

Coronavirus — Sustaining Supply Chains Amid Global Disruptions

The COVID-19 coronavirus has rapidly spread around the world, threatening lives and disrupting the global economy and global supply chains.

Executives around the world are scrambling to understand the risks within their supply chains and keep their businesses afloat. They know the problems they face — closed supplier plants and warehouses; an inability to source components and raw materials; and goods stuck in quarantined areas.

But given the breadth of their supplier networks, the volume and variety of goods they produce, and the range of supplier goods involved, assessing and reconfiguring a supplier network on the fly is a complex, resource-intensive challenge. It's also what we do every day at Argo. We are working with clients to redesign supply chains and source and qualify new suppliers in the wake of COVID-19 — and we're getting companies out of crisis-mode and de-risking their supply chains for the future.

Short-Term Actions

The effect of COVID-19 on business supply chains is likely to get worse before it gets better, and many companies have only begun to feel the strain on their supplier networks. Here are actions we are helping our clients take immediately to reduce the effects of COVID-19 disruptions and help them to prepare for the next natural disaster or geopolitical event:

- **Communication methods and structure:** Bad news should travel fast and to everyone that needs to act on it —to finance, procurement, production, planning teams, customers, suppliers, etc. As new supplier shortfalls are apparent and as customers revise their demands amid the COVID-19 disruption, a routine conveyance of information needs to be established.
- **Recast capacity and raw material availability:** Most companies operate like a well-oiled machine when it comes to managing the day-to-day transactions in their supply networks — but they're simply not used to dealing with production stoppages in China, South Korea, and elsewhere. The ability of many companies to react in real time and change underlying supply-chain characteristics, such as raw material movements from country to country, is limited.

Most executives have not faced this type of troubleshooting since SARS in 2003 or the Japan earthquake and tsunami in 2011. We are working with our clients monitoring multiple suppliers and the availability and timeliness of raw materials to determine what products they can make for customers and how their own schedules must be revised.

- **Prioritize production:** There are truly a new set of business rules being written, and past goals and objectives need to be reformulated given what's available. Old demand forecasts no longer apply. We are helping a number of companies reset priorities for the products, parts, components, and materials that are critical to company survival. If a client can only make 100 widgets, it needs to be making the 100 highest-margin widgets possible. Product lineups need to be assessed based on a variety of factors that are now changing rapidly — EBITDA, customer tolerances, ripple-down effects on demand from changing consumer habits (traveling, tourism, dining out, etc.). The decisions made will be critical to company bottom lines.

For a client launching a new product line and about to ramp up production, we are delaying the launch to limit disruptions and keep the supply base focused on components for what is currently selling. For another company selling three similar SKUs at different prices, we stopped making the middle-priced SKU in order to sustain sales of high- and low-priced SKUs. We are also helping management cost-effectively in-source production and optimize equipment with limited supplies (e.g., running only machines with the highest productivity). These are all difficult choices, but they must be made. Companies that try to produce everything as they did months ago will likely fail to adequately produce anything.

- **Real-time supply-chain reactions and lead times:** Supply-chain conditions are changing by the minute, and companies need to regularly update lead times based on changing supplier outputs, shipping schedules, and component and raw material availability. Shipping companies have taken vessels out of circuit and elongated routes — stopping in more ports — to keep vessels fully utilized, which has reduced overall shipping capacity and caused delays and price increases. In the air, as passenger airlines cut or eliminate flights to and from China, air freight is increasingly less available and rates are skyrocketing.

Daily tracking of supply-network conditions is a huge task, and not a normal activity for most companies. Executives understand, however, that without a clear view of current lead times, their supply chains fall apart. Many are used to running their supply chains based on historical data and budgets, and only rarely look for alternative scenarios. Argo has great exposure to this type of network information and we are working with a number of clients to rapidly reroute and redesign supply chains.

- **Reposition key production enablers:** Within companies' existing supply chains they may have answers for supply availability and be able to reposition capacity (e.g., raw materials, molds, semi-finished components, key ingredients) to different, qualified suppliers and production lines. This transition should occur immediately. We're conducting studies of supply networks in which we identify suppliers in all tiers and then assess a company's ability to efficiently move work from China and other affected countries to comparable suppliers elsewhere. Argo has a wealth of supply base data from around the globe and the information to quickly identify supplier options.

Our work also allows companies to see who really supplies their products, and they're often surprised by the results: For example, one company found that its Cambodian textile supplier had its fabrics coming from China, without which the supplier could not ship its product. We recently analyzed one client's critical components, and the suppliers for those goods, for its top three products (representing 80 percent of revenue); the company had two suppliers for most components, but was not aware that both suppliers sourced their raw materials from the same company in China. Since China's GDP is more than \$US 14 trillion (seven times what it was during the SARS outbreak), many companies will find similar reliances on China today if they dig deep into their supplier networks as Argo does.

In the short term, we're guiding companies through disruption recovery, but the real value we bring is via a complete assessment of the entire supply chain, reducing risks and allowing companies to have an effective Plan B in place long-term.

Long-Term Supply-Chain De-Risking

Our clients are overwhelmed right now with the effects of COVID-19 on their internal operations. They're developing plans for how to mitigate risks within their operations and to their employees (e.g., canceling business events, limiting business travel, closing offices, and setting up work-at-home networks). Few have the resources to de-risk their supply chains, but that's exactly what's required.

COVID-19 won't be the last natural disaster or geopolitical event to disrupt global supply chains. It's imperative for a company to build a more diversified, agile supply chain that adapts to the next catastrophe — instead of frantically reacting to emergencies. To de-risk a supply chain, we evaluate in great detail all supplier options, both domestic and overseas, and all conditions associated with existing and potential suppliers:

- *Total landed costs* (e.g., product costs, transportation costs, customs, duties, taxes)
- *Value-adding benefits* (e.g., quality, lead times, reliability, financial stability, intellectual property, branding)
- *Network infrastructure* (e.g., distribution centers, freight management, labor availability, transportation systems, customs procedures, political climate)

This work extends vertically beyond first-tier suppliers to suppliers' suppliers. It also addresses make vs. buy, and how to efficiently execute on those plans in the future.

Supply chains around the world are likely to forever be changed by COVID-19. Some smaller second- and third-tier suppliers may not be able to withstand production delays and disappear. Other suppliers outside of China may find this to be an opportunity for growth and investment. The worldwide dependency on China as a supplier and buyer is likely to change as companies rethink these long-standing relationships, many of which were already strained by inflationary pressures and trade regulations. We're guiding executive decision-making in this new world order and helping companies to develop more diverse, agile supplier networks.

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About Argo:

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Our focus is on Food & Beverage, Industrial Manufacturing, Medical Products, Pharmaceuticals & Life Sciences, Aerospace & Defense, Supply Chain, Transportation, Chemical, Energy & Natural Resources, Industrial Aftermarket, Sales Force Effectiveness, Private Equity & M&A and Turnaround.

#Coronavirus
#SupplyChainRisks