit worthiness assessments;
- Differentiate pricing frameworks considerations based on types of loans and borrowers;
- Include additional monitoring requirements for banks engaged in syndicated leveraged finance transactions and the inclusion of qualitative factors in gauging repayment capacity;
- Replace the definition of professionals with micro and small enterprises and midsized to large enterprises;
- Specify criteria for assessing the credit worthiness of real estate, leverage finance and project finance;
- Further consider automation of models.

Figure 2. Indicative areas of impact of the EBA Guidelines

EBA guidelines	Credit policies and procedures	Organisational design	Control environment	KRIs and monitoring	Data infrastructure
Governance	●	●	◑	◑	◑
Loan origination	●	●	●	●	●
Pricing	●	◔	◕	◕	◑
Collateral valuation	◑	◔	◕	◕	●
Monitoring	◑	◔	◕	●	●

Focus areas within the Guidelines

The Guidelines comprise five sections which are summarised below.

1. Internal governance

In addition to the provisions set out in the EBA Guidelines on Internal Governance (EBA-GL-2017-11), banks must ensure they:

- Define a credit risk strategy within their overall business strategy to ensure alignment with the bank's risk appetite framework in addition to capital (ICAAP) and liquidity (ILAAP);
- Set a credit risk appetite which should be supported by appropriate credit risk metrics and limits covering client segments, currency, collateral types and credit risk mitigation instrument with backward and forward-looking indicators;
- Outline a credit risk appetite which specifies concentration and diversification objectives relating to business lines, geographies, economic sectors and products;

The new Guidelines also set out specific conditions for the application of automated decision-making models for creditworthiness assessment and credit decision making.

- Develop an appropriate credit risk management culture;
- Set out the anti-money laundering (AML) and countering the financing of terrorism (CFT) requirements in the context of credit granting;
- Clearly define roles across the three lines of defence with regards to credit decision making process e.g., emphasising the principle of independence of different functions (e.g., business and risk) in decision-making;
- Set out the requirements for robust and effective credit risk management and internal control frameworks, as part of the institutions' overall risk management and control frameworks;
- Consider general remuneration requirements with regards to credit risk granting, with a view to mitigating excessive risk taking in lending activities.

This section of the Guidelines also introduces environmentally sustainable lending dimensions and defines requirements for institutions to take into account environmental, social and governance (ESG) factors with a view to environmentally sustainable lending and associated risks within their credit policies and procedures.

2. Loan origination procedures

As the title of the Guidelines would suggest, loan origination is the core chapter of the Guidelines focusing on the granularity of quantitative and qualitative information informing sound credit risk practices including:

- Additional requirements for collection of information from borrowers (consumers, micro and small enterprises or medium-sized and large enterprises), including the need to verify the authenticity of data and plausibility of all information provided by the borrower;

- Banks should enable a single aggregated, consistent and comprehensive customer view;
- In line with the European Commission's carbon neutral and green economy goals, the Guidelines require banks to take into account the impact of risks associated with ESG factors on the financial condition of borrowers.

The new Guidelines also set out specific conditions for the application of automated decision-making models for creditworthiness assessment and credit decision-making. In particular, banks should have in place:

- Measures to ensure the traceability, auditability, and robustness and resilience of the inputs and outputs;
- Internal policies and procedures ensuring that the quality of the model output is regularly assessed, using measures appropriate to the model's use, including back testing the performance of the model;
- Control mechanisms, model overrides and escalation procedures within the regular credit decision-making framework, including qualitative approaches, qualitative risk assessment tools (including expert judgement and critical analysis) and quantitative limits.

3. Pricing

The pricing section of the Guidelines defines the supervisory expectations for the risk-based approach, including the implementation of a comprehensive framework for the pricing of loans.

Banks will be required to differentiate between their pricing frameworks, depending on the types of loans and borrower. For consumers, micro and small enterprises, the pricing should be more portfolio and product based, whereas for medium-sized and large enterprises the pricing should be more transaction and loan specific.

For the purposes of loan pricing and measuring profitability, institutions should consider and account for risk-adjusted performance measures e.g. return on risk-weighted assets (RORWA), return on total assets (ROTA) and other measures that are relevant to the characteristics of the loan. Risk-adjusted performance measures should reflect the institutions' capital-planning strategies and policies.

The Guidelines also set out additional criteria for advanced statistical models used for valuation, revaluation and monitoring of collateral.

4. Valuation of the immovable and movable property

The valuation section of the Guidelines provides guidance regarding the valuation of immovable and movable property collateral at the point of granting credit, ongoing monitoring and review of the value of such collateral based on the outcomes of monitoring. This section presents the supervisory expectations for independent valuers as well as the conditions that allow for advanced statistical models to be used for the valuation, monitoring and revaluation of collateral.

The Guidelines also set out additional criteria for advanced statistical models used for valuation, revaluation and monitoring of collateral. Banks must ensure that advanced statistical models are:

- Property- and location-specific at a sufficient level of granularity (e.g., postcode for immovable property collateral);
- Valid, accurate and subject to robust and regular backtesting against the actual observed transaction prices;
- Based on a sufficiently large and representative sample, and observed transaction prices; and
- Based on up-to-date data of high quality.

5. Monitoring framework

The monitoring framework of the Guidelines specifies that a monitoring framework and data infrastructure should be put in place to provide automatic compilation of data regarding credit risk with minimal reliance on manual processes where feasible.

This section also outlines requirements with regards to:

- Monitoring of credit exposures and borrowers;
- Regular credit review of borrowers;
- Monitoring of covenants;
- Use of early warning indicators (EWI) and watch lists; and
- Follow-up and escalation process on triggered EWIs.

Back-tested lending metrics, covenant compliance and other monitoring activities will result in the embedding of early warning indicators in processes, building clear linkages between the ongoing monitoring and early detection of loans with deteriorating credit quality.

In addition, Banks engaged in syndicating leveraged transactions are now required to implement internal standards and monitoring functions for these activities including:

- Identification of transactions subject to failed syndications i.e. transactions were not syndicated within 90 days following the commitment date;
- Establishing a dedicated framework to deal with these 'hung transactions' in terms of holding strategy, booking and accounting practices, regulatory classification and subsequent capital requirements calculation.

- Lack of data quality/ infrastructure
- Limited integration of EWIs

Figure 3: Credit risk monitoring

- Enhanced monitoring framework
- Embedding of EWIs driven by leading metrics

Linkage with IFRS9 requirements

The introduction of IFRS 9 and Expected Credit Loss (ECL) model revealed the need for higher granularity on credit risk data as well as business implications on lending practices including pricing considerations, product design and monitoring of credit risk.

