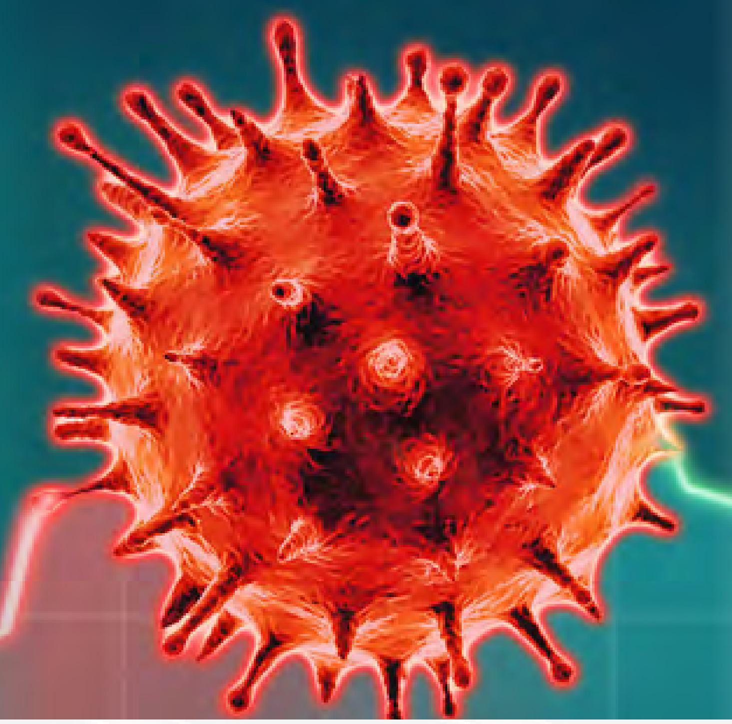


COVID-19: A Business Impact Series

Transitioning to a Post Twin Shocks World: Strategic Decisions

Issue 5 | 27 April 2020

Suddenly, we are living in a time of radical uncertainty. Nobody has a clear line of sight into the impact of the COVID-19 on the global economies. We are consumed with keeping our people, families and communities safe. Yet CEOs cannot wait to plan and act. They do not have a clue as to when the COVID-19 emergency will end or have a fix on the likely severity of the looming global recession. This is a moment no CEO expected. The global pandemic and the deepening economic impacts are developments of historic proportions, yet without clear historic precedence. Leaders will need courage and imagination in the coming months to forge ahead in their businesses.

Overview

The future favours those who act. While the Twin Shocks (COVID-19 pandemic and Oil price shock) are unprecedented, there are proven approaches from previous recessions that apply, we know that companies that remain inwardly focused and defensive are the least likely to survive or get back to where they were before COVID-19.

We are in uncharted territory. The speed and depth of this economic contraction is unique. One of the biggest questions among our clients now is how this will alter patterns of demand after the emergency has passed and how relationships with customers will change.

It is essential to build a robust response amid uncertainty. We believe that as companies plan for the post-COVID-19 world, the two most important factors shaping strategic options will be access to liquidity and the “inertia” or stickiness of their customers. Strong customer relationships will be critical.

What scenarios should CEOs be planning for post Twin Shocks World, when COVID-19 is under control and there is stability in the Oil market?

The scenarios should be a V-shaped, U-shaped or L-shaped recovery. A V-shaped recovery is a scenario where you have a steep drop in GDP followed by an almost equally rapid rebound. A U-shaped recovery is a shallower longer lasting downturn with delayed recovery. The L-shaped recovery is the worst scenario with a sharp drop in GDP followed by years of minimal growth. An L-shaped recession is typically the result of a credit crisis.

Uncertainty about the path of the economy is not going to go away anytime soon. Even so, companies can start planning for gradual transitioning into the “new reality.” The COVID-19 crisis is already accelerating certain trends that were already underway, such as the shift from bricks-and-mortar retail to e-commerce. It is also likely to accelerate changes in ways of working that are being adopted now and may continue after the COVID-19 emergency has passed.

For example, teleworking and reduced travel for face-to-face meetings may become new norms. This has implications for technology and communications providers as well as public transit, airline travel, and aerospace. Consumers, meanwhile, might permanently adopt behaviours such as ordering groceries and meals online and avoiding trips to the mall. Across consumer and B2B markets, we expect that digital customer connections will become even more important.

See the following KPMG Thought Leaderships on Impact of COVID-19:
https://bit.ly/2ztQnoE

Developing a robust and winning response to the downturn

The range of choices companies have to rewrite their futures during a downturn depends a good deal on their starting positions. But we believe that companies that start developing plans for improving profitability, gaining shares, and entering new markets no matter where they start will come out ahead. We recommend that companies should assess their starting position and immediately build financial resilience by rethinking and improving access to capital. Afterwards, companies should implement a three-pronged strategic action plan: stabilise the business, build resilience and adapt to the new reality. The following segment of the newsletter discusses the details of our recommendations.

