The future is not what it used to be: Thoughts on the shape of the next normal By Kevin Sneader and Shubham Singhal

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The future is not what it used to be: Thoughts on the shape of the next normal

The coronavirus crisis is a world-changing event. Here are seven elements for business leaders to consider as they plan for the next normal.
Dealing with the coronavirus crisis and its aftermath could be the imperative of our times. Indeed, we have argued that it augurs the "imminent restructuring of the global economic order." As Ian Davis, one of our previous managing partners, wrote in 2009 in the midst of the global financial crisis:

"For some organizations, near-term survival is the only agenda item. Others are peering through the fog of uncertainty, thinking about how to position themselves once the crisis has passed and things return to normal. The question is, 'What will normal look like?' While no one can say how long the crisis will last, what we find on the other side will not look like the normal of recent years."

It is impossible to know what will happen. But it is possible to consider the lessons of the past, both distant and recent, and on that basis, to think constructively about the future. We believe the following elements will be important in the shaping of the next normal—and that business leaders will need to come to terms with them.

1. Distance is back

In the mid-1990s, the idea of the "death of distance" gained currency. The thinking was that new web-based and telecom technologies had made it possible to communicate and work in new ways that dramatically reduced the value of physical proximity. As the flow of information became cheap and seamless, global supply chains of bewildering complexity were able to deliver just-in-time products as a matter of routine. Cross-border trade reached new peaks. And the world's burgeoning middle class took to travel and tourism with something like abandon.

Even before COVID-19 hit, there were signs of unease, expressed in calls for protectionism and more restrictive immigration and visa policies. In these ways, people sought, in effect, to create more distance from those unlike themselves.

Such attitudes were far from universal, of course. But to deal with the pandemic, governments around the world have imposed restrictions on people and goods of a severity not seen for decades. According to one study, more than three billion people live in countries whose borders are now totally closed to nonresidents; 93 percent live in countries that have imposed new limits on entry, because of the coronavirus. If a modern-day Hannibal wanted to cross the Alps peacefully, his elephants would be turned away. Eventually, the tourists will come back and the borders will reopen, but it is certainly possible that the previous status quo will not return.

Indeed, for businesses, the prospect of more border restrictions; a greater preference for local over global products and services; the need for resilience across supply chains driving a move to bring sourcing closer to end markets (see element 2, "Resilience AND efficiency"); and perhaps renewed resistance to globalization, are all possible second-order consequences of the actions being taken now to cope with the coronavirus. Technology continues to shrink physical distance, but in other ways, it could be set for a return.

2. Resilience AND efficiency

Even when lockdown restrictions begin to ease, businesses will need to figure out how to operate in new ways. In short, resiliency—the ability to absorb a shock, and to come out of it better than the competition—will be the key to survival and long-term prosperity.

Again, the past can be a prelude. McKinsey research on the 2008 financial crisis found that a small group of companies in each sector outperformed their peers. They did get hurt, with revenues falling about the industry average, but they recovered much faster. By 2009, the earnings of the resilient companies had risen 10 percent, while that of the nonresilients had gone down almost 15 percent. What characterized the resilient companies was preparation before the crisis—they typically had stronger balance sheets—and effective action during it—specifically, their ability to cut operating costs.

This advice is still sound—but insufficient. COVID-19 could end up dwarfing the financial crisis in economic damage. In that case, it will not be enough for many companies to tweak their business model; instead, they will need to rethink it.

One implication of this has to do with how supply chains operate; companies are finding themselves vulnerable because they cannot get the parts they need. Supply chains built on just-in-time inventory and distributed component sourcing may well have to be reconsidered, given the way many have been disrupted. Instead, companies will want to build backup and safety plans.

Other key elements of business structure will also be revisited. For example, the *Wall Street Journal* observed that the crisis has revealed weaknesses in succession plans as leaders get sick and deputies quickly need to be found across all aspects of operations. Companies are learning the hard way that succession planning has to go much deeper than the C-suite, and much broader, responding to possible short-term disruptions as well.

Investors are likely to take note, and to devise ways to incorporate resiliency more systematically into their valuations. Indeed, in the wake of recent natural disasters, the impact of climate change was increasingly being recognized by business leaders and investors, with consequent effects on decision making and valuations. This pressure to include environmental, social, and governance factors in valuing a business is likely to expand to incorporate resilience to outside shocks, such as pandemics. In sum, many companies will rebalance their priorities, so that resiliency—in all its manifestations—becomes just as important to their strategic thinking as cost and efficiency.

3. The rise of the contact-free economy

In three areas in particular—digital commerce, telemedicine, and automation—the COVID-19 pandemic could prove to be a decisive turning point.