The introduction of specific metrics based on IFRS 9 – Point in Time (PiT) – parameters, as required by the ECB's credit underwriting exercise, might change the perception over optimal lending growth and overall strategy depending on priorities set and time horizon. Advantages and disadvantages of IFRS 9 PiT parameters must be taken into consideration.

On the one hand, standard risk costs and equity costs are more precise when they move with an expected credit loss model over the next 12 months, more likely resulting in an accurate estimate of expected and unexpected losses. Moreover, the use of IFRS9 probability of default (PD) will enhance viability and foster common understanding within the bank since risk and the business will have a single point of reference when discussing credit risk.

On the other hand, the loan approval process may decline or drive away viable business, for example, higher risk profile clients who have a long-standing relationship with the bank and may overall be a steady source of risk-adjusted return. Furthermore, standard risk and equity costs will become more volatile based on IFRS 9 PiT risk metrics, creating unpredictability and uncertainty in the lending strategy.

Interaction between prudential and consumer protection frameworks

The Guidelines underline that the obligation of the creditor to assess the creditworthiness of a borrower is intended to protect consumers against the risks of over-indebtedness, bankruptcy and to ensure responsible lending. Whilst protecting the borrowers' interests, notably with regards to creditworthiness assessment, these Guidelines require institutions to take consumer protection into account within the credit risk policies and procedures, credit-granting criteria and within their design of the credit products that are offered to consumers.

It is also true to say, at a more macro level, that financial stability may be impacted if borrowers are not able to meet their contractual loan commitments. In this context the performance of an accurate and thorough creditworthiness assessment is crucial in order to mitigate against the potential impacts on financial stability.

Proportionality principle

Firstly, for implementing the requirements regarding internal governance, risk management and control, a proportionality principle based on the size, nature and complexity of the institution or other relevant criteria, should be considered by the institution.

Secondly, for implementing the requirements regarding the creditworthiness assessment, collateral valuation and credit risk monitoring institutions should take into account the type, size and complexity of the credit facility being originated or monitored.

Moreover, the proportionality within the collateral valuation is also driven by the size, nature and complexity of the collateral and the relationship between the loan and collateral.

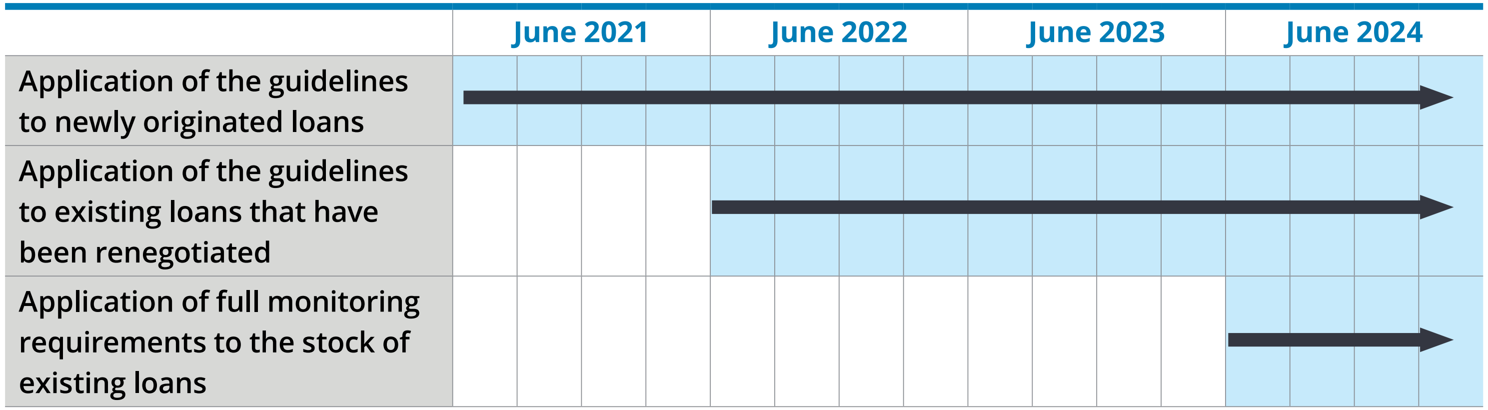
The differentiation regarding the application of the proportionality principle aims to ensure that loan origination and monitoring criteria are proportionate to the type, size, complexity and risk profile of the loans or credit facilities originated or monitored.

Application dates

These Guidelines will start to apply from 30 June 2021 with two further transitional deadlines as outlined in the graph below.

The timing of the two further transitional deadlines reflects consideration of the need for banks to focus on core operations today and to strengthen future lending given the unprecedented COVID-19 pandemic.

Figure 4: Implementation deadlines



Next steps

These forward-looking Guidelines which emphasise credit quality throughout the end-to-end loan cycle will have a considerable impact on banks' governance, credit risk processes, data, IT infrastructure, methodologies, lending practices and client interactions.

We would advise taking the following steps sooner rather than later given the uplift within these Guidelines:

- Reviewing any shortcomings or findings that were identified as part of the on-site inspections regarding credit underwriting;
- Performing a gap analysis against the Guidelines to identify shortfalls and provide a targeted roadmap to remediate any such shortfalls;
- Leveraging aspects of existing programmes for example, IFRS9, BCBS 239, Senior Executive Accountability Regime (SEAR) etc. as a starting point to build upon in order to meet the loan origination and monitoring Guidelines;
- Determining how the governance requirements as outlined in the Guidelines can be best interlinked with your existing governance and oversight structure;
- Understanding which businesses will be impacted the most to inform prioritisation;
- Assessing the adequacy and suitability of data in its current state.

THE MULTIPLIER EFFECT

The imperative for coordinated technology deployment in financial services. A perspective from the World Economic Forum and Deloitte.

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The report explores the multiplicative impacts that emerging technologies will have on the financial services industry when they are clustered together and deployed strategically against key business challenges.

Artificial intelligence does not exist in a vacuum and is already intertwined with a combination of other emerging technologies such as cloud, 5G networking, Internet of Things, distributed ledger technology, and others.

