The Strategy Summit

London, 16 April 2018

The Managing Partners' Forum Strategy Summit hosted by Kennedys on 16 April, discussed how the professions are defining their strategic plans during and post-Brexit. The aim of the meeting was to provide meaningful context around the current dialogue, consider the likely scenarios and identify how professional services organisations can gain strategic advantage.

The background from Brussels

Sebastian Remøy from international consultancy KREAB provided a Brussels and global perspective; Professor Raquel Ortega Argiles from Birmingham business school shared her research on the likely regional and sectoral impact of Brexit; and Andrew Hedley offered strategic advice to professional services leaders. The speakers then joined a panel discussion chaired by Henrietta Jowlett of the CBI, and also featuring Antony Rayne from Deloitte.

Remøy works in KREAB's Brexit team of 60 specialists advising on the financial, environmental, trade, competition and digital regulation aspects of Brexit. Brexit is an economic, political and emotional event that presents a multiplicity of challenges. There is still uncertainty, but we know more than we did, and it is time for businesses to start effective preparations.

Remøy's presentation covered the following:

- The Brexit timeline
- Brexit negotiations: Process and progress
- Future relationship: Key EU27 priorities and possible scenarios
- Preparation

Although the official Brexit date is 30 March 2019, transition will continue until December 2020, when the current EU budget ends, although there may be some flexibility to extend it by a few months.

The Irish border is a potential deal breaker, as the Republic of Ireland will continue to be an EU member state post-Brexit. Future arrangements are still under negotiation, and will be discussed at the June EC Summit, along with guidelines on the related EU-UK relationship post-Brexit. The EU is expecting the UK to revert with a solution. The fall-back position is regulatory alignment between the ROI and Northern Ireland. However, this also presents political risks.

It is anticipated that the Brexit Withdrawal Agreement will be ratified in October 2018. This in effect a blueprint agreement, as it does not cover trade. The official transition will start on 30 March 2019, followed by European Parliament elections and the appointment of a new Commission. There will be a new trade commissioner and possibly a new Brexit negotiating team. The final deadline is December 2020. The

EU are quite firm about that as they do not want an extended transition period. Most businesses agree.

The Brexit Withdrawal Agreement covers the UK's divorce from the EU: citizens' rights, the financial settlement, the Irish border, the transition, and the framework for the EU-UK relationship post-Brexit, including trade and security cooperation.

All migrants to the UK will have all their rights respected until December 2020, but there are questions around the position of family members of those migrants. The financial settlement will be around £48bn.

Remøy set out potential scenarios for the future relationship between the UK and the EU before turning to how companies are preparing for Brexit. An important point is this is not just about UK companies, or even companies with a UK presence; Brexit will affect trade globally.

Many organisations have established Brexit taskforces. The banks are farthest along, applying for licences in different jurisdictions, hiring office space and moving people. Other organisations are considering their options, making risk assessments and deciding whether to relocate headquarters or subsidiaries.

Finally, Remøy identified seven key focus areas for organisations preparing for Brexit:

1. Company law, as applied to companies incorporated in the UK and elsewhere, UK companies with European branches/subsidiaries, and foreign companies with UK branches. EU laws on disclosure, incorporation and cross border mergers will no longer apply to the UK, and EU companies will have no more automatic access to UK company information and there will be no more single market right of establishment.
2. Contracts: agency and distribution agreements, insurance and operating licences.
3. Employment: visas, mutual recognition of qualifications and family issues
4. Customs: Import/export declarations, rules of origin. Remøy reminds us that 180,000 UK traders will need to make customs declarations for the first time post-Brexit and most small and medium businesses are not prepared.
5. Product regulation
6. Data privacy and security
7. Intellectual property

Economic impact analysis

Professor Raquel Ortega-Argilés focused on Brexit's economic implications, having led several international research projects supported by the Economic and Social Research Council.

'The Continental Divide? Economic Exposure to Brexit in Regions and Countries on Both Sides of the Channel' is a detailed sectoral analysis of the impact of Brexit on UK sectors, regions and cities using trade and competition datasets and the only study that compares in detail the economic exposure to Brexit of UK and EU regions and countries.

Its objectives were to

- Study the degree to which EU regions and countries are exposed to negative trade-related consequences of Brexit;
- Analyse the heterogeneity of these consequences at the regional and sectoral levels; and
- Incorporate the effects due to geographically fragmented production processes within the UK, the EU and beyond.

This was achieved by developing a measure of regional exposure to Brexit, using global input-output tables to link trade to value-added, using a bilateral version of the Domestic Value Added in Exports (DVAiX) indicator. Linking this with regional relationships provides an indicator of the effect on gross domestic product (GDP).

