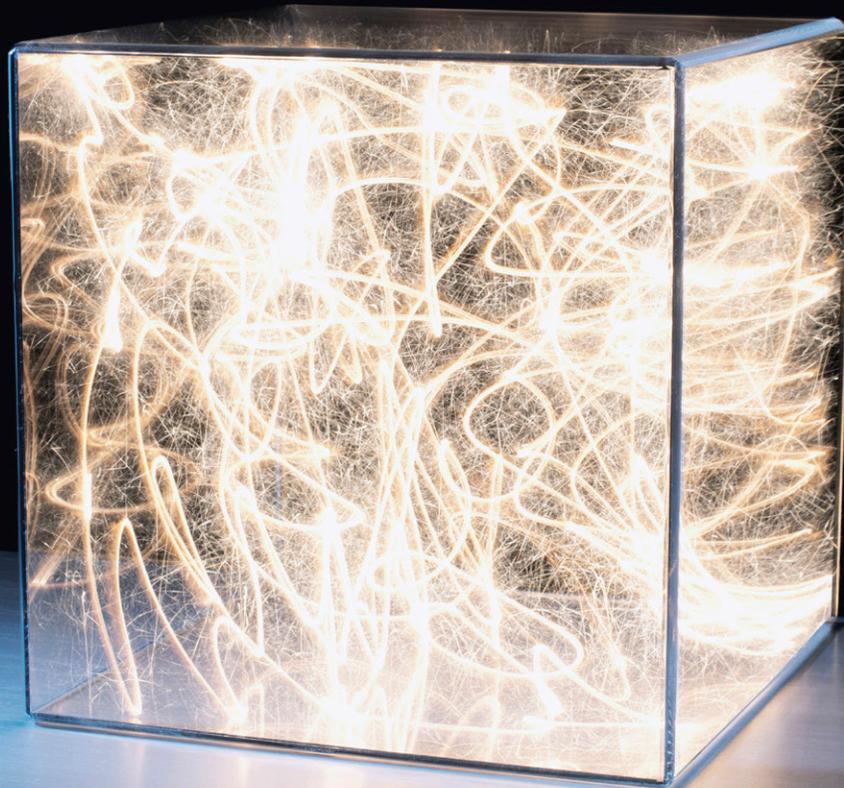


Strategy & Corporate Finance Practice

# The board's role during crisis and beyond

Three seasoned board directors discuss the role boards are playing in guiding their companies toward recovery from the COVID-19 crisis.



**In this episode of the *Inside the Strategy Room* podcast,** McKinsey senior partner Celia Huber, who leads board services work in North America, talks with three seasoned board directors about the role boards are playing in guiding their companies toward recovery from the COVID-19 crisis. Nora Aufreiter sits on the boards of Scotiabank, supermarket operator Kroger, and real-estate developer Cadillac Fairview, as well as a Toronto hospital. Peter Bisson is an independent director on the boards of HR services company ADP and research firm Gartner. And Margaret (Peggy) Mulligan serves on the boards of Canadian Western Bank and mining company New Gold. The panel discussion was hosted by Canada's Institute of Corporate Directors. This is an edited transcript of the discussion. For more conversations on the strategy issues that matter, subscribe to the series on Apple Podcasts or Google Play.

**Celia Huber:** I thought we would start by talking about how the board's role has evolved over time. After the financial crisis, we saw a trend toward more independent boards that brought their own perspectives as regulation and scrutiny increased. Today, boards are going beyond their core responsibility for oversight of corporate financials and staying on top of things like technological shifts and the company's impact on broader society. Even before the pandemic, we saw boards increasingly dealing with how to preserve corporate resilience, deal with activist investors, monitor corporate culture, and make the right decisions on risks around cybersecurity and other issues. So, the pressure on boards to be fully engaged and act as catalysts for change is coming from many directions now.

