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# The Coronavirus and the Financial Sector

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## Key impacts of coronavirus

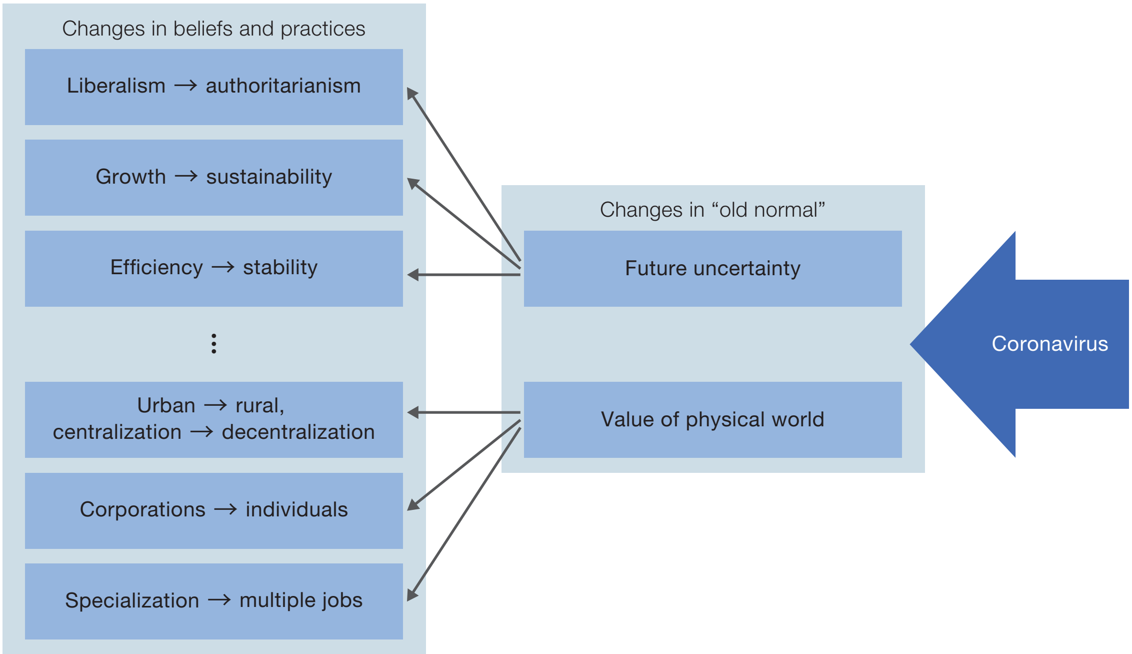
The coronavirus has had a far-reaching impact on society. Even today, several months after Japan lifted its state of emergency, it remains difficult to envision the ultimate ramifications of the pandemic. There is mounting criticism of capitalist economies that naively pursue growth at any cost and ignore the finite nature of the natural environment, and there is also a growing awareness of the importance of sustainability. On the conceptual line stretching from liberalism to authoritarianism, more are starting to seek an emphasis on public welfare over individual freedoms. Conceptual pairs like “growth vs. sustainability” and “liberalism vs. authoritarianism” are increasingly presented as binary opposites, with a growing sense that the coronavirus has flipped the switch from the former to the latter.

Many other issues, ranging from the role of the state and corporations to personal work arrangements, are also being viewed through the lens of conflict or opposition—global vs. national, urban vs. rural, corporations vs. individuals, specialization vs. side jobs, and offline vs. online—with the coronavirus seen as having prompted a move from one to the other. There are as many views on the impact of the pandemic as there are people, and in that sense it truly has led to the creation of a “new normal.”

Among the wide-ranging implications of the coronavirus, what specific changes has it wrought in the “old normal” of shared practices and beliefs? And what is the underlying source of these changes?

I would like to focus on two of these “epicenters”: future uncertainty and the value of the physical (offline) world. Regarding the first, views of future uncertainty have changed because many saw the coronavirus as nature’s revenge against a human society characterized by boundless growth. At a time when we were already experiencing first-hand the ferocity of nature, with global warming leading to an increasing number of floods and storms each year, the pandemic seemed like more evidence that nature was rebuking human civilization for its excesses. This has led some to believe it is time to change course and pursue a more sustainable economy. At the same time, the pandemic has ramped up the perceived level of future uncertainty. This has had a greater impact from a corporate perspective,

**Figure 1. Coronavirus ushers in "new normal"**




Source: NRI

and although uncertainty was growing even before the pandemic it has become even more important to address it now. This is also a direct cause of the shift from efficiency to safety and from methodical planning to flexibility that has occurred under COVID-19.