Nine emerging technologies that can transform the financial services industry:

- Artificial intelligence
- Quantum computing
- Distributed ledger technology
- Task-specific hardware
- Augmented and virtual reality
- 5G networking
- Internet of Things
- Cloud computing
- Privacy enhancing techniques

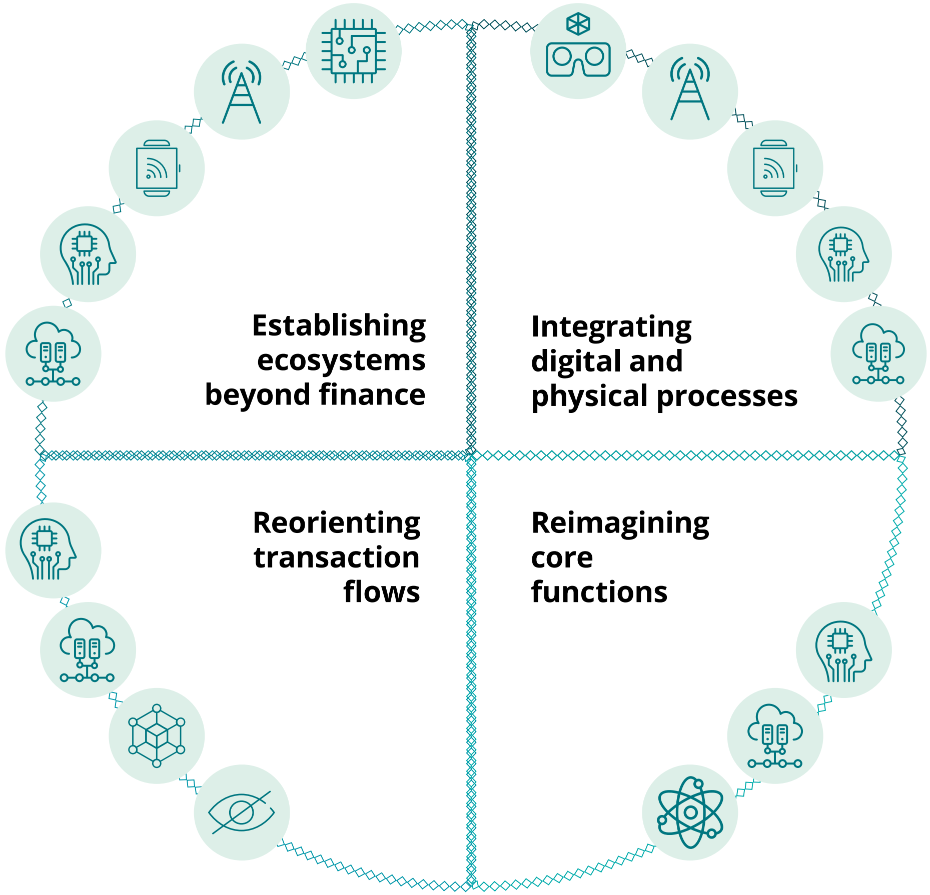
Three structural transformations we believe these emerging technology clusters will ultimately drive within the industry revealed:

- New tools to breakdown age-old barriers and unlock opportunity
- Changes to competitive dynamics and dominant operating models
- A new impetus to tackle systemic challenges in financial services

In addition, clusters of emerging technology will unlock capabilities that create new opportunity spaces for financial institutions in the future.

Read the full report, **Forging new pathways: The next evolution of innovation in financial services.**

Establishing ecosystems beyond finance
Combine financial and non-financial offerings by building on strong ecosystem relationships to deepen customer engagement and create entirely new value propositions.



Integrating digital and physical processes
Embed data about physical processes into financial products to improve risk and value assessment, assure the identity of transaction initiators, validate provenance of physical information, and optimise product distribution.

Reorienting transaction flows
Leverage modern data and value transfer rails to pursue more automated and direct movements of assets and funds between participants.

Reimagining core functions
Perform more granular, accurate, and robust calculations by tapping into leading-edge analysis methods and improve crossenterprise data organisation.

A SPECTRUM OF OPTIONS

Adaptable workforce strategies will be key for leaders planning for recovery after the COVID-19 crisis.

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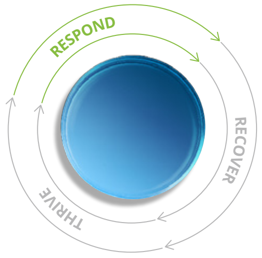
As a result of the COVID-19 pandemic, an estimated 2.7 billion people, or more than four out of five workers in the global workforce, have been affected by lockdowns and stay-at-home measures.[1]

Business and government leaders have been challenged to both respond to the crisis quickly and rethink their workforce strategies in real time.

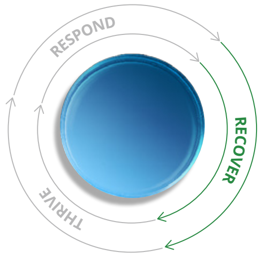
It is important to realise that the recovery won't be static. It will not occur on a specific date.

Most organisations' first priority has been crisis response and emphasising health, safety, essential services, and the virtualisation of work and education. Now, as organisations begin to emerge from this response phase, leaders are focusing on the next set of workforce challenges as they plan for the recovery.

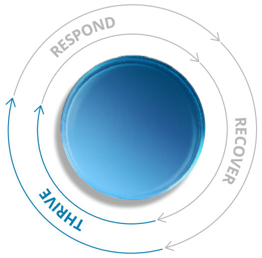
We see three phases that all resilient leaders will likely face amid the COVID-19 outbreak:



