

Advanced Electronics Practice

Coronavirus: Five strategies for industrial and automotive companies

To rebound from the coronavirus pandemic, industrials must undertake a journey that begins with resolve and ends with fundamental reform.

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We are still in the early stages of a global health crisis resulting from the coronavirus pandemic. Protecting lives is the first priority, but we must also protect our livelihoods. For automotive and industrial companies, surviving and emerging stronger at the far end of this crisis will require thinking beyond the next fiscal quarter. Success in the long run will require a journey across five stages: Resolve, Resilience, Return, Reimagination, and Reform (exhibit).

- screening and safeguarding the supply chain by understanding risks and taking action to address disruption
- adapting marketing and sales by identifying and mitigating the risks of declining sales while meeting critical customer needs
- maintaining financial health by improving liquidity, reducing costs, and establishing a spend control tower

Resolve

The first stage, Resolve, involves determining the scale, pace, and depth of action required. To do so, companies in advanced industries must take the following steps:

- establishing a nerve center to steer the organization, serve as the information hub, manage risk and responses, and align all stakeholders
- protecting employees by making their health the paramount concern and adjusting production as needed

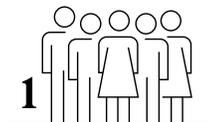
During the Resolve phase, companies must also make difficult choices, such as suspending production facilities, suspending discretionary spending, and furloughing workers. These decisions will require a comprehensive understanding of the situation, including data-driven scenarios for market evolution.

Consider the automotive industry. It is difficult to predict how the pandemic will affect sales in the European Union and the United States, two regions where coronavirus penetration is still emerging. We draw insights about potential developments by looking at the evolution of auto sales in China over

Exhibit

Companies in advanced industries need to think and act across five horizons.

Here's how it applies to automotive and industrial companies



1 Resolve

Address the immediate challenges that COVID-19 represents to institution's workforce, customers, and business partners



2 Resilience

Address near-term cash-management challenges and broader resiliency issues during virus-related shutdowns and economic knock-on effects



3 Return

Create detailed plan to return business to scale quickly, as COVID-19 situation evolves and knock-on effects become clearer



4 Reimagination

Reimagine the next normal: what a discontinuous shift looks like and implications for how institutions should reinvent



5 Reform

Be clear about how regulatory and competitive environments in industry may shift

the first quarter, since this country has already “bent the curve” and begun to recover from the coronavirus.

To translate the Chinese case study into scenarios for the European Union and the United States, we examined regional differences in viral spread, economic policy, and auto-specific supply and demand drivers. The latter includes OEM plant shutdowns, government restrictions on travel, consumer confidence, and overall loss of economic wealth. One scenario, which can help automotive companies move forward with greater resolve, is shown below as an example.

Scenario: Virus contained; slow recovery

In a scenario with containment of the coronavirus but a slow recovery, a strong public-health response succeeds in controlling the spread of the coronavirus within two to three months. Policy responses partially offset economic damage, a banking crisis is avoided, and recovery levels are muted.

In the European Union, 2020 real GDP contracts 4.4 percent, much more than the 0.4 percent in China. Temporary automotive plant closures are more extensive than those in China, leading to an estimated 8 percent reduction in production capacity. The strongest constraint, however, relates to consumer demand. Government lockdowns reduce auto sales to 10 percent of the pre-crisis forecast for April. Sales do not recover to 90 percent of the pre-crisis forecast until September, since consumer sentiment is less volatile in the European Union than it is in China. Over the course of 2020, more than five million unit sales, representing 25 to 30 percent of the pre-crisis forecast, are lost.

In the United States, 2020 real GDP contracts 2.4 percent. Similar to the European Union, government lockdowns force April and May auto sales to only 15 to 20 percent of the pre-crisis forecast. Consumer confidence then becomes the limiting factor. Experience from the recession of 2007 to 2009 suggests a slow, U-shaped recovery of consumer confidence. As a result, more than 5 million unit sales are lost in 2020, representing 30 to 35 percent of the pre-crisis forecast.

Globally, the automotive market could go down by as much as 20 to 25 in this scenario. The worldwide numbers are slightly better than those for the European Union and the United States because China is now recovering.

Resilience

As industrials experience virus-related shutdowns and economic pressures, they should move quickly to address near-term cash management challenges and broader resiliency issues.

To understand what makes companies resilient, past downturns provide helpful insight. Some companies also flourish during those hard times—typically those that took significant action at the outset. Our experience shows that resilient companies, defined as those in the top quintile of total revenue share within their sectors, took several key steps:

1. They sustained organic revenue growth throughout the recession and out-performed on earnings and on revenue in recovery.
2. They moved faster and harder on productivity, which preserved growth capacity.
3. They divested 1.5 times more during the downturn and acquired 1.2 times more in the recovery.
4. They maintain clean balance sheets long before a downturn starts.