The study calculated UK Brexit risk exposure at 12.2% of UK GDP as 4.6 times higher than the figure for the EU at 2.64% of EU GDP. Unsurprisingly, Brexit risk exposure is higher for regions with stronger trade relationships with the UK, and similar industrial structures to the UK, and, to a lesser extent, those that are geographically closer. For example, German regions are more exposed than French or Belgian regions. However, all trade flows are likely to be affected.

The sectors with the greatest exposure across Europe are manufacturing and services, to a much greater effect in 37 UK regions at 29-51% and 4-9% respectively. The hardest hit EU countries will be Ireland, with 24-30% of primary industries at risk, and Germany, where 42 regions will be exposed, predominantly in manufacturing.

A related analysis: ‘An Assessment of Brexit Risks for 54 industries: Most Services Industries are also Exposed’ linked Brexit exposure risk to value-added contribution, using World Input-Output Database www.wiod.org to

- analyse the heterogeneity of Brexit-exposure of UK industries;
- examine the extent to which they depend on trade with the EU; and
- consider the relative size of their value-added contribution and the role that some industries play in global supply chain.

Key indicators were the ‘jobs at risk’, ‘value-added at risk’ and ‘hyper-competitiveness’ indexes.

The study found that more than 2.5 million UK jobs are exposed to the trade effects of Brexit. Although primary industries and manufacturing industries are highly, so are many service industries. For as many as 15 out of 54 industries more than 20% (up to 36%) of the jobs and value added are at risk. Notably, the analysis found that 36% of the UK’s professional, scientific and technical services industry is at risk; 31% of auxiliary financial services and 14% of legal, accounting and consultancy.

Finally, the ‘hyper-competitiveness’ index explored the scenario that all products previously imported from the EU were purchased from domestic sources. But even in that unrealistic scenario, 14 industries would still contract as a result of Brexit.
Finally, Professor Ortega-Argilés highlighted concerns over Brexit’s impact on the

UK's important financial services sector and the UK's long-term productivity as the jobs most at risk are above the UK average in terms of productivity.

Practical strategy for professional services
Andrew Hedley envisaged a more positive outlook for professional services, which thrive on complexity, advising them to build Brexit uncertainty into their strategic planning and identify the opportunities it presents for them to advise and support their clients.

Hedley looked at the dynamic between firms, their clients, and their competition in a business environment which Brexit has turned upside down. "Strategy is about creating sustainable competitive advantage. This means making choices about where to play and how to win." Most professional services firms have the same ingredients in terms of people, technology, client base, brand. They differentiate themselves by how they combine those ingredients into different recipes. Therefore, their distinctive qualities are leadership and culture.

Firms that are good at dealing with complex environments have the following characteristics:

- They are ruthlessly honest about opportunities in the market and where they can match them, and this underpins their investment decisions.
- They are focused on their core purpose (explored in the next MTT meeting).
- They build skills that will help them adapt to new rules.
- They recognise that many decisions are not binary and adopt an incremental approach, which enables them to change direction.
- They embrace scenario planning (echoing both previous presentations) in order to understand what's driving change (for them/their sector/their business)

The first step is to identify what is critical and what is certain – and uncertain. You can then build these into developing potential scenarios, which include the possibility of issues/situations moving from low to high criticality and certainty, and vice-versa. Hedley uses strategic modelling, to plot certainty/uncertainty against high/low impact on a chart. The next step is to explore what each potential scenario means for different elements of the business – for example, shifting the focus from revenue to profit presents a different scenario for the business.

Client impact analysis is crucial as it determines whether to develop new services in relation to changing requirements, if indeed they are changing. As some decisions are taken, the position will become clearer and other decisions will fall away.

Nothing is agreed until everything is agreed, so although a lot of firms are hedging their bets by opening offices in Dublin, the important qualities are readiness and decisiveness.

Professional services organisations that will do well out of Brexit are scenario planning, says Hedley. They know the trigger points and when they need to take action. It's better to be 90% right and fast than 100% right and slow, and to manage the gap. This requires agility: the ability to reform, re-skill, redeploy resources in a changing business environment. They embrace change, and the more they practice it, the better they get. They are learning organisations who constantly acquire new knowledge. In a world where most organisations are the same, learning to do things differently is the key to competitive advantage. Leadership is another critical success factor, as leaders carry the responsibility for positioning their organisations for success in complex and uncertain times.

In summary, professional services need a Brexit plan that can be adapted to multiple scenarios in respect of risk, readiness and economic impact. [ENDS]

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