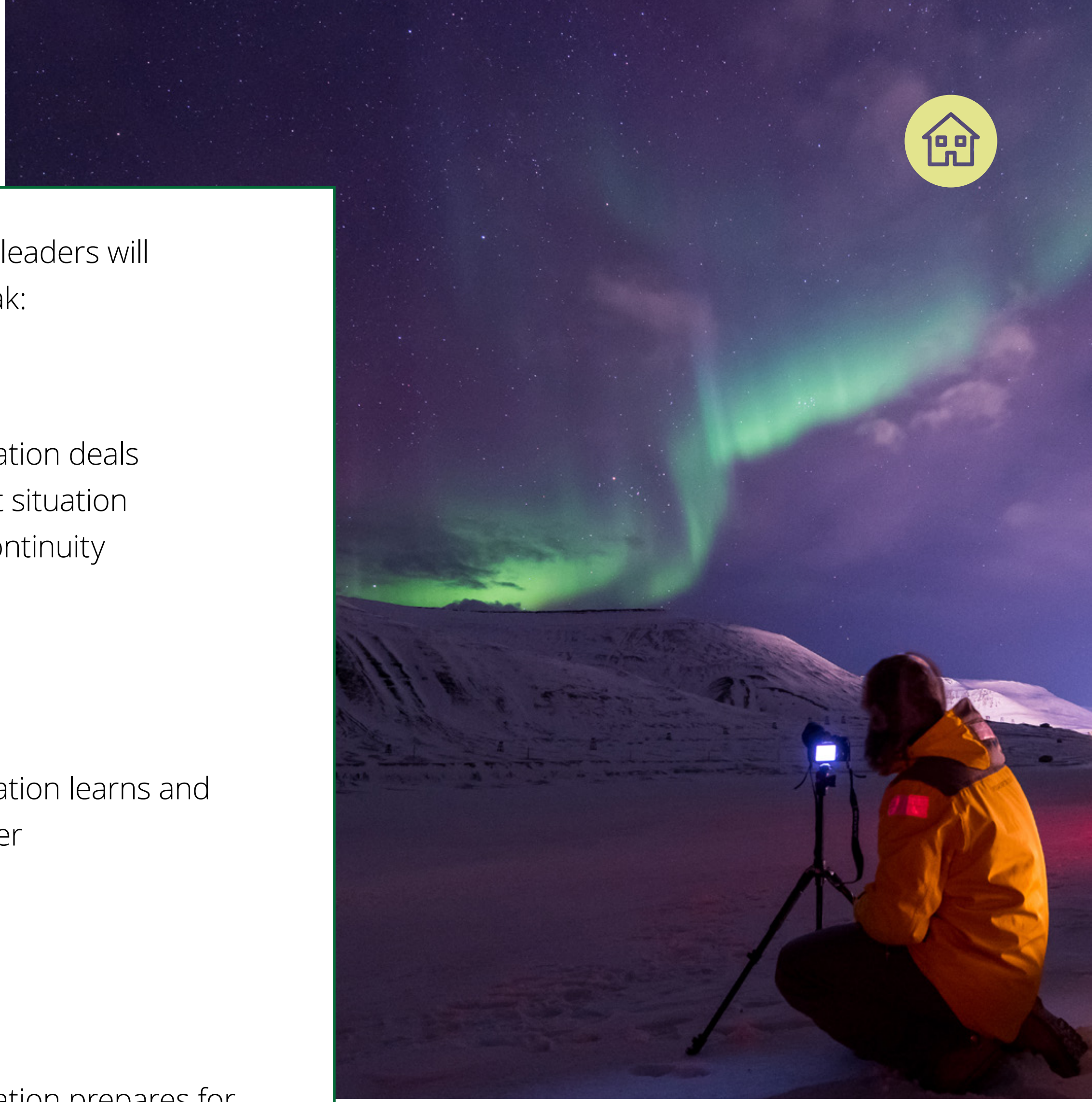
Respond
How an organisation deals with the present situation and manages continuity



Recover
How an organisation learns and emerges stronger



Thrive
How an organisation prepares for and shapes the 'new normal'



1. "COVID-19 causes devastating losses in working hours and employment,"International Labor Organization, April 7, 2020

Many organisations are planning for multiple scenarios[2] and time horizons as they shift from crisis response to recovery. Many are also planning for the possibility of multiple waves of the pandemic and its continuing global – uneven – footprint. As a result, we expect it will be a gradual transition from the respond phase to a new reality. Organisations must prepare for different outcomes of the pandemic – mild, harsh, or severe – and recognise that the recovery should be adaptable to different situations within different countries and industries worldwide.

To do so, it helps to think of this recovery process as a spectrum of options. Some organisations are hiring or expanding and others contracting. Some may bring more employees back to the workplace while others are still working remotely, perhaps permanently. Other organisations, especially those that expanded during the crisis, may reduce their workforce or adapt to new environments. Leaders should ask how they will integrate additional workers in the future, what services might be added or changed as a result, and what other operations may be maintained in a remote capacity.

The answers to these types of questions will help organisations redefine their workforces and set the direction to thrive in the aftermath of the pandemic. It is not essential that leaders have a detailed blueprint of the new working landscape at this stage, but they should start to actively envision it and work toward it. In sharing our insights on how to approach workforce recovery strategies, business leaders should begin with a sense of priorities and direction for their future. As we detail in our global report on **Human Capital Trends in 2020 (see figure 1)**, the future of any organisation's DNA, and critical guideposts for workforce recovery, should include its direction on organisational.

Purpose–integrating the well-being and contributions of individuals in the organisation's mission and work,

Potential–for what can be achieved by individuals and teams, and

Perspective–with a focus on moving boldly into the future.

2. Recovering from COVID-19: Economic cases for resilient leaders 18-24 months," Deloitte April 10, 2020

The recovery process adopted by each organisation will serve as a bridge between the response – how it dealt with the immediate demands of the crisis – and what its future will look like – the new normal.

It's not simply a return to old ways of doing business. The pandemic has created an imperative and an opportunity for organisations to re-engage with the workforce and reinvent their workplaces.

The biggest challenge organisations will likely face in recovery is the tension between preparing for a return to previous activities and routines – getting back to work – while also embracing a new reality – rethinking work. While many workforces have demonstrated resiliency in the face of crisis, it is important to remember that transformative change can be difficult and unsettling for many workers. While some may prefer working from home, others may be uncomfortable or unproductive outside of traditional work settings. How leaders accommodate and balance these divergent expectations will help define the future of trust in their organisation. Despite the uncertainty, one thing remains clear: customers, workers, suppliers, and other partners are watching. How organisations handle the recovery may define their brands with both their workforce and their customers, establish their reputations for years to come, determine their future competitiveness, and ultimately define whether they are truly operating as a social enterprise.

The biggest challenge organisations will likely face in recovery is the tension between preparing for a return to previous activities and routines - getting back to work – while also embracing a new reality – rethinking work.

The social enterprise

The social enterprise, as defined in our 2018 Global Human Capital Trends Report, clarified and expanded on the 'new social contract', proposing a more human-centred rewiring of the relationships between the individual and organisation and the organisation and society, with a goal of providing stability in a world that was quickly changing. Becoming a social enterprise was about much more than corporate social responsibility. It was about shifting the ways organisations worked to balance the concerns of the organisation with those of the broader ecosystem.[3]

In the context of the rise, and now acceleration, of the social enterprise and the short-term challenges in leading workforce strategies in the recovery, we believe planning and executing for the recovery should be done with a focus on the future direction. Having clear priorities can guide the organisation through the recovery and to the next phase: thrive. Our 2020 Global Human Capital Trends report – The Social Enterprise at Work[4] – offers organisational leaders a sustainable path for their workforce and organisational DNA for the future by embedding three attributes into the organisation's core:

Purpose, potential, and perspective

- Organisations that embrace **purpose** embed well-being and meaning into every aspect of work every day, optimising the power of individuals by harnessing workers' complementary strengths in the service of a common goal
- Organisations that embrace **potential** are designed and organised to maximise what humans are capable of thinking, creating, and doing in a world of machines, increasing their people's potential for long-term success in work
- Organisations that embrace **perspective** view uncertainty as offering possibilities rather than threats, positioning themselves to take decisive action to shape an unknown future.