In terms of the value of the physical (real) world, the pandemic has prompted a reassessment of the value of offline communication. As people are forced to avoid the "three Cs" (confined spaces, crowded places, and close contact) and mandatory constraints are placed on face-to-face communication, companies have rapidly introduced online communication for both sales activities and ordinary office work. This reduction in the perceived value of face-to-face communication will not only lead to more remote work but will also encourage people to take on more than one job and is threatening companies' very reason for existence, which has traditionally been to provide a place where people can communicate. And now that the act of establishing an office and gathering employees there has lost some of its significance, there will also be negative implications for the value of cities themselves, which are essentially an aggregation of numerous corporate offices. A concept taken for granted until now—that there is value in being located close to customers and suppliers—is now being called into question. This fresh look at the value of offline communication is prompting a reassessment of the value of physical location and may by extension force us to reconsider why companies exist and what sort of society we want.

## Corporate challenges in responding to coronavirus

Observing how companies are dealing with these changing views on future uncertainty and the value of the physical world can shed some light on their response to the coronavirus.

As for future uncertainty, it was recognized even before the pandemic that uncertainty in the business environment was gradually increasing as a result of the natural environment, technological factors, and geopolitical factors. Firms have continued their efforts to identify the bottlenecks that might cause business interruptions and ensure business continuity in the event of, say, a natural disaster. However, the ongoing pandemic has proved far more powerful than anyone expected. Businesses may be unable to meet with customers in the flesh for weeks at a time, and if a single employee is infected they can be forced to shut down an entire office the next day. In effect, the coronavirus is as powerful as a natural disaster but occurs with far greater frequency and has the potential to persist for an extended period of time. Addressing such uncertainty requires more than just a business continuity plan. Companies need to enhance their ability to control costs by fundamentally reviewing cost structures and making further efforts to reduce fixed costs. That, in turn, requires a strategic review of operations, including the possibility of outsourcing or automation. At a time when people’s views of what is normal are being completely rewritten, developments at customers also present a major source of uncertainty. Companies need to provide services that are tailored to the needs of their customers, but the framework of customer needs itself may undergo major changes as society evolves towards a “new normal.” Companies may have to go beyond simply understanding customer needs and undertake a major review of segment strategies themselves. Rethinking the current approach to future uncertainty will require fundamental changes in business and marketing strategies.

With regard to changing views of the value of the offline world, one obvious implication is that companies need to ensure that their communications systems are ready for the digital era. They must introduce videoconferencing systems allowing employees to work remotely and engage in sales activities without meeting clients in person. Videoconferencing has had difficulty making inroads in Japan until now for a number of reasons. There have been cases in which one company wanted to start holding online meetings but the other side—for a variety of reasons—could not. Many firms were also worried that potential customers would view online sales activities as being inferior to face-to-face meetings. But now that the coronavirus has created a new environment for all companies, including customers and suppliers, it is becoming increasingly commonplace to hold video meetings. The same is true of meetings within the same company. Some firms forced to introduce teleworking arrangements in response to the coronavirus discovered that they could accomplish more than expected remotely, leading them to declare that they would continue the remote working arrangements even after the pandemic is over[1]. Additionally, the coronavirus has prompted some large financial institutions to rethink their plans and accelerate planned reductions in physical branch networks[2]. Amid evolving views on the value of the physical world, companies are finding themselves forced to make major changes in how they allocate business resources to create more value for customers.

NOTE

1) The Nikkei, for example, reported on May 25, 2020 that Fujitsu would continue its work-at-home program and target an attendance rate of only 25%.