We see a few hallmarks of boards that are successful at serving as such catalysts. The first is a deep understanding of the industry and its context, including the key uncertainties. Boards can cultivate this knowledge by bringing in outside speakers, seeking input from external stakeholders, and exploring various scenarios. The second is thinking about strategy as part of every board meeting rather than as something that happens once a year or every three years. Lastly, the most effective

boards devote considerable attention to how they operate in terms of sharing feedback, strengthening team dynamics, and interacting with management.

Today, we are excited to hear our panelists' perspectives on serving as board members during this unique time. Peggy, what distinguishes a good board from a great board, especially now in the midst of this economic crisis?

**Margaret Mulligan:** I think the same factors distinguish a good board from a great board in normal and crisis times, but it takes a crisis to know if you actually have a great board. There's nothing like a true test to understand where you are. A great board, first and foremost, understands the difference between the management's role and the board's role, and respects that difference because board members fulfilled their key accountability, which is ensuring they have the right CEO and supporting cast of executives on whom they can rely in times of crisis. You also need the board, the management team, and the full organization to understand, respect, embrace, and live both the company's culture and strategy. I think a robust focus on enterprise risk is terribly important and not just as an annual check-the-box exercise but a real, living, vibrant function. And culture, strategy, and enterprise risk need to be embedded in everything that a company talks about and the board decides upon, because they are not disparate activities.

**Celia Huber:** Peter, as we were preparing for this session, you made the point that it is not as if the crisis has flipped a switch on corporate strategy; strategy endures. Can you elaborate?

**Peter Bisson:** Certainly. There are maybe 10 to 15 percent of companies for which this crisis is an existential threat. My comments do not apply to those. But for others, you are doing strategy in every board meeting. Typically, you would lay out a multiyear view of what you want to have in the market, the assets you would like to own, companies you would like to acquire. The pandemic does not really affect that. A company also typically has two or three transformation themes. For example, you are looking to change the customer experience and

develop some talent. The pandemic does not change most of those priorities. It might cause the acceleration of one or two; the shift online might cause you to move faster on the customer experience.

The test for the board is, can you keep your eye on the key strategic decisions or transformation programs you are pursuing, recognizing that the management team might be reaching the saturation point in what it can manage? The board needs to help the management team get done the additional work that comes with a crisis. Additionally, there may be a trade-off between maintaining long-term investments and delivering short-term performance. Each board has to make judgments on those trade-offs, and they are often not easy.

**Celia Huber:** Those trade-offs are the subject of my next question. Nora, you sit on boards of consumer-facing organizations, including a grocer and a hospital. Can you talk about how the crisis has affected those sectors?

**Nora Aufreiter:** Sure. I'm on the boards of three organizations that are in essential services, so the crisis had a dramatic impact on them. For example, grocery is an industry with typically 1 to 3 percent growth and during the pandemic, my company's sales were up 30 percent. In that situation, you face enormous pressure in terms of staffing, supply chain, and keeping food on the shelf, so having an engaged, experienced, and industry-knowledgeable board is critical. This is not a time for learning.

Secondly, the pandemic showed the importance of having a business-continuity plan or an incident response team so that when a crisis hits, you have the organizational structure, processes, and people in place. Keeping these plans well-practiced is incredibly important. Who is the emergency replacement for the CEO? What does the incident response team leadership look like? Have we dusted off those processes even though we may not have had a crisis in ten years? That has been one of my big takeaways.

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–Peter Bisson

**Celia Huber:** Have new topics emerged on the board agenda during this crisis? Peggy, can you speak to that?

**Margaret Mulligan:** We have not seen new topics, but certainly there has been some refocusing on how to implement the strategy that had been put in place. It was, I must say, very interesting trying to figure out how a mining company, one of whose major assets is on the US–Canada border and right beside a First Nations reserve would manage through COVID-19. Providing access to testing and healthcare was a new way of focusing on the ESG [environmental, social, and governance] issues that were always top of mind for that board.