E-commerce was already meaningfully and visibly eating into the sales of brick-and-mortar stores. What the coronavirus has done is to accelerate a change in shopping habits that was already well established. Early indications from China, for example, are that new customers and markets—specifically individuals aged 36 and over and residents of smaller, less prosperous cities—have begun to shop online in greater numbers. In Europe, 13 percent of consumers said in early April that they were planning to browse online e-tailers for the first time. In Italy alone, e-commerce transactions have risen 81 percent since the end of February.

The figures for telemedicine and virtual health are just as striking. Teladoc Health, the largest US stand-alone telemedicine service, reported a 50 percent increase in service in the week ending March 20, and is adding thousands of doctors to its network. The Federal Communications Commission is spending $200 million to improve connectivity between patients and virtual-healthcare providers, and the US Department of Health and Human Services has increased reimbursements for telemedicine and enabled cross-state provision of virtual care. Sweden's KRY International, one of Europe's biggest telehealth providers, reported that registrations were up more than 200 percent. France and Korea have both changed regulations to ease access to telemedicine. With a vaccine or treatment at least months away, patients and healthcare providers both have reason to expand virtual interactions.

Greater automation was already occurring before COVID-19. In late 2017, the McKinsey Global Institute estimated that 60 percent of all jobs could see more than 30 percent of their key tasks automated, affecting 400 million to 800 million jobs around the world by 2030. According to the Brookings Institution, over the three recessions that have occurred over the past 30 years, the pace of automation increased during each.

In effect, it is becoming possible to imagine a world of business—from the factory floor to the individual consumer—in which human contact is minimized. But not eliminated: for many people, getting back to normal will include popping into stores again, and the roadside kiosks typical of much of the developing world are not about to be replaced by cashless hyperstores. Patients with complex needs will still want to see their doctors in person, and many kinds of jobs are not automatable. But the trends are unmistakable—and probably irreversible.

4. More government intervention in the economy

During times of great crisis, such as World War II, citizens have proved willing to accept—even embrace—greater government control of the economy. Already, there has been economic intervention on a scale that hasn't been seen for decades, if at all. As of April 10, governments across the globe had announced stimulus plans amounting to $10.6 trillion—the equivalent of eight Marshall Plans. Most spending is directed to three areas—supporting citizens' basic needs, preserving jobs, and helping businesses to survive another day.

India is making direct cash transfers to needy citizens, and Indonesia is expanding social-welfare benefits to ten million more households. Britain and France are covering wages (up to 80 percent) of workers affected by COVID-19; Italy is suspending loan and mortgage payments; Brazil is easing labor regulations on companies. And central banks from Australia to Europe to South Africa to Canada are cutting rates.

As governments step up to serve, or save, the private sector, the means they choose will differ. Some countries will outright nationalize, some will take equity stakes, some will provide loans, and others will choose to regulate. If nonperforming loans require a second bailout, the banking sector could become something like a regulated utility in some markets.

A push to redefine the global public health ecosystem to better navigate possible future pandemics and related threats could provide additional impetus for cross-country public-sector intervention. In the same way that reform of financial institutions gained momentum in 2009, the same could be true for public health in the near future.

As McKinsey colleagues wrote in the context of climate change, "the tremendous costs of being the payor, lender, and insurer of last resort may prompt governments to take a much more active role in ensuring resiliency." The implications for the role of the state will materially affect the way business is conducted; business leaders in many more sectors will have to adjust to the next normal of greater government intervention.

At some point, governments may decide to get out of the business of business; how they do so will be complicated and differentiated. How much, how fast, and in what ways governments reduce their economic role will be one of the most important questions of the next decade.

5. More scrutiny for business

Rightly or wrongly, there is a perception in many countries that during the financial crisis, financial institutions were culpable for the trauma, accepted billions of dollars from taxpayers, and gave little back. Now citizens all over the world could face higher taxes and/or fewer services in order to pay for the $10.6 trillion committed so far. The public will expect—indeed, demand—that their money be used for the benefit of society at large. This raises complicated questions. What does it mean for businesses to do right by their employees and customers? If a financial institution accepts a bailout, how should it think about calling in loans? When, if ever, is it appropriate to resume buybacks and pay higher dividends?

Even before the coronavirus, there was a growing sense that shareholder value should not be the only corporate value. In August 2019, more than 181 US CEOs signed a statement committing themselves to other priorities—investing in employees, supporting communities, and dealing ethically with suppliers—in addition to shareholder value. The idea of the "triple bottom line"—profit, people, and planet—has become mainstream, as have socially responsible investment funds.