By embracing these attributes, organisations will have the power to put the social enterprise to work in 2020 – guiding the direction of the workforce recovery and shaping the years ahead.

3. The Rise of the Social Enterprise, 2018 Deloitte Global Human Capital Trends," Deloitte Insights, April 3, 2018
4. "The social enterprise at work: Paradox as a path forward, 2020 Deloitte Global Human Capital Trends," Deloitte Insights

We believe workforce-related strategies in the recovery are best orchestrated through five critical actions:

Reflect, Recommit, Re-engage, Rethink, and Reboot. These actions can help organisations bridge the crisis response to the new normal by laying the foundation to thrive in the aftermath of the crisis.

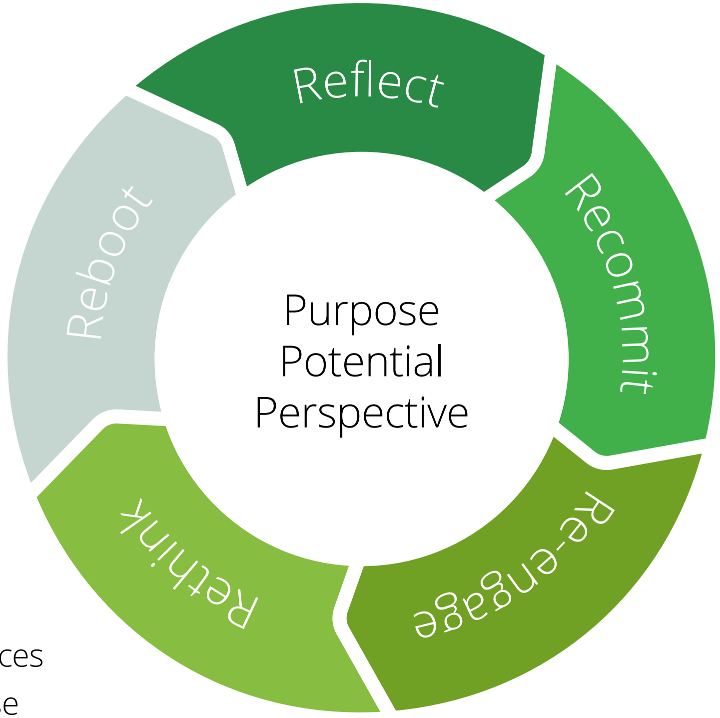
Reflect
on what has worked, what has been learned, and what has been missed in the response – bringing in different perspectives and voices.

Recommit
to workforce wellbeing and purpose through a focus on physical, psychological and financial concerns – at home and in the workplace.

Re-engage
and redeploy the workforce to maximise their contribution and potential for rapidly evolving organisational priorities.

Rethink work, workforces, and workplaces
to leverage the experiences of the COVID-19 response and the opportunity to accelerate the future of work.

Reboot – HR and People Operations Priorities
and realign the HR function and people operations with the most pressing business and workforce priorities and pivoting towards exponential HR.



Recommitment to the workforce involves a focus on purpose integrating employees' needs for individuality and belonging and the value of connecting well-being, contribution, and work.

01 Reflect

Create the time to reflect. A key difference between crisis response – which is largely about reaction – and recovery, is making the time, and taking the time, to reflect on what's next. In fact, reflection may be the most important first step and ongoing action in the recovery process. This starts with reflecting on what has worked, what has been learned, and what has been missed in the response. Reflection also involves making the time to bring in different perspectives, voices, and leaders at different levels as inputs to charting what comes next. Recovery for workforce strategies, given the severity, intensity, and impact on workers and businesses, requires action informed by continuous reflection. As most parts of the recovery process, it will not be easy, and will require deliberate action from leaders to make the time for this to happen.

02 Recommit

As organisations begin the recovery process, they should reinforce their commitment to well-being and purpose through a focus on physical, psychological, and financial concerns. Physical well-being will include an emphasis on health and safety, the cleanliness of workplaces, and the availability of testing and treatment. Psychological well-being will include workplace practices such as flexible schedules that address workers' mental and emotional health. Leaders should recognise the diversity of workers' individual expectations and support them through the crisis and the transition to recovery. The commitment to well-being should extend to well-being at home – as workers continue to take care of children and elderly family members. Employees are looking for meaning in their work: meaning for their organisations and its customers, meaning for them as individuals and their careers, and meaning for their communities. Recommitment to the workforce involves a focus on purpose integrating employees' needs for individuality and belonging and the value of connecting well-being, contribution, and work.

Organisations should communicate directly with individuals and teams in a timely manner to outline organisational missions and priorities and to connect business goals and outcomes. The workforce must feel connected to the mission. As part of this effort, organisations should assess, update, and implement essential policies and practices that promote the well-being of both their on-site and off-site workforce. Organisations must recognise that performance likely takes on new meaning in the post-COVID workplace. Health and productivity combine to help ensure workers thrive rather than simply deliver on objectives. Leaders should ask themselves how they will provide support for their workforces and ensure workers feel connected and engaged with the redefined priorities and strategy of the organisation.

03 Re-engage

The recovery process creates opportunities for organisations to redeploy their workforces and maximise their contribution and potential. While some employees will return onsite, others may continue to work remotely. Some will engage in hybrid activity in which they work remotely much of the time yet come together with team members for specific functions. Organisations should prepare workers with the skills and capabilities for the return. This includes providing them with the infrastructure and technology, such as bandwidth and tools for virtual work, as well as the critical knowledge resources and digital access they need to meet both immediate and future work requirements. Re-engaging and re-deploying the workforce will involve both assigning and creating meaningful and impactful opportunities for workers but also engaging workers and teams to apply their potential and capabilities. As we have broadly witnessed in crisis response, we are all – as individuals, teams, and organisations – capable of much more than we have been traditionally asked to do.

Teams will play an increasingly important role and should be designed and configured for shifting business priorities and outcomes. Given the ongoing challenges many workers will have with family and personal concerns in the recovery, team assignments should balance worker preferences for scheduling and flexibility with critical business needs. Team leaders will be critical to the short-term success of re-engaging the workforce and driving business results. Reinforcing the role of teams and team leaders, and redeploying workers to new teams and new roles will help foster a sense of agility and, ultimately, lasting resiliency.