While the agenda topics have not changed much, the frequency of meetings has, simply because management has to make many tactical decisions and conduct business differently. I do expect there could be some refocusing of agenda items once we all take a breath because we will revisit strategies and enterprise risks. The black swan scenario that we all model—we are living it. I hope there will be a lot of solemn learning from that.

**Celia Huber:** Has decision making become faster? Nora, have you seen this?

**Nora Aufreiter:** I think both management and boards have been surprised at how quickly they can take decisions when necessary. Once you have experienced that, it gives you the confidence to act more quickly. That does not cast aside the need for proper fact gathering and deliberation in a board meeting. On my boards, the frequency of meetings is not as high now as it was during the early days of the crisis. We were meeting weekly and then biweekly and then monthly. But for those boards meeting usually quarterly, we have kept a check-in every four to six weeks. Management finds that helpful, the boards find it helpful, and I think that higher level of engagement allows decision making to happen faster because people are more current.

**Peter Bisson:** I would make the point a little differently: the speed of decisions was increased by good management of the exceptions that had to be addressed. For example, when you suddenly move 60,000 people from working in an office to working from home, you need to keep track of what is

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happening to everybody and cybersecurity becomes an important topic. A lot of the efficiency in decision making has been driven by a strong board–management interface.

**Celia Huber:** Have you found the crisis affecting the demarcation between the board and management in terms of the decisions that boards get involved in?

**Peter Bisson:** The chair or lead director has an important role to play, in a sense, to police the boundary. Executional decisions are usually left to management, but if they carry a reputational dimension, then the management team tends to bring it to the board. You do not want the board trying to run the company operationally, but I go back to the idea of exception management.

**Nora Aufreiter:** With the higher speed of decisions, risk management is a big deal. Those frequent check-ins between management and the board are important so if something happens, you have not left the board out of the loop. But I don't think the roles have changed. The board is the supervisory and advisory body, but such decisions are management's call. What becomes challenging is the virtual nature of the interactions. Many of the sidebar-style interactions between individual executives and board members at the coffee bar, those natural touchpoints do not happen, so I have seen more outreach from management to individual board members or board member to board member.

**Margaret Mulligan:** I also have seen more outreach from the management because this is uncharted territory and it makes sense to seek the counsel of somebody who may have lived through an earlier crisis. I was running operations at Scotiabank during 9/11. Some of the experiences from that become relevant as people try to figure their way through this crisis. It is actually very heartening to see management using the board as a sober second thought and sounding board.

**Celia Huber:** Peggy, one of your boards brought in two new directors during this time, I presume virtually. Any practical tips on how to do that?

**Margaret Mulligan:** It was more complicated. In each case, any board member who was geographically close managed to have an outdoor coffee with the person because, as we all know, fit is tremendously important. But we found that the things you hope to achieve through a board refresh worked brilliantly. You get a new set of eyes, somebody asking fresh questions. You could see all our faces on the Zoom call going, "Gee, I should have thought of that." Anybody who is thinking of holding back on a board refresh right now: don't! It has proven to be just fantastic.

**Celia Huber:** One of the most important roles a board plays is deciding management compensation. Given that some companies are doing better and some are doing much worse than a year ago, do you hold to the original performance incentive plan?

**Peter Bisson:** In my experience, the management team objectives, and hence the compensation tied to them, have not shifted. The management team themselves do not recommend changes to the compensation system, fully knowing that it will be a bad year from a compensation point of view. It is a bit different when you look down the line. For example, if you have a direct sales force, they cannot sell nearly as much virtually, and that does not work for people trying to hit sales quotas. So there have been changes in compensation that lean in the direction of keeping key people whole.

**Margaret Mulligan:** Anybody whose equity compensation is coming due this year will get hurt because markets are still down. But if you look at equity comps, are you still on the same curve as your shareholders? Yes, arguably. On the flip side, equity grants happening this year will be, in theory, at a greatly reduced rate, with almost a guaranteed uptick. I have seen reports from compensation consultants arguing for modifications on both sides.