With many businesses likely to be operating to some extent with public money, the scrutiny will be intense. There will be real effects on the relations between government and business, and between business and society. That could show itself in the form of more regulation, particularly in regard to domestic sourcing and workforce safety. And as the coronavirus reveals or heightens awareness of social fractures, business will be expected to be part of finding long-term solutions.

The coronavirus could be the biggest global challenge since World War II. In the wake of that conflict came the question: "What did you do during the war?" That question will be asked, forcefully, of both government and business, once the COVID-19 battle has been won. Business leaders need to ask it of themselves now.

6. Changing industry structures, consumer behavior, market positions, and sector attractiveness

One of the key questions facing business leaders is whether their industry will rebound from the economic shock posed by the virus, or sustain lasting damage. The answer to this question likely lies in an assessment of the degree to which industries find themselves susceptible to the elements highlighted in this article. For example, those that have shown themselves to be less resilient may find it difficult to regain their pre-COVID-19 standing. In the auto sector, for example, companies have relied on global just-in-time-based supply chains; they will be under pressure to change so that continuity of supply is just as valued as cost and speed to market.

In addition, there could be lasting changes to consumer attitudes toward physical distance, health, and privacy. For example, increased health awareness and a corresponding desire to live more healthily could bring lasting change to where, how, and what people eat. Some consumers and governments—but by no means all—may change their attitudes toward the sharing and use of personal data if it can be demonstrated that the use of such data during the crisis helped safeguard lives.

For millennials and members of Generation Z—those born between 1980 and 2012—this crisis represents the biggest disruption they have faced. Their attitudes may be changed profoundly and in ways that are hard to predict. The tourism, travel, and hospitality sectors may see their businesses subject to long-term changes in business and individual travel preferences. Concern over the possibility of other "black swan" events could change how consumers approach financial security—saving more and spending less. The list of questions about how consumers will behave after COVID-19 is long, and uncertainty is high. As a result, this is the subject of much research by McKinsey and others.

Given the intensity of these pressures, it is reasonable to question whether existing market positions will be retained without significant effort to reposition and respond to changes confronting industries and sectors as a whole. To this can be added the economic impact of stretched balance sheets and valuations leading to changes in business ownership.

In this context, it is possible that institutions may find new and enduring ways to collaborate, prompted by the regulatory and other changes that have enabled corporations to work together in order to address the current crisis.

7. Finding the silver linings

If necessity is the mother of invention—and it often is—there could be some positive outcomes of the coronavirus crisis. These are unlikely to come anywhere near to compensating for the human and economic toll it is wreaking. However, given the general shortage of optimism at the moment, it may be heartening to consider a few encouraging possibilities.

One has to do with the human imperative to communicate. In this sense, the death of distance continues to be very real, and very positive. Individuals, communities, businesses, and governments alike are all learning new ways to connect: almost everyone knows a story of the grandparent who finally learned to Zoom, Skype, or FaceTime.

For businesses, the consequences have been profound. Many have learned how to operate remotely—at a high level and at far greater speed. These practices could well stick, making for better management and more flexible workforces. Flexible work is often critical to support employees at different life stages such as parents with young kids, women during parts of their career, or affinity groups such as the disabled.

Business leaders now have a better sense of what can, and cannot, be done outside their companies' traditional processes. Many are beginning to appreciate the speed with which their organizations can move once they change how they do things. In short, the coronavirus is forcing both the pace and scale of workplace innovation. Indeed, as businesses are forced to do more with less, many are finding better, simpler, less expensive, and faster ways to operate.

The urgency of addressing COVID-19 has also led to innovations in biotech, vaccine development, and the regulatory regimes that govern drug development, so that treatments can be approved and tried faster. In many countries, health systems have been hard to reform; this crisis has made the difficult much easier to achieve. The result should be more resilient, responsive, and effective health systems.

These silver linings are thin compared with the scale of the coronavirus catastrophe. Nurturing a next normal that will be better than what it replaced will be a long-term test of all our institutions, global and local, public and private. It will be critical to reconstruct for the future and not solve for the problems of the past.

One possible next normal is that decisions made during and after the crisis lead to less prosperity, slower growth, widening inequality, bloated government bureaucracies, and rigid borders. Or it could be that the decisions made during this crisis lead to a burst of innovation and productivity, more resilient industries, smarter government at all levels, and the emergence of a reconnected world. Neither is inevitable; indeed, the outcome is probably more likely to be a mix. The point is that where the world lands is a matter of choice—of countless decisions to be made by individuals, companies, governments, and institutions.

The early 20th-century British explorer Ernest Shackleton once noted, “Optimism is true moral courage.” Optimism and courage: these qualities are needed more than ever as leaders make the decisions that will shape the next normal.