Leaders should provide teams, managers, and workers with clear direction on changes in work priorities and in routines, including new technologies and digital ways of working. This is a critical point for re-engaging and redeploying the workforce: the recovery will require a shift in focus to new work priorities and new work routines, such as new schedules, combinations of onsite and virtual work, and new team assignments. How organisations prepare and support their workforces for these new routines, priorities, roles, and assignments will likely be a key driver of workforce performance.

04 Rethink work, workforces, and workplaces

"The coronavirus, and its economic and social fallout, is a time machine to the future. Changes that many of us predicted would happen over decades are instead taking place in the span of weeks.[5]"

This is how Anne-Marie Slaughter, President of the New America Foundation, summarised the COVID-19 moment. This is especially true of the future of work. We have seen rapid shifts to virtual and remote work and education, new levels of partnerships within and across ecosystems, and unprecedented levels of flexibility, teaming, and adaptability.

As they start to look toward the new realities of the post-pandemic world, organisations can use their new work priorities to rethink and reconfigure their workforces and balance ongoing and evolving business needs. It's important that organisations communicate how and why they are redeploying workers. They must identify their new business priorities – highlighting where returning to earlier work priorities is appropriate and where new work is required. This includes providing context and direction for the rationale behind the new priorities, the new workplace realities among onsite and online work, and the fairness of workforce policies. Rethinking work, workforces, and workplaces involves a shift in perspective – challenging leaders to be bold in the face of uncertainty. Perspective that will be even more important as we push forward in the workforce recovery.

During the initial phase of crisis response, some organisations began to review where digital technologies, automation, and AI could make work safer, faster, better, and more innovative. This will likely need to continue as organisations re-engage and rethink their work, workforce, and workplace priorities and opportunities.

How will the organisation perform with a more dispersed workforce? Workers who do return to offices will likely expect the working environments are safe, and that organisations are taking appropriate steps to protect them. It's also important to note that some countries and

Anne-Marie Slaughter, "Forget the Trump administration. America will save America," New York Times, March 21, 2020 cultures may be less attuned to remote work. In some countries, for example, remote work may require changes in worker education, performance management, organisational structures, and cultural beliefs or stigmas around not being in the office.

Rethinking work also means rethinking the workforce – composition, and compensation and performance management. Changing workforce composition creates the opportunity for wholesale reinvention. Over the past several years, organisations of all sizes increasingly have embraced the alternative workforce – off-balance-sheet workers such as contractors, freelancers, gig, and crowd workers.

The new workforce is often broadly distributed across employment models, which can pose a number of questions for leaders during the next 12 to 24 months:

- What will be the **composition** and size of the workforce requirements?
- What **skills** are needed? Are they needed onsiteor can they be accessed online or in a hybrid work environment?
- Which employees come back to work when?
- How do leaders instill **trust** in the new employer employee relationship – in onsite, online, and hybrid workplaces?
- How will they ensure employees can be **confident** about their own safety?
- If more work will be done remotely, what **support** will the organisation provide?
- How can alternative workers add **flexible** capacity to the organsation?
- Is the organisation **prepared** for the increased cyber risk that comes with a dispersed and remote workforce?
- What messages and commitments can the organisation make about compensation, job security, performance management, and promotions in the next few years?

Organisations will likely need to reconsider their workplaces as well, redesigning them around the best impulses that are in play right now in response to the crisis, including provisions for sanitation, distancing, and psychological safety. Many workplaces today are structured around rigid routines and structures – top-down, command-and-control structures, with standardised shifts and hours. As organisations shift from crisis response to recovery, we expect leaders will be more willing to take risks. This gives them an opportunity to adopt new talent practices such as non-linear career progressions – careers built around a portfolio of assignments – and opportunity and work experience marketplaces.

As a part of this process, leaders should also re-assess and explain compensation, reward programmes, and promotion plans for the short-term – the next year or two – while managing expectations through the recovery process and toward sustainable operations. Workers are looking for job and financial security and direction around career opportunity and growth.

The perspective during recovery can range from the global ("How will we serve our clients and communities and deliver on our mission?") to the mundane ("Will we ever wear suits again?"). This reassessment may also include a re-evaluation of business processes such as the flexibility needed to ensure deliveries in the next crisis and whether supply chains will run through global networks or be moved closer to home.

A critical goal is to use the recovery to pivot towards a more resilient workforce. This will involve fostering a new, dynamic environment that moves with a clear focus on mission, connecting the contributions and well-being of workers with the organisation's purpose: greater speed, more adaptability, a heightened team focus, and new priorities. These are key ingredients in the resilient workforce. Organisations should find ways to capture the energy and the rhythm of the recovery, setting a new pace, maintaining it, and instilling it at all levels.

The COVID-19 crisis can drive fundamental change and opportunity. It creates a chance to rebuild, but also to reposition the organisation for the future.

- How can it better incorporate and leverage digital technologies, automation, and AI?
- How can it address the benefits and the risks of a dispersed workforce?
- What tools can it adopt for virtual work and for adapting to the new practices and ways of work that will make teams and workplaces more effective in the future?
- How does the organisation capture and scale the productivity that can come with new ways of working specifically, new combinations of virtual and onsite work?

05 Reboot – HR and People Operations Priorities

This part of the recovery process pertains directly to realigning the HR function and people operations with the most pressing business and workforce priorities. The recovery process may not succeed if the HR function does not embrace a redefined role, one that anticipates and orchestrates the organisation's new priorities. HR leaders are uniquely positioned to prepare, support, and leverage their workforce through the recovery and position the organisation for a new era of resiliency and sustainability. But for many this requires a pivot towards exponential HR[6] – designed for speed, new ways of working, digital first, teams, adaptable organisational strategies, and changing business requirements.

At many organisations, HR teams, policies, and employee reward programmes are not prepared for the realities of the recovery. HR leaders should reassess, in a timely manner, total rewards and HR programmes. The HR function will need to focus its expertise on critical compensation, performance management, and promotion realities specific to the recovery period. HR leaders should ensure they have a thorough understanding and timely access to expertise on the complex legal labour requirements and changes in tax rules around the world, as well as the dizzying array of government programmes and subsidies.

HR may consider making people decisions locally rather than from the centre to support a new workplace that revolves around distributed leadership, power, and teams. Other priorities may include agile learning, in which people are quickly taught to use new tools in response to an unexpected change, such as the widespread adoption of video conferencing technology during the COVID-19 outbreak.