1. Assess your starting position

The framework below (Exhibit 1) shows how companies are positioned on two critical dimensions: access to capital and customer inertia, which is the degree to which customers will tend to continue to buy products or services from a company. When companies have low customer inertia a central theme of our analysis because we believe that one of the great strategic challenges will be understanding how customer behavior will change in the wake of COVID-19 and the recession. That understanding will build the customer inertia that not only allows the company to keep selling existing goods and services, but also gives it "permission" to move into new markets or lines of business.

Exhibit 1: Start-up position matrix

Access to capital (Low – High)

Leverage Capital
Position to improve customer inertia
Strategic Questions:
- What new products / services can I offer to improve my customer relevancy?
- Is an organic or inorganic strategy better given our strong cash position and competitive dynamics
- How do we leverage digital and e-commerce?
- What changes do I need to make to my supply-chain?

Seize Opportunities
To expand advantage through capital deployment and customer fulfillment
Strategic Questions:
- How do I use this downturn to protect and expand my customer relationships?
- What additional spaces / geographies can I move into?
- Can I move into them or do I need to buy into them?
- What is the right balance approach to use given all the uncertainties in the market
- What is the right balance between performance improvement and investment, given the uncertainties in the market?

Create Optionality
Given capital and customer constraints
Strategic Questions:
- What business units should I sell for cash? Should we consider selling the entire company?
- How deeply can we cut costs without limiting future choices? What happens if we don't make cuts?
- Which customers do I need to focus on? Can I drop unprofitable customers or charge them more?
- Which states and locations in Nigeria should I focus on?
- How can i access/leverage the Central Bank of Nigeria (CBN) intervention funds?

Optimizers
Optimise the business without hurting or risking customer relationships
Strategic Questions:
- Should I sell non-essential assets?
- Which functions can I target for cost improvements with minimal risk to customers?
- Is my CAPEX plan aligned to the new reality?

Customer inertia (Low – High)

Source: KPMG Economics, BEA, Macroeconomic Advisors by IHS Markit, Haver Analytics

2. Moving up (improving access to capital)

Access to capital is critical now, to fund operations when the COVID-19 lockdown has choked off income (see "Stabilize" below), but it is also essential for rebuilding growth strategy during recession. The ways to improve access to capital are well known:

- Pursue performance improvement, starting with projects that are less capital intensive and can improve free cash flow quickly.
- Free up working capital by tightly managing expenses.
- Divest non-core assets.
- Rethink large capital programs.
- Use this as an opportunity to adjust pricing and service levels.
- Access Central Bank of Nigeria (CBN) funding opportunities.
- Refinance debt.
- Access tax and other government incentives.

3. Action plan: Stabilize, build resilience, prepare for a "new reality"

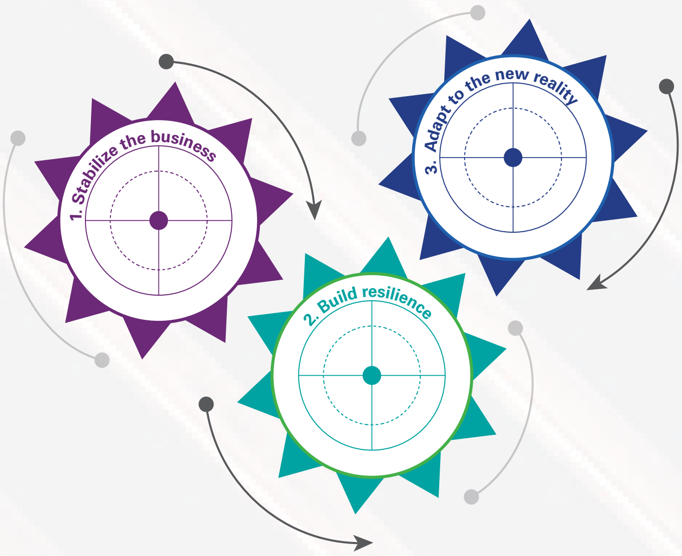
In the coming months, companies will make difficult decisions about how to cut costs and continue to operate. Companies that want to exit the recession in fighting shape will make these decisions with an eye to the future–taking strategic cuts rather than across-the-board reductions, maintaining investments in R&D, streamlining and automating processes. To prepare for new post Twin Shocks market realities, they will also frame these decisions around building capital and improving customer inertia.

A robust response involves three linked steps: stabilizing the business, building the resilience to manage through recession and developing strategies for a new post Twin Shocks reality (Exhibit 2). The overall effort should start with transparency about the company's financial and operational performance. Use data analytics to truly understand sources of value and value leaks– and back up the analysis with insights from managers on the front lines. In this environment, the pace of decision making also must accelerate. Eliminate layers of decision making and use simulation tools to test decisions. The COVID-19 response teams/committees that companies have set up can be a model for the agile decision making that can help throughout the recession–and beyond.