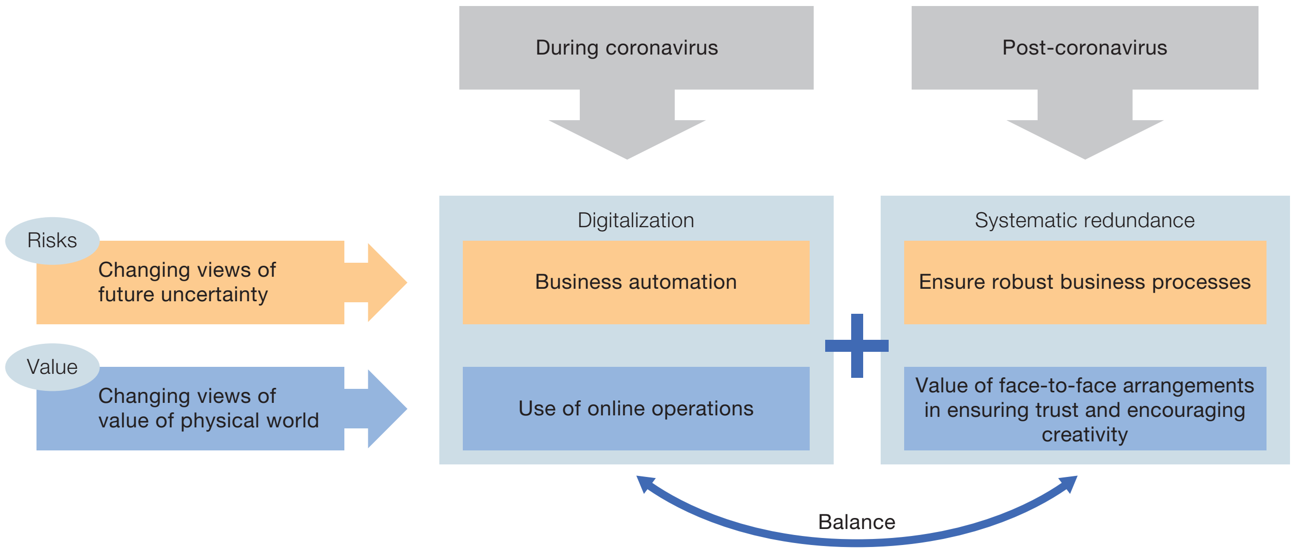
2) On May 20, 2020, the Nikkei reported that MUFG Bank planned to slash its physical branch network by 40% from FY17 levels by FY23.

## Looking ahead to post-pandemic world

Responses to the coronavirus are changing now that businesses are starting to look ahead to a post-pandemic world. Initially, the increased uncertainty prompted many companies to conclude that they needed to stop moving operations overseas and bring everything back home. But now that a certain amount of time has passed and companies are able to make a more dispassionate assessment of the situation—including what is happening at other businesses—many have decided that completely eliminating dependence on other countries is not a realistic option. Instead, they are emphasizing the importance of maintaining stable relationships with overseas partners. While it is important to manage risk by spreading operations across a number of countries instead of betting on just one, fewer are making the simplistic “bring everything home” arguments heard early on in the crisis.

Additionally, the virus outbreak initially focused attention on the automation of business processes because the dependence of certain tasks on specific employees was thought to leave companies in a highly vulnerable position. Companies that had made little progress in this area regretted their insufficient

**Figure 2. Adjusting risk-value balance for post-pandemic world**




Source: NRI

"digital transformation" (DX) initiatives. But automation can also hinder a company's ability to deal flexibly with a changing environment. While having more people involved increases the risk of infection, it also enables the organization to respond flexibly to uncertainty. As the focus shifts to the post-pandemic world, many have pointed out the importance of designing business processes that are robust against uncertainty instead of rushing pell-mell to automate everything.

Views of online communications are also changing. Many forms of communication were moved online as a stopgap measure when the coronavirus struck, but as we assess the impact of these measures it has become increasingly clear that online communication is lacking in some respects and that certain things are lost. For instance, we now know that online sales activities targeting potential customers tend to be less effective. When a leading US financial institution prohibited sales staff from meeting customers in person because of the coronavirus, it provided them with a variety of alternative tools and systems, including videoconferencing tools and systems enabling them to view customer data remotely. Consequently, there were no problems at all when dealing with existing customers. But new customer development activities, which traditionally included invitations to golf outings and parties, are difficult to replicate online, and the result was a loss of revenues. This company now has a renewed appreciation of the physical dimension when it comes to building relationships of trust with new customers.