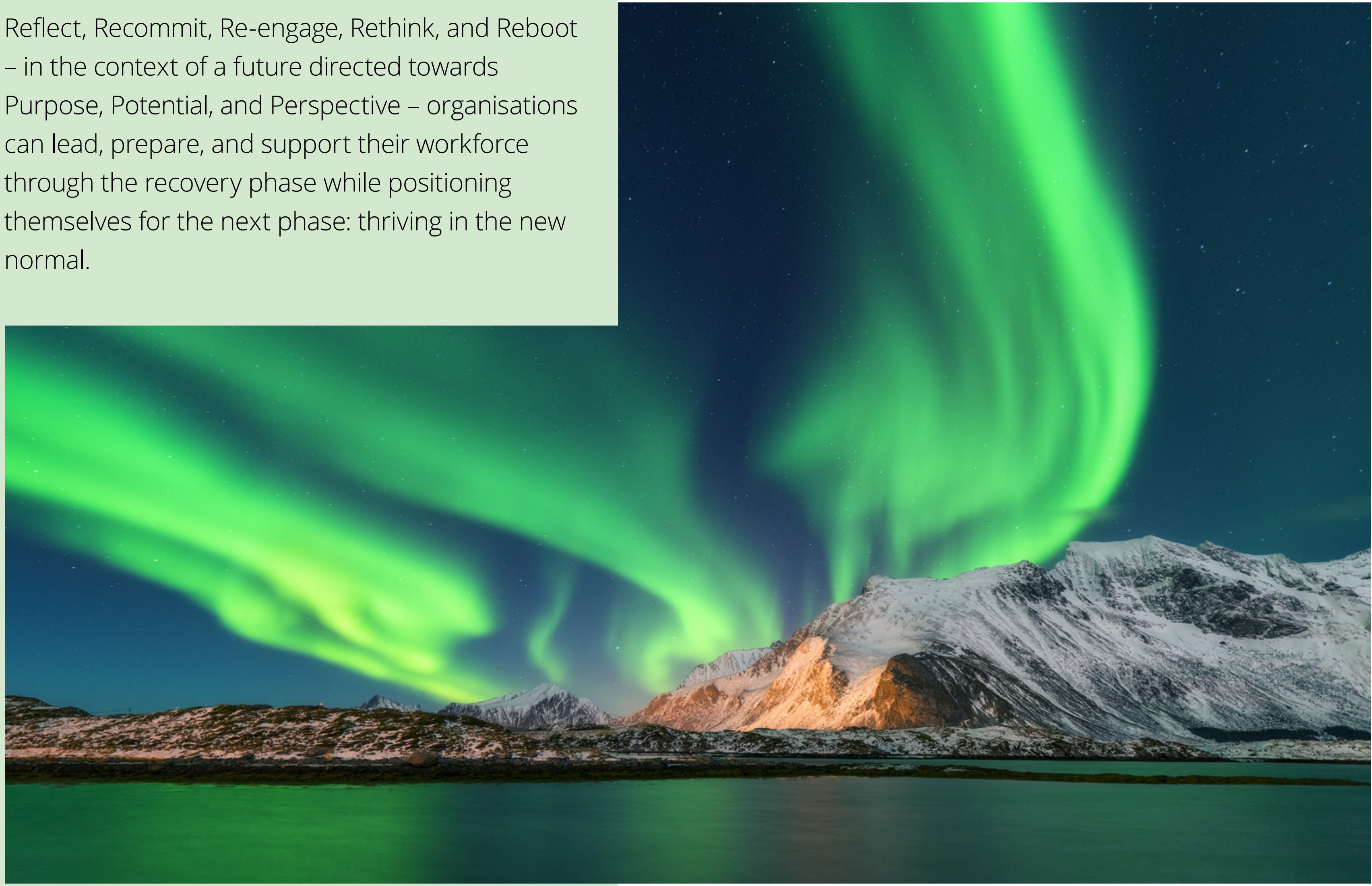
In the workplace of the future, HR can become the voice making bold decisions in the face of uncertainty. It can help integrate the workforce's need for individuality and belonging, and the business' need for security and reinvention. The choices and policies adopted during the recovery are an opportunity to make this shift towards purpose, potential, and perspective. The choices HR makes today will likely define its impact in the recovery and its role in the future. When employees and the broader workforce look back at this crisis and its aftermath, they should see that HR took a forward-looking perspective in its response while balancing critical short-term workforce and business needs and the opportunity to pivot to the future.

5. "Exponential HR," Deloitte Insights, April 12, 2020

Conclusion

The recovery from COVID-19 pandemic, given the human dimension of urgent workforce challenges and the uncertainties facing business leaders, requires workforce strategies which focus on both short-term recovery priority actions – Reflect, Recommit, Re-engage, Rethink and Reboot – and reaching for the future and new normal – integrating the attributes of Purpose, Potential, and Perspective.

These short-term actions – and long-term vision – present organisations with an opportunity to rapidly assess and evaluate their earlier workforce strategies and response priorities and to reposition themselves to thrive in the new realities to come. Organisations may be tempted to dismiss the need for change or imagine recovery as a return to the recent past. It is not. Organisations that return to their old ways of working may find their competitors have taken advantage of the recovery to re-imagine their workforce and business, positioning themselves to thrive in the future. By anticipating and orchestrating these five priorities – Reflect, Recommit, Re-engage, Rethink, and Reboot – in the context of a future directed towards Purpose, Potential, and Perspective – organisations can lead, prepare, and support their workforce through the recovery phase while positioning themselves for the next phase: thriving in the new normal.



From recover to thrive

New ways of working

As organisations begin the recovery process, they are thinking more strategically about essential versus non-essential personnel, processes, and policies. For example, they are deciding what work can be done remotely on an ongoing basis and what needs to return onsite when the crisis ends.

Of course, not all recoveries look the same to all organisations. Some are assessing how they can rehire or bring back furloughed workers, while others, such as delivery focused organisations, have increased staff during the crisis and now must decide what their future workforce needs will be.

Other organisations are reviewing policies for gig workers and determining how they will embrace flex work schedules. Some organisations have gone a step further, helping their displaced workers find new jobs and gigs with other organisations during the lockdowns in hopes of rehiring many of them when the crisis abates.

Some organisations, of course, are still managing the current crisis, trying to make it through the next week, while others are already looking long-term. They are assessing their virtual strategies and supply chains and evaluating how they can use automation to improve operations in the future.

Many organisations are looking to automation and AI to take over more routine tasks, allowing workers to focus on higher-level work. Others are making decisions about how much support to provide remote workers. For example, more than one investment banking firm provided its traders with dual computer screens and other equipment at home so they could switch to remote work without missing a beat.[7]

Real estate planning is also under scrutiny. Organisations are asking themselves how much office space they will need if more work is remote, and how much more workspace will be required per onsite employee because of social distancing measures. Still others are considering how to accommodate teams that may want to meet intermittently but can mostly work remotely. In addition, across organisations, the crisis is teaching teams how to make decisions more quickly and collaboratively on a global scale.