Stabilize the business

The most important priority is getting a handle on liquidity. Beyond securing the cash needed to continue operations, companies that have good liquidity now will have more choices as the downturn continues. Companies should carry out thorough and rapid diagnostics to understand their cash positions and make plans to preserve liquidity. They should be tapping lines of credit and revolving loan facilities. Some companies are cutting dividends to preserve cash. Others are creating cost "control towers" committees made up of top executives who meet weekly to review all spending and spending policies.

Exhibit 2. Three coordinated steps in a robust response to recession



1 Stabilize the business	2 Build resilience	3 Adapt to the new reality
Immediate actions that preserve cash, give confidence to customers and employees and ensure business continuity. Must be revisited throughout the disruption.	Performance Improvement actions to make it through the disruption and maximize options in the face of uncertainty.	Actions resulting from the development and evaluation of scenarios that lead to the business model the company will need in the new reality.

Source: KPMG Economics, BEA, Macroeconomic Advisors by IHS Markit, Haver Analytics

Build resilience

Inevitably companies will have to bring costs in line with recession market conditions. This is a good time to address performance-improvement issues, to make processes as efficient as possible, reduce waste, and drive revenue. Headcount, of course, will be a consideration. While the COVID-19 lockdown is in effect, there may be access to government support (to companies and employees), many companies will still need to trim headcount permanently after the COVID-19 crisis passes. Right-sizing for recession should be done in ways that allow the company to retain and develop critical talent and capabilities. Companies will need more creativity, more agility, better teamwork, not less. Creative approaches to talent–redefining roles, job-sharing, flexible work arrangements–can help companies remain whole and do a better job for customers. Firms that that cut too soon or too deeply will have a harder time growing during recession and afterwards. Some companies will want to consider sales of non-core assets as part of their recovery strategies. Divestitures can help sharpen strategic focus and provide money to sustain and strengthen the core.

Adapt to a "new reality"

Using scenario planning, companies can build a picture of the post-recession environment. These scenarios should take into account the trends that can already be seen, such as changes in workstyles, as well as changes in the global business environment. In general, companies may want to double-down on initiatives that improve digital connections to customers (in B2B and consumer markets). Where possible, companies may want to start thinking about acquisitions that would help them move into adjacent markets or new lines of business.

Finally, companies should strategise about what it will take to make their companies more resilient to future shocks, such as natural disasters and future disease outbreaks. Such threats will be part of the future landscape, too.

Economic and Regulatory Updates

Additional Palliative Fiscal Measures in Response to the COVID-19 Pandemic

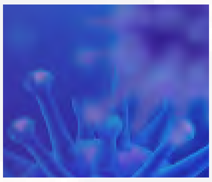
The Federal Inland Revenue Service (FIRS) has announced the following additional measures to further manage the impact of the Coronavirus disease (COVID-19) on taxpayers:

- Waiver of late returns penalty for taxpayers who pay their tax liabilities early but submit their tax returns later. Evidence of tax payment can be forwarded to the relevant FIRS e-mail address, or submitted later to the appropriate tax office.
- Extension of timeline for remittance of VAT from the 21st day to the last day of the month, following the month of deduction.
- Taxpayers facing challenges in sourcing foreign exchange (FOREX) to settle tax liabilities on their FOREX-denominated transactions are permitted to pay the Naira equivalent, based on the prevailing Investors & Exporters FOREX window rate on the day of payment.
- Extension of personal income tax (PIT) returns filing deadline for personnel of Foreign Affairs, Military and Police, and non-resident persons by three months from 31 March 2010 to 30 June 2020.
- Indefinite suspension of all field tax audit, investigation and monitoring visits.
- FRC issues fresh guidelines on financial reporting. The Financial Reporting Council of Nigeria has released guidelines on the impact of COVID-19 on financial reporting. The FRC said on its website that this was the second set of guidelines to be released by the council in two weeks. While the first guidelines targeted auditors of financial statements in Nigeria, it stated that the latest targeted preparers of financial statements during the COVID-19 period.
- Nigeria's March inflation accelerates to 12.26%. Inflation accelerated to almost a two-year high to 12.26 percent in March, some 0.06 percent points higher than the 12.20 percent reported in February 2020. Both food and core inflation moved up – but the National Bureau of Statistics (NBS) which released the figures Tuesday morning clearly ruled out possible impact from covid-19 lockdown on the inflation numbers.

Our Latest Publications

Impact of Covid-19 on the Nigerian Consumer and Industrial Markets

The COVID-19 pandemic brings unprecedented challenges. Demand for many goods and services has fallen dramatically, whilst some manufacturers either have shortages or are overwhelmed. For more details, follow this link: https://bit.ly/2W5EpZU



COVID-19 and Employee Rewards

COVID-19 is not only a pandemic with widespread impact, it is changing the way we view and approach different aspects of our lives, businesses and economic order. For more details, follow this link: https://bit.ly/3cMj0Ma

Navigating the Pandemic: A Board Lens

Navigating the uncertainty of a pandemic crisis requires organisations to focus on people, cashflow and operations.For more details, follow this link: https://bit.ly/3aK1kPO

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