The effectiveness of remote working arrangements for certain types of work has now been confirmed, but some companies argue that it is difficult to move highly creative activities, such as business development or planning, online. Their view is that opportunities for close communication and the sharing of information are the source of creativity. They argue that not only do people exchange more “informal” information, such as facial expressions and gestures, but the serendipities made possible by physical meetings are essential to the creative process. This argument is easy to understand for people who prefer brick-and-mortar bookstores to online retailers like Amazon. By being physically present in an actual store, customers can sense first-hand what is happening in the world, and fortuitous encounters with seemingly random new information can broaden their areas of interest. Google president Sundar Pichai has argued that face-to-face communication is essential to the creative process and says he wants to restore such communication in the office as soon as the pandemic subsides to some extent[3]. At a time when other big tech firms are talking about moving permanently to remote working arrangements, it is noteworthy that Google—which everyone acknowledges to be an extremely innovative company and which is perhaps the preeminent corporate leader in the digital era—is discussing the limitations inherent in remote work arrangements.

3) “Sundar Pichai Says Google Doesn’t Plan to Go Entirely Remote,” WIRED, May 22, 2020.

In summary, this need to develop robust business processes and take a fresh look at face-to-face working arrangements to ensure trust and encourage creativity is telling us that perhaps companies need to reconsider the digital technology and business automation initiatives undertaken as a stopgap measure during the pandemic. While digital technology is clearly essential to addressing the coronavirus, Google is saying that we should not overlook the new risks created by such technology or the possibility that it will end up destroying value. What is interesting here is that the views regarding operational risks and value added both take a positive view of a certain kind of redundancy. In terms of operational risks, the “double-tracking” of operations represents a kind of redundancy, as does (in the area of value added) the decision to send people for operations that could be performed remotely. Redundancy not only provides a buffer against uncertainty but also serves as a cradle for the creative process. Since the existing worldview views redundancy as waste or inefficiency, it has been unexpectedly difficult to incorporate it systematically. Nevertheless, it may become a key conceptual foundation for business strategies in the post-coronavirus era.

## Tailwinds for digital transformation

The importance of digital transformation (DX) has long been discussed in the financial sector, but it is questionable how many companies had achieved significant progress in this area prior to the coronavirus. Here, “significant” is used to mean that the measures undertaken were considered essential for the future of the business. While there are many instances of companies adopting new tools or partially automating certain operations, many of the people supervising this work would probably have had difficulty explaining how it fit into the company’s overarching business strategy. However, just when it seemed as though DX was approaching its “best-by” date as a buzzword, the coronavirus struck, and the importance of DX quickly became clear to all involved.

The pandemic made it possible for companies to adopt a variety of digital technologies without having to ask why. Examples included the hasty introduction of tools to allow remote sales activities after face-to-face sales activities had become increasingly problematic, the creation of systems enabling both head office employees and call center staff to work remotely, and the enhancement of web-based customer support services. It was clear that companies that did not promptly address these issues would fall behind competitors, and within firms these initiatives received higher priority since they were presented as crisis-response measures. In this way, the coronavirus gave the leaders of DX initiatives a powerful justification for their work.