And some organisations are confronting far more sweeping changes. Oil and gas organisations are facing weak commodity prices and declining demand for their products as fewer people drive and fly during lockdowns and stay-at-home orders. Even as the industry faces challenges, growing concerns about climate change and carbon-reduction policies mean some industry executives, are considering shifting more of their organisations' asset portfolios to alternative sources. In such scenarios, recovery isn't just about new ways of working, but potentially significant workforce changes to support new business strategies.

6. Matt Phillips, Emily Flitter, Kate Kelly, "Working From Home Feeds Market's Woes in Little Ways That Add Up," New York Times, April 12 2020

Managing cybersecurity in the workforce recovery process

The response and recovery from the COVID-19 crisis is creating risks at the intersection of the workforce and cybersecurity. Remote work is creating new threat exposures. The expanding number of remote devices creates new vulnerability to corporate networks. Cyber adversaries could view the shift to working at home and the increase in remote work as a major opportunity to take advantage of weak cyber controls and practices. Leaders need to be aware of these risks and consider them as they set the new workforce agenda. Executives should get regular cyber threat reports including those specific to remote work and the broader workforce.

Workers must be trained to recognise these threats and realise that not all of them are external. Shifts in the workforce – furloughs, new hires, gig workers – all can pose cybersecurity risks. If not already in place, management should consider reviewing and investing in programmes, policies, infrastructure, and training to protect against the exposure or release of data.

In this crisis, many leaders were unprepared for attacks or distracted by their response to the pandemic. As the amount of virtual and remote work increases, and cyber risk along with it, organisations may need to hire additional cyber talent.

To combat these potential threats, organisations should use the recovery process to design more secure systems and processes. They should develop plans for both responding to and recovering from the next crisis or cyberattack. These programmes should be built around three principles:

- Confidentiality
- Integrity
- Availability

As the amount of virtual and remote work increases, and cyber risk along with it, organisations should train and educate managers and workers to be aware of how to proactively prepare for and respond to cyber security concerns, hire and access the additional cyber talent they need, and invest in the cyber tools necessary to protect workers – at home and onsite – customers and the organisation.

Read more about cyber threats related to remote workforce and how to manage cyber security in **Deloitte's executive cyber briefing**.

Read more about
Future of work post COVID

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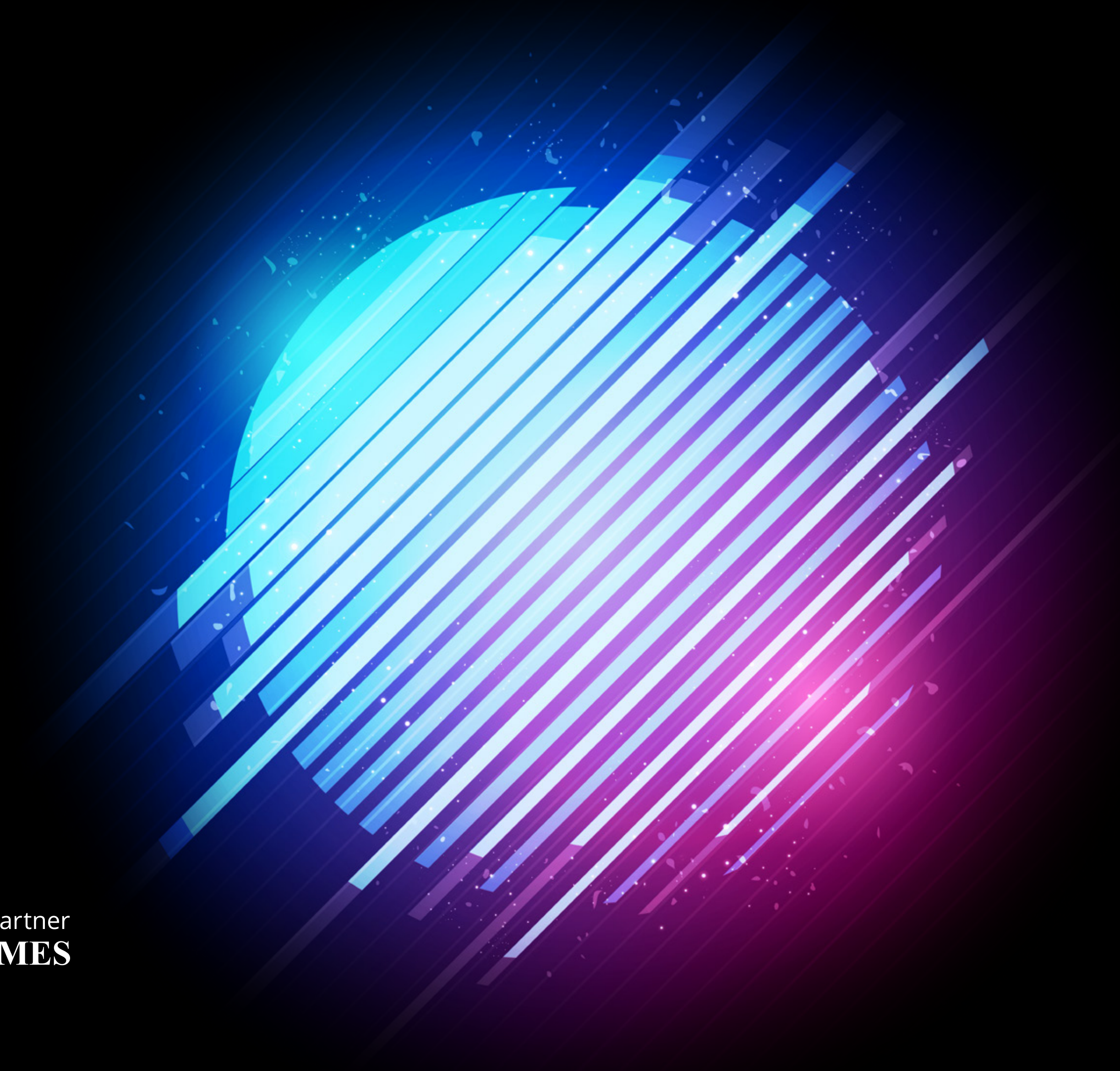

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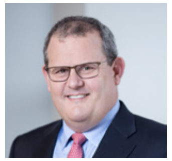

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