Compared with non-resilient companies, resilient businesses increased revenues by 30 percent and reduced operating costs three-fold.

The most resilient companies also created end-to-end plans to guide their recovery. They first identified key risks, both internal and external, and then developed a range of scenarios to predict future outcomes. Other important activities included stress-testing the P&L, balance sheet, and cash flows, and then establishing a portfolio of interventions. Resilient companies also set up “cash

war rooms” to improve transparency and implement tighter controls. Finally, the best companies built resiliency dashboards of leading indicators that could be easily monitored and updated.

Return

Restarting production facilities can be more challenging than shutting them down. It requires a thoughtful approach to revive the supply chain, match volume to actual demand, and, most importantly, protect the workforce.

For worker safety, we can again learn from what is already happening in China. Factories there have taken special steps to resume operations. First, they restarted capacity gradually. For example, 20 percent of workers return every two weeks. Second, factories monitor the health of workers continuously. For example, employees get daily body-temperature checks upon entering to screen for potential infection quickly. Third, workspaces are redesigned with modifications that include deactivating elevators, increasing ventilation, and ensuring that workers are well spaced and not stationed to face each other. Lastly, to guard against a single-point failure, workers of the same type are separated into multiple groups.

Given the complexity of global supply chains, ramping up factories in a coordinated way will be mission critical. This will include four important phases:

1. Preparation. Companies reach full transparency about systems, networks, and workforce, including the parts and people available.
2. System filling. Leaders monitor their global supplier networks to ensure readiness.
3. Stabilization. Employees become familiar with the new normal and prepare for volume increase.
4. Ramping up. Companies produce the full product portfolio, matching supply and demand.

Reimagination

The coronavirus pandemic could fundamentally shift how people live, work, and use technology. Advanced industries will likely see a shift in preferences as the expectations of workers and leaders begin to change. The organizations that reinvent themselves will emerge much stronger than those that simply work to reclaim their pre-COVID-19 position.

For industrial companies, this global health crisis may lead to a reimagination of the following:

- *the go-to market approach*, as businesses shift to e-commerce and companies digitize their sales experiences or place greater emphasis on new business models, such as rentals and leasing, to overcome consumer reluctance about purchases that involve a greater commitment

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- *cooperation and alliances*, as “frenemies” work together to promote technology innovation while reducing the funding burden
- *M&A opportunities*, as companies increasingly seek deals when market capitalization approaches historic lows
- *workers’ roles*, as businesses further automate warehouses, plants, and facilities
- *geographic footprint*, as global supply chains increase the exposure to health impacts, disruptive trade dynamics, and an uneven global recovery
- *sourcing*, as the incremental costs of redundant sourcing outweigh the hazards of sole sourcing
- *costs*, as a shift from fixed to variable cost enables a lower breakeven volume in times of high volatility

Reform

In addition to dealing with the significant societal changes coming in the next few months, industrial companies may want to consider strategies for addressing some of the persistent issues affecting the sector to avoid the next crisis. For example, they may want to minimize supply-chain risks by increasing local production or dividing production among more sites. Other imperatives include sustainability, workforce flexibility, and adaptability to accommodate changing tariffs. Above all, companies need early-warning systems to detect risks such as the coronavirus and get a head start on preparation.

We see two notable examples of reform emerging in the industrial sector. First, the spread of COVID-19

has already led to greater workforce flexibility, with teams adapting to remote or virtual ways of working. Additionally, companies have added flexible work hours, so that workers can care for children and elder family members during the crisis. In the next normal, we expect to see enterprise-wide flexible employment contracts at scale and more opportunities for remote working, which will allow better leverage of the global talent pool.

In another shift, industrials are likely to make fundamental changes to supply chains to improve their resilience. The current pandemic has revealed the global dependencies of most supply chains, and many industrial companies have shown a lack of contingency planning. With the high level of uncertainty arising from the pandemic, supply-chain leaders are placing more emphasis on forecasting efforts to help them determine global ramp-ups and improve reaction times. Going forward, we expect that local-to-local supply chains will provide more flexibility and that vendors will be more accommodating. We also expect that companies will increasingly adopt digital and analytical tools as they recognize the real value of predictive monitoring and supply/demand matching.

For more than 200 years, the advanced industries sector has underpinned economic and societal progress that has dramatically improved lives. Its technologies have had a flywheel effect, enabling other sectors of the economy and increasing productivity, and its future success will be critical to the world economy and the advance of technology. The new five-step approach can help automotive and industrial companies weather this pandemic and rebound quickly when it abates.

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