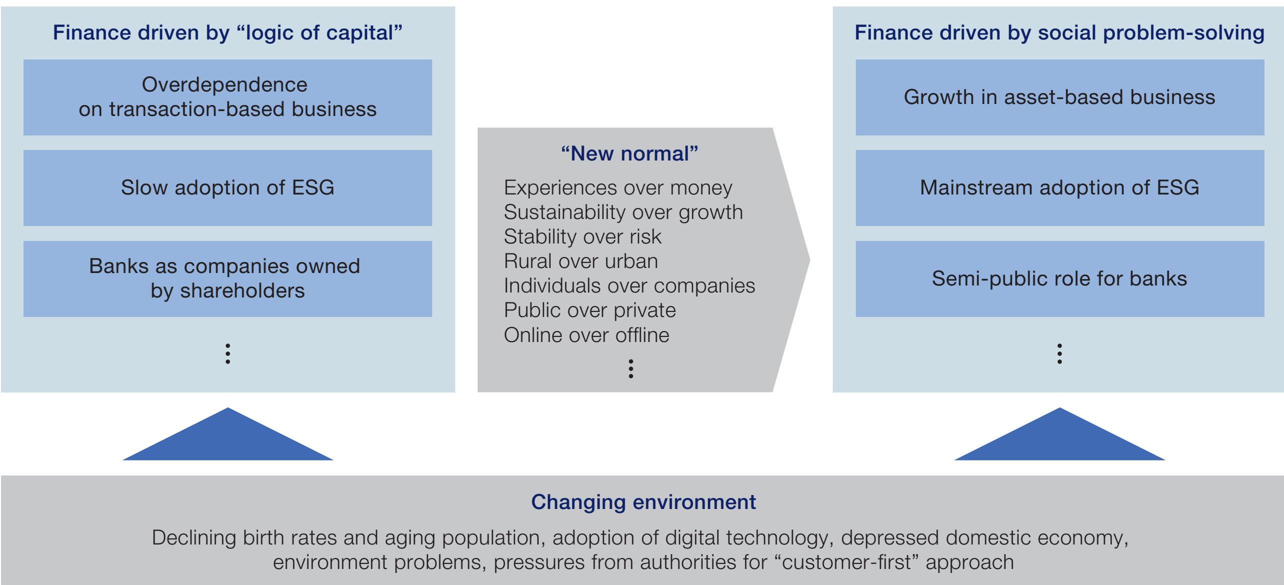
However, this will not last forever. Once the initial response to the pandemic is completed, it will be necessary to demonstrate how DX initiatives fit into the anticipated path of the business in the post-pandemic era. However, it should not be that difficult to explain the importance of digital technology if the coronavirus has in fact changed the way people think about future uncertainty and the value of the physical world. A variety of initiatives can be presented as being part of a company’s response to COVID-19, including improvements to analytics, the establishment of business systems, the development of open APIs, the expansion of virtual storefronts, the enhancement of sales staff support systems, and the creation of better smartphone apps and web services. Problems remain, including the question of how to build in redundancy, but for now, at least, DX project leaders are unlikely to have difficulty justifying their work.

## "New normal" could usher in use of finance to solve social problems

Given the massive impact of the coronavirus on society, it can be expected to affect not just individual financial institutions but also the broader financial sector. That raises the possibility that the industry will be able to implement changes that have been difficult for individual players to make. For instance, it has long been argued that Japan's retail financial industry needs to abandon its transaction-based business model, which offers limited potential for clientele growth, for a focus on asset-based fee businesses. Even though many understand the need for a new business model, we have yet to see the broader financial sector move in that direction. For individual institutions, a major change of course is complicated by such considerations as the short-term impact on earnings and employees' skill sets. They must also take into account customer expectations and developments at competitors. If the financial sector's current "rut" is the result of institutions being tied to existing notions of what a company is, what sorts of working arrangements are appropriate, and why people want to increase their assets, then the "new normal" might be able to break through this impasse by changing how people think.

One reason why ESG has received relatively little attention in the asset

**Figure 3. "New normal" may help financial sector solve social problems**




Source: NRI

management business is the financial sector's absolute focus on monetary performance. Banks struggle with conflicting expectations as publicly traded companies and semi-public providers of essential services because they are bound by a traditional belief in the primacy of shareholders. The "new normal" unleashed by the coronavirus has the potential to alter this state of affairs and unleash major change throughout the industry. A new worldview emphasizing a sustainable economy over growth and experiences over money may be perceived as a kind of self-negation by those who grew up under the current worldview. But at a time of dim prospects for future growth in value added, the "new normal" ushered in by the coronavirus offers an excellent opportunity for the financial sector to implement the reforms needed to help it solve society's problems.

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*Founded in 1965, Nomura Research Institute (NRI) is a leading global provider of system solutions and consulting services with annual sales above $4.8 billion. NRI offers clients holistic support of all aspects of operations from back- to front-office, with NRI's research expertise and innovative solutions as well as understanding of operational challenges faced by financial services firms. The clients include broker-dealers, asset managers, banks and insurance providers. NRI has its offices globally including New York, London, Tokyo, Hong Kong and Singapore, and over 13,000 employees.*

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