My boards have not reached any decisions, but it is certainly something we are discussing. The litmus test will be, have you properly remunerated the right people for the jobs they have done in this situation? And can you explain that in a way your shareholders

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accept? The wording in the proxy circulars is going to be very important. There are no easy answers and a whole lot of questions right now.

**Celia Huber:** Let’s turn to strategy. Peter, you started off saying that many strategies have stayed roughly the same. How are boards balancing short-term needs with original investment plans?

**Peter Bisson:** In terms of the trend acceleration or deceleration dimension, the elements of strategy that were tied to digitization or consumer experience have accelerated. The transactional dimension of strategy has slowed down a bit to the extent that acquisitions were part of the strategy because you cannot do due diligence easily, and agreeing on the fair value is trickier because stock prices have moved a lot. The area of biggest discussion is trading off the short term and the long term. In this environment, it would be easy to back off certain strategic investments to close earnings gaps, and I see thoughtful conversations about what can be deferred and just taking the short-term pain with the stock market.

**Celia Huber:** Have you encountered any pleasant surprises during these difficult past few months?

**Margaret Mulligan:** Nothing unites like a common enemy. We talked about resilience in the supply chain but, boy, the resilience of our management teams and entire organizations has been really

wonderful to see. I find people being very innovative and happy to express those thoughts. And they are being well listened to. With my boards, it has created a real team attitude and some strong advances on issues we have been working on.

**Peter Bisson:** I would echo Peggy’s view. The other thing I am very pleased to see is having tens of thousands of people go from working in an office to working from home and still maintaining an extremely positive customer experience. I regard that as nothing short of a miracle. It implies a huge amount of heroic effort by many people down the line. Often, the hesitation about making changes in processes hinges on concerns that employees will not be able to do it. People have proven the contrary during this forced change.

**Celia Huber:** How are your boards engaging on ESG issues, corporate purpose, and diversity and inclusion?

**Margaret Mulligan:** I think the corporate world is really advancing on the ESG front. And let’s be honest, we are getting a solid nudge from many extraordinarily influential shareholders. There is not just an acceptance of ESG in the companies I deal with but an embrace, and not just so we can publicize it. When you think about a gold miner, the risk of environmental impact is pretty catastrophic if you are not mindful and it is part of investors’ risk assessment.

**Nora Aufreiter:** In Canada, boards of directors are responsible for the health, wellness, and long-term sustainability of their companies rather than just being accountable to shareholders. But I would say, if you are focused only on the shareholders and not the staff and customers, those shareholders will end up unhappy so, to a certain extent, it is common sense. If you have a clear purpose, that will naturally enhance your commitments around ESG, and those companies that do not have one increasingly have to develop one because that is part of the corporate fabric now. If you have a purpose that is meaningful at the company level, it reinforces the culture and allows everyone to celebrate the great things they can do, which is highly motivating during a crisis.

**Celia Huber:** We talked about boards being catalysts for change and we talked about COVID-19 being a catalyst for change. Can you highlight one or two transformational opportunities you see in your companies?

**Peter Bisson:** In the organizations I am involved in, there are large digital transformations underway. By and large, the technologies are in place and the barrier has been behavioral change. Being forced to do so much behavioral change recently has been a silver lining here. The art of the possible now will be seen as far more robust than was the case six months ago.

**Nora Aufreiter:** To me, the big opportunity from the crisis is unlocking the inertia around behavior. Management teams are working together and many trends have been accelerated. The opportunity is not to lose the momentum for change.

**Margaret Mulligan:** To me, the crisis has shaken the idea that the annual strategy process can encompass everything that might happen. That's a good wake-up call.

**Nora Aufreiter** is a corporate director at Scotiabank, Kroger, and Cadillac Fairview. **Peter Bisson** is a board member of ADP and Gartner. **Margaret Mulligan** is a board director of Canadian Western Bank and New Gold. **Celia Huber** is a senior partner in McKinsey's Silicon Valley office.

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